

## 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.

210,467	+	Rental Income
98,794	-	Operating Expenses
57,869	-	Mortgage Payments
<hr/>		
53,804	=	Cash Flow
298,500	/	Downpayment + Closing Costs
18.0%	=	Return on Investment from Cash Flow

### 2 **Appreciation**

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

995,000	=	Acquisition Price
5%	*	First Year Appreciation
1,044,750	=	Value at the end of Year 1.
<hr/>		
49,750	=	Amount of Value Increase
298,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

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

4.75% 20 \$ 4,822.44

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

746,250	=	Loan Amount at Closing
723,333	=	Loan Amount at the end of Year 1
<hr/>		
22,917	-	Equity Build-Up in Year 1
298,500	/	Downpayment + Closing Costs
7.7%	=	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.

111,673	=	Cash Flow Before Loan Payments (rents less expenses)
28,192	-	Depreciation (assumes 15% land, 30 year recovery)
34,952	-	Mortgage Interest
48,529	=	Taxable Income Year 1
38,823	=	Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
14,364.64	=	Federal Income Tax
14,365	=	Federal Income Tax
53,804	/	Cash Flow
26.7%	=	Effective Tax Rate on This Investment
19,907	=	Tax if Cash Flow came from a non-preferred investment vehicle
14,365	-	Tax from this preferred investment vehicle.
<hr/>		
5,543	=	Income Tax Savings
1.9%	=	Return on Investment from Tax Savings

### **Total / Summary**

1:	53,804	Cash Flow
2:	49,750	Appreciation Year 1
3:	22,917	Equity Build Up Year 1
4:	5,543	Tax Savings Year 1
<hr/>		
	132,014	Total Return from this Investment
	298,500	Downpayment + Closing Costs
	44.2%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period  
5610 HARFORD ROAD**

Purchase Price	995,000	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028			
Annual Rent	4.0%	233,852	243,206	252,934	263,052	273,574	284,517	295,898	307,733	320,043	332,845			
Vacancy	3.0%	7,016	7,296	7,588	7,892	8,207	8,536	8,877	9,232	9,601	9,985			
Effective Income		226,837	235,910	245,346	255,160	265,367	275,981	287,021	298,501	310,442	322,859			
Expenses	4.0%	98,794	102,746	106,855	111,130	115,575	120,198	125,006	130,006	135,206	140,614			
Exp as a percent of Annual Rent		44%	44%	44%	44%	44%	44%	44%	44%	44%	44%			
Exp per unit	4	24,698	25,686	26,714	27,782	28,894	30,049	31,251	32,501	33,802	35,154			
NOI	0	128,043	133,164	138,491	144,031	149,792	155,784	162,015	168,496	175,235	182,245			
Debt Service	\$ 4,822	57,869	57,869	57,869	57,869	57,869	57,869	57,869	57,869	57,869	57,869			
<b>Before Tax Cash Flow</b>	<b>(298,500)</b>	<b>70,173</b>	<b>75,295</b>	<b>80,622</b>	<b>86,161</b>	<b>91,923</b>	<b>97,914</b>	<b>104,146</b>	<b>110,626</b>	<b>117,366</b>	<b>995,652</b>			
<b>32.1% Internal Rate of Return</b>														
NOI		128,043	133,164	138,491	144,031	149,792	155,784	162,015	168,496	175,235	182,245			
Less Interest		34,952	33,840	32,673	31,450	30,167	28,822	27,412	25,934	24,383	22,757			
Less Depreciation		26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533			
Taxable Income to Individuals		66,557	72,791	79,285	86,048	93,091	100,428	108,069	116,029	124,319	132,954			
Pass Thru Entity	20%	(13,311)	(14,558)	(15,857)	(17,210)	(18,618)	(20,086)	(21,614)	(23,206)	(24,864)	(26,591)			
Taxable Income	0	53,246	58,233	63,428	68,838	74,473	80,342	86,456	92,823	99,455	106,363			
Tax @ *	37%	19,701	21,546	23,468	25,470	27,555	29,727	31,989	34,344	36,798	39,354			
<b>After Tax Cash Flow</b>	<b>(298,500)</b>	<b>50,472</b>	<b>53,749</b>	<b>57,153</b>	<b>60,691</b>	<b>64,368</b>	<b>68,188</b>	<b>72,157</b>	<b>76,282</b>	<b>80,568</b>	<b>835,986</b>			
<b>24.8% Internal Rate of Return</b>														
Purchase	995,000							<b>Assume a Sale at End of Year 10</b>						
L-V	75%											332,845		
Loan	746,250											4.3		
Down Payment	248,750						annual appreciation 3.6%					1,416,195		
Cap Improvement	-											6%	84,972	
Closing Costs	49,750												729,667	
Initial Investment	298,500												601,557	
Rate	4.75%												20%	120,311
Term	20													459,947
P&I	\$4,822.44													871,276
														750,965
<b>Mortgage Amortization</b>		1	2	3	4	5	6	7	8	9	10			
746,250 Beg Bal		746,250	723,333	699,303	674,107	647,687	619,985	590,938	560,481	528,545	495,059			
4.75% Prin		22,917	24,030	25,196	26,419	27,702	29,047	30,457	31,936	33,486	35,112			
20.0 Int		34,952	33,840	32,673	31,450	30,167	28,822	27,412	25,934	24,383	22,757			
4,822 Bal EOY		723,333	699,303	674,107	647,687	619,985	590,938	560,481	528,545	495,059	459,947			
<b>Cost Recovery / Depreciation</b>		995,000	995,000	Building	80%	796,000	Land	20%	199,000	<b>Life</b>	<b>30</b>			
		26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533			
Basis		968,467	941,933	915,400	888,867	862,333	835,800	809,267	782,733	756,200	729,667			
* Tax rate of 35% applies to income of \$200,001 to \$500,000 for singles; \$400,001 to \$600,000 for married filing jointly. Marginal rate above \$500k/\$600k is 37%.														

Prepared by: Ben Frederick Realty Inc. For Illustration Purposes Only. Though believed accurate and reliable, information is not guaranteed.