

## 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.

46,208	+	Rental Income
13,170	-	Operating Expenses
23,652	-	Mortgage Payments
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9,387	=	Cash Flow
118,500	/	Downpayment + Closing Costs
7.9%	=	Return on Investment from Cash Flow

### 2 **Appreciation**

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

395,000	=	Acquisition Price
5%	*	First Year Appreciation
414,750	=	Value at the end of Year 1.
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19,750	=	Amount of Value Increase
118,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

### 3 **Equity Build-Up**

7.00%      30 \$      1,970.96

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

296,250	=	Loan Amount at Closing
293,241	=	Loan Amount at the end of Year 1
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3,009	-	Equity Build-Up in Year 1
118,500	/	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.

33,038	=	Cash Flow Before Loan Payments (rents less expenses)
11,192	-	Depreciation (assumes 15% land, 30 year recovery)
20,642	-	Mortgage Interest
1,204	=	Taxable Income Year 1
963		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
356.49	=	Federal Income Tax
356		Federal Income Tax
9,387	/	Cash Flow
3.8%	=	Effective Tax Rate on This Investment
3,473	=	Tax if Cash Flow came from a non-preferred investment vehicle
356	-	Tax from this preferred investment vehicle.
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3,117	=	Income Tax Savings
2.6%		Return on Investment from Tax Savings

### **Total / Summary**

1:	9,387	Cash Flow
2:	19,750	Appreciation Year 1
3:	3,009	Equity Build Up Year 1
4:	3,117	Tax Savings Year 1
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	35,263	Total Return from this Investment
	118,500	Downpayment + Closing Costs
	29.8%	Total Return from this Investment

**Illustration of Internal Rate of Return over a 10-Year Holding Period  
871 HOLLINS STREET**

Purchase Price	395,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	3.0%	46,208	47,594	49,022	50,493	52,008	53,568	55,175	56,830	58,535	60,291
Vacancy	3.0%	1,386	1,428	1,471	1,515	1,560	1,607	1,655	1,705	1,756	1,809
Effective Income		44,822	46,167	47,552	48,978	50,447	51,961	53,520	55,125	56,779	58,482
Expenses	3.0%	13,170	13,565	13,972	14,391	14,823	15,268	15,726	16,197	16,683	17,184
Exp as a percent of Annual Rent		29%	29%	29%	29%	29%	29%	29%	29%	29%	29%
Exp per unit	3	4,390	4,522	4,657	4,797	4,941	5,089	5,242	5,399	5,561	5,728
NOI	0	31,652	32,601	33,580	34,587	35,625	36,693	37,794	38,928	40,096	41,299
Debt Service	\$ 1,971	23,652	23,652	23,652	23,652	23,652	23,652	23,652	23,652	23,652	23,652
<b>Before Tax Cash Flow</b>	<b>(118,500)</b>	<b>8,000</b>	<b>8,950</b>	<b>9,928</b>	<b>10,935</b>	<b>11,973</b>	<b>13,042</b>	<b>14,143</b>	<b>15,276</b>	<b>16,444</b>	<b>247,890</b>
<b>14.5% Internal Rate of Return</b>											
NOI		31,652	32,601	33,580	34,587	35,625	36,693	37,794	38,928	40,096	41,299
Less Interest		20,642	20,425	20,191	19,941	19,673	19,385	19,077	18,746	18,392	18,011
Less Depreciation		10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533
Taxable Income to Individuals		476	1,644	2,855	4,112	5,418	6,775	8,184	9,648	11,171	12,754
Pass Thru Entity	20%	(95)	(329)	(571)	(822)	(1,084)	(1,355)	(1,637)	(1,930)	(2,234)	(2,551)
Taxable Income	0	381	1,315	2,284	3,290	4,335	5,420	6,547	7,719	8,937	10,203
Tax @ *	37%	141	486	845	1,217	1,604	2,005	2,422	2,856	3,307	3,775
<b>After Tax Cash Flow</b>	<b>(118,500)</b>	<b>7,859</b>	<b>8,464</b>	<b>9,083</b>	<b>9,718</b>	<b>10,369</b>	<b>11,036</b>	<b>11,720</b>	<b>12,421</b>	<b>13,138</b>	<b>205,156</b>
<b>12.1% Internal Rate of Return</b>											
Purchase	395,000										
L-V	75%										60,291
Loan	296,250										8.5
Down Payment	98,750										515,385
Cap Improvement	-									6%	30,923
Closing Costs	19,750										289,667
Initial Investment	118,500										194,796
Rate	7.00%									20%	38,959
Term	30										254,219
P&I	\$1,970.96										230,243
											191,284
<b>Mortgage Amortization</b>		1	2	3	4	5	6	7	8	9	10
296,250	Beg Bal	296,250	293,241	290,014	286,554	282,843	278,865	274,599	270,024	265,119	259,859
7.00%	Prin	3,009	3,227	3,460	3,710	3,979	4,266	4,575	4,905	5,260	5,640
30.0	Int	20,642	20,425	20,191	19,941	19,673	19,385	19,077	18,746	18,392	18,011
1,971	Bal EOY	293,241	290,014	286,554	282,843	278,865	274,599	270,024	265,119	259,859	254,219
<b>Cost Recovery / Depreciation</b>		395,000	395,000	Building	80%	316,000	Land	20%	79,000	Life	30
		10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533	10,533
Basis		384,467	373,933	363,400	352,867	342,333	331,800	321,267	310,733	300,200	289,667

\* 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%.