

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.

119,073	+	Rental Income
34,042	-	Operating Expenses
69,043	-	Mortgage Payments
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15,988	=	Cash Flow
233,825	/	Downpayment + Closing Costs
6.8%	=	Return on Investment from Cash Flow

2 Appreciation

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

995,000	=	Acquisition Price
5%	*	First Year Appreciation
1,044,750	=	Value at the end of Year 1.
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49,750	=	Amount of Value Increase
233,825	/	Downpayment + Closing Costs
21%	=	Return on Investment from Appreciation

3 Equity Build-Up

7.25% 25 \$ 5,753.54

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

796,000	=	Loan Amount at Closing
784,283	=	Loan Amount at the end of Year 1
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11,717	-	Equity Build-Up in Year 1
233,825	/	Downpayment + Closing Costs
5.0%	=	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.

85,031	=	Cash Flow Before Loan Payments (rents less expenses)
28,192	-	Depreciation (assumes 15% land, 30 year recovery)
57,326	-	Mortgage Interest
(487)	=	Taxable Income Year 1
(390)		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
(144.12)	=	Federal Income Tax
(144)		Federal Income Tax
15,988	/	Cash Flow
-0.9%	=	Effective Tax Rate on This Investment
5,916	=	Tax if Cash Flow came from a non-preferred investment vehicle
(144)	-	Tax from this preferred investment vehicle.
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6,060	=	Income Tax Savings
2.6%		Return on Investment from Tax Savings

Total / Summary

1:	15,988	Cash Flow
2:	49,750	Appreciation Year 1
3:	11,717	Equity Build Up Year 1
4:	6,060	Tax Savings Year 1
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	83,514	Total Return from this Investment
	233,825	Downpayment + Closing Costs
	35.7%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period
4711 1/2 - 4715 HARFORD ROAD

Purchase Price	995,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	4.0%	125,340	130,354	135,568	140,990	146,630	152,495	158,595	164,939	171,536	178,398
Vacancy	3.0%	3,760	3,911	4,067	4,230	4,399	4,575	4,758	4,948	5,146	5,352
Effective Income		121,580	126,443	131,501	136,761	142,231	147,920	153,837	159,991	166,390	173,046
Expenses	4.0%	34,042	35,404	36,820	38,293	39,825	41,418	43,075	44,798	46,589	48,453
Exp as a percent of Annual Rent		28%	28%	28%	28%	28%	28%	28%	28%	28%	28%
Exp per unit	8	4,255	4,426	4,603	4,787	4,978	5,177	5,384	5,600	5,824	6,057
NOI	0	87,537	91,039	94,680	98,468	102,406	106,503	110,763	115,193	119,801	124,593
Debt Service	\$ 5,754	69,043	69,043	69,043	69,043	69,043	69,043	69,043	69,043	69,043	69,043
Before Tax Cash Flow	(248,750)	18,495	21,996	25,638	29,425	33,364	37,460	41,720	46,151	50,758	826,564
20.2% Internal Rate of Return											
NOI		87,537	91,039	94,680	98,468	102,406	106,503	110,763	115,193	119,801	124,593
Less Interest		57,326	56,447	55,503	54,488	53,398	52,225	50,964	49,609	48,152	46,587
Less Depreciation		26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533
Taxable Income to Individuals		3,678	8,058	12,644	17,446	22,475	27,744	33,265	39,051	45,115	51,473
Pass Thru Entity	20%	(736)	(1,612)	(2,529)	(3,489)	(4,495)	(5,549)	(6,653)	(7,810)	(9,023)	(10,295)
Taxable Income	0	2,943	6,446	10,115	13,957	17,980	22,195	26,612	31,241	36,092	41,178
Tax @ *	37%	1,089	2,385	3,743	5,164	6,653	8,212	9,846	11,559	13,354	15,236
After Tax Cash Flow	(248,750)	17,406	19,611	21,895	24,261	26,711	29,248	31,874	34,592	37,404	677,003
17.1% Internal Rate of Return											
Purchase	995,000										
L-V	80%										178,398
Loan	796,000										8.4
Down Payment	199,000										1,490,732
Cap Improvement	-										89,444
Closing Costs	49,750										729,667
Initial Investment	248,750										671,621
Rate	7.25%										134,324
Term	25										630,275
P&I	\$5,753.54										771,013
											636,689
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
796,000 Beg Bal		796,000	784,283	771,688	758,149	743,595	727,950	711,132	693,054	673,621	652,731
7.25% Prin		11,717	12,595	13,539	14,554	15,645	16,818	18,078	19,433	20,890	22,456
25.0 Int		57,326	56,447	55,503	54,488	53,398	52,225	50,964	49,609	48,152	46,587
5,754 Bal EOY		784,283	771,688	758,149	743,595	727,950	711,132	693,054	673,621	652,731	630,275
Cost Recovery / Depreciation		995,000	995,000	Building	80%	796,000	Land	20%	199,000	Life	30
		26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533	26,533
Basis		968,467	941,933	915,400	888,867	862,333	835,800	809,267	782,733	756,200	729,667

* 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%.