

Spotlight UK Student Housing

2017



SUMMARY

Investors continue to pay premiums to aggregate greater student bed numbers

■ 68,000 beds traded last year with a total value of £4.5bn. In 2017 we expect this to rise to 75,000 beds trading for £5.3bn, a rise of 17% year on year.

■ Investors are willing to pay premiums for larger portfolios, driven by their need to allocate their investment capital and build scale quickly.

■ Investment from Singapore has grown massively, with GIC and Mapletree spending almost £1.2bn on UK student housing in 2016.

■ The General Election presents an opportunity for policy to become more welcoming to international students. If students are removed from migration targets, growth of overseas students in the UK could exceed worldwide growth of 6% per year.

■ Brexit may have intensified appetite for UK student housing. We saw over £2.1bn transacted after the referendum, compared to £1.9bn earlier in the year.

■ Development prospects are stronger this year in prime markets such as Exeter, Guildford and Leeds. They are weaker in cities such as Aberdeen and Liverpool.

Investment UNIVERSITY CHALLENGE

The UK student housing market performed well in 2016 despite a difficult set of circumstances

Words:
Jacqui Daly

Investors traded 68,000 student beds worth £4.5bn last year in the face of severe headwinds. We expect £5.3bn to trade in 2017, or 75,000 beds.

This represents 17% more money changing hands for just 10% more stock. There are some very large portfolios to come to market this year, which will trade at a premium to reflect their size. On the opposite page Brook Burton explains the portfolio premium in more detail.

2016's performance was slightly lower than the record set in 2015, which saw over £6bn worth of student housing change hands.

However, the volume traded in 2016 was still 54% higher than the average for the last five years.

Many more of these deals took place in the second half of the year, as investors opted to wait for any market movement following the outcome of the EU referendum. The UK's decision to leave the EU does not seem to have affected investment appetite – in fact, it may have intensified it. With sterling now worth less relative to many other international currencies, deals are highly attractive to overseas investors.

The appetite for student housing assets has outgrown the supply of available stock. Of the £4.5bn traded in 2016, £1.1bn (25%) involved forward funding developments while £223m (5%) were development sites. Existing stock made up 69% of trades, the lowest proportion on record.

We expect this higher level of investment in development to continue this year.

The trend towards consolidation has continued. This has had a striking effect on our rankings of student housing investors. Two of our Top Ten investors by number of beds are new entrants to the list, having not invested in the UK student market at all until last year. This shows how student housing has established itself as an attractive asset class worldwide, even in the face of political risk. ■



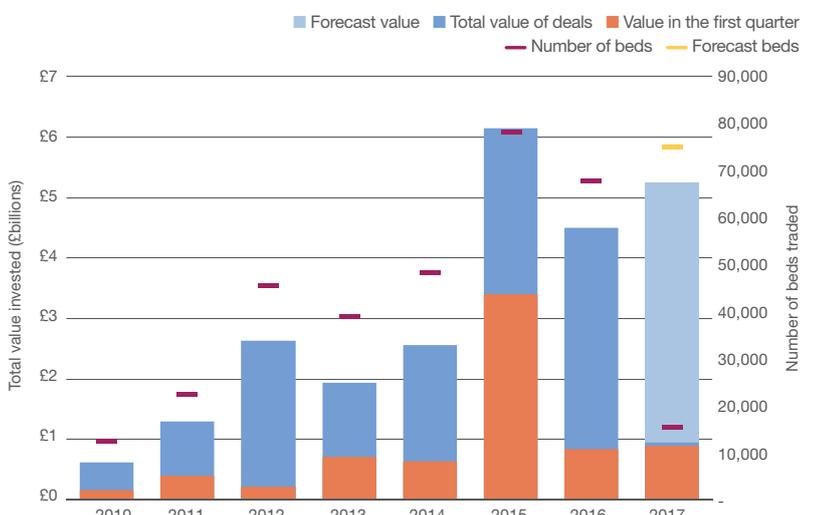
“We expect investment volumes to reach £5.3bn in 2017 as investor confidence returns after the EU referendum. This is a 17% increase on 2016” **Jacqui Daly, Savills Research**

FIGURE 1
2017 Initial Yields

	Lease	Nomination Agreement	Direct Let
Prime London	3.75%	4.25%	4.25%
Super Prime Regional	4.25%	4.75%	5.25%
Prime Regional	4.50%	5.00%	5.50%
Secondary Regional	5.00%	5.75%	6.50%

Source: Savills Research

FIGURE 2
UK Student Housing Investment Activity



Source: Savills Research

VIEW FROM VALUATIONS

Investors pay portfolio premiums to secure scale at speed

Words:
Brook Burton,
Director, Valuations

Several larger investors have demonstrated they're willing to pay a premium on larger portfolios. This premium is driven by their need to allocate investment capital, achieve target scale / returns and secure an income stream quickly and efficiently.

