

Abstract: If you're a homeowner and have some extra cash after paying the monthly bills, should you use it to pay down your mortgage or invest those dollars in the stock market? This brief article expresses some thoughts on this age-old question.

Mortgage matters: To pay down or not to pay down

If you're a homeowner and manage your finances well, you might have extra cash after you've paid your monthly bills. What should you do with this extra money? Some would say make additional mortgage payments toward your principal to pay off your mortgage early. Others would say: No, invest those dollars in the stock market!

The decision is very much about risk vs. return. There's little, if any, risk in prepaying a mortgage, because you already know what your rate of return will be: the interest rate on your mortgage. For instance, if your mortgage interest rate is 4.5%, this would be the return earned by every dollar that goes toward prepayment (not factoring in the mortgage interest deduction if you qualify).

However, if you invest the money in the stock market, you'll assume much more risk. The level of risk depends on the assets you invest in, but there's no such thing as a risk-free investment.

Your mortgage interest rate is indeed an important factor. If your rate is relatively low, so is the return from prepaying your mortgage. The final decision for many people comes down to whether they believe they can earn a higher return investing the money than they would prepaying their mortgage.

Clearly there's the potential to outperform your mortgage interest rate by investing your money for the long term. Remember, though, that the stock market may be volatile in the short term and offers no guarantees.

There's no single answer to the "pay down the mortgage or invest in the market?" question. We can provide additional, more specific guidance on making the right decision for you.

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