

Home Equity Basics for Borrowers

Home equity is one of the most important sources of wealth for many Americans. If managed carefully, it can help you finance home improvements, pay for education or consolidate debts to simplify those payments.

Here's what you need to know so you can make the best use of it.

What is home equity?

Your home equity is your property's appraised value minus the mortgage. So your equity generally increases as you pay down the mortgage principal and can change with local real estate values.

Best uses of home equity

You should gradually increase your home equity, with the ultimate goal of paying off any mortgages and owning the property outright. Not having a loan to pay each month will let you put money toward other big goals, such as saving for retirement.

But careful use of home equity during your working years can be a wise move. Interest on both primary and secondary mortgages is usually [tax deductible](#) and the loan rate is usually lower than other loans because you secure the debt against your property. You still need to pay upfront costs like you did with your first mortgage, such as appraisal, title check and loan-origination fees, though.

How to borrow using your equity

Lenders such as First National Bank of Raymond can help you borrow in the form of home equity lines of credit, or [HELOCs](#). These loans usually have variable rates that can move up or down based on a market index. That means your monthly payment can vary, too. But because they are lines of credit, you only pay interest on the amount you've borrowed.

A word of caution

When you take on a HELOC, which is a [second mortgage](#), the lender can start foreclosure proceedings if you fail to repay the loan, or default. Home equity can be a powerful tool to pay for big-ticket items, but it should be used carefully.

Ideally, you'd prepare for major expenses by [saving money](#), but when you need financing for major life events such as a college education or projects such as home improvements, using home equity may be the best solution.

When it comes to financial planning, home equity can be a helpful last resort. Use it wisely to finance big life-changing purchases, but don't squander it on insignificant things.