

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.

79,200	+	Rental Income
33,562	-	Operating Expenses
29,254	-	Mortgage Payments
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16,384	=	Cash Flow
180,000	/	Downpayment + Closing Costs
9.1%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

600,000	=	Acquisition Price
5%	*	First Year Appreciation
630,000	=	Value at the end of Year 1.
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30,000	=	Amount of Value Increase
180,000	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

4.25% 25 \$ 2,437.82

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

450,000	=	Loan Amount at Closing
439,671	=	Loan Amount at the end of Year 1
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10,329	-	Equity Build-Up in Year 1
180,000	/	Downpayment + Closing Costs
5.7%	=	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.

45,638	=	Cash Flow Before Loan Payments (rents less expenses)
17,000	-	Depreciation (assumes 15% land, 30 year recovery)
18,925	-	Mortgage Interest
9,712	=	Taxable Income Year 1
7,770	=	Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
2,874.85	=	Federal Income Tax
2,875		Federal Income Tax
16,384	/	Cash Flow
17.5%	=	Effective Tax Rate on This Investment
6,062	=	Tax if Cash Flow came from a non-preferred investment vehicle
2,875	-	Tax from this preferred investment vehicle.
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3,187	=	Income Tax Savings
1.8%	=	Return on Investment from Tax Savings

Total / Summary

1:	16,384	Cash Flow
2:	30,000	Appreciation Year 1
3:	10,329	Equity Build Up Year 1
4:	3,187	Tax Savings Year 1
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	59,899	Total Return from this Investment
	180,000	Downpayment + Closing Costs
	33.3%	Total Return from this Investment

