

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.

40,188	+	Rental Income
14,014	-	Operating Expenses
15,784	-	Mortgage Payments
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10,390	=	Cash Flow
90,000	/	Downpayment + Closing Costs
11.5%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

300,000	=	Acquisition Price
5%	*	First Year Appreciation
315,000	=	Value at the end of Year 1.
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15,000	=	Amount of Value Increase
90,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

5.00% 25 \$ 1,315.33

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

225,000	=	Loan Amount at Closing
220,361	=	Loan Amount at the end of Year 1
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4,639	-	Equity Build-Up in Year 1
90,000	/	Downpayment + Closing Costs
5.2%	=	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.

26,174	=	Cash Flow Before Loan Payments (rents less expenses)
8,500	-	Depreciation (assumes 15% land, 30 year recovery)
11,145	-	Mortgage Interest
6,530	=	Taxable Income Year 1
5,224		Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
1,932.81	=	Federal Income Tax
1,933		Federal Income Tax
10,390	/	Cash Flow
18.6%	=	Effective Tax Rate on This Investment
3,844	=	Tax if Cash Flow came from a non-preferred investment vehicle
1,933	-	Tax from this preferred investment vehicle.
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1,912	=	Income Tax Savings
2.1%		Return on Investment from Tax Savings

Total / Summary

1:	10,390	Cash Flow
2:	15,000	Appreciation Year 1
3:	4,639	Equity Build Up Year 1
4:	1,912	Tax Savings Year 1
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	31,941	Total Return from this Investment
	90,000	Downpayment + Closing Costs
	35.5%	Total Return from this Investment

Illustration of Internal Rate of Return over a 10-Year Holding Period
28 EAST 25th STREET

Purchase Price	300,000	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Annual Rent	4.0%	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Vacancy	3.0%	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Effective Income		#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Expenses	4.0%	14,014	14,574	15,157	15,763	16,394	17,050	17,732	18,441	19,179	19,946
Exp as a percent of Annual Rent		#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Exp per unit	4	3,503	3,644	3,789	3,941	4,098	4,262	4,433	4,610	4,795	4,986
NOI	0	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Debt Service	\$ 1,315	15,784	15,784	15,784	15,784	15,784	15,784	15,784	15,784	15,784	15,784
Before Tax Cash Flow	(90,000)	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
#VALUE!	Internal Rate of Return										
NOI		#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Less Interest		11,145	10,907	10,658	10,396	10,120	9,830	9,525	9,205	8,869	8,515
Less Depreciation		8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000
Taxable Income to Individuals		#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Pass Thru Entity	20%	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Taxable Income	0	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
Tax @ *	37%	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
After Tax Cash Flow	(90,000)	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!	#REF!
#VALUE!	Internal Rate of Return										
Purchase	300,000								Assume a Sale at End of Year 10		
L-V	75%								Annual Rent Roll		#REF!
Loan	225,000								GRM		7.5
Down Payment	75,000								Price		#REF!
Cap Improvement	-								Sale Costs	6%	#REF!
Closing Costs	15,000								Less: Basis		220,000
Initial Investment	90,000								Gain		#REF!
Rate	5.00%								Tax @	20%	#REF!
Term	25								Mortgage Balance		166,330
P&I	\$1,315.33								Sale Proceeds Before Tax		#REF!
									Sale Proceeds After Tax		#REF!
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
225,000	Beg Bal	225,000	220,361	215,484	210,358	204,970	199,305	193,352	187,093	180,514	173,599
5.00%	Prin	4,639	4,877	5,126	5,388	5,664	5,954	6,258	6,579	6,915	7,269
25.0	Int	11,145	10,907	10,658	10,396	10,120	9,830	9,525	9,205	8,869	8,515
1,315	Bal EOY	220,361	215,484	210,358	204,970	199,305	193,352	187,093	180,514	173,599	166,330
Cost Recovery / Depreciation		300,000	300,000	Building	80%	240,000	Land	20%	60,000	Life	30
		8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000
Basis		292,000	284,000	276,000	268,000	260,000	252,000	244,000	236,000	228,000	220,000

* 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%.