## Question #1 of 18

The *most likely* consequence of the high income distribution that REITs are required to make is:

**A)** dividend yields that are nearly on-par with the yields of other publicly traded equities.

**B)** high volatility of reported income.

**C)** frequent secondary equity offerings compared to other kinds of companies.

**Explanation**

Because REITs are not able to retain earnings as other companies do, REITs make frequent secondary equity offerings, in order to finance growth and property acquisitions. REITs' required distributions result in a dividend yield that is significantly higher than those of most other publicly-traded equities. REITs' focus on income from rental properties leads to low volatility of reported income.

(Study Session 15, Module 43.1, LOS 43.c)

**Related Material**

SchweserNotes - Book 5



---

## Question #2 of 18

Mortgage REITs:

**A)** take ownership positions in income-producing real estate.

**B)** are the most common form of REITs.

**C)** have a smaller total market value than do equity REITs.

**Explanation**

The total market value of mortgage REITs is small compared with the total value of equity REITs. Equity REITs are the most common form of REITs. Equity REITS invest in ownership positions of income-producing real estate.

(Study Session 15, Module 43.1, LOS 43.c)

**Related Material**

SchweserNotes - Book 5

---

## Question #3 of 18

Patricia Ly, CFA is a portfolio manager who wishes to add diversification to her portfolio through the addition of a real estate investment. Ly finds the following data for a particular industrial REIT:

Net operating income (NOI): $710,000

Funds from operations (FFO): $630,000

Assumed cap rate: 6%

Shares outstanding: 90,000 shares

Storage property average P/FFO multiple: 13x.

Industrial property average P/FFO multiple: 10x.

Ly decides to perform a valuation on this REIT. The value per share of this REIT using a price-to-FFO approach is closest to:

**A)** $112

**B)** $91

**C)** $70

**Explanation**

FFO/share = FFO / Shares outstanding = $630,000/90,000 shares = $7/share.

The relevant subsector average P/FFO multiple is the value for industrial properties of 10x.

FFO/share x P/FFO multiple = $7.00 x 10x = $70.00

(Study Session 15, Module 43.3, LOS 43.h)

**Related Material**

SchweserNotes - Book 5

---

## Question #4 of 18

Compared with REITs, real estate operating companies (REOCs) are *most likely* to feature higher:

**A)** operating flexibility.

**B)** yields.

**C)** levels of income tax exemption.

**Explanation**

REOCs have greater operating flexibility to invest in a wide range of real estate than do REITs. REITs offer higher yields compared to REOCs. REITs offer income tax exemption while REOCs generally do not.

(Study Session 15, Module 43.1, LOS 43.c)

**Related Material**

SchweserNotes - Book 5

---

## Question #5 of 18

Which of the following types of REITs is more common in Europe and Asia than in the United States?

**A)** Multi-family / Residential REITs

**B)** Diversified REITs

**C)** Industrial REITs

**Explanation**

Diversified REITs own and operate more than one type of property. Diversified REITs are more common in Europe and Asia than in the United States. Diversification allows for reduced risk and wider opportunities.

(Study Session 15, Module 43.1, LOS 43.d)

**Related Material**

SchweserNotes - Book 5



---

## Question #6 of 18

Which of the following *least accurately* identifies a type of publicly traded real estate security?

**A)** Operating companies

**B)** Direct mortgage lending

**C)** Investment trusts

**Explanation**

The main types of publicly traded real estate securities are REITs (Real Estate Investment Trusts), REOCs (Real Estate Operating Companies), and RMBS and CMBS (Residential and Commercial Mortgage-Backed Securities). An investment in mortgages is most likely to be a private rather than public investment.

