Homeowners "Crying with Joy" as New Home Equity Investment Product Solves Real Financial Problems

Most Americans dream about owning 100% of their home. But what about owning less than 100% - say, 70%, with the remainder freed up as cash to use for life's many expenses? With a new, game-changing home equity financing solution that enables this kind of flexibility, many homeowners across the country are now breathing a huge sigh of relief, as equity that was once tied up in their homes has now become accessible. And perhaps most attractive of all, they don't incur any additional debt in the process.

No end in sight for "house rich, cash poor" homeowners

Home ownership represents the biggest financial obligation for millions of Americans in their lifetimes. And yet to date, there have been surprisingly few traditional ways for homeowners to access the value locked up in their homes. While companies are able to raise capital and share their equity risk with investors by selling shares, opportunities for homeowners to similarly share the equity in their homes without having to service additional debt have been scarce.

The situation has forced homeowners to either sell their homes outright to unlock funds, or take on more debt through often costly options such as a cash-out refinance or a home equity line of credit (HELOC). And while some products have been designed to have "equity-like" features such as the shared appreciation mortgage, they still incur debt obligations for the homeowner.

As such, a significant proportion of the population have ended up "house rich, cash poor," whereby with such an enormous portion of their income being tied up with housing expenses such as mortgage payments and maintenance, they struggle to afford much else.

Source: Hometap

Last October’s first annual Hometap Homeownership Study of 675 US homeowners found that 19.5% of those surveyed feel “house rich, cash poor” most or all of the time, while 73% feel it at least some of the time. Experiencing such a dire situation is mainly due to the uncertainty homeowners have over their future income (according to 82% of respondents), as well as having to anticipate the costs of home maintenance and repairs (81%).

Even more startling is that two-thirds of homeowners are experiencing housing costs rising faster than their income, more than three-quarters expect this gap to worsen, and 57% have been unable to find solutions to escape their “house rich, cash poor” state.

Relief from financial stress is now here

Thanks to the Home Equity Contract (HEC), however, there is now a genuine opportunity to resolve this stressful predicament. First launched around ten years ago, the HEC began gathering steam during the latter half of the decade, as originators including Point Digital Finance, Hometap, Patch and Unison launched their own versions of the product. As virtually the sole non-debt solution for homeowners seeking to raise capital, today the HEC is proving crucial in offering much-needed financial flexibility to those who have the majority of their wealth tied up in their homes.

With over $100 million cumulative originations to date, Point is an unequivocal market leader in HECs. The Palo Alto-based originator applies a data-intensive approach to identify homeowners who could most benefit from the HEC. Upon agreement of the contract with the homeowner, Point buys into a portion of the home, thus providing the homeowner with liquidity which can be repaid at any point over an agreed period - for example, 30 years.

Point also lowers the appraised value of the home to give it a risk-adjusted buffer, whilst participating in any future appreciation of the home’s price during the life of the contract. As such, homeowners gain much-needed liquidity to alleviate some their most onerous financial burdens, and Point’s investors gain exposure to residential house prices, whilst receiving risk-adjusted, equity-like returns for participating in the future price appreciation of the home, and doing so at a discounted purchase price.

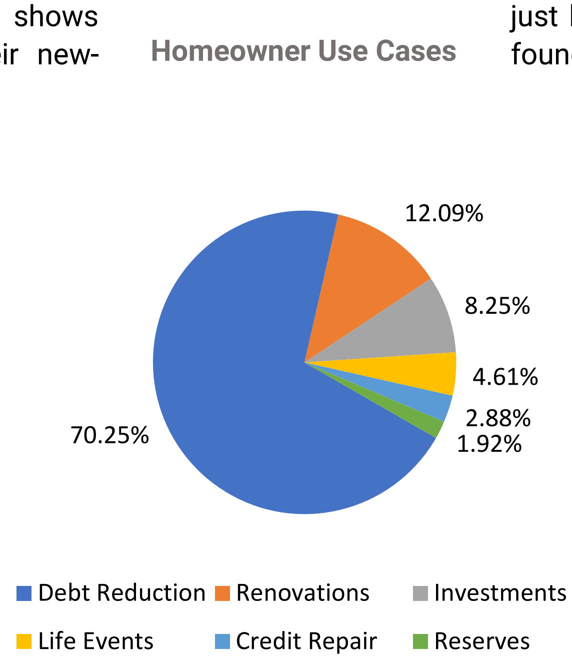
In Point’s case, the decidedly organic genesis of the HEC highlights a genuine goal of this product: to be a widespread and tangible real-world problem-solver. Rather than being engineered by a team of structurers in the offices of an investment bank, the HEC was born after Point founder Eddie Lim himself tried – without much success – to borrow on his home. In response, Lim began Point as an alternative to traditional home equity financing.

In the 5 or so years since launching, Point has received substantial backing from some of the most renowned investors in the venture capital space, further underlining the HEC’s transformative potential. Names including Andreesen Horowitz, DAG Ventures and Bloomberg Beta, as well as Orogen Group CEO and former Citigroup chief Vikram S. Pandit have provided support for Point’s development.

