

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.

30,000	+	Rental Income
7,891	-	Operating Expenses
11,427	-	Mortgage Payments
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10,682	=	Cash Flow
81,000	/	Downpayment + Closing Costs
13.2%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

270,000	=	Acquisition Price
5%	*	First Year Appreciation
283,500	=	Value at the end of Year 1.
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13,500	=	Amount of Value Increase
81,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

3.88% 30 \$ 952.23

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

202,500	=	Loan Amount at Closing
198,856	=	Loan Amount at the end of Year 1
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3,644	-	Equity Build-Up in Year 1
81,000	/	Downpayment + Closing Costs
4.5%	=	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.

22,109	=	Cash Flow Before Loan Payments (rents less expenses)
8,345	-	Depreciation (assumes 15% land, 27.5 year recovery)
7,783	-	Mortgage Interest
5,981	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
1,974	=	Federal Income Tax
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10,682	/	Cash Flow
18.5%	=	Effective Tax Rate on This Investment
3,525	=	Tax if Cash Flow came from a non-preferred investment vehicle
1,974	-	Tax from this preferred investment vehicle.
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1,551	=	Income Tax Savings
1.9%		Return on Investment from Tax Savings

Total / Summary

1:	10,682	Cash Flow
2:	13,500	Appreciation Year 1
3:	3,644	Equity Build Up Year 1
4:	1,551	Tax Savings Year 1
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	29,378	Total Return from this Investment
	81,000	Downpayment + Closing Costs
	36.3%	Total Return from this Investment