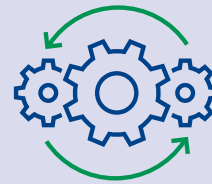


OPERATIONAL REAL ESTATE: RISK & REWARD

DIFFERENTIATING ORE FROM TRADITIONAL REAL ESTATE



ORE assets are NOT
"alternative" real estate
Any asset could be deemed
operational in nature during
its investment lifecycle



Returns are directly and
deliberately linked to the
revenues & profits of the
business conducted on or
from the premises

INVESTOR MODELS & TYPES



Hybrid Lease

Vary in structure but
linked to underlying
business & focused on
revenue/profit



Franchise

Know-how, procedures,
IP & brand(s) licensed to
franchisee



Management Contract

Third party operated
the asset on for the
investor + investor
carries the risk



Owner operator

Fully integrated
model whereby the
owner operates their
own asset

DIVERGENCE BETWEEN THEORY & PRACTICE

Too little analysis
of cashflow
variability

Over-reliance
on modifying
a 'traditional'
discount rate

Insufficient
emphasis on NPV
as preferred
method of
appraisal

Inappropriate
use of concept/
terms 'tenant',
'tenancy' &
'rent'

Financial
modelling
skills lacking
or poorly
utilised



RESEARCH

OPERATIONAL REAL ESTATE: RISK & REWARD FEBRUARY 2021

Key Findings

- Investor demand for ORE assets has risen dramatically over the last decade.
- Many attributes that are important to assessing risk in ORE may be unfamiliar to real estate professionals, for example understanding the key components of corporate accounts relevant to a property owner's investment. Uncertainty and inconsistency in this area may affect the liquidity of such assets and, therefore, price transparency.
- There is no standard approach to assessing ORE within the real estate investment industry.
- Gaps exist between the theory and practice of assessing and quantifying risk, especially the under-analysis of the variability of cash flows and in the calculation and application of discount rates.
- The gap analysis does not suggest the requisite skills do not exist in an organisation, but questions whether those skills are being utilised efficiently.

Recommendations

- Separate risks associated with the physical asset from those attached to the skill of the operator.
- Use equity skill sets to examine the tenant/operator's revenues, costs and profits.
- Seek out data sources outside the traditional real estate market.
- Use Net Present Value approach to appraise opportunities.
- Build a comprehensive discount rate.
- Broaden skill base and financial knowledge; use risk modelling from other asset classes.

The full and summary reports may be downloaded from the [IPF website](#).

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