

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.

182,232	+	Rental Income
52,715	-	Operating Expenses
87,885	-	Mortgage Payments
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41,631	=	Cash Flow
555,000	/	Downpayment + Closing Costs
7.5%	=	Return on Investment from Cash Flow

2 Appreciation

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

1,850,000	=	Acquisition Price
5%	*	First Year Appreciation
1,942,500	=	Value at the end of Year 1.
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92,500	=	Amount of Value Increase
555,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 Equity Build-Up

4.00% 25 \$ 7,323.74

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

1,387,500	=	Loan Amount at Closing
1,354,515	=	Loan Amount at the end of Year 1
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32,985	-	Equity Build-Up in Year 1
555,000	/	Downpayment + Closing Costs
5.9%	=	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.

129,516	=	Cash Flow Before Loan Payments (rents less expenses)
52,417	-	Depreciation (assumes 15% land, 30 year recovery)
54,900	-	Mortgage Interest
22,200	=	Taxable Income Year 1
17,760		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
6,571.19	=	Federal Income Tax
6,571		Federal Income Tax
41,631	/	Cash Flow
15.8%	=	Effective Tax Rate on This Investment
15,404	=	Tax if Cash Flow came from a non-preferred investment vehicle
6,571	-	Tax from this preferred investment vehicle.
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8,832	=	Income Tax Savings
1.6%		Return on Investment from Tax Savings

Total / Summary

1:	41,631	Cash Flow
2:	92,500	Appreciation Year 1
3:	32,985	Equity Build Up Year 1
4:	8,832	Tax Savings Year 1
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	175,949	Total Return from this Investment
	555,000	Downpayment + Closing Costs
	31.7%	Total Return from this Investment

