Your Home as Nest Egg for Retirement

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Focus on finance

Your Home as Nest Egg for Retirement

The COVID-19 pandemic was expected to hurt real estate markets. Instead, urban flight and historically low mortgage rates have spurred demand for suburban housing in major metropolitan areas. As you look forward to retirement in the current economic context, should you be planning to use your home as a nest egg or safety net? ***Our latest newsletter looks at these issues in detail below.***

Downsizing

You could choose to downsize your home, giving up a larger suburban home either for a smaller, less expensive home in the same metropolitan area or perhaps, selling and moving to a retirement community. The successful sell-down lowers your annual taxes, insurance, and utilities costs and increases the funds available in retirement. Its success depends on both the market sales price achieved and the debt outstanding on the home when sold.

Timing the sale of the home can therefore be crucial. Though we tend to think of housing markets as relatively stable, economic conditions do change and can affect housing market prices. The current coronavirus pandemic is an example of an unexpected event that has affected housing markets. If you were planning to sell your home at this time, you might achieve more than the sales price you planned due to unexpected market demand.

However, **overall demographic trends may not favor rising prices in many home markets.** As older Americans, many of them Boomers, retire and sell their homes, Gen Xers and Millennials may not be able or willing to absorb the number of homes being sold. Although a number of metropolitan areas are expected to be affected, including Tampa, Florida; Tucson, Arizona; Cleveland, Ohio; Pittsburgh, Pennsylvania; and Greensboro, North Carolina, prices in the Washington Metro area will likely continue increasing in the future.

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Refinancing

You could tap the equity in your home by refinancing your mortgage debt. A refinancing can work successfully if you wish to remain in your home, are carrying a home mortgage into retirement, but want to reduce your operating expenses. By refinancing your existing mortgage debt, but at a lower interest rate and a longer term, your monthly mortgage payments are reduced, thereby increasing your discretionary retirement income.

Your could remain in your home but refinance your mortgage for a larger amount, taking cash out to pay for current expenditures. You use take-out refinancing when you need additional cash now, such as for retirement-related home improvements or medical expenses. **However, because you will pay both principal and interest from your retirement income**, you might have fewer dollars of income in the future, and if your refinancing is poorly conceived or executed, it could jeopardize your long-term retirement income.

As with all re-financings, the willingness of bankers to extend mortgage loans at favorable interest rates depends on your credit rating, the overall economy, and mortgage loan markets. Further, when you are in or approaching retirement, bankers might require larger equity participation, perhaps 40% to 50% equity, and grant shorter total tenors, perhaps 20-year rather than 30-year mortgages. Take-out cash re-financings are a useful strategy but often diminish the estate left to heirs.

Renting out Your Home for Additional Income

You could decide to rent out (rather than selling) your existing home, and then use the net rental income to lease a place to live. This can be a cost-effective strategy because it preserves the home as a nest egg that you can tap by selling or refinancing later in your retirement. It is particularly useful if you own and rent out a home in a high demand metropolitan area, but want to rent one for yourself in a retirement community that offers sports facilities and organized social activities. Rents in retirement communities may be less than in dynamic metropolitan areas due to the same demographic changes noted above. The rent you received for your home in Arlington, Virginia, may allow you to lease beachfront retirement community property in Florida.

Bottom line - You can use your home to support your retirement, but you must be cognizant of real estate and mortgage market trends and developments, and remember that real estate is an investment subject to risk of loss, where past results are no guarantee of future success.

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