

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.

24,600	+	Rental Income
8,862	-	Operating Expenses
10,522	-	Mortgage Payments
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5,216	=	Cash Flow
58,500	/	Downpayment + Closing Costs
7.0%	=	Return on Investment from Cash Flow

2 **Appreciation**

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

195,000	=	Acquisition Price
5%	*	First Year Appreciation
204,750	=	Value at the end of Year 1.
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9,750	=	Amount of Value Increase
58,500	/	Downpayment + Closing Costs
17%	=	Return on Investment from Appreciation

3 **Equity Build-Up**

6.00% 30 \$ 876.84

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

146,250	=	Loan Amount at Closing
144,454	=	Loan Amount at the end of Year 1
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1,796	-	Equity Build-Up in Year 1
58,500	/	Downpayment + Closing Costs
3.1%	=	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.

15,738	=	Cash Flow Before Loan Payments (rents less expenses)
5,525	-	Depreciation (assumes 15% land, 30 year recovery)
8,726	-	Mortgage Interest
1,487	=	Taxable Income Year 1
1,190	=	Less 20% Exclusion for LLC Ownership under new tax law
37%	*	Marginal Tax Rate
440.19	=	Federal Income Tax
440	=	Federal Income Tax
5,216	/	Cash Flow
8.4%	=	Effective Tax Rate on This Investment
1,930	=	Tax if Cash Flow came from a non-preferred investment vehicle
440	-	Tax from this preferred investment vehicle.
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1,490	=	Income Tax Savings
2.5%	=	Return on Investment from Tax Savings

Total / Summary

1:	5,216	Cash Flow
2:	9,750	Appreciation Year 1
3:	1,796	Equity Build Up Year 1
4:	1,490	Tax Savings Year 1
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	18,252	Total Return from this Investment
	58,500	Downpayment + Closing Costs
	31.2%	Total Return from this Investment

