Savills OCM – Q2 2022

SPOTLIGHT
Savills Research

UK Co-living

A market poised for huge growth

Strong demand • Growing pipeline • Increasing investment

KEY POINTS

24,000

Total operational and pipeline units

725,000

Estimated people in the 'core target market'

Leeds City Centre

MSOA* area with the largest potential market

£550m

Of investment transactions expected in H1 2022

79%

Of residents aged between 18 to 35 in The Collective's operational schemes

18-27 sqm

Range in room sizes set out in London Plan planning guidance

*Middle super output area

Co-living attracts young professionals looking for amenity and community

Co-living is a form of housing generally comprising studio bedroom units and large amounts of high quality communal amenity space such as gyms, co-working spaces, resident lounges and cinemas.

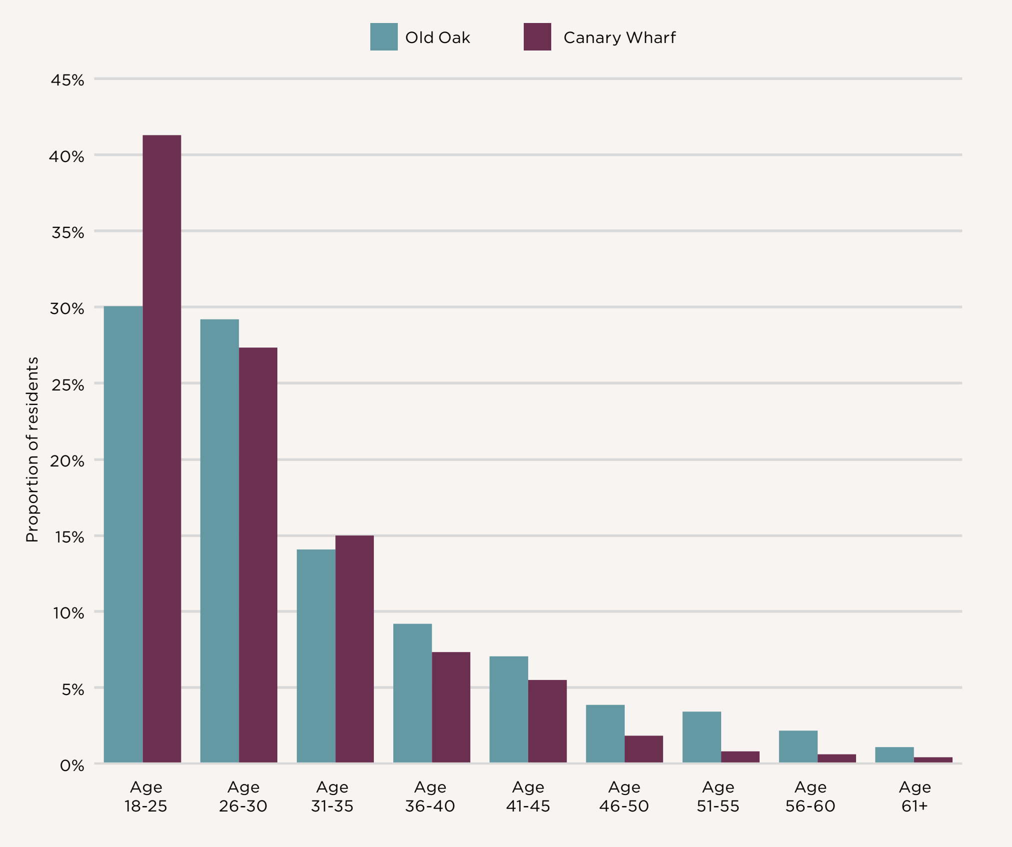
The sector has a growing pipeline across the UK, with investors, developers and operators all looking to diversify away from more 'traditional' real estate asset classes and into the 'Living' sectors. A number of factors underpin the investment case for Co-living, including the chronic housing shortage, increasing population, urbanisation, decreasing household size and shifting consumer attitudes.

Much of the demand for Co-living comes from recent graduates and young professionals starting out in their career. This demographic is attracted to a professionally managed product that is typically close to city centre attractions and job opportunities.

Co-living offers them the amenities and promise of community they are seeking (and which many of them are accustomed to from PBSA) – all at an attractive price point.

The current age profile of the two largest operational schemes, The Collective's Old Oak and Canary Wharf schemes shows that a significant majority of residents, 79%, are aged between 18 and 35. Co-living's focus on facilitating interaction between residents can also reduce loneliness, an important factor in supporting young people's mental health and wellbeing.

Age of residents in The Collective's operational schemes



Source GCP Co-living IPO Prospectus

Co-living offers greater choice for those unable to buy, or who want the flexibility of renting

Housing values have risen to a point in comparison with average earnings that has made buying increasingly unaffordable for many, especially young people, who wish to live in cities, close to their jobs and amenities.

