

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.

33,600	+	Rental Income	
7,800	-	Operating Expenses	
14,872	-	Mortgage Payments	
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10,928	=	Cash Flow	
86,250	/	Downpayment + Closing Costs	
12.7%	=	Return on Investment from Cash Flow	

2 **Appreciation**

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

345,000	=	Acquisition Price	
5%	*	First Year Appreciation	
362,250	=	Value at the end of Year 1.	
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17,250	=	Amount of Value Increase	
86,250	/	Downpayment + Closing Costs	
20%	=	Return on Investment from Appreciation	

3 **Equity Build-Up** 3.50% 30 \$ 1,239.36

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

276,000	=	Loan Amount at Closing	
270,703	=	Loan Amount at the end of Year 1	
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5,297	-	Equity Build-Up in Year 1	
86,250	/	Downpayment + Closing Costs	
6.1%	=	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.

25,800	=	Cash Flow Before Loan Payments (rents less expenses)	
10,664	-	Depreciation (assumes 15% land, 27.5 year recovery)	
9,576	-	Mortgage Interest	
5,561	=	Taxable Income Year 1	
33%	*	Marginal Tax Rate	
1,835	=	Federal Income Tax	
1,835		Federal Income Tax	
10,928	/	Cash Flow	
16.8%	=	Effective Tax Rate on This Investment	
3,606	=	Tax if Cash Flow came from a non-preferred investment vehicle	
1,835	-	Tax from this preferred investment vehicle.	
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1,771	=	Income Tax Savings	
2.1%		Return on Investment from Tax Savings	

Total / Summary

1:	10,928	Cash Flow	
2:	17,250	Appreciation Year 1	
3:	5,297	Equity Build Up Year 1	
4:	1,771	Tax Savings Year 1	
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	35,246	Total Return from this Investment	
	86,250	Downpayment + Closing Costs	
	40.9%	Total Return from this Investment	

**Illustration of Internal Rate of Return over a 10-Year Holding Period
3041 GUILFORD AVENUE**

Purchase Price	345,000	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
Annual Rent	4.0%	33,600	34,944	36,342	37,795	39,307	40,880	42,515	44,215	45,984	47,823
Expenses	3.0%	7,800	8,034	8,275	8,523	8,779	9,042	9,313	9,593	9,881	10,177
Exp as a percent of Annual Rent		23%	23%	23%	23%	22%	22%	22%	22%	21%	21%
Exp per unit	1	7,800	8,034	8,275	8,523	8,779	9,042	9,313	9,593	9,881	10,177
NOI	0	25,800	26,910	28,067	29,272	30,528	31,837	33,201	34,622	36,103	37,646
Debt Service	\$ 1,239	14,872	14,872	14,872	14,872	14,872	14,872	14,872	14,872	14,872	14,872
Before Tax Cash Flow	(86,250)	10,928	12,038	13,194	14,400	15,656	16,965	18,329	19,750	21,231	270,656
23.0% Internal Rate of Return											
NOI		25,800	26,910	28,067	29,272	30,528	31,837	33,201	34,622	36,103	37,646
Less Interest		9,576	9,387	9,192	8,990	8,781	8,564	8,340	8,107	7,867	7,618
Less Depreciation		10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036
Taxable Income	0	6,188	7,487	8,838	10,246	11,711	13,237	14,825	16,479	18,200	19,992
Tax @	25%	1,547	1,872	2,210	2,561	2,928	3,309	3,706	4,120	4,550	4,998
After Tax Cash Flow	(86,250)	9,381	10,166	10,985	11,838	12,728	13,656	14,623	15,630	16,681	222,269
19.4% Internal Rate of Return											
Purchase	345,000										
L-V	80%										
Loan	276,000										
Down Payment	69,000										
Cap Improvement	-										
Closing Costs	17,250										
Initial Investment	86,250										
Rate	3.50%										
Term	30										
P&I	\$1,239.36										
				annual appreciation			3.6%				
Assume a Sale at End of Year 10											
											47,823
											10.3
											491,043
									6%		29,463
											244,636
											216,944
										20%	43,389
											213,698
											247,882
											204,493
Mortgage Amortization		1	2	3	4	5	6	7	8	9	10
276,000 Beg Bal		276,000	270,703	265,218	259,538	253,655	247,564	241,256	234,723	227,958	220,953
3.50% Prin		5,297	5,485	5,680	5,882	6,092	6,308	6,533	6,765	7,005	7,255
30.0 Int		9,576	9,387	9,192	8,990	8,781	8,564	8,340	8,107	7,867	7,618
1,239 Bal EOY		270,703	265,218	259,538	253,655	247,564	241,256	234,723	227,958	220,953	213,698
Cost Recovery / Depreciation		345,000	345,000	Building	80%	276,000	Land	20%	69,000	Life	27.5
		10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036	10,036
Basis		334,964	324,927	314,891	304,855	294,818	284,782	274,745	264,709	254,673	244,636