Our tracking of deals suggests that these premiums tend to kick in on deals over £150m. The precise geography, location and composition of the portfolio appears to be less important. We have observed premiums on regional, London, and recently even development funding deals where investors want to assemble a large-scale pipeline quickly.

Blended yields paid for portfolios ranged from 4.6% to 5.8% over the last two years, based on our analysis of all major portfolio trades. The portfolio premium in these deals represents a yield shift of 10 to 85 basis points relative to how those schemes would be valued individually, or 38 bps on average. Premiums are particularly high for stabilised stock with a well-established cash flow.

This is because investors tend to value portfolios on an IRR basis, targeting ungeared returns of 6-7% and geared returns of 11-12%. Acquiring a portfolio quickly, even at a premium, allows investors to meet these targets much faster than through many years of organic growth.



Average blended
yield on large
portfolios was
5.23%



Value-weighted
average portfolio
premium is
38 bps



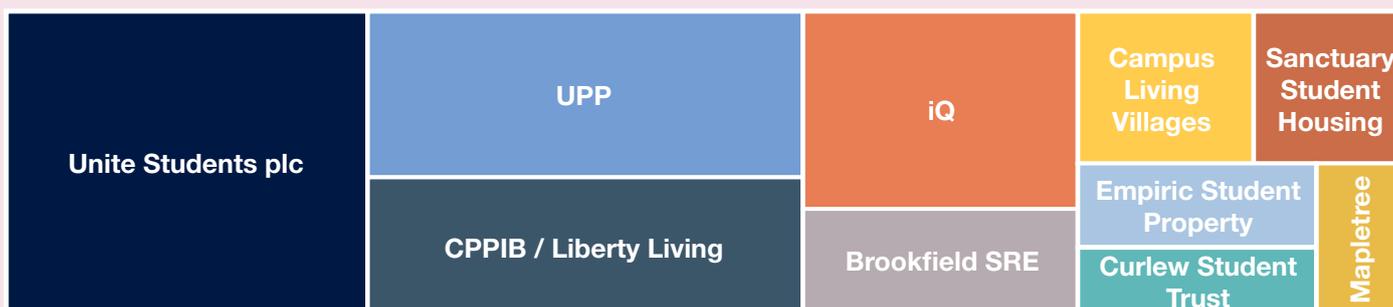
Average
cap value
per bed of
£95,300

FIGURE 3
Largest Private Sector Owners by Number of Beds

Investor	Beds	2016 Rank	2015 Rank
Unite Students plc	49,000	1	1
UPP	31,500	2	2
CPPIB / Liberty Living	27,000	3	4
iQ	23,500	4	3
Brookfield SRE	13,500	5	New
Campus Living Villages	11,600	6	6
Sanctuary Student Housing	10,000	7	5
Empiric Student Property plc	9,000	8	9
Curlew Student Trust	7,500	9	8
Mapletree	6,000	10	New

Source: Savills Research

FIGURE 4
Relative Sizes of the Top Private Sector Owners



Source: Savills Research

International GLOBAL INVESTMENT FLOWS

The Far East leads the way in UK student investment

Words:
Paul Tostevin

Last year we saw UK student housing continue its evolution into a global investment market. The proportion of international investment flowing into the market has almost doubled in the last two years. Foreign investment grew from 35% of transactions in 2014 to 64% in 2016.

There was a huge increase in Singaporean investment in 2016, up to almost £1.2 billion from just £35 million the year before. Almost two thirds of this came from just one investor: a JV between Singaporean sovereign wealth fund GIC and GSA, who acquired over 7,000 beds.

“GIC’s £700 million investment in UK student housing is a vote of confidence in the sector from one of its most experienced investors”

Paul Tostevin, Savills Research

Another Singaporean fund, Mapletree, also invested heavily in UK student last year. They acquired over 6,000 beds. We expect to see continued high transaction volumes from this part of the globe.

