

FREE READER BONUS

# Private Markets Interview Cheat Sheet

*40 questions with model answers*

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Fund mechanics, private equity, valuation, private credit, real estate, infrastructure, secondaries and fund finance, with the arithmetic worked out.

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## Forty questions that come up again and again

These are the questions that interviewers for private equity, private credit, real estate, infrastructure and fund roles return to most often: the definitions you must have cold, the arithmetic you must do without a spreadsheet, and the judgment questions that separate a prepared candidate from a memorised one.

Each answer is a model, not a script. Read it, close the page, and say it again in your own words. Where a question has numbers, the shaded box works one example through so that you can check your own arithmetic. Every figure in these boxes has been recomputed; returns are rounded to one decimal place.

Conventions differ between firms, funds and jurisdictions. When a question turns on a definition (a waterfall, a fee base, an EBITDA adjustment), say which convention you are using. Interviewers reward that more than they reward the right number.

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|------------------------------------------------------------|--------------------|
| <b>1. Fund mechanics and performance</b>                   | Questions 1 to 5   |
| <b>2. Private equity and the LBO</b>                       | Questions 6 to 10  |
| <b>3. Valuation and modelling</b>                          | Questions 11 to 15 |
| <b>4. Private credit</b>                                   | Questions 16 to 20 |
| <b>5. Real estate</b>                                      | Questions 21 to 25 |
| <b>6. Infrastructure</b>                                   | Questions 26 to 30 |
| <b>7. Secondaries, continuation funds and fund finance</b> | Questions 31 to 35 |
| <b>8. Judgment, the case study and fit</b>                 | Questions 36 to 40 |

## Fund mechanics and performance

### 1. What is the difference between IRR and MOIC, and when do they disagree?

MOIC (multiple on invested capital) is total value returned divided by capital invested. It ignores time. IRR is the discount rate at which the net present value of all cash flows is zero, so it rewards speed. They disagree whenever holding periods differ: a quick 1.5x can beat a slow 2.0x on IRR while losing on MOIC. Investors look at both because a fund cannot pay its LPs in IRR.

**The numbers.** 2.0x over 3 years is about 26.0% IRR; 2.0x over 5 years is about 14.9%.

### 2. Define DPI, RVPI and TVPI.

All three are divided by paid-in capital. DPI (distributions to paid-in) is the cash actually returned. RVPI (residual value to paid-in) is the remaining NAV. TVPI is the sum of the two. DPI is the only one that is realised, which is why LPs focus on it late in a fund's life.

**The numbers.** Paid-in 100, distributions 60, remaining NAV 90: DPI 0.60x, RVPI 0.90x, TVPI 1.50x.

### 3. Walk me through a whole-fund (European) distribution waterfall.

Tier 1: LPs receive their contributed capital. Tier 2: LPs receive a preferred return, commonly 8% a year. Tier 3: a GP catch-up, often 100% to the GP, until the GP holds its carried interest share of all profits distributed so far. Tier 4: the remaining profit is split, commonly 80/20. In a deal-by-deal (American) waterfall carry is paid deal by deal, which is why a clawback matters more there.

**The numbers.** Contributed 100, total distributions 180, accrued preferred return 20. LPs get 100, then 20. Catch-up X solves  $X = 20\% \times (20 + X)$ , so  $X = 5$ . The remaining 55 splits 44 to LPs and 11 to the GP. GP total 16, which is 20% of the 80 of profit; LPs total 164.

### 4. Why does a fund show a J-curve?

In the early years management fees and set-up costs are paid while new investments are held at cost or marked down, so net returns are negative. Value creation and exits come later. Subscription lines delay capital calls and therefore flatten the early part of the curve; they do not change the underlying economics.

### 5. How is a management fee usually calculated?

During the investment period the fee is typically charged on committed capital. After it, the base usually steps down to net invested capital (cost of unrealised investments), sometimes at a lower rate. Always check the LPA: fee offsets, the definition of invested capital and the treatment of write-downs all move the number.

**The numbers.** A \$500m fund at 2.0% on commitments pays \$10.0m a year. Later, at 1.5% on \$350m of invested capital, the fee is \$5.25m.

