

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.

134,975	+	Rental Income
40,920	-	Operating Expenses
69,971	-	Mortgage Payments
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24,084	=	Cash Flow
330,000	/	Downpayment + Closing Costs
7.3%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

1,100,000	=	Acquisition Price
5%	*	First Year Appreciation
1,155,000	=	Value at the end of Year 1.
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55,000	=	Amount of Value Increase
330,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

7.00% 25 \$ 5,830.93

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

825,000	=	Loan Amount at Closing
812,379	=	Loan Amount at the end of Year 1
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12,621	-	Equity Build-Up in Year 1
330,000	/	Downpayment + Closing Costs
3.8%	=	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.

94,055	=	Cash Flow Before Loan Payments (rents less expenses)
31,167	-	Depreciation (assumes 15% land, 30 year recovery)
57,350	-	Mortgage Interest
5,538	=	Taxable Income Year 1
4,431		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
1,639.35	=	Federal Income Tax
1,639		Federal Income Tax
24,084	/	Cash Flow
6.8%	=	Effective Tax Rate on This Investment
8,911	=	Tax if Cash Flow came from a non-preferred investment vehicle
1,639	-	Tax from this preferred investment vehicle.
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7,272	=	Income Tax Savings
2.2%		Return on Investment from Tax Savings

Total / Summary

1:	24,084	Cash Flow
2:	55,000	Appreciation Year 1
3:	12,621	Equity Build Up Year 1
4:	7,272	Tax Savings Year 1
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	98,977	Total Return from this Investment
	330,000	Downpayment + Closing Costs
	30.0%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period
4017 - 4019 EASTERN AVENUE**

Purchase Price	1,100,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	4.0%	134,975	140,374	145,989	151,829	157,902	164,218	170,787	177,618	184,723	192,112
Vacancy	3.0%	4,049	4,211	4,380	4,555	4,737	4,927	5,124	5,329	5,542	5,763
Effective Income		130,926	136,163	141,609	147,274	153,165	159,291	165,663	172,290	179,181	186,348
Expenses	4.0%	40,920	42,557	44,259	46,029	47,871	49,785	51,777	53,848	56,002	58,242
Exp as a percent of Annual Rent		31%	31%	31%	31%	31%	31%	31%	31%	31%	31%
Exp per unit	7	5,846	6,080	6,323	6,576	6,839	7,112	7,397	7,693	8,000	8,320
NOI	0	90,006	93,606	97,350	101,244	105,294	109,506	113,886	118,442	123,179	128,107
Debt Service	\$ 5,831	69,971	69,971	69,971	69,971	69,971	69,971	69,971	69,971	69,971	69,971
Before Tax Cash Flow	(330,000)	20,035	23,635	27,379	31,273	35,323	39,535	43,915	48,471	53,208	855,672
16.5% Internal Rate of Return											
NOI		90,006	93,606	97,350	101,244	105,294	109,506	113,886	118,442	123,179	128,107
Less Interest		57,350	56,438	55,459	54,410	53,286	52,079	50,786	49,399	47,912	46,317
Less Depreciation		29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333
Taxable Income to Individuals		3,322	7,835	12,558	17,501	22,675	28,093	33,767	39,709	45,934	52,456
Pass Thru Entity	20%	(664)	(1,567)	(2,512)	(3,500)	(4,535)	(5,619)	(6,753)	(7,942)	(9,187)	(10,491)
Taxable Income	0	2,658	6,268	10,046	14,001	18,140	22,475	27,014	31,767	36,747	41,965
Tax @ *	37%	983	2,319	3,717	5,180	6,712	8,316	9,995	11,754	13,597	15,527
After Tax Cash Flow	(330,000)	19,051	21,316	23,662	26,093	28,611	31,219	33,920	36,717	39,612	712,226
13.7% Internal Rate of Return											
Purchase	1,100,000										
L-V	75%										192,112
Loan	825,000										8.0
Down Payment	275,000										1,538,576
Cap Improvement	-										92,315
Closing Costs	55,000										806,667
Initial Investment	330,000										639,595
Rate	7.00%										127,919
Term	25										648,726
P&I	\$5,830.93										797,536
											669,617
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
825,000 Beg Bal		825,000	812,379	798,846	784,334	768,773	752,088	734,196	715,011	694,439	672,379
7.00% Prin		12,621	13,533	14,512	15,561	16,686	17,892	19,185	20,572	22,059	23,654
25.0 Int		57,350	56,438	55,459	54,410	53,286	52,079	50,786	49,399	47,912	46,317
5,831 Bal EOY		812,379	798,846	784,334	768,773	752,088	734,196	715,011	694,439	672,379	648,726
Cost Recovery / Depreciation		1,100,000	1,100,000	Building	80%	880,000	Land	20%	220,000	Life	30
		29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333	29,333
Basis		1,070,667	1,041,333	1,012,000	982,667	953,333	924,000	894,667	865,333	836,000	806,667

* 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%.