

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.

54,900	+	Rental Income
14,612	-	Operating Expenses
27,843	-	Mortgage Payments
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12,445	=	Cash Flow
139,500	/	Downpayment + Closing Costs
8.9%	=	Return on Investment from Cash Flow

2 Appreciation

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

465,000	=	Acquisition Price
5%	*	First Year Appreciation
488,250	=	Value at the end of Year 1.
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23,250	=	Amount of Value Increase
139,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 Equity Build-Up

7.00% 30 \$ 2,320.24

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

348,750	=	Loan Amount at Closing
345,207	=	Loan Amount at the end of Year 1
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3,543	-	Equity Build-Up in Year 1
139,500	/	Downpayment + Closing Costs
2.5%	=	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.

40,288	=	Cash Flow Before Loan Payments (rents less expenses)
13,175	-	Depreciation (assumes 15% land, 30 year recovery)
24,300	-	Mortgage Interest
2,813	=	Taxable Income Year 1
2,250		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
832.63	=	Federal Income Tax
833		Federal Income Tax
12,445	/	Cash Flow
6.7%	=	Effective Tax Rate on This Investment
4,605	=	Tax if Cash Flow came from a non-preferred investment vehicle
833	-	Tax from this preferred investment vehicle.
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3,772	=	Income Tax Savings
2.7%		Return on Investment from Tax Savings

Total / Summary

1:	12,445	Cash Flow
2:	23,250	Appreciation Year 1
3:	3,543	Equity Build Up Year 1
4:	3,772	Tax Savings Year 1
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	43,010	Total Return from this Investment
	139,500	Downpayment + Closing Costs
	30.8%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period
7704 FREDKERT AVENUE**

Purchase Price	465,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	4.0%	54,900	57,096	59,380	61,755	64,225	66,794	69,466	72,245	75,134	78,140
Vacancy	3.0%	1,647	1,713	1,781	1,853	1,927	2,004	2,084	2,167	2,254	2,344
Effective Income		53,253	55,383	57,598	59,902	62,298	64,790	67,382	70,077	72,880	75,796
Expenses	4.0%	14,612	15,196	15,804	16,436	17,094	17,777	18,489	19,228	19,997	20,797
Exp as a percent of Annual Rent		27%	27%	27%	27%	27%	27%	27%	27%	27%	27%
Exp per unit	3	4,871	5,065	5,268	5,479	5,698	5,926	6,163	6,409	6,666	6,932
NOI	0	38,641	40,187	41,794	43,466	45,205	47,013	48,893	50,849	52,883	54,998
Debt Service	\$ 2,320	27,843	27,843	27,843	27,843	27,843	27,843	27,843	27,843	27,843	27,843
Before Tax Cash Flow	(139,500)	10,798	12,344	13,951	15,623	17,362	19,170	21,051	23,006	25,040	350,014
17.4% Internal Rate of Return											
NOI		38,641	40,187	41,794	43,466	45,205	47,013	48,893	50,849	52,883	54,998
Less Interest		24,300	24,044	23,770	23,475	23,159	22,821	22,458	22,068	21,651	21,203
Less Depreciation		12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400
Taxable Income to Individuals		1,941	3,743	5,625	7,591	9,645	11,792	14,036	16,381	18,832	21,395
Pass Thru Entity	20%	(388)	(749)	(1,125)	(1,518)	(1,929)	(2,358)	(2,807)	(3,276)	(3,766)	(4,279)
Taxable Income	0	1,553	2,994	4,500	6,073	7,716	9,434	11,229	13,105	15,066	17,116
Tax @ *	37%	575	1,108	1,665	2,247	2,855	3,490	4,155	4,849	5,574	6,333
After Tax Cash Flow	(139,500)	10,224	11,236	12,286	13,376	14,507	15,680	16,896	18,158	19,466	287,456
14.6% Internal Rate of Return											
Purchase	465,000										
L-V	75%										78,140
Loan	348,750										8.5
Down Payment	116,250										661,840
Cap Improvement	-										39,710
Closing Costs	23,250										341,000
Initial Investment	139,500										281,130
Rate	7.00%										56,226
Term	30										299,271
P&I	\$2,320.24										322,859
											266,633
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
348,750 Beg Bal		348,750	345,207	341,409	337,335	332,967	328,284	323,262	317,877	312,102	305,910
7.00% Prin		3,543	3,799	4,073	4,368	4,684	5,022	5,385	5,774	6,192	6,640
30.0 Int		24,300	24,044	23,770	23,475	23,159	22,821	22,458	22,068	21,651	21,203
2,320 Bal EOY		345,207	341,409	337,335	332,967	328,284	323,262	317,877	312,102	305,910	299,271
Cost Recovery / Depreciation		465,000	465,000	Building	80%	372,000	Land	20%	93,000	Life	30
		12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400	12,400
Basis		452,600	440,200	427,800	415,400	403,000	390,600	378,200	365,800	353,400	341,000

* 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%.