Average first-time buyer deposits are at record highs, meaning that generally only those lucky enough to benefit from the 'Bank of Mum and Dad' have a chance to get on the housing ladder. This has meant the private rented sector has continued to grow.

Across the UK there were nearly 2 million more households in the private rented sector (PRS) in 2019 than there were in 2011. This represented a 50% increase, with the total number rising from 3.9 million to 5.9 million. In London alone there are 1.1 million PRS households, an increase of more than 300,000 over the same period.

While this is not a new trend, the extensive house price growth over the past 18 months has pushed home ownership even further out of reach for first-time buyers, adding to the attractiveness of Co-living.

Impact of house price growth

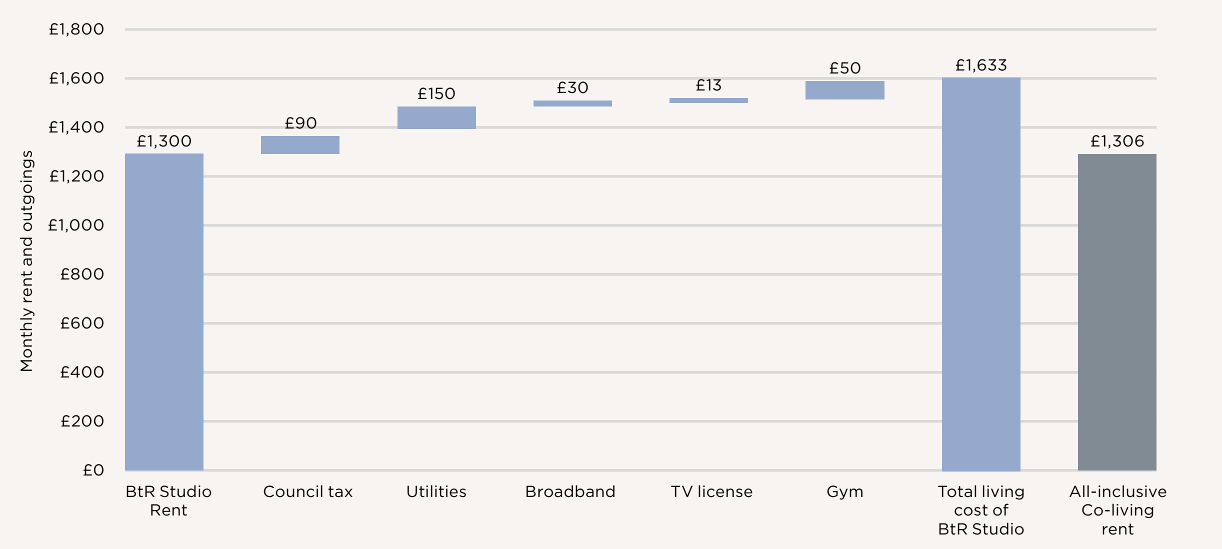
Key Stats	London	UK
Average first-time buyer deposit	£158,196	£60,718
Affordability ratio (median income to house price)	13.7	8.9*
% increase in number of PRS households (2019 vs 2011)	38%	50%*

England and Wales* **Source UK Finance, ONS, Census, Experian

Rental values in Co-living schemes are often mistakenly thought to be at a premium to the wider residential market and therefore only available to higher earners. However, the reality is that Co-living rents are targeted at a c. 20% discount versus the all-in cost of living in other PRS accommodation. This is an approximate discount and will depend on room sizes offered, amenity and so on.

For many tenants, having high quality amenities within their building and everything included in one simple monthly rental payment, more than compensates for the smaller bedroom space and makes Co-living a compelling offer.

Hypothetical value proposition



Source Savills

Demand is highly concentrated in London and major regional city centres

We have measured the 'core target market' by only including people who meet all of five key criteria:

