

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.

58,356	+	Rental Income
27,350	-	Operating Expenses
19,835	-	Mortgage Payments
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11,170	=	Cash Flow
113,100	/	Downpayment + Closing Costs
9.9%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

377,000	=	Acquisition Price
5%	*	First Year Appreciation
395,850	=	Value at the end of Year 1.
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18,850	=	Amount of Value Increase
113,100	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

5.00% 25 \$ 1,652.93

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

282,750	=	Loan Amount at Closing
276,920	=	Loan Amount at the end of Year 1
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5,830	-	Equity Build-Up in Year 1
113,100	/	Downpayment + Closing Costs
5.2%	=	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.

31,005	=	Cash Flow Before Loan Payments (rents less expenses)
11,653	-	Depreciation (assumes 15% land, 27.5 year recovery)
14,005	-	Mortgage Interest
5,347	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
1,765	=	Federal Income Tax
1,765		Federal Income Tax
11,170	/	Cash Flow
15.8%	=	Effective Tax Rate on This Investment
3,686	=	Tax if Cash Flow came from a non-preferred investment vehicle
1,765	-	Tax from this preferred investment vehicle.
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1,921	=	Income Tax Savings
1.7%		Return on Investment from Tax Savings

Total / Summary

1:	11,170	Cash Flow
2:	18,850	Appreciation Year 1
3:	5,830	Equity Build Up Year 1
4:	1,921	Tax Savings Year 1
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	37,772	Total Return from this Investment
	113,100	Downpayment + Closing Costs
	33.4%	Total Return from this Investment

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

Purchase Price	377,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	4.0%	62,748	65,258	67,868	70,583	73,406	76,343	79,396	82,572	85,875	89,310
Vacancy	3.0%	1,882	1,958	2,036	2,117	2,202	2,290	2,382	2,477	2,576	2,679
Effective Income		60,866	63,300	65,832	68,465	71,204	74,052	77,014	80,095	83,299	86,631
Expenses	4.0%	27,350	28,444	29,582	30,766	31,996	33,276	34,607	35,991	37,431	38,928
Exp as a percent of Annual Rent		45%	45%	45%	45%	45%	45%	45%	45%	45%	45%
Exp per unit	6	4,558	4,741	4,930	5,128	5,333	5,546	5,768	5,999	6,238	6,488
NOI	0	33,515	34,856	36,250	37,700	39,208	40,776	42,407	44,104	45,868	47,702
Debt Service	\$ 1,653	19,835	19,835	19,835	19,835	19,835	19,835	19,835	19,835	19,835	19,835
Before Tax Cash Flow	(113,100)	13,680	15,021	16,415	17,865	19,373	20,941	22,572	24,268	26,033	323,239
21.7% Internal Rate of Return											
NOI		33,515	34,856	36,250	37,700	39,208	40,776	42,407	44,104	45,868	47,702
Less Interest		14,005	13,707	13,393	13,064	12,717	12,353	11,970	11,568	11,145	10,700
Less Depreciation		10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967
Taxable Income	0	8,543	10,182	11,889	13,669	15,523	17,456	19,470	21,568	23,756	26,035
Tax @	25%	2,136	2,545	2,972	3,417	3,881	4,364	4,867	5,392	5,939	6,509
After Tax Cash Flow	(113,100)	11,544	12,475	13,442	14,448	15,492	16,577	17,705	18,876	20,094	269,317
18.1% Internal Rate of Return											
Purchase	377,000								Assume a Sale at End of Year 10		
L-V	75%								Annual Rent Roll		89,310
Loan	282,750								GRM		6.0
Down Payment	94,250						annual appreciation	3.6%	Price		536,589
Cap Improvement	-								Sale Costs	6%	32,195
Closing Costs	18,850								Less: Basis		267,327
Initial Investment	113,100								Gain		237,066
Rate	5.00%								Tax @	20%	47,413
Term	25								Mortgage Balance		209,021
P&I	\$1,652.93								Sale Proceeds Before Tax		295,372
									Sale Proceeds After Tax		247,959
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
282,750	Beg Bal	282,750	276,920	270,792	264,350	257,578	250,460	242,978	235,114	226,846	218,156
5.00%	Prin	5,830	6,128	6,442	6,771	7,118	7,482	7,865	8,267	8,690	9,135
25.0	Int	14,005	13,707	13,393	13,064	12,717	12,353	11,970	11,568	11,145	10,700
1,653	Bal EOY	276,920	270,792	264,350	257,578	250,460	242,978	235,114	226,846	218,156	209,021
Cost Recovery / Depreciation		377,000	377,000	Building	80%	301,600	Land	20%	75,400	Life	27.5
		10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967	10,967
Basis		366,033	355,065	344,098	333,131	322,164	311,196	300,229	289,262	278,295	267,327