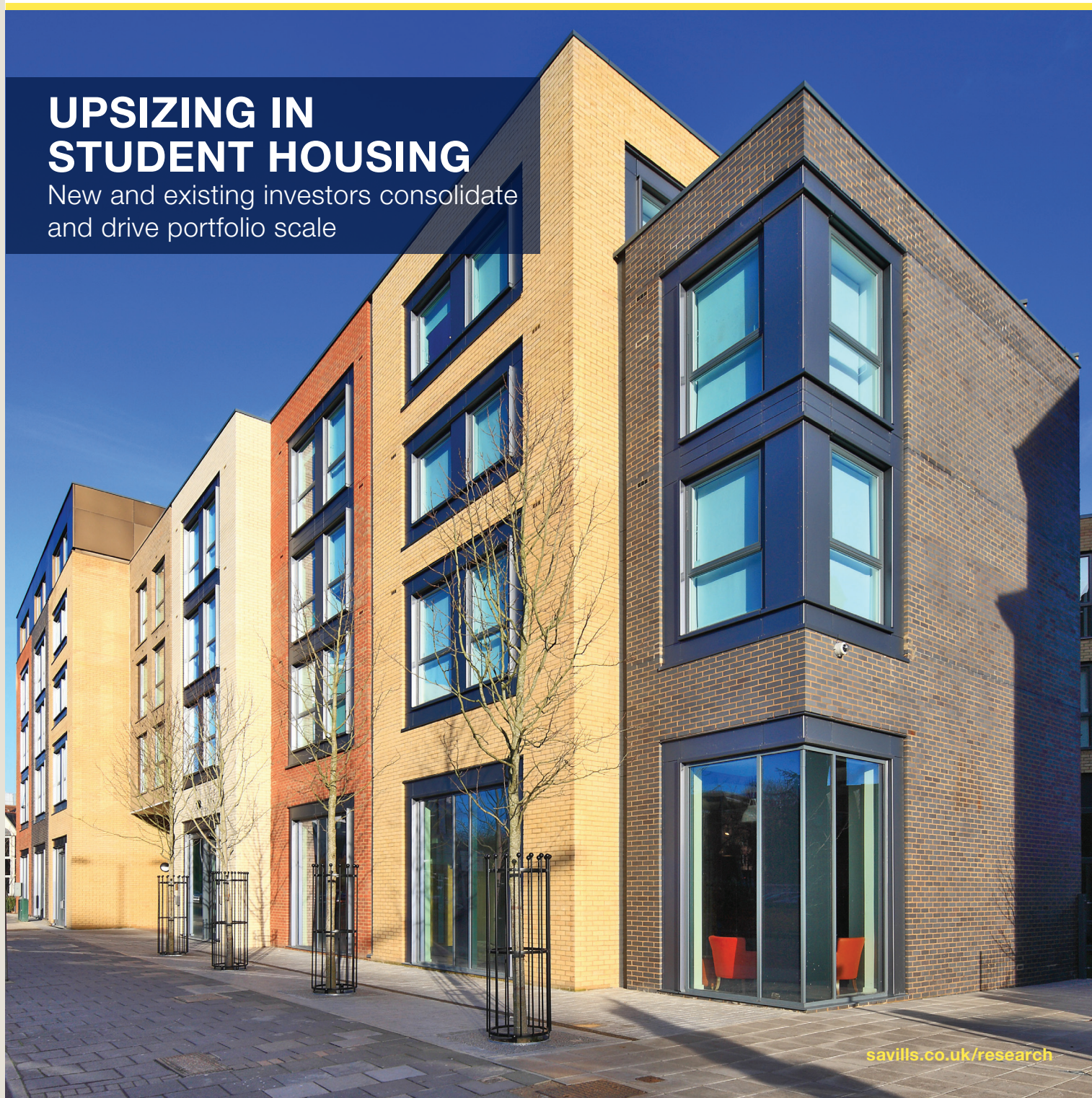


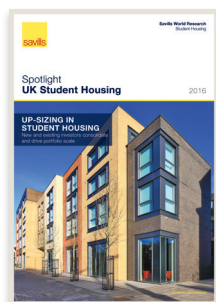
Spotlight **UK Student Housing**

2016

UPSIZING IN STUDENT HOUSING

New and existing investors consolidate
and drive portfolio scale





Spotlight UK Student Housing

The market will continue to see high levels of consolidation, as investors and operators drive to achieve economies of scale through amassing even greater sized portfolios

Words:
Jacqui Daly

The student investment market experienced an exceptionally strong year in 2015, with 74,500 beds traded at a total value of £5.9bn.