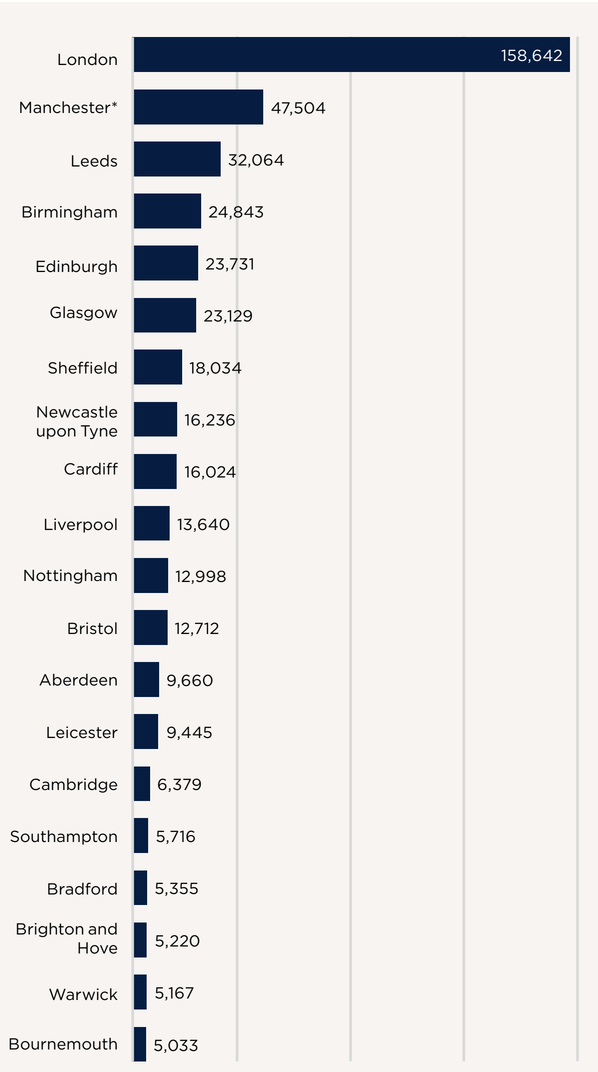
1	Currently live in the private rented sector
2	Between 18 and 35 years of age
3	Live in households without children
4	Classified within an affluent demographic, with a high propensity to live in shared accommodation (City Prosperity, Prestige Positions, Rental Hubs, Aspiring Homemakers)
5	Have personal incomes such that they can afford the median 1-bed property in their local authority, if spending a maximum of 35% of their gross income on rent

We estimate the potential size of the 'core target market' for Co-living across the UK to be c.725,000 units. Within that, London accounts for nearly 160,000 units – around 22% of the total market. In descending order of size, Manchester, Leeds, and Birmingham then have the largest potential target markets, outside of London.

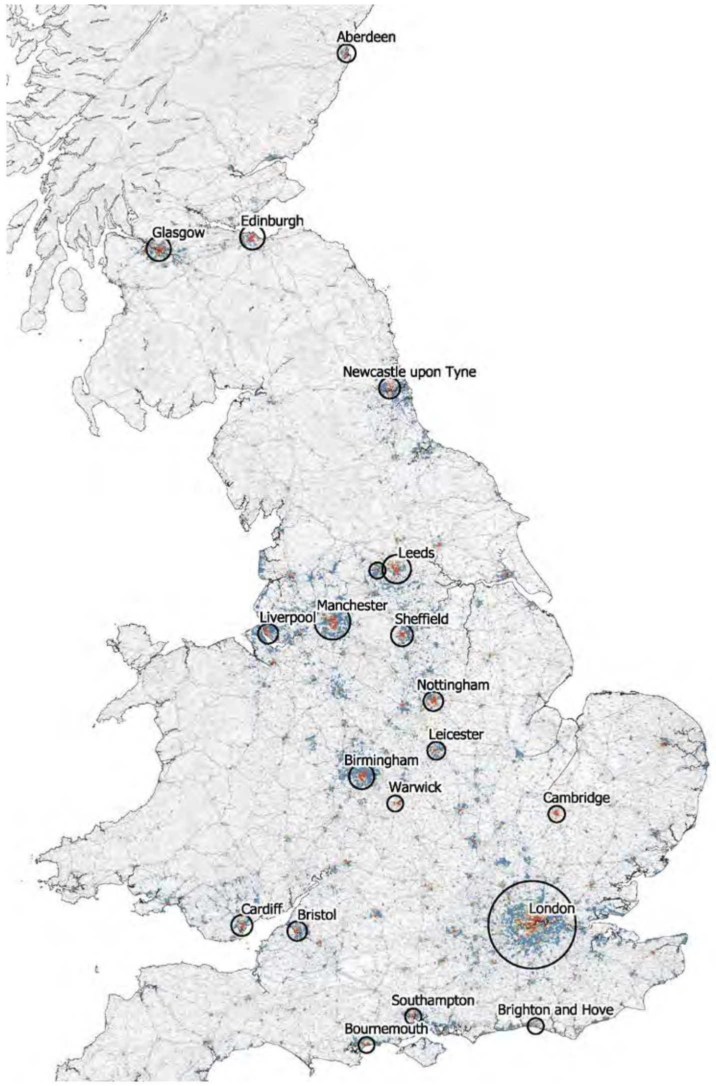
Our formula doesn't include a number of other potential sources of tenants for Co-living, for example adult children living at home with their parents, professionals using a Co-living bed as a pied-a-terre, and corporate lets. If we also include people of all ages (as 21% of The Collective residents are aged 35+), the wider 'addressable market' increases to around 1.56 million people.