## Private equity and the LBO

### 6. Walk me through a simple LBO.

Set the entry price as EBITDA times a multiple. Fund it with debt and equity. Project the cash flow that pays down debt. At exit, apply a multiple to exit EBITDA to get enterprise value, deduct net debt to get equity value, and compare it with the equity invested to get MOIC and IRR.

**The numbers.** EBITDA 50 at 10.0x: EV 500, funded with 250 of debt and 250 of equity (fees ignored). In year 5 EBITDA is 70, exit at 10.0x gives EV 700, debt has been paid down to 150, so equity is 550. MOIC 2.2x, IRR about 17.1%.

### 7. Break that return into its value creation drivers.

Use an equity bridge: EBITDA growth at the entry multiple, multiple expansion or contraction on exit EBITDA, and debt paydown (or cash build). The three must add up to the change in equity value; if they do not, the model has a leak.

**The numbers.** EBITDA growth  $20 \times 10.0 = 200$ ; multiple change 0; debt paydown 100. Total 300, equal to 550 minus 250.

### 8. What makes a good LBO candidate?

Predictable cash flow, modest capital expenditure and working capital needs, a defensible market position, a management team that can execute, several value creation levers that do not rely on multiple expansion, a price that leaves room for error, and a credible route to exit.

### 9. How does leverage change returns?

When the return on the asset is above the after-tax cost of debt, leverage raises the equity return; it also raises the volatility of that return and the risk of losing control in a downturn. Show the same deal with and without debt to make the point.

**The numbers.** Same deal, all equity: 500 invested, exit EV 700 plus about 100 of accumulated cash, so roughly 800 of equity. MOIC 1.6x, IRR about 9.9%, against 2.2x and about 17.1% with leverage (ignoring the interest the unlevered case would save).

### 10. Why can EBITDA overstate the cash a business generates?

EBITDA ignores capital expenditure, changes in working capital, cash taxes, interest and, under some accounting, lease costs. Adjusted EBITDA can also carry add-backs that never become cash. A good answer names the gap and says how you would test it: a cash conversion ratio, and a quality of earnings review of the add-backs.

## Valuation and modelling

### 11. Depreciation rises by 10. Walk it through the three statements (tax rate 25%).

Income statement: operating profit falls 10 and net income falls 7.5. Cash flow statement: net income down 7.5, add back depreciation of 10, so cash from operations rises 2.5. Balance sheet: PP&E; down 10, cash up 2.5, so assets fall 7.5; retained earnings fall 7.5, and the sheet balances.

### 12. How do you get from enterprise value to equity value?

Deduct debt and debt-like items (including preferred equity, minority interests and, where relevant, underfunded pensions and some leases) and add cash and non-operating assets. Be consistent: if EBITDA is measured before lease costs, the leases belong in the bridge.

**The numbers.** EV 1,000, debt 300, cash 50, minority interest 20: equity value 730.

### 13. How do you compute a terminal value, and how do you sanity-check it?

Gordon growth: next year's free cash flow divided by (WACC minus growth). Cross-check by converting it into an implied exit multiple and comparing it with trading multiples; and check what share of total value sits in the terminal value.

**The numbers.** Free cash flow of 100 next year, WACC 9.0%, growth 2.5%:  $100 / 0.065 =$  about 1,538.

### 14. Why use a mid-year discounting convention?

Because cash arrives through the year rather than on the last day. Discounting each year's flow at  $t$  minus 0.5 rather than  $t$  raises the value slightly and is closer to reality for an operating business.

### 15. Why are precedent transaction multiples usually higher than trading multiples?

Precedents reflect the price of control, so they include a control premium and expected synergies. They are also tied to the market conditions at the time of each deal, which is why their dates matter as much as their multiples.

## Private credit

### 16. What is a unitranche loan?

A single loan, under one set of documents, that replaces a senior and a junior tranche with one blended price. Behind the scenes, lenders may split it into first-out and last-out pieces through an agreement among lenders, which the borrower may never see.

### 17. How do you estimate the all-in yield of a floating-rate loan?

Base rate plus spread, plus the original issue discount spread over the expected life of the loan. Market shorthand divides the OID by three years, because loans are usually repaid early.

