

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.

50,040	+	Rental Income
13,550	-	Operating Expenses
27,728	-	Mortgage Payments
<hr/>		
8,763	=	Cash Flow
142,500	/	Downpayment + Closing Costs
6.1%	=	Return on Investment from Cash Flow

2 Appreciation

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

475,000	=	Acquisition Price
5%	*	First Year Appreciation
498,750	=	Value at the end of Year 1.
<hr/>		
23,750	=	Amount of Value Increase
142,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 Equity Build-Up

6.75% 30 \$ 2,310.63

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

356,250	=	Loan Amount at Closing
352,453	=	Loan Amount at the end of Year 1
<hr/>		
3,797	-	Equity Build-Up in Year 1
142,500	/	Downpayment + Closing Costs
2.7%	=	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.

36,490	=	Cash Flow Before Loan Payments (rents less expenses)
13,458	-	Depreciation (assumes 15% land, 30 year recovery)
23,931	-	Mortgage Interest
(899)	=	Taxable Income Year 1
(719)		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
(266.04)	=	Federal Income Tax
(266)		Federal Income Tax
8,763	/	Cash Flow
-3.0%	=	Effective Tax Rate on This Investment
3,242	=	Tax if Cash Flow came from a non-preferred investment vehicle
(266)	-	Tax from this preferred investment vehicle.
<hr/>		
3,508	=	Income Tax Savings
2.5%	=	Return on Investment from Tax Savings

Total / Summary

1:	8,763	Cash Flow
2:	23,750	Appreciation Year 1
3:	3,797	Equity Build Up Year 1
4:	3,508	Tax Savings Year 1
<hr/>		
	39,818	Total Return from this Investment
	142,500	Downpayment + Closing Costs
	27.9%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period
1632 SOUTH CHARLES STREET**

Purchase Price	475,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	3.0%	50,040	51,541	53,087	54,680	56,320	58,010	59,750	61,543	63,389	65,291
Vacancy	3.0%	1,501	1,546	1,593	1,640	1,690	1,740	1,793	1,846	1,902	1,959
Effective Income		48,539	49,995	51,495	53,040	54,631	56,270	57,958	59,697	61,487	63,332
Expenses	3.0%	13,550	13,956	14,375	14,806	15,250	15,708	16,179	16,664	17,164	17,679
Exp as a percent of Annual Rent		28%	28%	28%	28%	28%	28%	28%	28%	28%	28%
Exp per unit	2	6,775	6,978	7,187	7,403	7,625	7,854	8,089	8,332	8,582	8,840
NOI	0	34,989	36,039	37,120	38,234	39,381	40,562	41,779	43,032	44,323	45,653
Debt Service	\$ 2,311	27,728	27,728	27,728	27,728	27,728	27,728	27,728	27,728	27,728	27,728
Before Tax Cash Flow	(142,500)	7,262	8,311	9,392	10,506	11,653	12,834	14,051	15,305	16,596	296,622
13.1% Internal Rate of Return											
NOI		34,989	36,039	37,120	38,234	39,381	40,562	41,779	43,032	44,323	45,653
Less Interest		23,931	23,666	23,384	23,081	22,758	22,412	22,042	21,646	21,222	20,769
Less Depreciation		12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667
Taxable Income to Individuals		(1,608)	(294)	1,070	2,486	3,956	5,484	7,071	8,720	10,434	12,217
Pass Thru Entity	20%	322	59	(214)	(497)	(791)	(1,097)	(1,414)	(1,744)	(2,087)	(2,443)
Taxable Income	0	(1,287)	(235)	856	1,989	3,165	4,387	5,657	6,976	8,347	9,774
Tax @ *	37%	(476)	(87)	317	736	1,171	1,623	2,093	2,581	3,089	3,616
After Tax Cash Flow	(142,500)	7,738	8,398	9,076	9,770	10,482	11,211	11,958	12,724	13,507	246,156
11.0% Internal Rate of Return											
Purchase	475,000										
L-V	75%										65,291
Loan	356,250										9.5
Down Payment	118,750										619,767
Cap Improvement	-									6%	37,186
Closing Costs	23,750										348,333
Initial Investment	142,500										234,248
Rate	6.75%									20%	46,850
Term	30										303,885
P&I	\$2,310.63										278,696
											231,847
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
356,250	Beg Bal	356,250	352,453	348,392	344,048	339,402	334,432	329,116	323,430	317,348	310,843
6.75%	Prin	3,797	4,061	4,344	4,646	4,970	5,316	5,686	6,082	6,505	6,958
30.0	Int	23,931	23,666	23,384	23,081	22,758	22,412	22,042	21,646	21,222	20,769
2,311	Bal EOY	352,453	348,392	344,048	339,402	334,432	329,116	323,430	317,348	310,843	303,885
Cost Recovery / Depreciation		475,000	475,000	Building	80%	380,000	Land	20%	95,000	Life	30
		12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667	12,667
Basis		462,333	449,667	437,000	424,333	411,667	399,000	386,333	373,667	361,000	348,333

* 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%.