With growing affordability constraints and an increasing desire on the part of many to live in an urban location with a sense of community, Co-living looks set to establish itself, just like BtR and PBSA have done before it – offering greater housing choice to a part of the market which has often lacked it.

Total number of people in the 'core target market'



Top 20 largest markets (total number of people in the 'core target market')



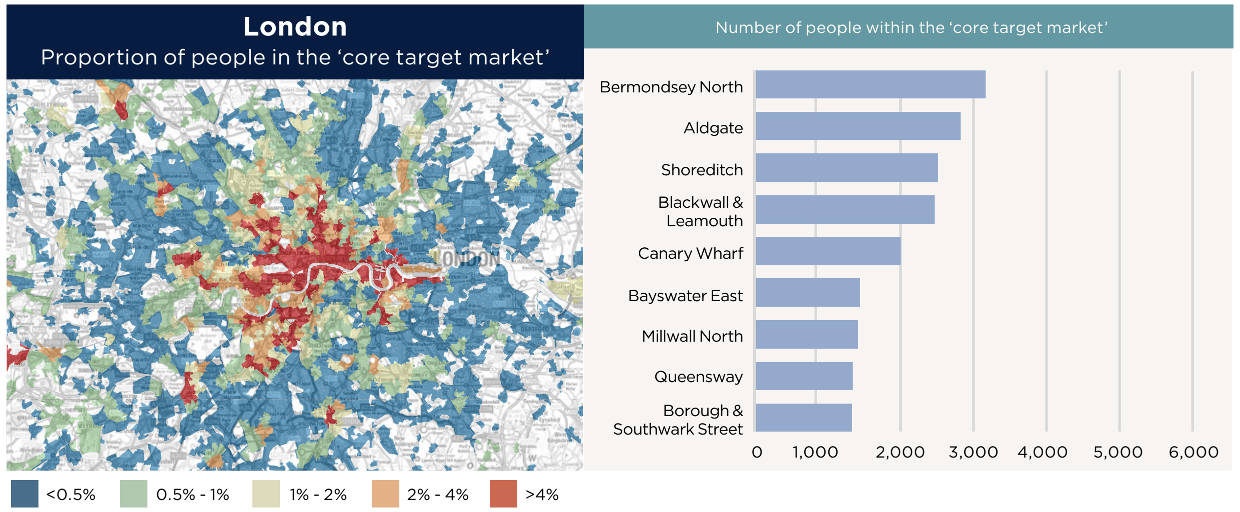
*Includes Salford **Source** Savills Research using Experian, Rightmove

