Take Advantage of Your Home Equity: A Homeowner's Guide

Homeownership offers many advantages over renting, including a stable living environment, predictable monthly payments, and the freedom to make modifications. But one of the biggest benefits it offers is the opportunity to build wealth over time. Researchers at the Urban Institute found that homeownership is financially beneficial for most families,[1] and studies have shown that the median net worth of homeowners can be up to 80 times greater than that of renters in some areas.[2]

So how does purchasing a home help you build wealth? And what steps should you take to maximize the potential of your investment? Find out how to harness the power of home equity for a secure financial future.

WHAT IS HOME EQUITY?

Home equity is the difference between what your home is worth and the amount you owe on your mortgage. So, for example, if your home would currently sell for $250,000 and the remaining balance on your mortgage is $200,000, then you have $50,000 in home equity.

The equity in your home is considered a non-liquid asset. It's your money; but rather than sitting in a bank account, it's providing you with a place to live. And when you factor in the potential of appreciation, an investment in real estate will likely offer a better return than any savings account available today.

HOW DOES HOME EQUITY BUILD WEALTH?

A mortgage payment is a type of "forced savings" for home buyers. When you make a mortgage payment each month, a portion of it goes towards interest on your loan, and the remaining part goes towards paying off your principal, or loan balance. As your loan balance goes down, your home equity goes up.

Additionally, the value of your home generally increases, or appreciates, over time. And when you sell it, even if you've only paid off a small portion of your mortgage, you get to keep 100% of your property's appreciated value. That's the wealth-building power of real estate.

WHAT CAN I DO TO GROW MY HOME'S EQUITY FASTER?

There are two basic ways to increase the equity in your home:

1. **Pay down your mortgage.** Some homeowners do this by adding a little extra to their monthly payment, making one additional payment per year, or making a lump-sum payment when extra money becomes available. Another option is to decrease your amortization period. For example, if you can afford the higher monthly payment, consider refinancing from a 30-year or 25-year mortgage to a 15-year mortgage.

2. **Raise your home's market value.** Many homeowners enjoy do-it-yourself projects that add value at a relatively low cost. Others choose to invest in larger, strategic renovations. Keep in mind, you won't necessarily get back every dollar you spend on upgrades, so consult a professional before making any major investments.

A word of caution: neglecting routine maintenance could decrease your home's value (and equity), so be sure to stay on top of recommended upkeep and repairs.

HOW DO I ACCESS MY HOME EQUITY IF I NEED IT?

What if you want to tap into your home's equity while you're still living in it? There are several ways to borrow against your home equity, depending on your needs and qualifications:[3]

1. **A Second Mortgage** (or Home Equity Loan) enables you to borrow a lump sum, which you are responsible for paying back—with interest—over a set period of time. Most second mortgages have a fixed interest rate and provide the borrower with a predictable monthly payment.

2. With a **Cash-Out Refinance,** you refinance your mortgage for a higher amount than you currently owe. Then you pay off your original mortgage and keep the difference as cash. This option may be preferable if you have a high interest rate on your current mortgage or prefer to make just one payment per month.

3. A **Home Equity Line of Credit (HELOC)** is a revolving line of credit, similar to a credit card. It allows you to draw out money as you need it. The interest rate on a HELOC is variable, so your payment each month could change depending on how much you borrow and how interest rates fluctuate.

4. A **Reverse Mortgage** enables qualifying seniors to borrow against the equity in their home to supplement their retirement income. In most cases, the loan (plus interest) doesn't need to be repaid until the homeowners sell, move, or are deceased.[4]

It's important to note that borrowing against your home's equity isn't always the best option, and it carries the risk of foreclosure if you default. Ask us for a referral to a lender or financial adviser to find out if a home equity loan is right for you.

Sources: 1. Urban Institute 2. Census Bureau 3. Investopedia 4. Bankrate

WE'RE HERE TO HELP YOU

If you're ready to begin building equity with a new home purchase, grow the value of your current home, or access your equity through a home sale or loan—we can help. Contact us today to schedule a complimentary consultation!

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