This investment activity was due to a surge in the number of large portfolios traded in the first quarter of 2015 and much higher levels of consolidation in the sector than

we have seen in the past. Was this record breaking year just a one-off or can it continue?

The student investment market has grown strongly since the recession, with an average of 44,000 beds and £2.4bn traded each year between 2012 and 2014. The doubling in the value of assets traded during 2015 was a result of fortuitous timing; a number of development-led portfolios hit maturity

and others went through re-structuring at the time that new global investors began to take serious interest in the sector and the opportunities to invest in portfolios and achieve instant scale.

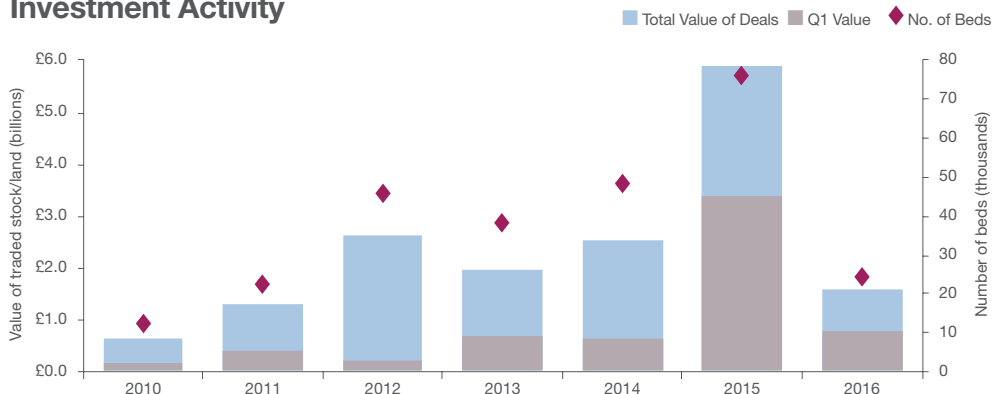
As a result, investors' appetite for existing assets with stable income streams has never been stronger. Of the £5.9bn traded in 2015, £850m of investment was targeting the delivery of new stock through forward funding and forward commitment deals, and around £250m was deals involving the acquisition of development sites. Therefore, £4.75bn (80%) of activity in 2015 involved trading existing stock and 8.5% of total existing beds.

The consolidation in the market reflects two key trends: existing investors seeking to crystallise profit and either exit the market or target higher returns in less mature international markets, and a second wave of larger global investors interested in the UK's maturing market.

Unlike earlier investors who achieved higher returns from development and investing in newly built stock, many recent global investors are searching for longer-term secured income streams. The primary aim for many of them will be to achieve sufficient economies of scale to deliver their target rates of returns. The challenge will be in finding enough appropriate investment opportunities for them to do so.

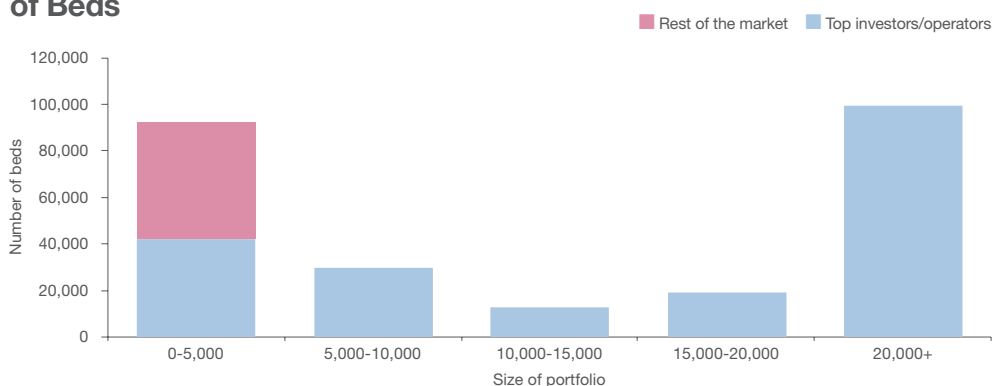
Many of these new investors are looking to amass large portfolios, akin to the portfolios of scale in both the US student and multi-family markets. For example; Wellcome Trust's IQ merger with Goldman Sachs and Greystar's Prodigy Living demonstrates the drive to achieve scale quickly in the market. But achieving economies of scale in