North America was the second largest source of capital into UK student housing in 2016, investing over £1.3 billion. The vast majority of that came from two Canadian investors: Brookfield SRE and CPPIB.

The effect of the EU referendum has been mixed. Although the decision to leave the EU may affect universities’ ability to secure valuable overseas students, the falling value of sterling makes the UK more attractive to international investors and students. We saw over £2.1 billion transacted after the referendum compared to £1.9 billion in the earlier part of the year. ■

FIGURE 5
Global Investment into UK Student Housing

UK	2015	2016	2017
Value	£1,670m	£1,490m	£300m
Beds	28,000	27,000	6,000
Deals	108	93	24

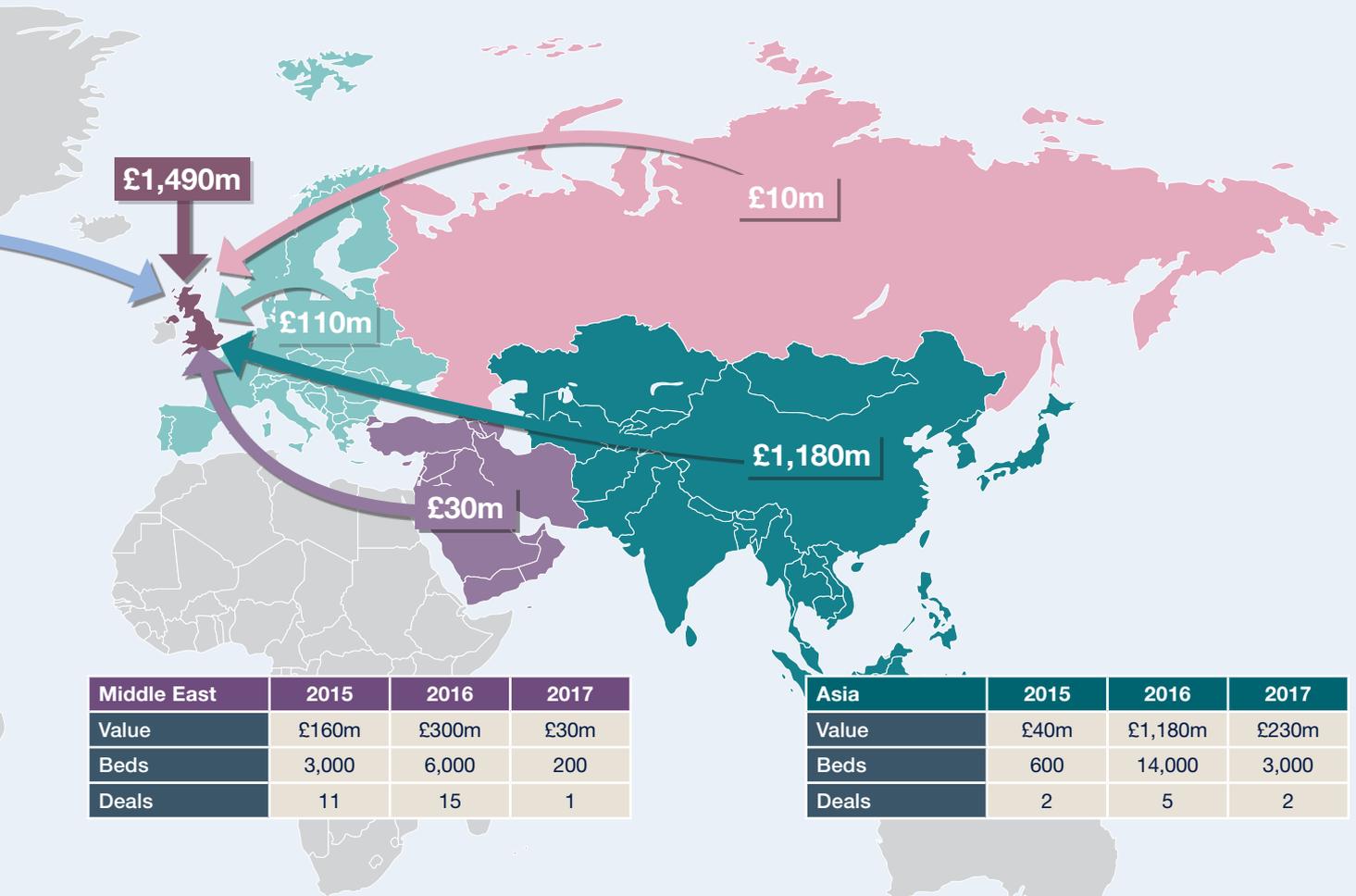


North America	2015	2016	2017
Value	£3,370m	£1,380m	£320m
Beds	39,000	18,000	5,000
Deals	18	17	2

