

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.

68,229	+	Rental Income
27,394	-	Operating Expenses
25,045	-	Mortgage Payments
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15,789	=	Cash Flow
115,500	/	Downpayment + Closing Costs
13.7%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

385,000	=	Acquisition Price
5%	*	First Year Appreciation
404,250	=	Value at the end of Year 1.
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19,250	=	Amount of Value Increase
115,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

7.25% 25 \$ 2,087.10

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

288,750	=	Loan Amount at Closing
284,500	=	Loan Amount at the end of Year 1
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4,250	-	Equity Build-Up in Year 1
115,500	/	Downpayment + Closing Costs
3.7%	=	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.

40,834	=	Cash Flow Before Loan Payments (rents less expenses)
10,908	-	Depreciation (assumes 15% land, 30 year recovery)
20,795	-	Mortgage Interest
9,131	=	Taxable Income Year 1
7,305		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
2,702.79	=	Federal Income Tax
2,703		Federal Income Tax
15,789	/	Cash Flow
17.1%	=	Effective Tax Rate on This Investment
5,842	=	Tax if Cash Flow came from a non-preferred investment vehicle
2,703	-	Tax from this preferred investment vehicle.
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3,139	=	Income Tax Savings
2.7%	=	Return on Investment from Tax Savings

Total / Summary

1:	15,789	Cash Flow
2:	19,250	Appreciation Year 1
3:	4,250	Equity Build Up Year 1
4:	3,139	Tax Savings Year 1
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	42,429	Total Return from this Investment
	115,500	Downpayment + Closing Costs
	36.7%	Total Return from this Investment

