Markets and Property Types

Interview preparation summary · RE track

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INT.EM.1.a · Office, Retail and Industrial and Logistics

Assess an office building on net effective rent, lease structure, obsolescence and the capex needed to stay lettable, and explain why prime and secondary offices behave differently.

Office demand follows employment, space per worker and the occupier's choice between staying, shrinking and moving. Supply is slow, so a weak market lingers: voids lengthen and landlords pay for tenants through rent-free periods and fit-out contributions. Headline rent is therefore not the number to underwrite. Net effective rent spreads the incentives over the lease term, and a tenant break shortens that term and raises the effective cost. The metrics that matter are the passing rent against estimated rental value, WALT to breaks as well as expiry, void rate and the leasing cost per square foot to re-let. Obsolescence is the real office risk: floorplates, ceiling heights, energy performance and amenities decide whether occupiers still pay a premium, and a building that misses the standard needs capex just to hold its rent. Prime holds up because occupiers move toward quality; secondary assets carry the voids and refurbishment bills. The usual mistake is to buy a high yield without pricing the capex and the re-letting costs that explain it.

WORKED EXAMPLE: NET EFFECTIVE RENT FOR MARLOWE HOUSE

An interviewer shows you Marlowe House, an invented 40,000 square foot office. The tenant has a 10-year lease at a headline rent of 60 per square foot a year, 12 months rent-free and a landlord contribution of 15 per square foot. The tenant can break at year 5. Seller asks for a 6.5% yield on the headline rent. How would you think about the income? Convention: pounds per square foot, ignore discounting and tax, rent paid evenly.

Answer: Headline 60 psf gives 2.40m and 36.9m of value; net effective rent is 52.5 psf if the tenant stays and 45.0 psf if it breaks at year 5, worth about 32.3m and 27.7m at a 6.5% yield.

> **Interview tip:** Say: I would not capitalise the headline rent. After the rent-free year and the contribution it is 52.5 psf over ten years and 45 psf if they break at year 5, so I would price off the effective rent and test how likely the break is.

INT.EM.1.b · Office, Retail and Industrial and Logistics

Analyse a retail asset using occupancy cost ratio, tenant sales and the role of anchors, and judge how much of the rent is genuinely secure.

Retail income depends on tenant trading, so the first question is whether tenants can afford the rent. The occupancy cost ratio divides rent, service charge and business rates by the tenant's sales, and a ratio well above the norm for its category signals rent at risk at the next review or renewal. Demand follows consumer spending, online substitution and footfall, and not every format suffers alike: grocery-anchored and necessity-led schemes have held rents better than discretionary fashion space. Anchor tenants draw visitors for the smaller units, often pay lower rent per square foot, and may carry co-tenancy clauses, so losing one can cut the rents and values of others. Check turnover rents, which add upside but are less secure, tenant failure and company voluntary arrangements, lease expiries and breaks, and the cost of reletting or repurposing units. The usual mistake is to value passing rent at face value without testing whether it is affordable.

WORKED EXAMPLE: OCCUPANCY COST RATIO AT FENWICK ROW

A fashion tenant at Fenwick Row, an invented shopping parade, pays rent of 150k, service charge of 30k and business rates of 60k a year. Its sales are 1.20m. Sales then fall 10% and the tenant asks for a rent cut so that its occupancy cost ratio returns to 18%. The parade is valued at a 7.5% yield. What do you conclude? Convention: service charge and rates stay fixed, ignore tax and discounting.

Answer: The ratio is 20.0% now and 22.2% after the sales fall; restoring 18% means a rent of 104.4k, a 30.4% cut worth 608k of capital value at a 7.5% yield.

> **Interview tip:** Say: a 10% sales fall takes the ratio from 20% to 22%, and because rates and service charge are fixed the whole adjustment lands on rent, so a 30% rent cut is the tenant's real ask and worth about 600k of value.

INT.EM.1.c · Office, Retail and Industrial and Logistics

Underwrite an industrial or logistics asset by weighing rent reversion against yield movement, supply response and building specification.

Logistics demand comes from retail and e-commerce, third-party logistics operators, manufacturing and supply-chain reconfiguration, and tenants pay for location, clear height, yard depth, power and speed of delivery. Supply responds faster than for offices because simple buildings go up in 12 to 18 months on available land, so rent growth is held back wherever planning is easy and land is plentiful, and protected where land and power are scarce, as in urban last-mile locations. The key metric is reversion: passing rent against estimated rental value, and when the lease lets you capture the gap at review or expiry. Yields moved sharply as rates changed, so a business plan that relies on rent growth must be tested against yield expansion. Look at site coverage, specification against modern occupier needs, tenant covenant and concentration, and alternative use value, which supports urban sites. The usual mistake is to count reversion without asking whether the market rent is still rising and whether yields will absorb it.

WORKED EXAMPLE: REVERSION AT TERN PARK

Tern Park is an invented 100,000 square foot warehouse let at a passing rent of 7.50 per square foot. Market rent (ERV) is 9.50. The next review is in four years. You buy at a 5.0% net initial yield on passing rent. What are the reversion and the risk to value? Convention: ignore purchase costs, assume the review resets to the then ERV, income received in full.

Answer: Reversion is 26.7% and the reversionary yield 6.3%; value is 19.0m if rent and yield hold, 16.5m if yield moves to 5.75%, and 14.8m if the ERV also slips to 8.50, against a price of 15.0m.

> **Interview tip:** Say: there is 27% of reversion, worth 4m if nothing else moves, but a 75 basis point yield move takes back most of it and a lower ERV takes it below the price, so I would underwrite the reversion as an option.