Source: Savills Research

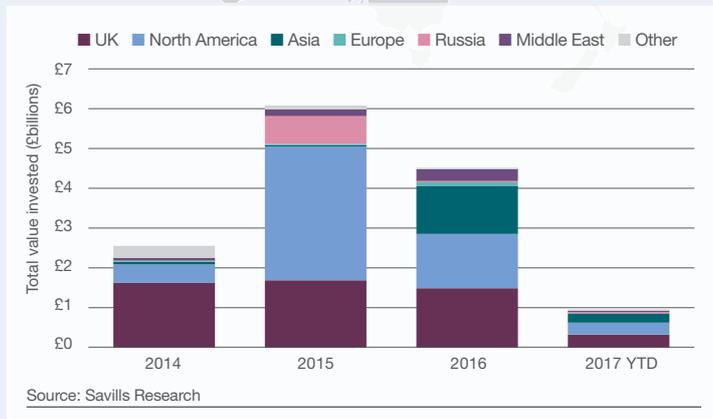
Europe	2015	2016	2017
Value	£30m	£110m	-
Beds	400	900	-
Deals	4	2	-

Russia	2015	2016	2017
Value	£720m	£10m	£10m
Beds	4,000	100	200
Deals	4	1	1



Middle East	2015	2016	2017
Value	£160m	£300m	£30m
Beds	3,000	6,000	200
Deals	11	15	1

Asia	2015	2016	2017
Value	£40m	£1,180m	£230m
Beds	600	14,000	3,000
Deals	2	5	2



Development & Finance

IN A LEAGUE OF THEIR OWN

In a highly competitive market, developers will have to be careful when selecting sites

Words:
Andrew Smith

Our student housing development league table has changed substantially since last year. With more towns falling down the rankings than rising, it's more important than ever for investors to be selective.

Well-located assets in strong markets will enjoy high occupancy and rental growth. Assets in secondary locations could struggle with competition for occupancy and rental growth regardless of the university town.

Our analysis takes account of a range of factors such as current and future supply, demand, affordability and the potential for rental growth.

We combine this with our knowledge of advising in these markets to create a single, simple indicator of each city's development potential (see Figure 6).

Best in class

Each of our top cities is attractive for development because of strong demand characteristics, high occupancy levels, strong rents and good prospects for rental growth.

In 2017 three new markets moved up to the First tier: Exeter, Guildford and Leeds. Continued strong demand in these markets, demonstrated by their success in attracting new students alongside limited supply, make these cities particularly attractive for new student development.

FIGURE 6
Student Housing Development League Table

FIRST	UPPER SECOND	LOWER SECOND	THIRD
➔ Bath	➔ Belfast	➔ Bangor	⬇️ Aberdeen
⬆️ Birmingham	➔ Cambridge	➔ Bournemouth	➔ Aberystwyth
➔ Brighton	➔ Canterbury	➔ Buckingham	➔ Chelmsford
➔ Bristol	➔ Chichester	➔ Cardiff	➔ Cheltenham
➔ Edinburgh	➔ Norwich	⬇️ Chester	➔ Derby
⬆️ Exeter	➔ Nottingham	⬆️ Colchester	➔ Dundee
⬆️ Guildford	➔ Portsmouth	⬇️ Coventry	⬇️ Falmouth
⬆️ Leeds	⬆️ Reading	➔ Durham	➔ Farnham
➔ London	➔ Winchester	➔ Egham	➔ High Wycombe
➔ Manchester		➔ Glasgow	⬇️ Huddersfield
➔ Oxford		➔ Hatfield	➔ Inverness
➔ St Andrews		➔ Leicester	⬇️ Kingston-upon-Thames
		➔ Newcastle upon Tyne	➔ Lancaster
		➔ Northampton	➔ Lincoln
		⬇️ Plymouth	➔ Loughborough
		⬇️ Sheffield	➔ Salford
		➔ Southampton	⬆️ Stoke on Trent
		➔ Stirling	
		➔ Swansea	
		➔ Twickenham	
		➔ York	

KEY

- ⬆️ Up from last year
- ➔ Same as last year
- ⬇️ Down from last year

Source: Savills Research

See me after class

Liverpool has fallen down the rankings to a pass this year. There are now 21,700 PBSA units in the city, meaning 2.1 students for each unit. With supply of a further 12,400 units either under construction or with planning permission, this ratio just 1.4.

