

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.

27,900	+	Rental Income
8,556	-	Operating Expenses
11,033	-	Mortgage Payments
<hr/>		
8,311	=	Cash Flow
70,500	/	Downpayment + Closing Costs
11.8%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

235,000	=	Acquisition Price
5%	*	First Year Appreciation
246,750	=	Value at the end of Year 1.
<hr/>		
11,750	=	Amount of Value Increase
70,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

4.75% 30 \$ 919.40

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

176,250	=	Loan Amount at Closing
173,530	=	Loan Amount at the end of Year 1
<hr/>		
2,720	-	Equity Build-Up in Year 1
70,500	/	Downpayment + Closing Costs
3.9%	=	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.

19,344	=	Cash Flow Before Loan Payments (rents less expenses)
7,264	-	Depreciation (assumes 15% land, 27.5 year recovery)
8,313	-	Mortgage Interest
3,767	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
1,243	=	Federal Income Tax
1,243		Federal Income Tax
8,311	/	Cash Flow
15.0%	=	Effective Tax Rate on This Investment
2,743	=	Tax if Cash Flow came from a non-preferred investment vehicle
1,243	-	Tax from this preferred investment vehicle.
<hr/>		
1,500	=	Income Tax Savings
2.1%		Return on Investment from Tax Savings

Total / Summary

1:	8,311	Cash Flow
2:	11,750	Appreciation Year 1
3:	2,720	Equity Build Up Year 1
4:	1,500	Tax Savings Year 1
<hr/>		
	24,280	Total Return from this Investment
	70,500	Downpayment + Closing Costs
	34.4%	Total Return from this Investment

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

869 WEST LOMBARD STREET

Purchase Price	235,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	3.0%	27,900	28,737	29,599	30,487	31,402	32,344	33,314	34,313	35,343	36,403
Expenses	3.0%	8,556	8,813	9,078	9,350	9,630	9,919	10,217	10,523	10,839	11,164
Exp as a percent of Annual Rent		31%	31%	31%	31%	31%	31%	31%	31%	31%	31%
Exp per unit	3	2,852	2,938	3,026	3,117	3,210	3,306	3,406	3,508	3,613	3,721
NOI	0	19,344	19,924	20,522	21,137	21,771	22,424	23,097	23,790	24,504	25,239
Debt Service	\$ 919	11,033	11,033	11,033	11,033	11,033	11,033	11,033	11,033	11,033	11,033
Before Tax Cash Flow	(70,500)	8,311	8,891	9,489	10,104	10,738	11,392	12,064	12,757	13,471	160,157
18.9% Internal Rate of Return											
NOI		19,344	19,924	20,522	21,137	21,771	22,424	23,097	23,790	24,504	25,239
Less Interest		8,313	8,181	8,043	7,898	7,745	7,586	7,418	7,243	7,059	6,866
Less Depreciation		6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836
Taxable Income	0	4,194	4,906	5,643	6,403	7,190	8,002	8,842	9,711	10,609	11,537
Tax @	25%	1,049	1,227	1,411	1,601	1,797	2,001	2,211	2,428	2,652	2,884
After Tax Cash Flow	(70,500)	7,262	7,664	8,078	8,504	8,941	9,391	9,854	10,330	10,819	132,955
15.8% Internal Rate of Return											
Purchase	235,000								Assume a Sale at End of Year 10		
L-V	75%								Montly Rent Roll		3,033.60
Loan	176,250								GRM		101.1
Down Payment	58,750							annual appreciation	2.7%	Price	306,622
Cap Improvement	-								Sale Costs	6%	18,397
Closing Costs	11,750								Less: Basis		166,636
Initial Investment	70,500								Gain		121,588
Rate	4.75%								Tax @	20%	24,318
Term	30								Mortgage Balance		142,273
P&I	\$919.40								Sale Proceeds Before Tax		145,951
									Sale Proceeds After Tax		121,634
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
176,250	Beg Bal	176,250	173,530	170,679	167,688	164,553	161,266	157,819	154,204	150,414	146,440
4.75%	Prin	2,720	2,852	2,990	3,135	3,288	3,447	3,614	3,790	3,974	4,167
30.0	Int	8,313	8,181	8,043	7,898	7,745	7,586	7,418	7,243	7,059	6,866
919	Bal EOY	173,530	170,679	167,688	164,553	161,266	157,819	154,204	150,414	146,440	142,273
Cost Recovery / Depreciation		235,000	235,000	Building	80%	188,000	Land	20%	47,000	Life	27.5
		6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836	6,836
Basis		228,164	221,327	214,491	207,655	200,818	193,982	187,145	180,309	173,473	166,636