FIGURE 1
Investment Activity



Source: Savills Research

FIGURE 2
Private Sector Student Accommodation Ownership by Number of Beds



Source: Savills Research

the UK student market is difficult given the composition of the market and as investment activity continues, there will be fewer large portfolios available. The student market is highly fragmented and, although only 8.5% of total beds were traded in 2015, the figure rises to 30% for privately owned beds. Of the top 30 operators/investors in the UK market by size (number of operational beds), 50% of the market is owned by those with less than 10,000 beds.

Therefore, as the appetite from global investors continues unabated, it appears likely that consolidation via mergers and acquisitions will be one of the defining features of the market in coming years. ■

FIGURE 3

Largest Owners by Number of Beds

	Owner / Investor	Number of beds
Unite Students	Operator	46,000
UPP	Operator	30,000
Vero (formerly IQ & Prodigy)	Operator	23,500
Liberty Living/CPPIB	Operator	19,200
Sanctuary Student Housing	Operator	13,000
Campus Living Villages	Operator	8,400
360 Developments	Operator	7,200
Curlew Capital	Institutional	6,400
Empiric Student Property	REIT	6,100

Source: Savills Research

INVESTMENT PERFORMANCE

Stable returns

With the large inflow of investment in 2015, yields on student accommodation across all locations and lease types compressed by 50-75 basis points (excluding portfolio premiums of up to 75 basis points).

Looking ahead, we are forecasting total investment of £4 billion in 2016. This is down on last year's record-breaking total but still an increase of 57% on the investment seen in 2014. We expect yields to remain static during 2016 and, with rental growth averaging out at 3.5%, our forecast is for average total returns of 9.5%.

FIGURE 4

2016 Yields

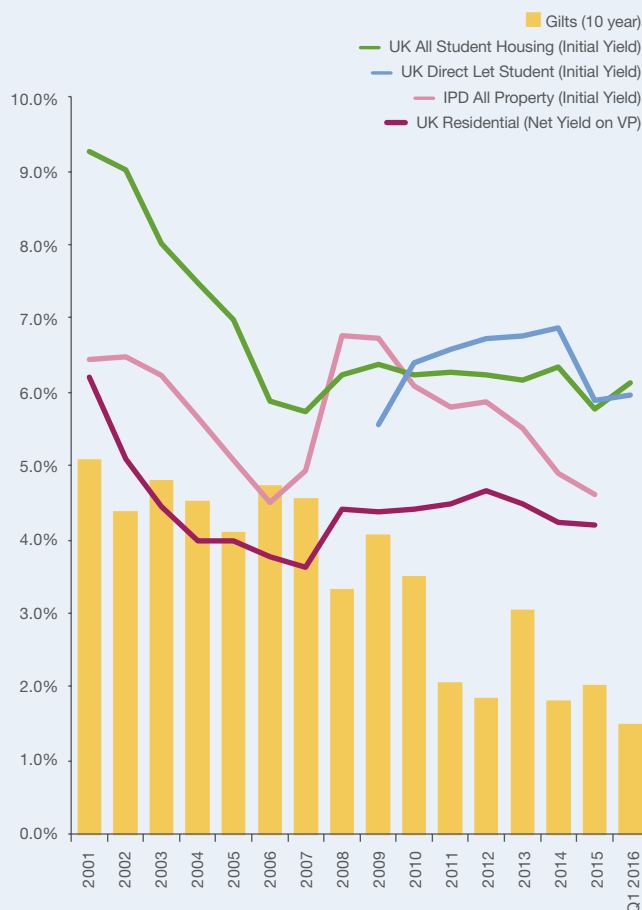
	Lease	Nomination Agreement	Direct Let
Prime London	4.00%	4.50%	4.75%
Super Prime Regional	4.25%	4.75%	5.50%
Prime Regional	4.50%	5.25%	6.00%
Secondary Regional	5.00%	5.75%	6.75%