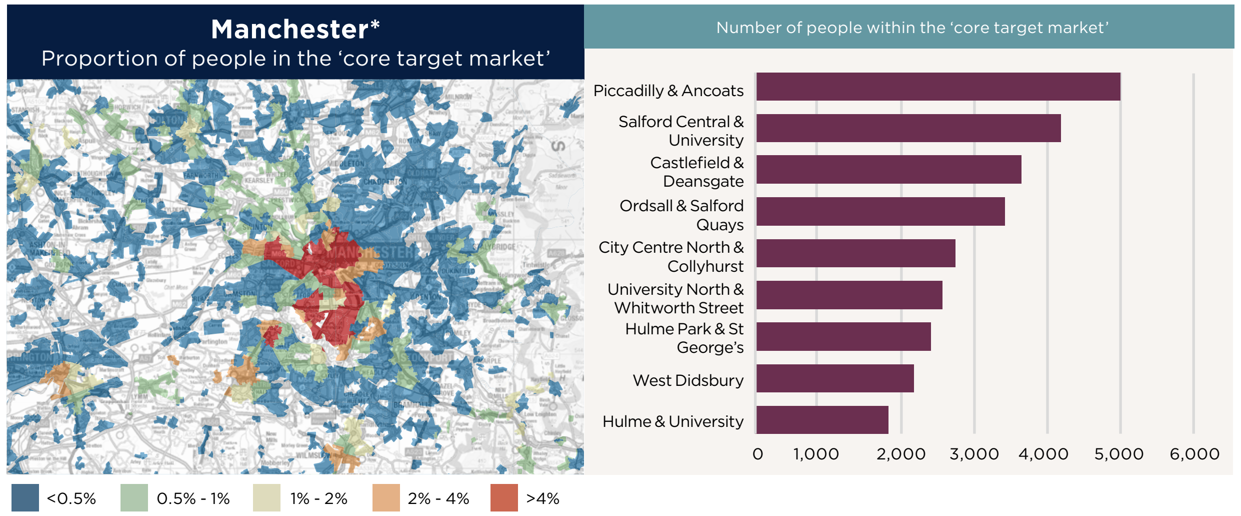
The largest potential Co-living markets

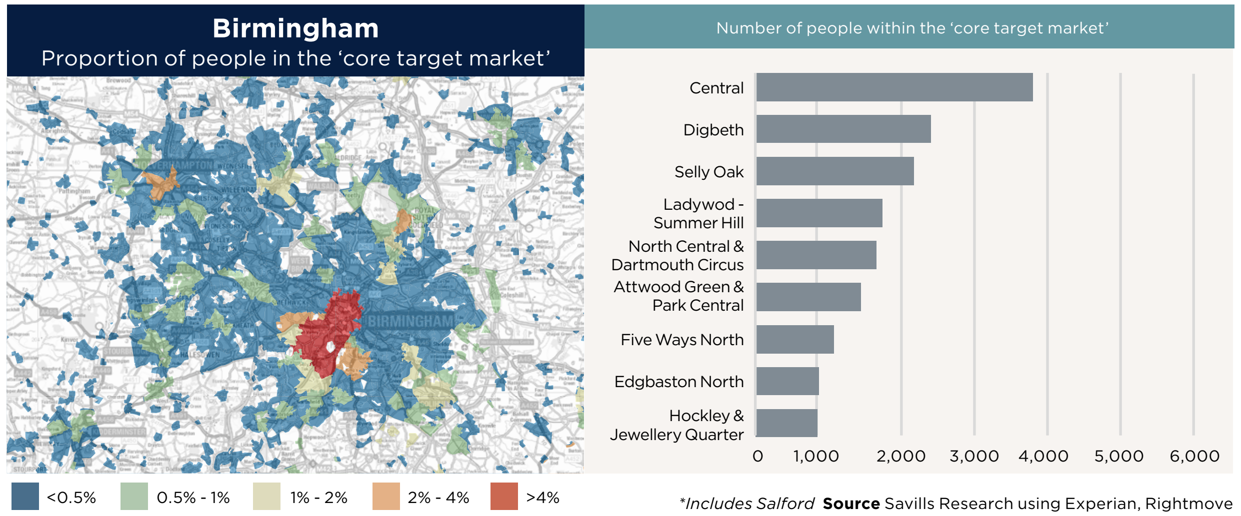
The following maps show the proportion of the total population that fall within all five key criteria of our 'core target market' for Co-living. The urban centres of major cities dominate, but there are also pockets outside of these. In London, places such as Mile End, Lewisham, Tooting, Stoke Newington and Ealing stand out.

Outside of the capital, Ancoats in Manchester, Central Birmingham and City Centre Leeds are all places that have a large 'core' Co-living 'target market'.

The areas with the largest number of people within the 'core target market'







*Includes Salford **Source** Savills Research using Experian, Rightmove

More Local Authorities are planning for Co-living

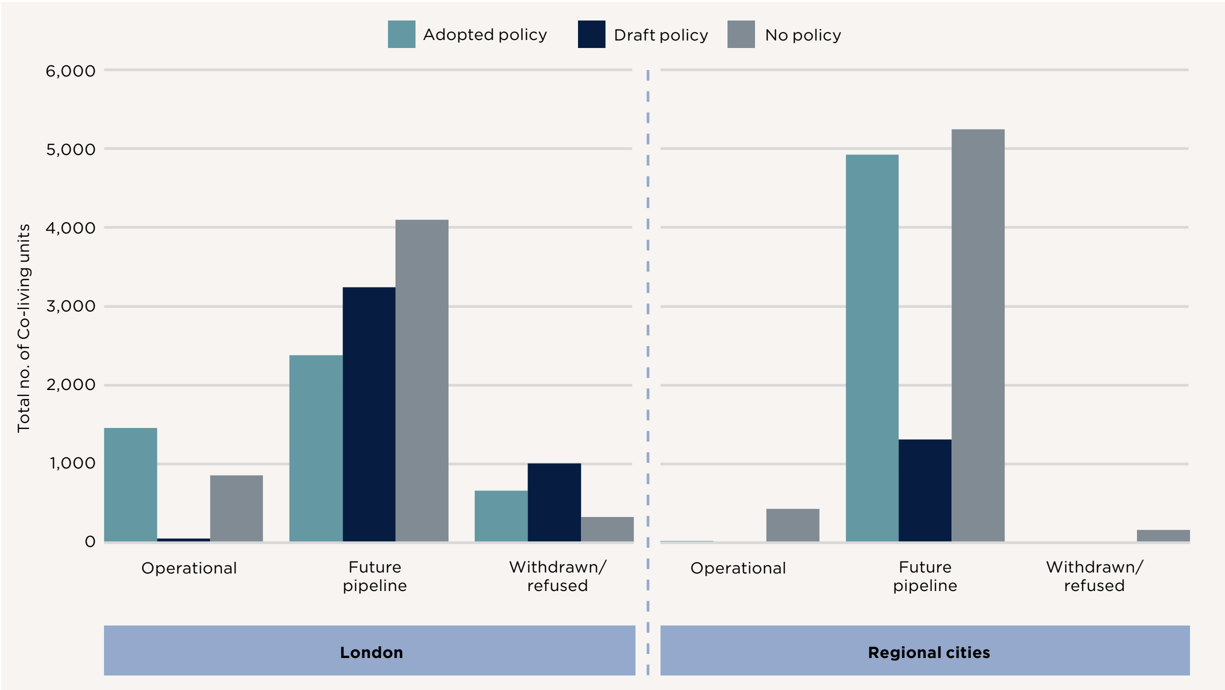
As tenants and the investment community become comfortable with Co-living, Local Authorities are increasingly acknowledging its benefits, accepting it and actively planning for it. The 2021 London Plan outlines 'large-scale purpose-built shared living' (LSPDSL), which broadly defines a framework of criteria. These include a minimum scheme size of around 50 units, a contribution to off-site affordable housing and a need for schemes to be under single management, amongst other policies.