INT.EM.2.a · Residential, Hotels, Data Centres and Alternatives

Underwrite a multifamily or residential rental asset, using loss-to-lease, vacancy, expense ratio and the limits set by affordability and regulation.

Residential rental income is spread across many tenants on short leases, so cash flow is diversified and tracks wages and inflation closely, and demand rests on household formation and a shortage of homes to buy. The building blocks of NOI are gross potential rent at market, loss-to-lease (market rent less in-place rent), vacancy and bad debt, other income, and an operating expense ratio, which is often in the region of a third to two fifths of effective income, depending on who pays utilities and how the property is managed. Value creation comes from marking leases to market as they turn over, renovating units and trimming costs. The limits are affordability, because rent as a share of household income cannot rise indefinitely, and regulation such as rent caps and security of tenure. The usual mistake is to extrapolate recent rent growth, or to assume leases reset to market faster than turnover and caps allow.

WORKED EXAMPLE: VALUING QUILL COURT, A 240-UNIT BLOCK

Quill Court is an invented block of 240 flats. Market rent is 1,500 a month but in-place rents average 1,350. Vacancy is 5% of in-place rent and operating expenses are 35% of effective rent. Buyers use a 5.0% cap rate. Value the block, then say what marking leases to market is worth. Convention: no other income, annual figures, ignore capex and tax.

Answer: In-place NOI is 2.40m, worth 48.0m (200k per flat); resetting to market adds about 0.27m of NOI and 5.3m of value, but only as leases roll.

> **Interview tip:** Say: it is a 48m block on in-place rents, with a 10% loss-to-lease worth about 5m, but I would only credit that as leases turn over and I would check what regulation and affordability allow.

INT.EM.2.b · Residential, Hotels, Data Centres and Alternatives

Analyse a hotel using occupancy, average daily rate, RevPAR, operating leverage, the operating model and the FF&E reserve.

A hotel is an operating business in a building, so income is profit that moves every day, not rent. Revenue per available room (RevPAR) equals occupancy times average daily rate (ADR), and the better measure of a hotel's health is the full chain from RevPAR to total revenue per room, gross operating profit (GOP) and EBITDA after the reserve for furniture, fixtures and equipment (FF&E). Costs are largely fixed, so a small fall in revenue produces a much larger fall in profit, which is why

hotels are valued on a higher yield than leased property. Check the operating model: a management contract leaves the owner with the operating risk and pays the operator fees, a lease passes risk to the operator at a fixed or turnover-linked rent, and a franchise rents the brand. Diligence demand mix, supply pipeline, brand fit and the capex cycle. The usual mistake is to value the peak year without a through-cycle occupancy, or to forget the FF&E reserve.

WORKED EXAMPLE: OPERATING LEVERAGE AT THE SALTMARSH HOTEL

The Saltmarsh, an invented 150-room hotel, runs at 74% occupancy and an ADR of 140. Rooms are 65% of total revenue. GOP margin is 38%, and 55% of operating costs are fixed. Next year occupancy falls to 66% with ADR unchanged. What happens to RevPAR, revenue and GOP? Convention: 365 days, fixed costs unchanged, variable costs move with revenue.

Answer: RevPAR falls from 103.6 to 92.4 (-10.8%), revenue from 8.73m to 7.78m, and GOP from 3.32m to 2.64m (-20.5%), because 55% of costs do not move.

> **Interview tip:** Say: revenue is down 11% and profit is down 20%, roughly double, because more than half the cost base is fixed, which is why I would underwrite a through-cycle occupancy and value on a higher yield than a lease.

INT.EM.2.c · Residential, Hotels, Data Centres and Alternatives

Evaluate a data centre or another alternative sector on power access, contract structure, yield on cost, obsolescence and tenant concentration.

Alternatives such as data centres, student housing, self-storage and life sciences are priced on the strength of their niche demand, and each has its own constraint. In a data centre the scarce input is grid power, measured in megawatts of critical IT load, and delays in connection are the main development risk. Hyperscale tenants usually sign long take-or-pay leases with escalators, which gives bond-like cash flow but concentration in a few tenants, while colocation lets space to many smaller users at higher rent per megawatt and more churn. Check the development yield on cost against the exit cap rate, the power and cooling specification as chips and rack densities change, the lease term left and the retrofit cost if the tenant leaves. In student housing look at university partnerships and occupancy. In self-storage look at street rate against in-place rate and occupancy. In life sciences look at specialist fit-out and funded tenants. The usual mistake is to pay a core yield for a niche without pricing obsolescence and tenant concentration.

WORKED EXAMPLE: YIELD ON COST FOR THE ORRIN DATA CENTRE

Orrin is an invented 20 megawatt data centre costing 15m per megawatt to build. A hyperscale tenant has signed for the full capacity at 1.3m per megawatt a year, with 5% of that eaten by non-recoverable costs. A similar stabilised asset trades at a 6.25% cap rate, and construction financing costs 7% a year. Is it attractive, and what if grid connection slips by 12 months? Convention: ignore tax, escalators and ramp-up, interest simple.

Answer: Yield on cost is 8.2% against a 6.25% exit cap rate, giving value of 395.2m and a profit of 95.2m (31.7%); a 12-month power delay costs about 21.0m of extra interest.

> **Interview tip:** Say: it builds at 8.2% against a 6.25% exit, so about a 32% margin on cost, but the real risk is power timing, since each year of delay costs around 21m in carry, so the power agreement is the first thing I would read.

Summary of the Charta interview-preparation topic. Companies and figures in the examples are invented. Draft content, not yet expert reviewed.