

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.

57,672	+	Rental Income
11,266	-	Operating Expenses
32,435	-	Mortgage Payments
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13,971	=	Cash Flow
165,000	/	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.

550,000	=	Acquisition Price
5%	*	First Year Appreciation
577,500	=	Value at the end of Year 1.
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27,500	=	Amount of Value Increase
165,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

6.85% 30 \$ 2,702.94

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

412,500	=	Loan Amount at Closing
408,187	=	Loan Amount at the end of Year 1
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4,313	-	Equity Build-Up in Year 1
165,000	/	Downpayment + Closing Costs
2.6%	=	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.

46,406	=	Cash Flow Before Loan Payments (rents less expenses)
15,583	-	Depreciation (assumes 15% land, 30 year recovery)
28,123	-	Mortgage Interest
2,700	=	Taxable Income Year 1
2,160		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
799.32	=	Federal Income Tax
799		Federal Income Tax
13,971	/	Cash Flow
5.7%	=	Effective Tax Rate on This Investment
5,169	=	Tax if Cash Flow came from a non-preferred investment vehicle
799	-	Tax from this preferred investment vehicle.
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4,370	=	Income Tax Savings
2.6%	=	Return on Investment from Tax Savings

Total / Summary

1:	13,971	Cash Flow
2:	27,500	Appreciation Year 1
3:	4,313	Equity Build Up Year 1
4:	4,370	Tax Savings Year 1
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	50,154	Total Return from this Investment
	165,000	Downpayment + Closing Costs
	30.4%	Total Return from this Investment