Lease: 25 year lease to institutional grade university covenant on annual RPI linked increases with a cap and collar
Nomination Agreement: 15 years+ nomination agreement to institutional grade university covenant on annual RPI linked increases with a cap and collar

Source: Savills Research

FIGURE 5

Investment Yields



Source: IPD & Savills Research

Words:
Jacqui Daly

GLOBAL INVESTMENT FLOWS

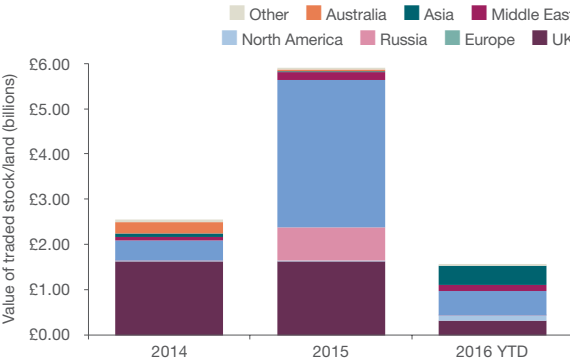
Last year was not only record-breaking in terms of investment activity but also highlighted the sector's ongoing evolution into a mature and global investment market.

Traditionally, the market has been dominated by UK investors and operators. Last year, the total value of deals involving UK buyers was £1.6 billion, the same as the previous year. However, rather than being responsible for the majority of deals (by value) as they were in 2014, they were put firmly into second place by North American institutional investors who bought £3.3 billion of assets. There were also significant purchases by Russian investors and, to a lesser degree, investors from the Middle East.

Although the first quarter of 2016 has seen significantly less investment activity than in the same period last year, it is still 17% higher than the average for the 2013 and 2014 first quarters. Asian investors showed considerable interest last year and that has been converted into activity this year with £420million of investment, accounting for 50% of deals by value.

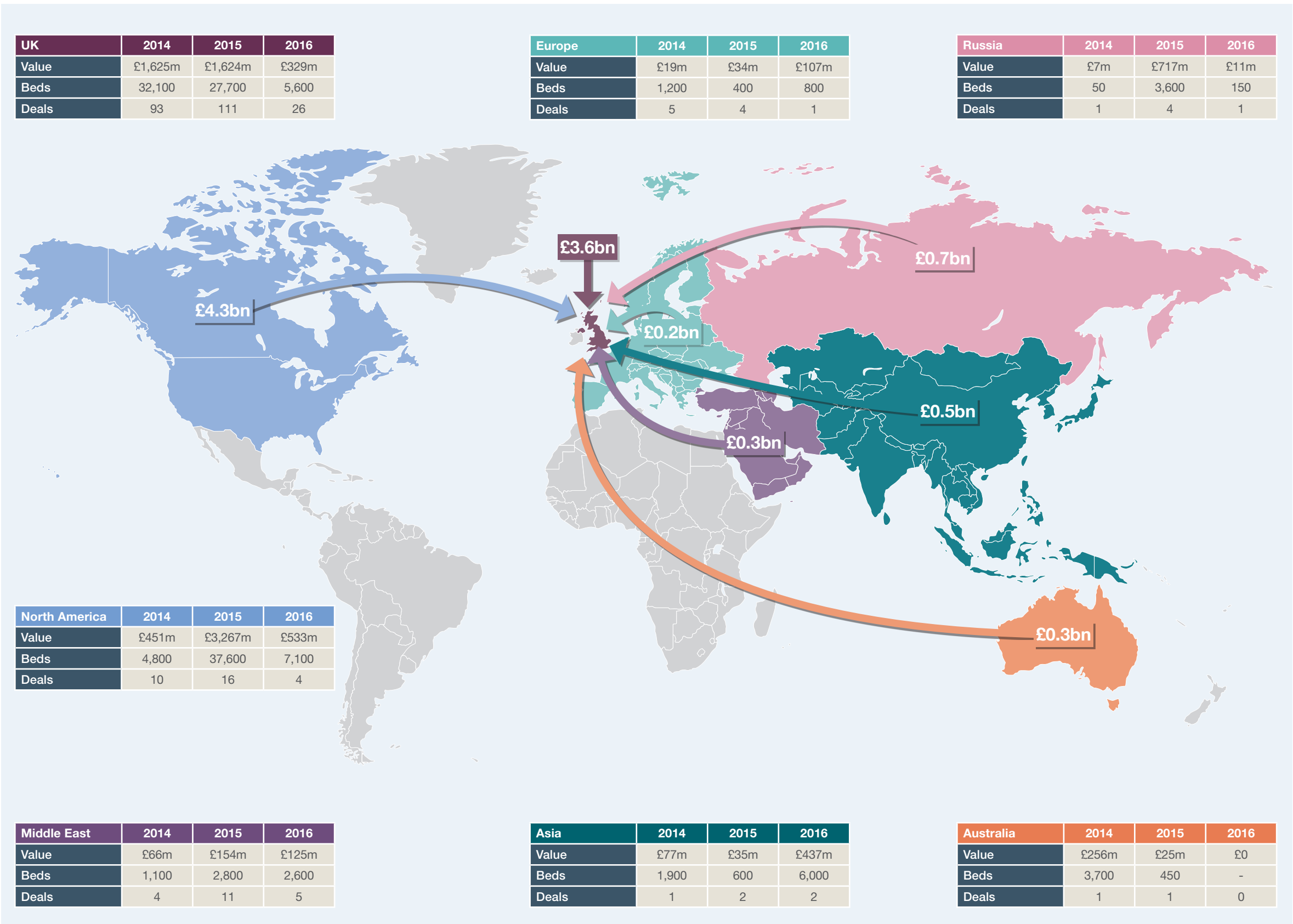
Interest in the sector remains strong but it is unlikely that total investment will hit last year's heights. The impact of the EU referendum on activity has been limited to date and we will probably see a strong second half of the year as the sector remains attractive to global investors.

