

## 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.

45,000	+	Rental Income
14,124	-	Operating Expenses
19,241	-	Mortgage Payments
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11,635	=	Cash Flow
112,500	/	Downpayment + Closing Costs
10.3%	=	Return on Investment from Cash Flow

### 2 **Appreciation**

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

375,000	=	Acquisition Price
5%	*	First Year Appreciation
393,750	=	Value at the end of Year 1.
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18,750	=	Amount of Value Increase
112,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

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

4.75%      25    \$    1,603.46

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

281,250	=	Loan Amount at Closing
275,238	=	Loan Amount at the end of Year 1
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6,012	-	Equity Build-Up in Year 1
112,500	/	Downpayment + Closing Costs
5.3%	=	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.

30,876	=	Cash Flow Before Loan Payments (rents less expenses)
10,625	-	Depreciation (assumes 15% land, 30 year recovery)
13,230	-	Mortgage Interest
7,022	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
2,317	=	Federal Income Tax
2,317		Federal Income Tax
11,635	/	Cash Flow
19.9%	=	Effective Tax Rate on This Investment
3,839	=	Tax if Cash Flow came from a non-preferred investment vehicle
2,317	-	Tax from this preferred investment vehicle.
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1,522	=	Income Tax Savings
1.4%		Return on Investment from Tax Savings

### **Total / Summary**

1:	11,635	Cash Flow
2:	18,750	Appreciation Year 1
3:	6,012	Equity Build Up Year 1
4:	1,522	Tax Savings Year 1
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	37,919	Total Return from this Investment
	112,500	Downpayment + Closing Costs
	33.7%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period  
2429 SAINT PAUL STREET**

Purchase Price	375,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	3.5%	45,000	46,575	48,205	49,892	51,639	53,446	55,316	57,253	59,256	61,330
Vacancy	3.0%	1,350	1,397	1,446	1,497	1,549	1,603	1,659	1,718	1,778	1,840
Effective Income		43,650	45,178	46,759	48,396	50,089	51,843	53,657	55,535	57,479	59,490
Expenses	3.5%	14,124	14,618	15,130	15,659	16,207	16,775	17,362	17,969	18,598	19,249
Exp as a percent of Annual Rent		32%	32%	32%	32%	32%	32%	32%	32%	32%	32%
Exp per unit	4	3,531	3,655	3,782	3,915	4,052	4,194	4,340	4,492	4,650	4,812
NOI	0	29,526	30,560	31,629	32,736	33,882	35,068	36,295	37,566	38,880	40,241
Debt Service	\$ 1,603	19,241	19,241	19,241	19,241	19,241	19,241	19,241	19,241	19,241	19,241
<b>Before Tax Cash Flow</b>	<b>(112,500)</b>	<b>10,285</b>	<b>11,318</b>	<b>12,388</b>	<b>13,495</b>	<b>14,640</b>	<b>15,826</b>	<b>17,054</b>	<b>18,324</b>	<b>19,639</b>	<b>295,277</b>
<b>18.3% Internal Rate of Return</b>											
NOI		29,526	30,560	31,629	32,736	33,882	35,068	36,295	37,566	38,880	40,241
Less Interest		13,230	12,938	12,632	12,311	11,974	11,622	11,252	10,864	10,457	10,031
Less Depreciation		10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000
Taxable Income	0	6,297	7,622	8,997	10,425	11,908	13,446	15,044	16,702	18,423	20,211
Tax @	25%	1,574	1,905	2,249	2,606	2,977	3,362	3,761	4,175	4,606	5,053
<b>After Tax Cash Flow</b>	<b>(112,500)</b>	<b>8,711</b>	<b>9,413</b>	<b>10,138</b>	<b>10,888</b>	<b>11,664</b>	<b>12,465</b>	<b>13,293</b>	<b>14,149</b>	<b>15,033</b>	<b>249,140</b>
<b>15.2% Internal Rate of Return</b>											
Purchase	375,000								<b>Assume a Sale at End of Year 10</b>		
L-V	75%								Annual Rent Roll		61,330
Loan	281,250								GRM		8.3
Down Payment	93,750						annual appreciation	3.1%	Price		511,087
Cap Improvement	-								Sale Costs	6%	30,665
Closing Costs	18,750								Less: Basis		275,000
Initial Investment	112,500								Gain		205,421
Rate	4.75%								Tax @	20%	41,084
Term	25								Mortgage Balance		206,144
P&I	\$1,603.46								Sale Proceeds Before Tax		274,277
									Sale Proceeds After Tax		233,193
<b>Mortgage Amortization</b>		1	2	3	4	5	6	7	8	9	10
281,250	Beg Bal	281,250	275,238	268,934	262,325	255,394	248,127	240,507	232,517	224,140	215,355
4.75%	Prin	6,012	6,304	6,610	6,931	7,267	7,620	7,990	8,378	8,784	9,211
25.0	Int	13,230	12,938	12,632	12,311	11,974	11,622	11,252	10,864	10,457	10,031
1,603	Bal EOY	275,238	268,934	262,325	255,394	248,127	240,507	232,517	224,140	215,355	206,144
<b>Cost Recovery / Depreciation</b>		375,000	375,000	Building	80%	300,000	Land	20%	75,000	Life	30
		10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000	10,000
Basis		365,000	355,000	345,000	335,000	325,000	315,000	305,000	295,000	285,000	275,000