More recently, the Greater London Authority (GLA) published further guidance on Co-living, which will be a material consideration within the London Plan. This is more prescriptive, with requirements on aspects including amenity and communal areas, as well as minimum and maximum room space standards - of 18 sqm and 27 sqm respectively.

A broad spectrum of industry stakeholders, including Savills, have made representations on this guidance to try and ensure the establishment and continued innovation of the sector, to ultimately improve the quality and variety of consumers' residential rental choices.

At the same time, outside of the capital, some Local Authorities have set planning guidance that makes Co-living harder from a viability perspective. Birmingham for example has a draft planning document that states rooms should be a minimum of 27.5 sqm, whilst in Liverpool, the council signed off on a planning advice note saying Co-living schemes should adhere to nationally prescribed minimum space standards of 37 sqm.

Are Co-living planning policies in place at local level, where schemes are coming forward?



Source Savills

The market is moving towards larger room sizes

The design of Co-living has naturally evolved since the first generation of schemes began operating in 2016 and the ambition of new developments, whilst still offering flexibility on length of stay, is generally to attract a less transient resident. This has led to the incorporation of improved and better-integrated common amenity space such as resident lounges, as well as larger units.

On the latter, according to the Gravis Prospectus, on the paused GCP Co-living REIT IPO, occupancy rates and renewals were meaningfully higher for larger units.

Looking ahead, the 'second generation' of Co-living schemes now coming forward are generally proposing larger studio units with an average size range of c. 20-25sqm and developers are adjusting to cater for this.

Some are calling for the GLA to remove their proposed maximum room size of 27 sqm units to create further choice and diversity in price points within schemes.

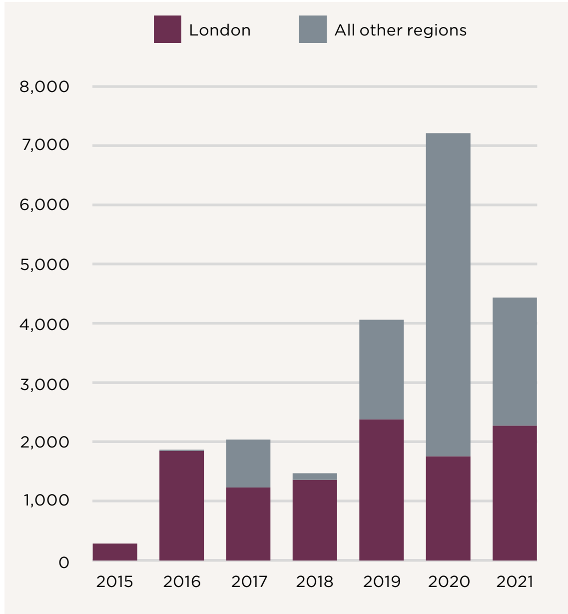
This is not to say that a format akin to a 'Friends' shared flat is not viable, it just hasn't been delivered at scale to date in the UK. This particular format of Co-living has been delivered in the US and is very successful.

London has led the way, but regional cities are catching up

Similar to the trend we saw previously in the Build to Rent (BtR) / Multifamily market, London has led the way in the emergence of Co-living. This is perhaps no surprise given that affordability constraints are most severe in the capital and so there is heightened demand for high quality rental accommodation. However, the regions have since caught up, with 60% of units submitted for planning over the past three years being outside of London.