In this highly competitive market, we see little capacity for investors to drive rental growth unless they have the very best quality stock in the best location.

Another market to watch is Plymouth. It has just 5,900 PBSA units, putting its student to bed ratio at 3.7. However, the planning pipeline looks full, with almost 3,300 units committed. This amounts to 56% growth relative to existing supply.

With such a large concentration of supply in the pipeline, it could be challenging for operators to let their schemes unless they are priced attractively relative to their competitors. ■

PASS

- ➔ Bolton
- ➔ Bradford
- ➔ Carlisle
- ➔ Cirencester
- ➔ Hull
- ➔ Ipswich
- ▼ Liverpool
- ➔ Luton
- ➔ Middlesbrough
- ➔ Newport
- ➔ Paisley
- ➔ Pontypridd
- ➔ Preston
- ➔ Sunderland
- ➔ Uxbridge
- ➔ Wolverhampton
- ➔ Worcester
- ➔ Wrexham

FINDINGS FROM FINANCE

More Lenders Compete to Fund Student Housing

Words:
David Yeadon,
Director, SPF

Lenders now see student housing as a secure sector. We are seeing a growing number of lenders willing to lend in the space, at higher loan to value ratios and at cheaper financing rates than we've typically seen in the past.

Traditional lenders, including the UK and European Banks, are growing more comfortable lending on schemes without a long-term university lease or a nominations agreement. European banks tend to focus on larger loans over £20m and are usually more willing to finance schemes over a longer term than their UK counterparts. As a consequence we have seen many more deals involve European lenders in the past 12 months and their appetite to fund student development is strong.

Debt funds, offering higher cost / higher leverage finance, have also been increasing their activity in the student market. We have seen an increase in specialist debt funds with a pure focus on development finance. They often finance deals with loan to cost ratios as high as 80-85%, which typically translates to a 70% loan to value (day one). However, these loans are only available as a short-term option, so developers / investors need to refinance or sell their assets soon after construction is complete.

Interest rates are the lowest they have ever been, and we expect this low interest environment to continue over the next few years. Long-term loans can be secured at an all-in rate of just over 3%, the lowest rates we have seen.



3%
All-in rate for the
cheapest long-term
loans available now

Student Demand

QUALITY OVER QUANTITY

Students are moving up the university rankings for extra cash

Words: **Lawrence Bowles**



“Average annual graduate earnings increase £930 for each 20 UCAS points”

Lawrence Bowles, Savills Research

Our research shows a link between graduate earnings and university entry requirements.

We expect continued growth in the demand for places at more selective institutions, while demand weakens further at lower ranked universities.

In 2015-16, the UK Government completely lifted the restrictions on student recruitment, allowing universities to bring in more undergraduate students to help boost their finances.

Initially this was advertised as a way to increase student numbers, but in reality the effect has been very different: rather than more students applying to university, similar numbers of students have applied but to a smaller range of higher ranked institutions.

This makes a lot of economic sense. With tuition fees hitting £9,250 in the 2017/18 academic year and living costs also on the rise, students want to ensure they get a

good return on their investment in education.

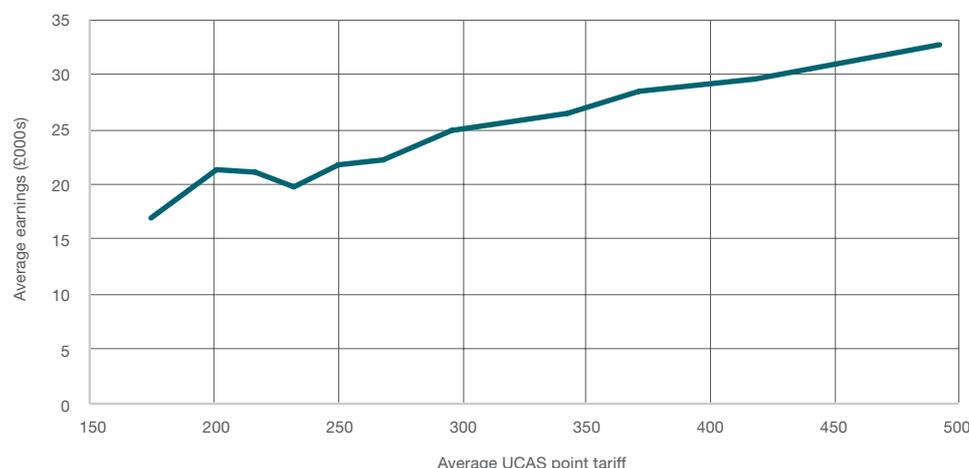
Of course there's a huge range of benefits from going to university, from learning from world-leading academics to meeting your future partner – The Student Room reports 20% of students meet the love of their life on campus. But in purely monetary terms, the easiest way to assess the impact is to analyse typical graduate salaries.

