

The Best Ways to Finance a Home Reno

In love with that shiny new marble countertop in your renovated kitchen? Be careful it doesn't blind you into thinking it's going to make you money.

Contrary to what the shelter magazines and home decor TV shows would have you believe, expensive home renovations don't necessarily yield high returns, according to some real estate experts.

Those dazzling before-and-after images? They provide great entertainment.

For something with more substantial value, forgo the bells and whistles and stick to the basics, such as furnaces, windows and basement rental units, industry experts say.

"Home renos, in general, should not be looked upon as investments," says Arpad Komjathy, certified financial planner and mortgage broker at arpadwealth.ca in Toronto.

"They are only going to make you money if the reno elevates the buyer's heart rate, as in, 'Wow, that is an awesome kitchen,' and you are selling the home within a year or two of the upgrade. Longer than that, wear and tear will take its toll: Styles may change, property values may decline and all the while your money that you invested in the reno is tied up while you may be paying interest charges on the money borrowed to finance the reno."

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Debt and Renos

Taking on debt to finance a home renovation is not a smart move anyway, says Paul Rhodes, a partner in the audit and advisory practice at Crowe Soberman LLP, with clients in Canada's construction and real-estate industries.

"We are currently in a low-interest environment that will not last forever. A homeowner taking on debt to finance a renovation should bear in mind that rates will turn at some point in the not too distant future," Mr. Rhodes explains.

"It may be desirable to keep some repayment flexibility if it is possible, so that the debt can be repaid early, such as through an open mortgage or line of credit. Alternatively, if the term to repay the debt is expected to be longer, the homeowner should consider a fixed-rate mortgage, many of which still allow an annual prepayment."

Mr. Komjathy advises homeowners to consider various financing options before using their own funds.

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Financing Options

One place to look is the homeowner's existing mortgage. Two things can happen to a mortgage when the owner sells, Mr. Komjathy says: First, it is "ported" to a new property, which does not incur any extra costs, or secondly, it needs to be broken, which incurs penalties.

If owners can port the mortgage when they sell, it is a good option to finance a reno, Mr. Komjathy says. *"In this case the reno should be financed through an increased mortgage to achieve the lowest possible financing cost, at around 2.4 per cent for a variable rate or 2.8 per cent for a five-year fixed rate."*

If the mortgage is one that needs to be broken, it becomes more risky, but can still be used to finance a reno, he adds. The key is whether the original and new mortgages are variable-rate ones. Variable-rate mortgages have just a three-month penalty, and, considering their low-interest cost, this outweighs the penalty amount. If the mortgage is a fixed-rate one, the increased mortgage amount will attract a larger penalty that is often impossible to quantify in advance.

The next best option is to request a home equity line of credit (HELOC) and that will cost currently 3.5 per cent to 4 per cent. This type of loan will attract no penalty at the time of payout, Mr. Komjathy says.

"If there is insufficient equity in the home to increase the mortgage or add a HELOC, the next best option is an unsecured personal line of credit," he says, though these come with higher rates. *"Utilizing favourable promotional interest rates from credit card companies could be also an option, and that may lower the rate somewhat."*

But how do you know if renovating a home makes good financial sense?

Does a reno make sense?

The answer often depends on the situation at hand.

A family may have outgrown its current space and is considering renovation instead of buying a more expensive home, for example.

But if the renovation is intended to add value to the home when selling, *"beware the effect of increasing interest rates,"* Mr. Rhodes warns.

The types of renovations that make for a good investment when selling include adding living space in underused areas, such as basements and garages, according to Manjinder Grewal, a real-estate broker with Homelife Liberty Realty Inc. in Mississauga.

But it is still updated kitchens and bathrooms that remain the key renovations that help a home sell, says Charlene Kalia, a real-estate agent with Chestnut Park Real Estate in Toronto.

On a smaller scale, hardwood flooring, stainless steel appliances and ceramic sinks with multifunction faucets remain popular, says Tina Smith, a real-estate agent with Re/Max Hallmark Realty Ltd. in Toronto.

And if a renovation is not possible, even a quick refresh, including a coat of paint and decluttering, can add value to a sale, Mr. Komjathy says.

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