(Study Session 15, Module 43.1, LOS 43.a)

**Related Material**

SchweserNotes - Book 5

---

## Question #7 of 18

Which of the following *most accurately* identifies one of the disadvantages of investing in real estate through publicly traded securities? Compared to other real estate investment vehicles, publicly traded securities expose investors to:

**A)** inferior liquidity.

**B)** more-volatile returns.

**C)** unlimited liability.

**Explanation**

Disadvantages of investing in real estate through publicly traded securities include the volatile returns that result from pricing that is determined by the stock market. Publicly traded real estate securities offer investors the advantages of superior liquidity, and liability that is limited to the amount invested.

(Study Session 15, Module 43.1, LOS 43.b)

**Related Material**

SchweserNotes - Book 5



---

## Question #8 of 18

Retail sales growth is *most likely* to be a top economic factor affecting the economic value of a(n):

**A)** residential REIT.

**B)** health care REIT.

**C)** industrial REIT.

**Explanation**

After growth in the GDP, the most important factor driving demand for industrial properties is retail sales growth. More important to the value of a residential REIT than retail sales growth is job creation and population growth. More important to the value of a health care REIT is population growth.

(Study Session 15, Module 43.1, LOS 43.c)

**Related Material**

SchweserNotes - Book 5

---

## Question #9 of 18

When calculating NAVPS, a real estate company's assets and liabilities are valued at their:

**A)** market value.

**B)** book value.

**C)** liquidation value.

**Explanation**

All assets and liabilities of a company are taken at current market value when calculating NAVPS. NAVPS is a superior measure of a company's net worth when compared to its book value per share.

(Study Session 15, Module 43.2, LOS 43.e)

**Related Material**

SchweserNotes - Book 5



---

## Question #10 of 18

Which of the following *most accurately* identifies one of the advantages of investing in real estate through publicly traded securities?

**A)** Structural conflicts of interest are eliminated.

**B)** Publicly traded corporate structures cost less to maintain.

**C)** Diversification by geography and property type is facilitated.

**Explanation**

One of the advantages of publicly traded real estate securities is that they offer investors greater potential for diversification by geography, property, and property type. Disadvantages of publicly traded real estate securities include the costs of maintaining a publicly traded corporate structure, and the potential for structural conflicts of interest that can occur between the partnership and REIT shareholders under an UPREIT or DOWNREIT structure.

(Study Session 15, Module 43.1, LOS 43.b)

**Related Material**

SchweserNotes - Book 5

---

## Question #11 of 18

Which of the following is an expense normally deducted from accounting net earnings but not from FFO?

**A)** Property operating expenses

**B)** Depreciation expense

**C)** Property taxes

**Explanation**

Depreciation on real estate is excluded from FFO because most investors believe that real estate maintains its value to a greater extent than does other types of long-term business assets. Therefore, taking depreciation deductions, which reduce the value of the real estate, does not represent economic reality. FFO is accounting net earnings excluding depreciation charges on real estate, deferred tax charges, and gains or losses from sales of property and debt restructuring. Property operating expenses and property taxes are both normal rental expenses deducted to arrive at operating income.

(Study Session 15, Module 43.3, LOS 43.f)

**Related Material**

SchweserNotes - Book 5

---

## Question #12 of 18

The net asset value approach to valuation makes sense for REITs because:

**A)** NAV equals the value that public equity investors attach to a REIT.

**B)** there exist active private markets for real estate assets.

**C)** the price at which a REIT trades very closely tracks NAV.

**Explanation**

Because active private markets for real estate assets exist, REITs lend themselves to a net asset value approach to valuation. NAV reflects the estimated value of REIT assets to a private market buyer, however this may be different from the value that public equity investors would attach to the REIT. REITs have historically traded at a large premium or discount to NAV.

(Study Session 15, Module 43.2, LOS 43.e)

**Related Material**

SchweserNotes - Book 5



---

## Question #13 of 18

Which of the following is *most likely* to represent a publicly traded real estate debt investment?

**A)** A real estate operating company (REOC).

**B)** A mortgage real estate investment trust (Mortgage REIT).

**C)** Secured bank debt collateralized by real estate.

**Explanation**

Mortgage REITs are publicly traded securities that make loans secured by real estate, therefore they are publicly traded debt investments. REOCs are classified as equity (not debt) securities, while bank debt is classified as a private rather than public investment.