A report from the Institute for Fiscal Studies released earlier this year identified a clear correlation between university entry requirements and graduate earnings. For every 20 UCAS points required – the difference between two A level grades – students can expect to earn an extra £930 per year once they graduate.

Graduate surveys tell a similar story. Our analysis of HESA's graduate survey shows an even starker difference, with graduates earning £1,200 more per year for every 20 point difference in UCAS entry tariff. With such a clear route to higher potential earnings, it's no wonder that students are applying to more selective universities.

With university fees so high, students want to feel certain that this large investment of time and money will pay off in the long term. With increased government support for apprenticeships and vocational qualifications – which have much lower fees than universities, or may even be paid – we expect students to become even more selective in their university choices. ■

FIGURE 7 **Average Graduate Earnings by University UCAS Point Tariff**



Source: IFS

FIGURE 8 **UCAS Points by A Level Grade[^]**

Grade	Points for full A level
A*	140
A	120
B	100
C	80
D	60
E	40

[^] UCAS tariff points change from 2017 admissions cycle onwards. We expect correlation to continue.

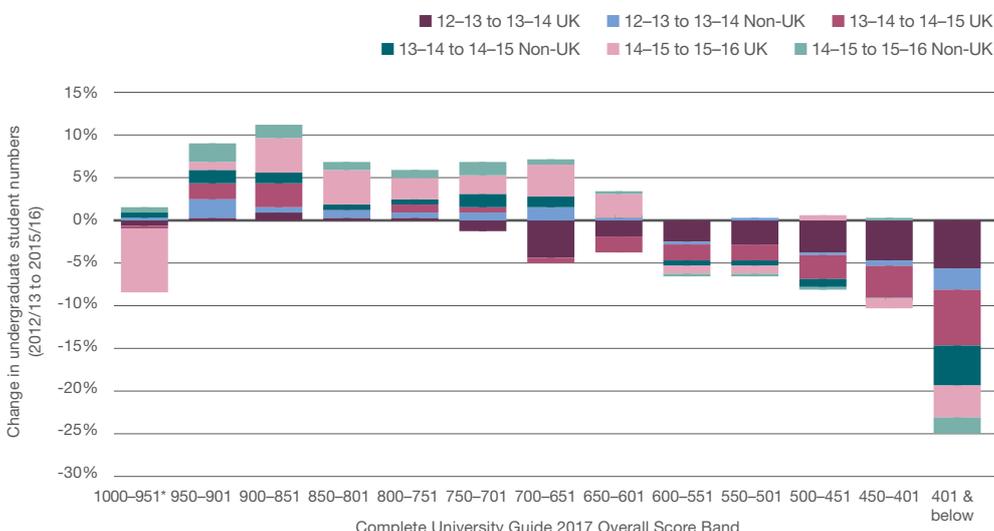
Source: UCAS

FIGURE 9
First Year Undergraduate Numbers

Year	First Year full time undergraduates
2010-11	509,065
2011-12	521,605
2012-13	466,260
2013-14	502,230
2014-15	513,295
2015-16	525,489
2016-17*	531,900
2017-18*	523,900

Source: HESA, UCAS, Savills *Forecasts

FIGURE 10
Change in Full Time Student Numbers by University Rank



Source: HESA *Drop in top tier universities reflects cuts to Oxford University part time numbers

“International students contribute tens of billions to the economy each year”

Jacqui Daly, Savills Research

A VITAL EXPORT

International student numbers may rise after the General Election

Assuming students are excluded from immigration targets in party manifestos, we forecast international student numbers to rise by 6% per year over the next three years.

This reflects the growth in the number of students worldwide who study overseas (OECD). In reality, growth may be much higher than this as access to UK higher education has been restricted to overseas students for so long.