Noted investment manager and alternative investments specialist Kingsbridge Wealth Management has also pledged $100 million to back Point's contracts. "Homeowners with substantial home equity now have access to liquidity, without the burdens that come with debt financing," David Dunn, Kingsbridge's Chief Investment Officer, recently observed.

HECs already solving real-world financial problems for homeowners

Data from Kingsbridge shows just how homeowners engaged in HECs are using their new-found liquidity.



Overwhelmingly, the most popular use case is to pay off outstanding debt expenses, with more than 70% of capital obtained being used to pay off outstanding obligations including student loans, medical debt and credit card debt. As a result, this debt reduction should translate to an improvement in the homeowner's credit rating, which in turn bodes well for any future borrowing requirements.

Then comes "renovations" at over 12%, with homeowners now able to use their new funds to make home improvements. And with the median age of owner-occupied homes at 37 years and rising according to the National Association of Home Builders, it is perhaps no surprise that such a hefty proportion is being spent on refurbishments. Over 8% of the capital from HECs is being invested, whereby homeowners can now diversify their wealth by swapping out of their illiquid home equity and into other asset classes such as dividend-paying stocks, or private company equity.

And just how much does this newly-sourced liquidity mean to homeowners? A whole lot, the evidence suggests. "I have had Point homeowners call me crying with joy that they received their funds and are free from the financial – and emotional – burden of debt or to pursue the opportunity of their dreams," Point's investor operations lead Jordan Fox acknowledges. Eligible homeowners feel "a deep sense of relief" that this option is now available to them. "We often hear that our product sounds, 'too good to be true.'"

The HEC as an instrument for positive change

The growing interest in the HEC, specifically as a problem-solver for homeowners, also comes at a time when investors globally are ensuring their investments not only generate sufficient returns, but that they also have a positive impact on the world. With impact investing, responsible investing and ESG (Environmental, Social and Governance) investing all having taken off in recent years, the potential to relieve such a huge chunk of the population of longstanding financial troubles firmly places the Home Equity Contract in a similar ‘positive investing’ bracket.

Indeed, Point has already seen considerable interest for the HEC from this new crowd of conscientious investors. “When you have a product that aligns itself with the best interest of customers – like shared equity – ESG/responsible investors are interested,” notes Fox. “Debt has been around for thousands of years, and it hasn’t changed. Regardless of whether times are good or bad, borrowers have to make payments. Because Point breaks that cycle and aligns with homeowners, responsible investors are interested.” And by investing in Main Street as opposed to Wall Street, HECs offer investors the chance to directly address the financial struggles of homeowners all across the country.

Being an equity investment, moreover, aligns the interests of the homeowner and investor: when the homeowner does well through an appreciation in the home’s value, the investor also does well by sharing in that upside. As Fox explains, “We often tell homeowners, "We only do well when you do well," and our investors know that, too.” Conversely, should the value fall below the risk-adjusted level, both the investor and homeowner also share in the downside, something that a mortgage lender would not do in a traditional lending agreement.

“Our customers find the alignment between homeowners and investors very refreshing,” Fox reveals. “Many homeowners have a lot of mistrust in traditional financial companies but feel like Point is in their corner. As for investors, they can feel good about making (a risk-adjusted) investment in the success of homeowners.”

Investors can also be assured that those homeowners deemed eligible for the HEC won’t have problems honoring the terms of their contracts, thanks at least in part to the in-house eligibility process applied by the originator. According to Point, most homeowners have already successfully exited their 2015 and 2016 vintage contracts, with 99% repaid for the 2015 vintage and 79% for 2016. “We want to be sure that our funds will improve the lives of our homeowners, that homeowners will be able to exit the contract when the time comes, and that our investors are buying a perfected instrument,” Fox states.

As the 2008 housing crisis showed, introducing mechanisms that enable homeowners to effectively manage the risk from home ownership has been long overdue. Indeed, US residential real estate has been ripe for significant disruption for quite some time. But the HEC is now justifiably positioned among the most transformative disruptors within the space. It injects much-needed flexibility and innovation into a somewhat antiquated marketplace, whilst proving itself to be a major problem-solver that could ultimately end up reversing the worrying trend of America's rising "house rich, cash poor" numbers.

With originators now committing billions of dollars' worth of capital to this burgeoning space, it clearly demonstrates not just how successful the HEC has been thus far, but also how much potential there is in this rapidly expanding new market. With that in mind, there is now a golden opportunity to reimagine the possibilities of financing within the American residential real estate market - no longer does acquiring capital from the value of one's home need to be accompanied by monthly loan repayments.

Whether you're a millennial struggling to keep up with mortgage payments, a Gen X-er looking to make some refurbishments to your home, or a recently retired baby boomer needing to give that retirement account a boost, the HEC fulfills needs for multiple demographics of homeowners. As such, the days of having to sell your home or accumulate more debt to access liquidity could soon be over.