

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.

67,140	+	Rental Income
12,804	-	Operating Expenses
28,159	-	Mortgage Payments
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26,177	=	Cash Flow
173,500	/	Downpayment + Closing Costs
15.1%	=	Return on Investment from Cash Flow

2 Appreciation

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

495,000	=	Acquisition Price
5%	*	First Year Appreciation
519,750	=	Value at the end of Year 1.
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24,750	=	Amount of Value Increase
173,500	/	Downpayment + Closing Costs
14%	=	Return on Investment from Appreciation

3 Equity Build-Up

6.50% 30 \$ 2,346.55

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

371,250	=	Loan Amount at Closing
367,100	=	Loan Amount at the end of Year 1
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4,150	-	Equity Build-Up in Year 1
173,500	/	Downpayment + Closing Costs
2.4%	=	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.

54,336	=	Cash Flow Before Loan Payments (rents less expenses)
14,025	-	Depreciation (assumes 15% land, 30 year recovery)
24,009	-	Mortgage Interest
16,302	=	Taxable Income Year 1
13,042	=	Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
4,825.39	=	Federal Income Tax
4,825	=	Federal Income Tax
26,177	/	Cash Flow
18.4%	=	Effective Tax Rate on This Investment
9,686	=	Tax if Cash Flow came from a non-preferred investment vehicle
4,825	-	Tax from this preferred investment vehicle.
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4,860	=	Income Tax Savings
2.8%	=	Return on Investment from Tax Savings

Total / Summary

1:	26,177	Cash Flow
2:	24,750	Appreciation Year 1
3:	4,150	Equity Build Up Year 1
4:	4,860	Tax Savings Year 1
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	59,937	Total Return from this Investment
	173,500	Downpayment + Closing Costs
	34.5%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period
2937 NORTH CALVERT STREET

Purchase Price	495,000	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Annual Rent	4.0%	67,140	69,826	72,619	75,523	78,544	81,686	84,954	88,352	91,886	95,561
Vacancy	3.0%	2,014	2,095	2,179	2,266	2,356	2,451	2,549	2,651	2,757	2,867
Effective Income		65,126	67,731	70,440	73,258	76,188	79,235	82,405	85,701	89,129	92,694
Expenses	4.0%	12,804	13,316	13,849	14,403	14,979	15,578	16,201	16,849	17,523	18,224
Exp as a percent of Annual Rent		20%	20%	20%	20%	20%	20%	20%	20%	20%	20%
Exp per unit	2	6,402	6,658	6,924	7,201	7,489	7,789	8,101	8,425	8,762	9,112
NOI	0	52,322	54,415	56,591	58,855	61,209	63,658	66,204	68,852	71,606	74,470
Debt Service	\$ 2,347	28,159	28,159	28,159	28,159	28,159	28,159	28,159	28,159	28,159	28,159
Before Tax Cash Flow	(148,500)	24,163	26,256	28,433	30,696	33,051	35,499	38,045	40,693	43,447	427,295
25.2% Internal Rate of Return											
NOI		52,322	54,415	56,591	58,855	61,209	63,658	66,204	68,852	71,606	74,470
Less Interest		24,009	23,731	23,435	23,118	22,781	22,421	22,036	21,626	21,189	20,722
Less Depreciation		13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200
Taxable Income to Individuals		15,113	17,484	19,957	22,537	25,228	28,037	30,968	34,026	37,217	40,548
Pass Thru Entity	20%	(3,023)	(3,497)	(3,991)	(4,507)	(5,046)	(5,607)	(6,194)	(6,805)	(7,443)	(8,110)
Taxable Income	0	12,090	13,987	15,965	18,029	20,183	22,430	24,774	27,221	29,774	32,439
Tax @ *	37%	4,473	5,175	5,907	6,671	7,468	8,299	9,166	10,072	11,016	12,002
After Tax Cash Flow	(148,500)	19,690	21,081	22,526	24,026	25,583	27,200	28,879	30,622	32,431	348,750
20.5% Internal Rate of Return											
Purchase	495,000								Assume a Sale at End of Year 10		
L-V	75%								Annual Rent Roll		95,561
Loan	371,250								GRM		7.7
Down Payment	123,750					annual appreciation	4.1%		Price		740,122
Cap Improvement	-								Sale Costs	6%	44,407
Closing Costs	24,750								Less: Basis		363,000
Initial Investment	148,500								Gain		332,715
Rate	6.50%								Tax @	20%	66,543
Term	30								Mortgage Balance		314,731
P&I	\$2,346.55								Sale Proceeds Before Tax		380,983
									Sale Proceeds After Tax		314,440
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
371,250 Beg Bal		371,250	367,100	362,673	357,949	352,909	347,531	341,793	335,670	329,138	322,168
6.50% Prin		4,150	4,427	4,724	5,040	5,378	5,738	6,122	6,532	6,970	7,437
30.0 Int		24,009	23,731	23,435	23,118	22,781	22,421	22,036	21,626	21,189	20,722
2,347 Bal EOY		367,100	362,673	357,949	352,909	347,531	341,793	335,670	329,138	322,168	314,731
Cost Recovery / Depreciation		495,000	495,000	Building	80%	396,000	Land	20%	99,000	Life	30
		13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200	13,200
Basis		481,800	468,600	455,400	442,200	429,000	415,800	402,600	389,400	376,200	363,000

* 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%.