

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.

61,956	+	Rental Income
18,028	-	Operating Expenses
24,046	-	Mortgage Payments
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19,882	=	Cash Flow
178,500	/	Downpayment + Closing Costs
11.1%	=	Return on Investment from Cash Flow

2 Appreciation

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

595,000	=	Acquisition Price
5%	*	First Year Appreciation
624,750	=	Value at the end of Year 1.
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29,750	=	Amount of Value Increase
178,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 Equity Build-Up

3.50% 30 \$ 2,003.86

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

446,250	=	Loan Amount at Closing
437,686	=	Loan Amount at the end of Year 1
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8,564	-	Equity Build-Up in Year 1
178,500	/	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.

43,928	=	Cash Flow Before Loan Payments (rents less expenses)
16,858	-	Depreciation (assumes 15% land, 30 year recovery)
15,482	-	Mortgage Interest
11,588	=	Taxable Income Year 1
9,270		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
3,430.01	=	Federal Income Tax
3,430		Federal Income Tax
19,882	/	Cash Flow
17.3%	=	Effective Tax Rate on This Investment
7,356	=	Tax if Cash Flow came from a non-preferred investment vehicle
3,430	-	Tax from this preferred investment vehicle.
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3,926	=	Income Tax Savings
2.2%		Return on Investment from Tax Savings

Total / Summary

1:	19,882	Cash Flow
2:	29,750	Appreciation Year 1
3:	8,564	Equity Build Up Year 1
4:	3,926	Tax Savings Year 1
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	62,123	Total Return from this Investment
	178,500	Downpayment + Closing Costs
	34.8%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period
3020 NORTH CALVERT STREET

Purchase Price	595,000	2023	2024	2025	2026	2027	2028	2029	2030		2031	2032
Annual Rent	4.0%	61,956	64,434	67,012	69,692	72,480	75,379	78,394	81,530		84,791	88,183
Vacancy	3.0%	1,859	1,933	2,010	2,091	2,174	2,261	2,352	2,446		2,544	2,645
Effective Income		60,097	62,501	65,001	67,601	70,305	73,118	76,042	79,084		82,247	85,537
Expenses	4.0%	18,028	18,749	19,499	20,279	21,090	21,933	22,811	23,723		24,672	25,659
Exp as a percent of Annual Rent		30%	30%	30%	30%	30%	30%	30%	30%		30%	30%
Exp per unit	4	4,507	4,687	4,875	5,070	5,272	5,483	5,703	5,931		6,168	6,415
NOI	0	42,070	43,753	45,503	47,323	49,216	51,184	53,232	55,361		57,575	59,878
Debt Service	\$ 2,004	24,046	24,046	24,046	24,046	24,046	24,046	24,046	24,046		24,046	24,046
Before Tax Cash Flow	(178,500)	18,023	19,706	21,456	23,276	25,169	27,138	29,185	31,315		33,529	542,138
20.2% Internal Rate of Return												
NOI		42,070	43,753	45,503	47,323	49,216	51,184	53,232	55,361		57,575	59,878
Less Interest		15,482	15,178	14,862	14,536	14,197	13,847	13,484	13,109		12,720	12,317
Less Depreciation		15,867	15,867	15,867	15,867	15,867	15,867	15,867	15,867		15,867	15,867
Taxable Income to Individuals		10,721	12,708	14,774	16,921	19,152	21,471	23,881	26,386		28,989	31,695
Pass Thru Entity	20%	(2,144)	(2,542)	(2,955)	(3,384)	(3,830)	(4,294)	(4,776)	(5,277)		(5,798)	(6,339)
Taxable Income	0	8,577	10,167	11,819	13,536	15,321	17,177	19,105	21,109		23,191	25,356
Tax @ *	37%	3,173	3,762	4,373	5,008	5,669	6,355	7,069	7,810		8,581	9,382
After Tax Cash Flow	(178,500)	14,850	15,945	17,083	18,268	19,500	20,783	22,117	23,504		24,948	449,658
16.7% Internal Rate of Return												
Purchase	595,000											
L-V	75%											
Loan	446,250											
Down Payment	148,750											
Cap Improvement	-											
Closing Costs	29,750											
Initial Investment	178,500											
Rate	3.50%											
Term	30											
P&I	\$2,003.86											
										Assume a Sale at End of Year 10		
										Annual Rent Roll		
										GRM		
										Price		
										Sale Costs		
										Less: Basis		
										Gain		
										Tax @		
										Mortgage Balance		
										Sale Proceeds Before Tax		
										Sale Proceeds After Tax		
Mortgage Amortization		1	2	3	4	5	6	7	8		9	10
446,250 Beg Bal		446,250	437,686	428,817	419,633	410,122	400,273	390,074	379,512		368,574	357,247
3.50% Prin		8,564	8,869	9,184	9,511	9,849	10,199	10,562	10,938		11,327	11,730
30.0 Int		15,482	15,178	14,862	14,536	14,197	13,847	13,484	13,109		12,720	12,317
2,004 Bal EOY		437,686	428,817	419,633	410,122	400,273	390,074	379,512	368,574		357,247	345,517
Cost Recovery / Depreciation		595,000	595,000	Building	80%	476,000	Land	20%	119,000		Life	30
		15,867	15,867	15,867	15,867	15,867	15,867	15,867	15,867		15,867	15,867
Basis		579,133	563,267	547,400	531,533	515,667	499,800	483,933	468,067		452,200	436,333

* 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%.