

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.

42,792	+	Rental Income
13,442	-	Operating Expenses
9,093	-	Mortgage Payments
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20,257	=	Cash Flow
67,500	/	Downpayment + Closing Costs
30.0%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

225,000	=	Acquisition Price
5%	*	First Year Appreciation
236,250	=	Value at the end of Year 1.
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11,250	=	Amount of Value Increase
67,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

3.50% 30 \$ 757.76

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

168,750	=	Loan Amount at Closing
165,511	=	Loan Amount at the end of Year 1
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3,239	-	Equity Build-Up in Year 1
67,500	/	Downpayment + Closing Costs
4.8%	=	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.

29,350	=	Cash Flow Before Loan Payments (rents less expenses)
6,955	-	Depreciation (assumes 15% land, 27.5 year recovery)
5,855	-	Mortgage Interest
16,541	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
5,458	=	Federal Income Tax
5,458		Federal Income Tax
20,257	/	Cash Flow
26.9%	=	Effective Tax Rate on This Investment
6,685	=	Tax if Cash Flow came from a non-preferred investment vehicle
5,458	-	Tax from this preferred investment vehicle.
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1,226	=	Income Tax Savings
1.8%		Return on Investment from Tax Savings

Total / Summary

1:	20,257	Cash Flow
2:	11,250	Appreciation Year 1
3:	3,239	Equity Build Up Year 1
4:	1,226	Tax Savings Year 1
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	35,972	Total Return from this Investment
	67,500	Downpayment + Closing Costs
	53.3%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period

4223 AUDREY AVE & 3901 PASCAL AVE

Purchase Price	225,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	4.0%	42,792	44,504	46,284	48,135	50,061	52,063	54,146	56,311	58,564	60,906
Expenses	4.0%	13,442	13,980	14,539	15,121	15,725	16,354	17,009	17,689	18,397	19,132
Exp as a percent of Annual Rent		31%	31%	31%	31%	31%	31%	31%	31%	31%	31%
Exp per unit	4	3,361	3,495	3,635	3,780	3,931	4,089	4,252	4,422	4,599	4,783
NOI	0	29,350	30,524	31,745	33,015	34,335	35,709	37,137	38,622	40,167	41,774
Debt Service	\$ 758	9,093	9,093	9,093	9,093	9,093	9,093	9,093	9,093	9,093	9,093
Before Tax Cash Flow	(67,500)	20,257	21,431	22,652	23,921	25,242	26,615	28,044	29,529	31,074	203,053
36.8% Internal Rate of Return											
NOI		29,350	30,524	31,745	33,015	34,335	35,709	37,137	38,622	40,167	41,774
Less Interest		5,855	5,739	5,620	5,497	5,369	5,236	5,099	4,957	4,810	4,658
Less Depreciation		6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545
Taxable Income	0	16,950	18,239	19,579	20,972	22,421	23,927	25,492	27,120	28,812	30,571
Tax @	25%	4,237	4,560	4,895	5,243	5,605	5,982	6,373	6,780	7,203	7,643
After Tax Cash Flow	(67,500)	16,019	16,871	17,757	18,678	19,637	20,634	21,671	22,749	23,871	167,114
29.8% Internal Rate of Return											
Purchase	225,000							Assume a Sale at End of Year 10			
L-V	75%							Annual Rent Roll			60,906
Loan	168,750							GRM			5.3
Down Payment	56,250						annual appreciation 3.6%	Price			320,245
Cap Improvement	-							Sale Costs		6%	19,215
Closing Costs	11,250							Less: Basis			159,545
Initial Investment	67,500							Gain			141,485
Rate	3.50%							Tax @		20%	28,297
Term	30							Mortgage Balance			130,658
P&I	\$757.76							Sale Proceeds Before Tax			170,373
								Sale Proceeds After Tax			142,076
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
168,750 Beg Bal		168,750	165,511	162,158	158,685	155,088	151,364	147,507	143,513	139,377	135,093
3.50% Prin		3,239	3,354	3,473	3,597	3,724	3,857	3,994	4,136	4,283	4,436
30.0 Int		5,855	5,739	5,620	5,497	5,369	5,236	5,099	4,957	4,810	4,658
758 Bal EOY		165,511	162,158	158,685	155,088	151,364	147,507	143,513	139,377	135,093	130,658
Cost Recovery / Depreciation		225,000	225,000	Building	80%	180,000	Land	20%	45,000	Life	27.5
		6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545	6,545
Basis		218,455	211,909	205,364	198,818	192,273	185,727	179,182	172,636	166,091	159,545