FIGURE 6 Investment by Region



Source: Savills Research

FIGURE 7 Global Investment into UK Student Housing Over Last Three Years



Source: Savills Research

Words:
Lawrence Bowles

STABLE NUMBERS

Full-time student numbers increased for the 2014/15 academic year and are nearly back at 2010/11 numbers. But it is not good news everywhere as total student numbers fell by 1.4%. This overall fall reflects students' search for quality and value for money in the higher fee environment.

As in previous years, the 1.4% fall in total student numbers in the 2014/15 academic year hides a wide variation in performance. The majority of the decline (91%) was due to fewer UK part-time undergraduates and this trend has continued to affect student numbers at lower ranking institutions hardest. Meanwhile, the higher

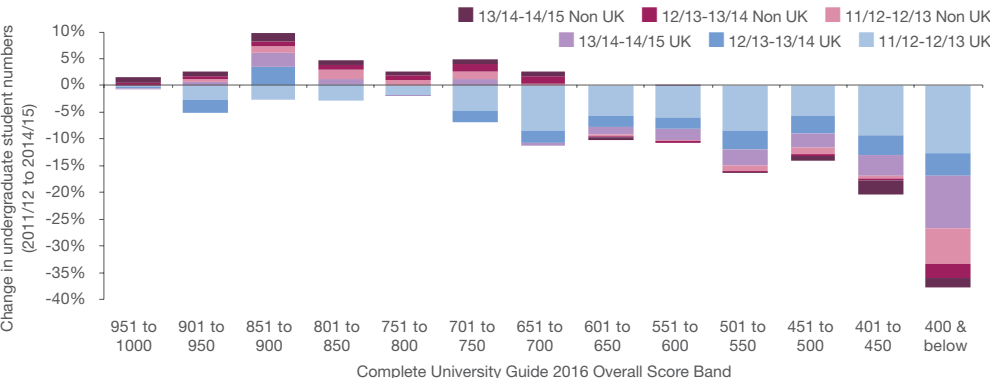
ranked institutions have continued to attract overseas students, but UK undergraduate numbers at the top 20 institutions (according to the Complete University Guide) were only up by 1.4% on the previous year.

