

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.

| | | |
|---------|---|-------------------------------------|
| 39,540 | + | Rental Income |
| 13,136 | - | Operating Expenses |
| 15,039 | - | Mortgage Payments |
| <hr/> | | |
| 11,366 | = | Cash Flow |
| 105,000 | / | Downpayment + Closing Costs |
| 10.8% | = | Return on Investment from Cash Flow |

2 Appreciation

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

| | | |
|---------|---|--|
| 350,000 | = | Acquisition Price |
| 5% | * | First Year Appreciation |
| 367,500 | = | Value at the end of Year 1. |
| <hr/> | | |
| 17,500 | = | Amount of Value Increase |
| 105,000 | / | Downpayment + Closing Costs |
| 17% | = | Return on Investment from Appreciation |

3 Equity Build-Up

4.00% 30 \$ 1,253.22

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

| | | |
|---------|---|---|
| 262,500 | = | Loan Amount at Closing |
| 257,877 | = | Loan Amount at the end of Year 1 |
| <hr/> | | |
| 4,623 | - | Equity Build-Up in Year 1 |
| 105,000 | / | Downpayment + Closing Costs |
| 4.4% | = | 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.

| | | |
|----------|---|---|
| 26,404 | = | Cash Flow Before Loan Payments (rents less expenses) |
| 9,917 | - | Depreciation (assumes 15% land, 30 year recovery) |
| 10,416 | - | Mortgage Interest |
| 6,072 | = | Taxable Income Year 1 |
| 4,857 | | Less 20% Exclusion for LLC Ownership under new tax law |
| 37% | * | Marginal Tax Rate |
| 1,797.20 | = | Federal Income Tax |
| 1,797 | | Federal Income Tax |
| 11,366 | / | Cash Flow |
| 15.8% | = | Effective Tax Rate on This Investment |
| 4,205 | = | Tax if Cash Flow came from a non-preferred investment vehicle |
| 1,797 | - | Tax from this preferred investment vehicle. |
| <hr/> | | |
| 2,408 | = | Income Tax Savings |
| 2.3% | = | Return on Investment from Tax Savings |

Total / Summary

| | | |
|-------|---------|-----------------------------------|
| 1: | 11,366 | Cash Flow |
| 2: | 17,500 | Appreciation Year 1 |
| 3: | 4,623 | Equity Build Up Year 1 |
| 4: | 2,408 | Tax Savings Year 1 |
| <hr/> | | |
| | 35,896 | Total Return from this Investment |
| | 105,000 | Downpayment + Closing Costs |
| | 34.2% | Total Return from this Investment |