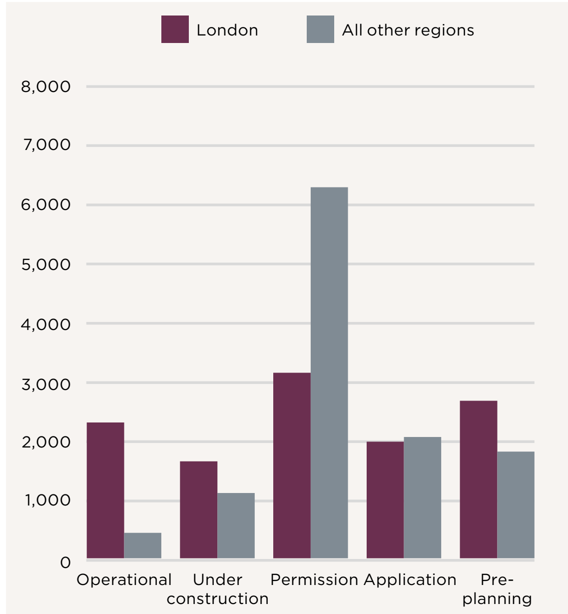
The total operational and future pipeline now stands at around 24,000 units. This is split 50/50 between the regions and London. Again, similar to the wider Build to Rent (BtR) market, outside of London it is Manchester with the largest pipeline, followed by Sheffield, Glasgow, and Birmingham.

Co-living units submitted for planning



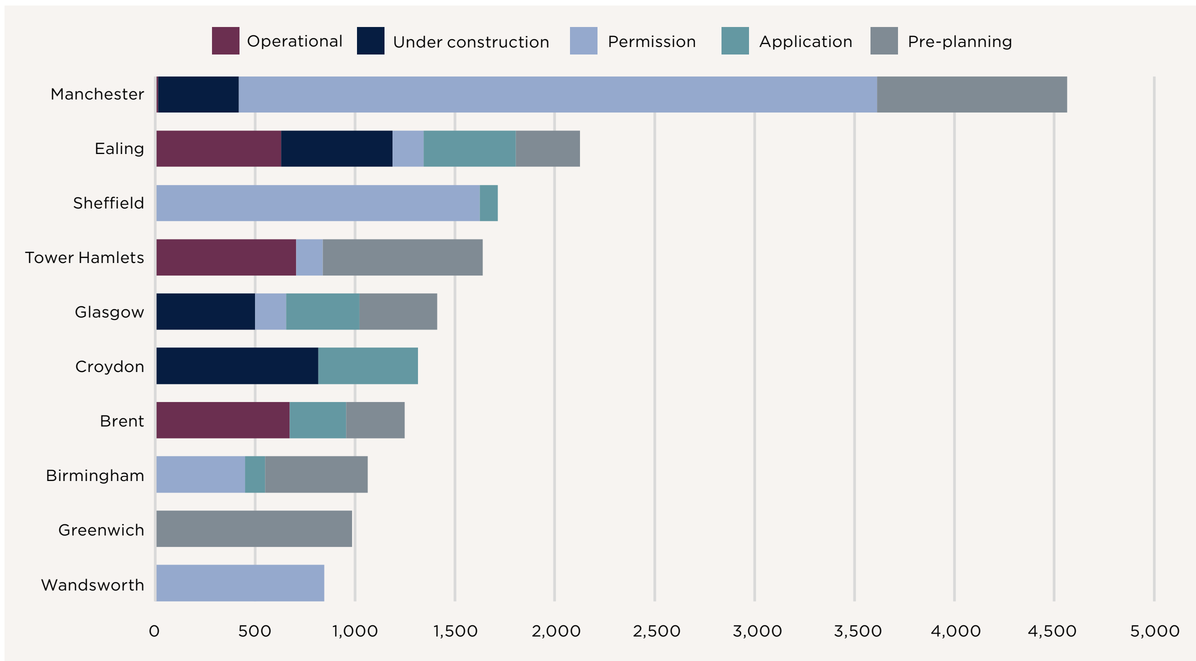
Source Savills

Operational and pipeline by status



Source Savills

Co-living units submitted by local authority



Source Savills

Investment trends

Largest 8 Co-living schemes

	Scheme	Units	Developer	Status	Local Authority	Region
1	Water Street	1,676	Vita	Under Construction	Manchester	North West
2	First Street	1,518	Downing	Under Construction	Manchester	North West
3	Rockingham Street	1,230	CODE	Under Construction	Sheffield	Yorkshire & Humber
4	Croydon College	817	Tide	Under Construction	Croydon	London
5	56-58 Marsh Wall	795	Olympian	Application	Tower Hamlets	London
6	Canary Wharf	705	The Collective	Operational	Tower Hamlets	London
7	Old Oak	550	The Collective	Operational	Ealing	London
8	Castle Public House	462	Tide	Under Construction	Ealing	London

Source Savills

Investment continues to increase, supporting viability

Whilst the amount of operational stock is currently limited due to the nascency of the sector, there are a number of significant transactions, equating to around £540m in total, that are currently under offer and due to complete in H1 2022.

These include the £425m private acquisition of three The Collective assets (previously in exclusivity as a potential IPO listing) and two Greater London forward fundings. The largest single asset transaction to date has been Oaktree's forward funding of Tide's 49-storey tower in Croydon, in March 2021.