■ **SHOW ME THE MONEY:** The UK attracted 112,000 full-time students from the EU and 285,000 from other countries last year, making up just under 23% of the full-time student population. These students contribute £25bn (Universities UK) to the UK economy each year through tuition fees and other spending such as accommodation and services.

They are also a key asset contributing to the UK’s “soft power” – our ability to influence and negotiate with other nations. According to research from the British Council, one in seven world leaders has studied in the UK. With Brexit brokering and trade talks on the horizon, international relations more important than ever. Maintaining these links will be absolutely vital.

■ **CHINESE SATELLITES:** University applications from Chinese students have almost doubled over the last decade, to 14,000 in 2016. With the sterling – yuan exchange rate 8%

lower than it was before the EU referendum, we can expect this demand growth to continue.

Peking University’s satellite campus in Oxford marks an exciting step forward for education links between the two countries, further to increased student numbers. Peking is ranked 27th in the world on the Times Higher Education University Guide, making it highly competitive with many UK institutions. It will allow students to spend their first year in Oxford, before continuing the rest of their course in Shenzhen, China.

■ **MANIFESTO MADNESS:** Any hope for a quiet, politics-free summer was smashed last month with the announcement of a June General Election. There are many reasons we should be accepting – welcoming – international students into the UK. With students cut from government immigration targets, UK universities could open their arms to overseas markets and drive growth in international student numbers.

Politicians of all parties must recognise that international students make an enormous cultural and economic contribution to the UK – to the tune of tens of billions of pounds each year. This election presents them with the chance to reflect this in their manifestos.

Alternative tenures

VALUES BEGIN TO CONVERGE

Can student operators deliver and operate Build to Rent?

Words: **Lawrence Bowles**

“There may be opportunities for developers and investors to switch delivery from student to BTR”

Lawrence Bowles, Savills Research

While some markets look less attractive for the delivery and development of new student housing, our analysis of values across a number of alternative sectors shows that values have converged in many markets.

For example, while the student pipeline looks full in Plymouth, there has been little if any development of new Build to Rent (BTR) stock. The value differential between BTR and student in Plymouth is negligible and running a cash flow shows that the IRR derived from BTR is highly competitive with student, especially in markets that are looking less favourable to absorb new student supply.

It's a similar story in Liverpool but there is more evidence for demand for BTR. Liverpool has seen the delivery of a number of

BTR schemes, and take up rates are high. We believe the market is well placed to absorb new BTR while student looks less attractive.

Can student operators stretch to BTR?

We have been saying on record for some time that student operators are well placed to deliver and operate BTR. They have vast amounts of experience of developing purpose built stock, establishing brands that attract students and operating a business that meets investors' return requirements.

So what's holding back the Student Players?

Fresh Student Living has around 16,700 student beds under management and they have recently set up Five Nine Living to deliver management solutions on PRS / BTR schemes.

The only real difference between operating student and BTR is the profile of let up and stabilisation. Instead of one letting cycle per year, there is constant letting and churn in a BTR scheme. Evidence shows that the typical tenancy length of an occupier in a purpose built professionally managed unit is three years.

So while the let up profile might be different, the longer occupancy length means that cash flows should be roughly equivalent over the long term.

What is clear from other markets like the US is that there is a key demographic group that want purpose built accommodation.

These occupiers are willing to pay for the services and amenities that go with this type of stock and they typically start their journey in PBSA

What's more, student demand has shaped demand for multifamily in America. It can do the same for BTR here in the UK. ■

FIGURE 11 Relative capital values of PBSA and BTR, £psf



Source: Savills

ALTERNATIVE PROPERTY LADDER

Purpose built rental products span the whole range of age groups from students through graduates and professionals to family housing.

For operators working in both the student housing and BTR markets, this presents an opportunity to build cohorts of lifetime customers. By providing a fantastic experience for students at university and earning their customer's loyalty, they can continue to house those people through their time as young professionals and when they move to start a family.

■ HIGHER EXPECTATIONS

Student housing used to be seen as a rite of passage. Young people would spend three or four years in grotty, overcrowded flats while barely scraping enough money together to afford instant noodles and a night out.

Those days are long gone. Now, student accommodation is some of the highest quality housing in the country. New, purpose-built blocks have facilities and amenities designed to accommodate every need. This raises the question: why would graduates want to leave?

Of course, nobody is suggesting graduates should stay living in student housing forever. But they can experience the same quality and level of service elsewhere, namely in co-living or Build to Rent homes.