(Study Session 15, Module 43.1, LOS 43.a)

**Related Material**

SchweserNotes - Book 5

---

## Question #14 of 18

A key difference between Funds From Operations (FFO) and Adjusted Funds From Operations (AFFO) is that AFFO excludes:

**A)** non-cash rent while FFO does not.

**B)** deferred tax charges while FFO does not.

**C)** depreciation while FFO does not.

**Explanation**

AFFO is FFO adjusted to remove straight-line rent and to provide for leasing costs and maintenance-type capital expenditures. FFO is accounting net earnings excluding deferred tax charges, depreciation, and gains or losses on sales of property and debt restructuring.

(Study Session 15, Module 43.3, LOS 43.f)

**Related Material**

SchweserNotes - Book 5

---

## Question #15 of 18

If a REIT has assets with a current market value of $3,000,000, liabilities with a current market value of $2,000,000, and 100,000 shares outstanding, what is the NAVPS per share?

**A)** $10.00

**B)** $30.00

**C)** $50.00

**Explanation**

NAVPS per share can be calculated by beginning with assets, subtracting liabilities, and then dividing the result by the number by shares outstanding. Thus, $3,000,000-$2,000,000 = $1,000,000 and $1,000,000/100,000 = $10.00 per share.

(Study Session 15, Module 43.2, LOS 43.e)

**Related Material**

SchweserNotes - Book 5



---

## Question #16 of 18

The rate of population growth is *most likely* to be a top driver of economic value for a(n):

**A)** office REIT.

**B)** storage REIT.

**C)** retail REIT.

**Explanation**

Population growth has been found to be a major economic factor driving economic value for storage REITs. Job creation is a more important driver of economic value for an office REIT than is population growth. Retail sales growth is a more important driver of economic value for a retail REIT than is population growth.

(Study Session 15, Module 43.1, LOS 43.d)

**Related Material**

SchweserNotes - Book 5

---

## Question #17 of 18

Which of the following *most accurately* describes an approach to REIT valuation?

**A)** The P/FFO approach adjusts for the impact of recurring capital expenditures needed to keep properties operating smoothly.

**B)** The P/AFFO approach avoids estimates and assumptions in its calculation.

**C)** The discounted cash flow approach typically consists of intermediate-term cash flow projections plus a terminal value based on cash flow multiples.

**Explanation**

In discounted cash flow REIT models, investors generally use intermediate-term cash flow projections and a terminal value based on historical cash flow multiples. FFO does not adjust for the impact of recurring capital expenditures needed to keep properties operating. AFFO adjusts for routine maintenance type capital expenditures, but assumptions and estimates (which may vary widely) are required in the calculation of AFFO.

(Study Session 15, Module 43.3, LOS 43.g)

**Related Material**

SchweserNotes - Book 5



---

## Question #18 of 18

Mortgage REITs are publicly traded securities that make loans secured by real estate, therefore they are publicly traded debt investments. REOCs are classified as equity (not debt) securities, while bank debt is classified as a private rather than public investment. Which of the following is the *most likely* to represent an advantage of investing in publicly traded real estate securities over direct ownership of property? Publicly traded real estate securities offer:

**A)** lower price volatility. ✗

**B)** more control over investment decisions. ✗

**C)** greater liquidity. ✓

**Explanation**

One of the main advantages of investing in publicly traded equity real estate securities stems from the fact that these securities trade on stock exchanges, which results in greater liquidity compared with buying and selling real estate directly. The downside of trading on a stock exchange is that publicly traded equity real estate securities have greater price volatility than do directly owned properties. Another disadvantages of publicly traded real estate securities is that they offer investors little to no control over investment decisions.

(Study Session 15, Module 43.1, LOS 43.b)

**Related Material**

SchweserNotes - Book 5