

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.

100,151	+	Rental Income
29,272	-	Operating Expenses
50,570	-	Mortgage Payments
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20,308	=	Cash Flow
238,500	/	Downpayment + Closing Costs
8.5%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

795,000	=	Acquisition Price
5%	*	First Year Appreciation
834,750	=	Value at the end of Year 1.
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39,750	=	Amount of Value Increase
238,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

7.00% 25 \$ 4,214.17

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

596,250	=	Loan Amount at Closing
587,128	=	Loan Amount at the end of Year 1
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9,122	-	Equity Build-Up in Year 1
238,500	/	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.

70,878	=	Cash Flow Before Loan Payments (rents less expenses)
22,525	-	Depreciation (assumes 15% land, 30 year recovery)
41,449	-	Mortgage Interest
6,905	=	Taxable Income Year 1
5,524		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
2,043.87	=	Federal Income Tax
2,044		Federal Income Tax
20,308	/	Cash Flow
10.1%	=	Effective Tax Rate on This Investment
7,514	=	Tax if Cash Flow came from a non-preferred investment vehicle
2,044	-	Tax from this preferred investment vehicle.
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5,470	=	Income Tax Savings
2.3%	=	Return on Investment from Tax Savings

Total / Summary

1:	20,308	Cash Flow
2:	39,750	Appreciation Year 1
3:	9,122	Equity Build Up Year 1
4:	5,470	Tax Savings Year 1
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	74,650	Total Return from this Investment
	238,500	Downpayment + Closing Costs
	31.3%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period

#REF!

Purchase Price	795,000	2025	2026	2027	2028	2029	2030	2031	2032	2033	2034
Annual Rent	4.0%	103,248	107,378	111,673	116,140	120,786	125,617	130,642	135,867	141,302	146,954
Vacancy	3.0%	3,097	3,221	3,350	3,484	3,624	3,769	3,919	4,076	4,239	4,409
Effective Income		100,151	104,157	108,323	112,656	117,162	121,848	126,722	131,791	137,063	142,545
Expenses	4.0%	29,272	30,443	31,661	32,927	34,244	35,614	37,039	38,520	40,061	41,663
Exp as a percent of Annual Rent		29%	29%	29%	29%	29%	29%	29%	29%	29%	29%
Exp per unit	5	5,854	6,089	6,332	6,585	6,849	7,123	7,408	7,704	8,012	8,333
NOI	0	70,878	73,714	76,662	79,729	82,918	86,235	89,684	93,271	97,002	100,882
Debt Service	\$ 4,214	50,570	50,570	50,570	50,570	50,570	50,570	50,570	50,570	50,570	50,570
Before Tax Cash Flow	(238,500)	20,308	23,144	26,092	29,159	32,348	35,664	39,114	42,701	46,432	645,101
18.7% Internal Rate of Return											
NOI		70,878	73,714	76,662	79,729	82,918	86,235	89,684	93,271	97,002	100,882
Less Interest		41,449	40,789	40,082	39,324	38,511	37,639	36,704	35,702	34,627	33,475
Less Depreciation		21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200
Taxable Income to Individuals		8,230	11,724	15,380	19,205	23,207	27,395	31,780	36,369	41,175	46,207
Pass Thru Entity	20%	(1,646)	(2,345)	(3,076)	(3,841)	(4,641)	(5,479)	(6,356)	(7,274)	(8,235)	(9,241)
Taxable Income	0	6,584	9,380	12,304	15,364	18,566	21,916	25,424	29,095	32,940	36,966
Tax @ *	37%	2,436	3,470	4,553	5,685	6,869	8,109	9,407	10,765	12,188	13,677
After Tax Cash Flow	(238,500)	17,872	19,673	21,540	23,474	25,479	27,555	29,707	31,936	34,244	535,296
15.5% Internal Rate of Return											
Purchase	795,000										
L-V	75%										146,954
Loan	596,250										7.7
Down Payment	198,750										1,131,533
Cap Improvement	-										67,892
Closing Costs	39,750										583,000
Initial Investment	238,500										480,641
Rate	7.00%										96,128
Term	25										468,852
P&I	\$4,214.17										594,789
											498,661
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
596,250 Beg Bal		596,250	587,128	577,348	566,860	555,613	543,554	530,623	516,758	501,890	485,947
7.00% Prin		9,122	9,781	10,488	11,246	12,059	12,931	13,866	14,868	15,943	17,095
25.0 Int		41,449	40,789	40,082	39,324	38,511	37,639	36,704	35,702	34,627	33,475
4,214 Bal EOY		587,128	577,348	566,860	555,613	543,554	530,623	516,758	501,890	485,947	468,852
Cost Recovery / Depreciation		795,000	795,000	Building	80%	636,000	Land	20%	159,000	Life	30
		21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200	21,200
Basis		773,800	752,600	731,400	710,200	689,000	667,800	646,600	625,400	604,200	583,000

* Tax rate of 35% applies to income of \$243,726 to \$609,350 for singles; \$487,451 to \$731,200 for married filing jointly. Marginal rate above \$609,351/\$731,201 is 37%.