HOW TO USE THE EQUITY IN YOUR HOME TO PURCHASE AN INVESTMENT PROPERTY

The great Aussie dream of repaying your mortgage and owning your home can sometimes feel like a lifetime away. While outright home ownership might be some time away it is worth acknowledging that each additional loan repayment builds equity in your home. Equity is the difference between the value of your property and the amount you still owe on your mortgage.

One of the most popular ways adopted by many homeowners to make progress financially is to purchase an investment property.

Did you know that you do not necessarily have to wait until you have repaid your home loan before you can start utilising your 'available' equity to purchase an investment property?

The good news is you can access the equity without having to sell your home!

How does it work?

Rather than contributing a cash deposit towards the purchase of an investment property, the equity in your existing home can be utilised as security for the purchase. In many instances, investors have borrowed the full cost of the investment property using this strategy.

When purchasing an investment property, it is important to understand that you can't use all the equity you have built up in your family home. Generally, lenders will allow you to borrow up to 80% of the value of your home (being the loan to value ratio – LVR), subject to serviceability and assessment.

If this was the case, the available equity in your home that may be utilised as security for the purchase of an investment property would be calculated by taking 80% of your home's current value less outstanding loan amounts.

The example below shows how the equity from a home valued at $850,000 with a loan of $550,000 can be used for this purpose.

Property value:	$850,000
An 80% LVR is:	$680,000
Debt owing:	$550,000
Available equity:	$130,000

This $130,000 available in your home equity can be utilised as security to cover the 20% (or less) deposit and associated costs required to be contributed for an investment property.

In this instance, subject to serviceability and lending guidelines, an investment property having a value of approximately $650,000 could be purchased.

Having purchased an investment property, the combined loans will equal no more than 80% of the combined value of the two properties.

Things to know:

- Lenders tend to value properties conservatively so the available equity in your home may be lower than your expectation. This may affect your purchase price.
- Having an LVR of less than 80% will help avoid the payment of lenders' mortgage insurance (LMI). Avoiding LMI is a good thing, however sometimes paying LMI on the investment purchase allows you to purchase a higher price or a better quality property.

  It isn't always a bad thing to pay LMI on an investment property as it is also tax deductable. This is a personal decision and you should seek professional advice from your adviser or accountant in conjunction with your finance team on the benefits and consequences.

Lenders consider several factors when determining your potential borrowing capacity.

These may include:

- your credit score
- your income, other loans, debts and serviceability of any shortfall between the rental income and the costs of holding the investment property
- the loan to value ratio (LVR)
- rental income
- your age and exit strategy when you retire
- any dependants and other costs that may affect your serviceability

Ultimately, the success of your loan application is determined by your individual circumstances.

Before making a decision and starting your search, we encourage you to book an appointment with us to determine your borrowing capacity and timing as to when you may be able to consider purchasing an investment property.

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