■ DIFFERENT PRODUCT, SAME EXPERIENCE

For those still happy living the communal student lifestyle, co-living spaces such as the Collective at Old Oak Common offers a similar experience to student housing. The private living space is similar to PBSA, but residents can also access all sorts of shared space such as kitchens, gardens, a games room and even a spa.

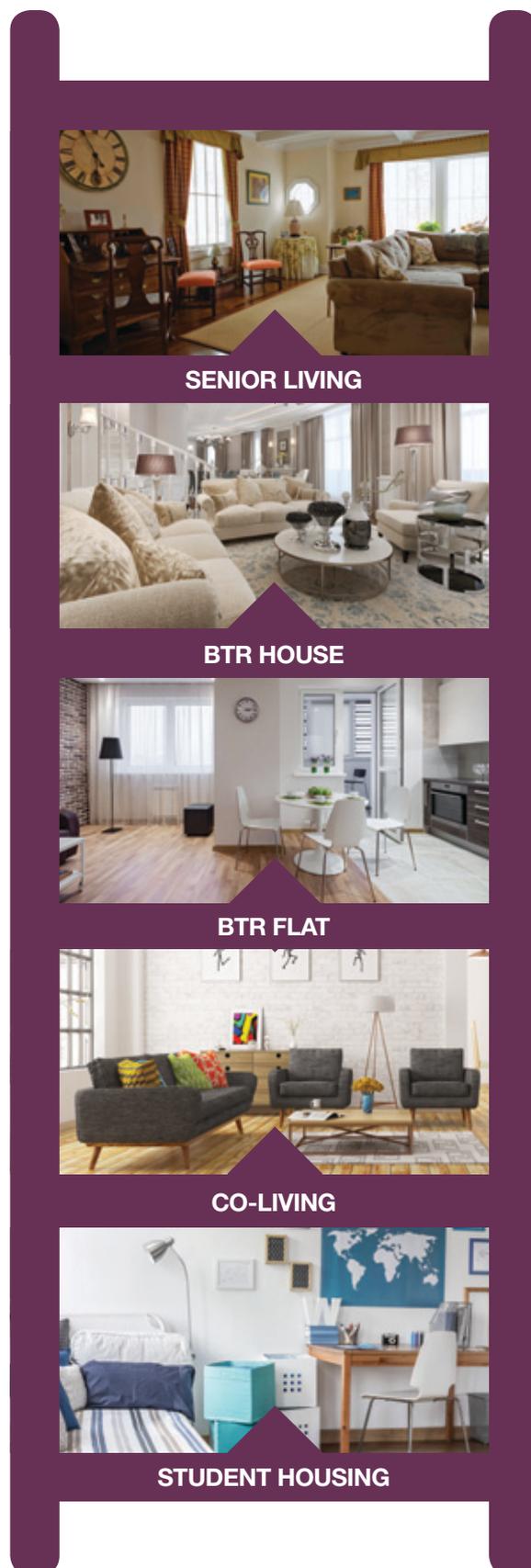
Following on from this, those graduates can move on to a more private space in a Build to Rent scheme with more traditionally sized apartments such as those at Vantage Point or East Village, both in London. Another option further up the ladder is BTR housing designed with families in mind – such as offered by Sigma.

Beyond that, we have started to see companies such as Hanover and Girlings investing in rental accommodation for senior or retirement living. This accommodation provides the space and amenities valued by older people while providing additional support with daily tasks and medical care as people age and their needs evolve.

“New, purpose-built blocks have facilities and amenities optimised to attract demand”

Lawrence Bowles, Savills Research

FIGURE 12
The Build to Rent Life Cycle



OUTLOOK

Yields in prime locations will sharpen in 2017

■ **We forecast there will be £5.3bn traded in 2017, or 75,000 beds.**

■ **Brexit will drive international investment** because of currency discount due to fall in value of sterling.

■ **Investors are becoming pickier.** Yields in prime locations will sharpen this year. In the weakest markets they will soften.

■ **This year's development league table has more fallers than risers.**

Developers will have to be careful when selecting sites.

■ **There will be more sites switching from PBSA to Build to Rent.** There are opportunities for investors that can adopt a flexible delivery approach in over supplied markets.

■ **If the Government removes students from its immigration targets, we expect international student numbers to grow 6% per annum.**

■ **There is an even greater opportunity for diversification,** with the same investor providing rented housing for students, young professionals, families and older people.

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