

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.

26,400	+	Rental Income
8,689	-	Operating Expenses
10,899	-	Mortgage Payments
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6,812	=	Cash Flow
71,700	/	Downpayment + Closing Costs
9.5%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

239,000	=	Acquisition Price
5%	*	First Year Appreciation
250,950	=	Value at the end of Year 1.
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11,950	=	Amount of Value Increase
71,700	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

4.50% 30 \$ 908.23

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

179,250	=	Loan Amount at Closing
176,358	=	Loan Amount at the end of Year 1
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2,892	-	Equity Build-Up in Year 1
71,700	/	Downpayment + Closing Costs
4.0%	=	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.

17,711	=	Cash Flow Before Loan Payments (rents less expenses)
7,387	-	Depreciation (assumes 15% land, 27.5 year recovery)
8,007	-	Mortgage Interest
2,317	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
765	=	Federal Income Tax
765		Federal Income Tax
6,812	/	Cash Flow
11.2%	=	Effective Tax Rate on This Investment
2,248	=	Tax if Cash Flow came from a non-preferred investment vehicle
765	-	Tax from this preferred investment vehicle.
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1,484	=	Income Tax Savings
2.1%	=	Return on Investment from Tax Savings

Total / Summary

1:	6,812	Cash Flow
2:	11,950	Appreciation Year 1
3:	2,892	Equity Build Up Year 1
4:	1,484	Tax Savings Year 1
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	23,138	Total Return from this Investment
	71,700	Downpayment + Closing Costs
	32.3%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period
4104 BUENA VISTA AVENUE**

Purchase Price	239,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	4.0%	26,400	27,456	28,554	29,696	30,884	32,120	33,404	34,741	36,130	37,575
Expenses	4.0%	8,689	9,036	9,398	9,774	10,165	10,571	10,994	11,434	11,891	12,367
Exp as a percent of Annual Rent		33%	33%	33%	33%	33%	33%	33%	33%	33%	33%
Exp per unit	1	8,689	9,036	9,398	9,774	10,165	10,571	10,994	11,434	11,891	12,367
NOI	0	17,711	18,420	19,157	19,923	20,720	21,548	22,410	23,307	24,239	25,209
Debt Service	\$ 908	10,899	10,899	10,899	10,899	10,899	10,899	10,899	10,899	10,899	10,899
Before Tax Cash Flow	(71,700)	6,812	7,521	8,258	9,024	9,821	10,650	11,512	12,408	13,340	190,511
18.8% Internal Rate of Return											
NOI		17,711	18,420	19,157	19,923	20,720	21,548	22,410	23,307	24,239	25,209
Less Interest		8,007	7,874	7,735	7,590	7,438	7,279	7,113	6,939	6,757	6,567
Less Depreciation		6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953
Taxable Income	0	2,751	3,593	4,468	5,380	6,329	7,317	8,345	9,415	10,530	11,689
Tax @	25%	688	898	1,117	1,345	1,582	1,829	2,086	2,354	2,632	2,922
After Tax Cash Flow	(71,700)	6,125	6,623	7,141	7,679	8,239	8,820	9,425	10,054	10,708	157,531
16.0% Internal Rate of Return											
Purchase	239,000							Assume a Sale at End of Year 10			
L-V	75%							Annual Rent Roll			37,575
Loan	179,250							GRM			9.1
Down Payment	59,750						annual appreciation	3.6%	Price		340,172
Cap Improvement	-							Sale Costs	6%		20,410
Closing Costs	11,950							Less: Basis			169,473
Initial Investment	71,700							Gain			150,289
Rate	4.50%							Tax @	20%		30,058
Term	30							Mortgage Balance			143,560
P&I	\$908.23							Sale Proceeds Before Tax			176,201
								Sale Proceeds After Tax			146,143
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
179,250	Beg Bal	179,250	176,358	173,334	170,170	166,861	163,401	159,781	155,995	152,035	147,893
4.50%	Prin	2,892	3,025	3,164	3,309	3,461	3,620	3,786	3,960	4,142	4,332
30.0	Int	8,007	7,874	7,735	7,590	7,438	7,279	7,113	6,939	6,757	6,567
908	Bal EOY	176,358	173,334	170,170	166,861	163,401	159,781	155,995	152,035	147,893	143,560
Cost Recovery / Depreciation		239,000	239,000	Building	80%	191,200	Land	20%	47,800	Life	27.5
		6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953	6,953
Basis		232,047	225,095	218,142	211,189	204,236	197,284	190,331	183,378	176,425	169,473