Given the similarities to PBSA, it is no surprise to see the early movers in the Co-living market being predominantly PBSA specialists given their existing development and management capabilities.

Key examples include Watkin Jones, Scape, Vita and Downing, all of whom are currently developing out Co-living product and have the in-house management to successfully transition to and maximise income generation.

Selected transactional activity

Scheme	Location	Net Price (approx.)	Date	NIY (approx.)	Units	Price Per Unit (approx.)	Purchaser
The Collective Portfolio	London	£425m	Under offer	4.60%	1,583	£270k	Confidential
Fife Lane	Kingston	£50m	Under offer	4.50%	200	£250k*	Confidential
Guildford Plaza	Guildford	£63m	Under offer	4.50%	301	£210k*	Confidential
The Mall	Ealing	£20m	Dec-21	4.50%	81	£245k*	Moorfield
Gladstone Road	Exeter	£17m	Sep-21	4.90%	133	£130k*	BP
College Road	Croydon	£200m	Mar-21	4.50%	817	£245k*	Oaktree

Forward funding, net of coupon pricing reflected* **Source Savills

The debt market continues to get comfortable with Co-living, as the pool of lenders widens

It has been the case for some time that there are strong levels of liquidity across all leverage points for traditional Built to Rent product, from both the bank and non-bank market.

This was previously not the case however for Co-living schemes, where lender appetite was far more modest. Many lenders were hesitant to throw support behind a less established sector and were therefore very selective in backing new opportunities. Some of this hesitancy was due to an absence of market information, with limited schemes having gone through a full development and operational lifecycle. This, combined with a more challenging credit process when approving lending into a new concept, meant a lot of lenders prioritised deals within their existing 'comfort zone' / sectors.

A major obstacle for borrowers was therefore the limited number of lenders willing to provide debt, as the majority of deals were being funnelled through a fairly narrow lending pool.

However, over the last 18 months a far greater number of lenders are actively pursuing Co-living financing opportunities, with borrowers achieving terms comparable to those on more traditional Build to Rent product. Savills' Debt Advisory team has secured over £280m of debt for Co-living projects since Q2 2021 and are expecting to have secured more than £500m by the end of 2022.

Whilst non-bank lenders operating at higher leverage points were initially more supportive of Co-living, the bank market, keen to deploy capital, seems to have recognised that Co-living is here to stay. This is evidenced by the increasing level of institutional capital being deployed into the sector, competing heavily with non-bank lenders for access to new deals.

Highlighting the number of different structures available to investors when accessing the Co-living market, Savills has secured debt for investors as part of a forward funding, a develop and hold strategy, for converting standing assets (such as Hotels) to Co-living and as a bridge facility to support a change of use planning process.

Savills Research

We are a dedicated team with an unrivalled reputation for producing well-informed and accurate analysis, research and commentary across all property sectors throughout the Americas, the UK, continental Europe, Asia Pacific, Africa, India and the Middle East.

Paul Wellman
Associate Director, Research
+44 (0) 7866 117 709
paul.wellman@savills.com

Richard Valentine-Selsey
Director, Research
+44 (0) 7870 403 193
richard.valentineselsey@savills.com

Lawrence Bowles
Director, Research
+44 (0) 7855 999 466
lbowles@savills.com

Jacqui Daly
Director, Research
+44 (0) 7968 550 399
jdaly@savills.com

Savills Operational Capital Markets

We provide our clients with valuation, consultancy, transactional and financing advice in the Residential (PRS), Student Accommodation, Co-living, Senior Living and Healthcare sectors - across the UK and Europe. Our track record is unrivalled, having advised our clients on over £20bn of transactions in the last three years.

James Hanmer
Head of UK PBSA
Investment & Co-living
+44 (0) 7967 555 897
jhanmer@savills.com

Lizzie Beagley
Director, UK PBSA
Investment & Co-living
+44 (0) 7807 999 174
lizzie.beagley@savills.com

Richard McKenna
Director, UK PBSA
Investment & Co-living
+44 (0) 7972 000 092
rmckenna@savills.com

Rachel Coates
Director, Head of PBSA
& Co-living Valuation
+44 (0) 7732 211 205
rachel.coates@savills.com

Andrew McMurdo
Co-Head of Savills
Capital Advisors
+44 (0) 7787 503 243
andrew.mcmurdo@savills.com

Ralph Watson
Head of Corporate Transactions
Savills Capital Advisors
+44 (0) 7870 838 917
ralph.watson@savills.com

Morgan Scale
Associate Director,
Savills Capital Advisors
+44 (0) 7971 953 147
morgan.scale@savills.com

Ben Thomas
Senior Associate,
Savills Capital Advisors
+44 (0) 7807 999 686
ben.thomas@savills.com