

## Illustration of the **Four Components of "Return on Investment"**

### 1 **Cash Flow**

This first and perhaps most obvious component is "cash flow" - rental income minus expenses - or how much cash ends up in your pocket.

42,000	+	Rental Income
17,593	-	Operating Expenses
18,817	-	Mortgage Payments
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5,590	=	Cash Flow
127,500	/	Downpayment + Closing Costs
4.4%	=	Return on Investment from Cash Flow

### 2 **Appreciation**

As the value of the property increases, your return on investment increases.

425,000	=	Acquisition Price
5%	*	First Year Appreciation
446,250	=	Value at the end of Year 1.
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21,250	=	Amount of Value Increase
127,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

### 3 **Equity Build-Up**

4.25%      30 \$      1,568.06

Even if the property did not increase in value, Equity will increase solely from paying down the mortgage.

318,750	=	Loan Amount at Closing
313,376	=	Loan Amount at the end of Year 1
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5,374	-	Equity Build-Up in Year 1
127,500	/	Downpayment + Closing Costs
4.2%	=	Return on Investment from Equity Build-Up

### 4 **Tax Benefits**

One pays less income taxes on a real estate investment than on other investment vehicles.

24,407	=	Cash Flow Before Loan Payments (rents less expenses)
13,136	-	Depreciation (assumes 15% land, 27.5 year recovery)
13,443	-	Mortgage Interest
(2,172)	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
(717)	=	Federal Income Tax
(717)		Federal Income Tax
5,590	/	Cash Flow
-12.8%	=	Effective Tax Rate on This Investment
1,845	=	Tax if Cash Flow came from a non-preferred investment vehicle
(717)	-	Tax from this preferred investment vehicle.
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2,562	=	Income Tax Savings
2.0%		Return on Investment from Tax Savings

### **Total / Summary**

1:	5,590	Cash Flow
2:	21,250	Appreciation Year 1
3:	5,374	Equity Build Up Year 1
4:	2,562	Tax Savings Year 1
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	34,776	Total Return from this Investment
	127,500	Downpayment + Closing Costs
	27.3%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period**

**1216 BOLTON STREET**

Purchase Price	425,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	4.0%	42,000	43,680	45,427	47,244	49,134	51,099	53,143	55,269	57,480	59,779
Expenses	4.0%	17,593	18,297	19,029	19,790	20,581	21,405	22,261	23,151	24,077	25,040
Exp as a percent of Annual Rent		42%	42%	42%	42%	42%	42%	42%	42%	42%	42%
Exp per unit	4	4,398	4,574	4,757	4,947	5,145	5,351	5,565	5,788	6,019	6,260
NOI	0	24,407	25,383	26,399	27,455	28,553	29,695	30,883	32,118	33,403	34,739
Debt Service	\$ 1,568	18,817	18,817	18,817	18,817	18,817	18,817	18,817	18,817	18,817	18,817
<b>Before Tax Cash Flow</b>	<b>(127,500)</b>	<b>5,590</b>	<b>6,567</b>	<b>7,582</b>	<b>8,638</b>	<b>9,736</b>	<b>10,878</b>	<b>12,066</b>	<b>13,301</b>	<b>14,586</b>	<b>331,310</b>
<b>14.6% Internal Rate of Return</b>											
NOI		24,407	25,383	26,399	27,455	28,553	29,695	30,883	32,118	33,403	34,739
Less Interest		13,443	13,210	12,967	12,714	12,449	12,173	11,885	11,585	11,271	10,944
Less Depreciation		12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364
Taxable Income	0	(1,400)	(190)	1,068	2,377	3,740	5,158	6,634	8,169	9,768	11,431
Tax @	25%	(350)	(48)	267	594	935	1,290	1,658	2,042	2,442	2,858
<b>After Tax Cash Flow</b>	<b>(127,500)</b>	<b>5,940</b>	<b>6,614</b>	<b>7,315</b>	<b>8,044</b>	<b>8,801</b>	<b>9,589</b>	<b>10,408</b>	<b>11,259</b>	<b>12,144</b>	<b>275,002</b>
<b>12.6% Internal Rate of Return</b>											
Purchase	425,000								<b>Assume a Sale at End of Year 10</b>		
L-V	75%								Annual Rent Roll		59,779
Loan	318,750								GRM		10.1
Down Payment	106,250							annual appreciation	3.6%	Price	604,908
Cap Improvement	-								Sale Costs	6%	36,294
Closing Costs	21,250								Less: Basis		301,364
Initial Investment	127,500								Gain		267,249
Rate	4.25%								Tax @	20%	53,450
Term	30								Mortgage Balance		253,225
P&I	\$1,568.06								Sale Proceeds Before Tax		315,388
									Sale Proceeds After Tax		261,938
<b>Mortgage Amortization</b>		1	2	3	4	5	6	7	8	9	10
318,750	Beg Bal	318,750	313,376	307,770	301,920	295,817	289,450	282,806	275,875	268,643	261,098
4.25%	Prin	5,374	5,607	5,850	6,103	6,368	6,644	6,931	7,232	7,545	7,872
30.0	Int	13,443	13,210	12,967	12,714	12,449	12,173	11,885	11,585	11,271	10,944
1,568	Bal EOY	313,376	307,770	301,920	295,817	289,450	282,806	275,875	268,643	261,098	253,225
<b>Cost Recovery / Depreciation</b>		425,000	425,000	Building	80%	340,000	Land	20%	85,000	Life	27.5
		12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364	12,364
Basis		412,636	400,273	387,909	375,545	363,182	350,818	338,455	326,091	313,727	301,364