**The numbers.** Assume SOFR at 4.00%, a spread of 5.75% and 2 points of OID:  $4.00 + 5.75 + 2/3 =$  about 10.4% on the shorthand convention.

### 18. Which covenants matter most, and what is covenant-lite?

Maintenance covenants (leverage, interest cover, fixed charge cover) are tested every quarter and give the lender an early seat at the table. Incurrence covenants are only tested when the borrower takes an action, such as raising debt. Covenant-lite loans have no maintenance covenants. In every case, read the EBITDA definition: generous add-backs can loosen a covenant more than its headline level.

### 19. Compute leverage and interest cover for this borrower.

Leverage is debt divided by EBITDA. Interest cover is EBITDA divided by interest expense. A credit committee looks at both, then at fixed charge cover, which also takes in capital expenditure and taxes.

**The numbers.** EBITDA 60, debt 300 at 10%: interest 30, leverage 5.0x, interest cover 2.0x.

### 20. How would you estimate recovery in a default?

Value the business at default, deduct priority claims, then allocate what is left down the capital structure in order of priority. Recovery is the value reaching each tranche divided by its claim.

**The numbers.** Enterprise value at default 240, senior claim 300, junior claim 100: senior recovers 80%, junior recovers nothing.

## Real estate

### 21. What is a cap rate, and how sensitive is value to it?

Cap rate is net operating income divided by value (or price). Because value is NOI divided by the cap rate, a small move in the rate moves value a lot when rates are low.

**The numbers.** NOI 6.0m at a 5.50% cap rate: value about 109.1m. At 6.00%: 100.0m, a fall of about 8.3%.

### 22. What is the difference between NOI and cash flow?

NOI is rental income less property operating expenses. It excludes debt service, capital expenditure, tenant improvements and leasing commissions, depreciation and income tax. Cash flow to equity deducts all of those that are cash.

### 23. Compute DSCR and debt yield.

Debt service coverage ratio is NOI divided by debt service. Debt yield is NOI divided by the loan amount. Lenders like debt yield because it does not depend on the interest rate or the amortisation profile.

**The numbers.** NOI 6.0m, interest-only loan of 70m at 6.0%: debt service 4.2m, DSCR about 1.43x, debt yield about 8.6%.

### 24. Explain core, core-plus, value-add and opportunistic.

They describe rising risk and rising expected return. Core: stabilised, well-let assets with low leverage, where most of the return is income. Core-plus: similar assets with some management or leasing to do. Value-add: refurbishment, repositioning or re-leasing, with more leverage. Opportunistic: development, distress or new markets, where most of the return comes from capital growth.

### 25. What is WALT and why does it matter?

Weighted average lease term (or unexpired lease term), usually weighted by rent. It tells you how long the income is secured and how much re-letting risk the buyer is taking on. Always check break options: WALT to first break and WALT to expiry can tell very different stories.

**The numbers.** Two leases: rent 600 with 2 years left and rent 400 with 8 years left. Rent-weighted WALT =  $(600 \times 2 + 400 \times 8) / 1,000 = 4.4$  years.

# Infrastructure

## 26. What makes an asset infrastructure?

It provides an essential service, has high barriers to entry, long useful life and high upfront capital cost, and its revenues are regulated, contracted or otherwise stable, often with inflation linkage. The investment case rests on predictable cash yield over a long period rather than on fast growth.

## 27. How does a regulated asset base model work?

The regulator sets allowed revenue as a return on the regulated asset base (RAB) plus regulatory depreciation plus allowed operating costs. Value creation comes from outperforming the allowances and from growing the RAB through approved investment.

**The numbers.** RAB 1,000 at an allowed return of 5.0% gives 50; plus regulatory depreciation of 40 and allowed opex of 30: allowed revenue 120 (simplified).

## 28. How is project finance different from corporate lending?

The borrower is a special purpose vehicle, lenders have limited or no recourse to the sponsor, and the loan is sized on the project's cash flow available for debt service (CFADS) rather than on a balance sheet. Security covers the project's contracts, accounts and shares.

## 29. What is debt sculpting?

Shaping each period's debt service so that it equals CFADS divided by a target DSCR. Debt capacity is then the present value of that sculpted debt service at the cost of debt.

