

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.

76,800	+	Rental Income
15,510	-	Operating Expenses
39,536	-	Mortgage Payments
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21,754	=	Cash Flow
208,500	/	Downpayment + Closing Costs
10.4%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

695,000	=	Acquisition Price
5%	*	First Year Appreciation
729,750	=	Value at the end of Year 1.
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34,750	=	Amount of Value Increase
208,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

6.50% 30 \$ 3,294.65

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

521,250	=	Loan Amount at Closing
515,424	=	Loan Amount at the end of Year 1
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5,826	-	Equity Build-Up in Year 1
208,500	/	Downpayment + Closing Costs
2.8%	=	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.

61,290	=	Cash Flow Before Loan Payments (rents less expenses)
21,482	-	Depreciation (assumes 15% land, 27.5 year recovery)
33,710	-	Mortgage Interest
6,099	=	Taxable Income Year 1
33%	*	Marginal Tax Rate
2,013	=	Federal Income Tax
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21,754	/	Cash Flow
9.3%	=	Effective Tax Rate on This Investment
7,179	=	Tax if Cash Flow came from a non-preferred investment vehicle
2,013	-	Tax from this preferred investment vehicle.
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5,166	=	Income Tax Savings
2.5%		Return on Investment from Tax Savings

Total / Summary

1:	21,754	Cash Flow
2:	34,750	Appreciation Year 1
3:	5,826	Equity Build Up Year 1
4:	5,166	Tax Savings Year 1
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	67,497	Total Return from this Investment
	208,500	Downpayment + Closing Costs
	32.4%	Total Return from this Investment

