Borrowing to Invest

Borrowing to invest, also known as leveraging, can help grow your money, but it can also lead to larger losses. Be sure you understand these key points before borrowing money to invest:

How leverage works:

Taking a loan from a bank or lending institution:
Use caution - if you choose to use the equity in your home to secure this loan and the investment doesn't work out, you may have to sell your home to pay back the loan. If the investment is used as collateral for the loan and it drops in value, you still have to make payments. Also, you may be required to provide additional collateral to make up the difference.

Borrowing money through a brokerage firm: This is also known as buying on margin. Have a back-up plan if the investment doesn't work out because you will have to put more of your own money into your margin account if the investment loses money.

Is it right for me?

The risks of borrowing to invest are high. Be sure to fully understand the real cost of borrowing and the risks. Have a back-up plan to cover losses in case your investments don't work out. If you are not comfortable taking on this risk, talk to a financial advisor about other ways you can invest to help meet your goals.

Leveraging may not be appropriate for investors who:

- Have indicated they have limited investment knowledge
- Have low risk tolerance
- Are retired or nearing retirement
- Will need to access the money in less than 5 years
- Would have debt payments higher than 35% of their gross income
- Have or would have a debt load greater than 30% of their net worth

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What are the Risks? You could lose money. Whether the returns on your leveraged investments are positive or negative – you still have to pay back the loan, plus interest.

It may cost more to invest: Although returns on leveraged investments may be positive, you don't get to keep it all. You still have to pay the interest costs on the loan, and these could exceed your returns. There can also be fees to set up the investment or the loan, on-going maintenance fees and a fee for early withdrawal of the loan or the investment. Be sure to fully understand all associated borrowing costs before making any final decision.

You could damage your credit: If you are relying on the returns from leveraged investments to cover the cost of borrowing, you could default on the loan if the value of the investment decreases.

Questions to ask yourself:

- Do I fully understand how borrowing to invest (leveraging) works?
- Am I comfortable with the risk in the investment I want to make?
- How much interest will I pay each month? How does that compare with what I hope to make from my investment? What happens if the investment returns are not enough to pay the interest on the loan?
- If interest rates rise, will my costs increase?How will this affect what I make on the investment?
- Can I afford to lose some, or even all of the investment I made with the borrowed money?
- Will I be able to pay back what I borrowed from my savings?

Questions to ask your adviser:

- What are the risks associated with this investment?
- What happens if the investment drops in value?
- What happens if I want to get out early?
- How are you paid for selling this investment or for setting up the loan?
- How will this help me reach my goals?
- Are you and your firm registered with FCNB?

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