**The numbers.** CFADS of 13 with a 1.30x target DSCR allows debt service of 10 in that period.

## 30. Contrast availability, contracted and merchant revenue.

Availability payments are made for keeping an asset available, whatever the usage, so the main risk is performance. Contracted revenue depends on a counterparty under a long-term agreement, so the risk is counterparty credit and contract terms. Merchant revenue is sold at market prices, so the investor takes price and volume risk and needs more equity.

## Secondaries, continuation funds and fund finance

### 31. How are LP secondaries priced?

As a percentage of the most recent reported NAV, adjusted for events since the reference date. The buyer also takes on the unfunded commitments, which belong in the analysis even though they are not in the price.

**The numbers.** NAV 100 bought at 90%: a 10% discount, 90 paid, plus any unfunded commitment assumed.

### 32. Is buying at a discount to NAV automatically a good deal?

No. The NAV may be stale or optimistic, the assets may be weak, and the time to liquidity drives the return. A discount on a slow portfolio can produce a low IRR.

**The numbers.** Buy at 90 a NAV of 100 that is realised at 100 three years later: MOIC about 1.11x, IRR about 3.6%.

### 33. What is a continuation fund, and what are the conflicts?

A GP-led secondary in which the GP moves one or more assets from an existing fund into a new vehicle it also manages. Existing LPs choose to sell or roll. The GP sits on both sides of the price, so the process needs a credible price test (often a competitive process led by a secondary buyer), adequate election time and a fairness opinion. The SEC's 2023 private fund adviser rules would have required such an opinion; they were vacated by the Fifth Circuit in June 2024, but the practice remains standard.

### 34. What does a subscription line do to fund returns?

It is a revolving facility secured on LPs' uncalled commitments. By delaying capital calls it shortens the time LP money is at work, which raises IRR, while MOIC barely moves (slightly down, because of interest).

**The numbers.** A deal turning 100 into 150 over 3 years is about 14.5% IRR. If the line delays the call by one year, the LP's money is out for 2 years and the IRR is about 22.5% (interest ignored).

### 35. How is a NAV facility different from a subscription line?

A NAV facility is secured on the fund's investments rather than on uncalled commitments, so it is used later in a fund's life, at low loan-to-value. Uses include follow-on capital, liquidity and, more controversially, early distributions to LPs, which need clear disclosure.

## Judgment, the case study and fit

### 36. Why private markets, and why this firm?

Answer in three parts: what draws you to the work (ownership, long horizon, being close to the asset), evidence that you have done it or something close to it, and a specific reason tied to this firm's strategy, a deal it has done, or its sector focus. Specific beats enthusiastic.

### 37. Pitch me an investment.

Thesis in one sentence; why the asset is attractive; how value would be created; the returns with the key assumptions; the three biggest risks and how you would diligence or mitigate each; and the exit. Finish with what would make you walk away.

### 38. What are the biggest risks in this deal, and how would you diligence them?

Rank risks by impact on value, not by length of the list. For each, name the evidence that would confirm or kill it: customer calls, cohort data, a quality of earnings review, technical or environmental reports, legal review of key contracts.

### 39. Tell me about an error you caught in a model.

Use a short structure: what the model was for, what looked wrong, how you traced it (for example a balance sheet that did not balance, or a return that moved the wrong way in a sensitivity), the fix, and the control you added so it could not happen again.

### 40. Do a paper LBO in five minutes.

Write down entry EV and equity, grow EBITDA, apply the exit multiple, estimate cumulative debt paydown from free cash flow, compute exit equity and MOIC, then convert MOIC to IRR with known anchors. Speak your assumptions out loud.

**The numbers.** Anchors over 5 years: 2.0x is about 15% IRR, 2.5x about 20%, 3.0x about 25%. Over 3 years, 2.0x is about 26%.

## ABOUT THIS SHEET

# From the author

Julian R. Sterling writes practitioner guides for people who have to produce a number and defend it: analysts, credit officers, fund managers, lenders and investors. Each book follows one worked case from the first document to the final figure, and the workbooks that reproduce every number are free on the companion pages at [julianrsterling.com](http://julianrsterling.com).

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