How to protect and grow your home equity

One of the smartest things that homeowners can do in these days of uncertain investment markets is to build up the equity they have in their properties - or at least stop any existing equity from "leaking".

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Home equity is simply the difference between what a buyer would be prepared to pay for your home today (its market value) and the amount still outstanding on your home loan, and consumers shouldn't be daunted by the terminology.

They just need to focus on the fact that the bigger your equity in a property, the more you stand to put in your pocket when you sell that property – or the more you will be able to borrow for further investments using your property as security.

To some extent equity will grow by itself, provided that home prices keep rising – even slowly - and that the home owner keeps making his or her home loan repayments.

For example, our statistics show that home prices have risen by an average of almost 6% over the past 12 months, so a home purchased in June last year for R1m could now be worth R1,060m, immediately giving the homeowner R60,000 worth of equity.

Any deposit paid at the time of purchase and any reduction of the capital portion of the home loan would increase this equity amount, which can also be boosted by the homeowner paying an additional amount off the home loan every month.

On the other hand, equity build-up can be adversely affected by factors such as a softening economy, rising unemployment and a general loss of confidence among consumers that can cause property sales and appreciation to slow down.

Avoid refinancing

But even in such circumstances there are things that homeowners can do to manage and increase their home equity, the first of these being to avoid any thought of refinancing their home or switching their home loan to a different lender, even to take advantage of a lower interest rate.

There are usually costs and fees involved in refinancing or switching that will significantly reduce any benefit you might gain, and on top of that, home owners often take out cash when they make such a move, reset their loan term to 20 years and deplete all the equity they have built up for no good reason.

If they are then suddenly forced to sell, they may even find that the bigger home loan settlement amount plus selling costs actually exceeds the current market value of the property. This could mean that they walk away with zero 'profit' – or even that they have to pay in extra cash to liquidate the loan.

Guard against equity 'leakage'

Secondly, home owners need to guard against equity "leakage" through improper use of revolving home loan credit. Tapping into your accumulated equity - or the amount that you have already paid off your home loan - may be fine if you wish to pay for a child's education, deal with a major medical emergency or make appreciable improvements to your home, but using the money to buy a holiday or a depreciating asset such as a car really does not make financial sense.

Other no-no's for those keen to maximise their equity are secondary liens and debts against the property, as well as unpaid municipal rates and taxes, which all have to be paid when the time comes to sell.

And finally, while most additions and alterations will add value to the property, this must be weighed against what they will cost, to ensure that they will also increase the owner's equity in the property. Current market conditions and the area in which the home is located must be taken into account, and it would be best to seek the advice of a reputable local estate agent before going ahead with such projects."

ABOUT THE AUTHOR

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