Analysis of full-time student numbers by degree subject reinforces this trend towards value for money and shows a continuing preference for STEM subjects. A comparison with the Institute for Fiscal Studies' April 2016 report on graduate earnings offers some interesting additional information on the earning potential of students at different institutions and studying different subjects. The report highlighted that studying at higher ranked institutions tends to result in higher earnings after ten years but is also dependent on the course chosen and family background. Although there

is not a direct correlation between the trends in full-time student numbers and earnings potential, it is perhaps unsurprising that creative arts courses have seen the biggest fall in numbers since 2011/12 and students graduating with a creative arts degree had the lowest average earnings after ten years.

Looking ahead it is always worth noting that the HESA data provides a view of the market last year. Our analysis of other indicators suggests that there was a 20,000 increase in number of first year full-time undergraduates for this academic year (2015/16). However, early indicators from UCAS applications suggests that student numbers for the 2016/17 academic year may be static, with applications from UK and non-EU students similar to last year and a 6% increase in applications from the EU. ■

FIGURE 8
Change in Total Undergraduate Students Since 2011/12



Source: HESA, Complete University Guide

FIGURE 9
Change In Full Time Students by Course Since 2011/12



Source: HESA

FIGURE 10
Student Numbers

	First-Year Full-Time Undergraduates
2010/11	509,000
2011/12	522,000
2012/13	466,000
2013/14	502,000
2014/15	513,000
2015/16*	534,000
2016/17*	533,000

Source: HESA, UCAS, *Savills Estimates



The flight to quality continues with growth at higher ranked institutions

R U EU?

Uncertain risks from Brexit

The EU Referendum on the 23rd of June has created plenty of short-term economic uncertainty and even more debate about what might happen if the UK votes to leave. It is difficult to assess what might happen across the whole economy, but it is clear that there could be a sizeable impact on the UK's higher education sector.

Last year there were 125,000 students from across the EU studying at UK universities and they generate around £3.7 billion per year for the economy, according to estimates from Universities UK. A vote to leave could lead to the tuition fees they pay rising to match those paid by non-EU students. If that happens then the costs versus benefits of studying in the UK may become less attractive than in their own or other countries, leading to falling EU student numbers in this country.

Meanwhile, EU funding, shared research facilities, and shared knowledge are all important components of UK university research. Leaving the EU would have an impact on all these factors and others, at least until new individual country by country agreements are reached.

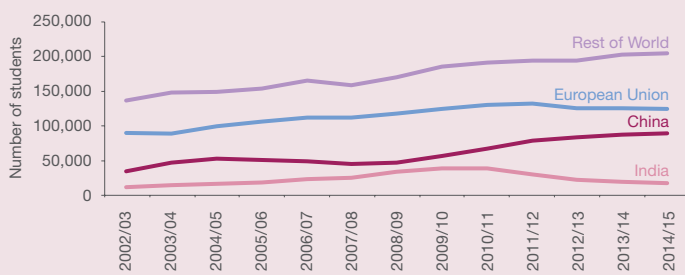
The threat of a vote to leave is creating short-term economic uncertainty and that is having a impact on activity across all real estate assets. This uncertainty would be increased in the event of a vote to leave and the higher education sector would not be immune. However, EU students are only 5.5% of total student numbers and there remains a requirement for modern purpose built student accommodation

in most towns and cities across the UK. Therefore, the long term investment potential of purpose built student accommodation would remain, possibly even boosted by any resulting currency movements post referendum. Meanwhile, a vote to stay in the EU would provide greater certainty to the markets and probably lead to increased investment and developer appetite in the months after the result.

However, in addition to the immediate challenges is the risk that a vote to leave might bring in its wake more aggressive anti-immigration policies. The current Government's approach has so far limited the growth in numbers of non-EU students coming to study in the UK but has not had a significantly negative impact on total numbers, though we have seen falling numbers of certain student groups. For example, the number of Indian students in UK higher education is less than half the number enrolled in 2010.

A stricter cap on numbers could have a devastating impact on funding into the higher education sector. Ideally, any attempt to lower net migration should exclude higher education students given their important contribution to the economy. The UK's ageing population and slow growth economy should make attracting the best and brightest young people from around the world and allowing them to continue working in the UK once they have finished their studies a priority. Hopefully, this will be recognised by policy makers irrespective of the result on the 23rd of June.

FIGURE 11
Domicile of Overseas Students



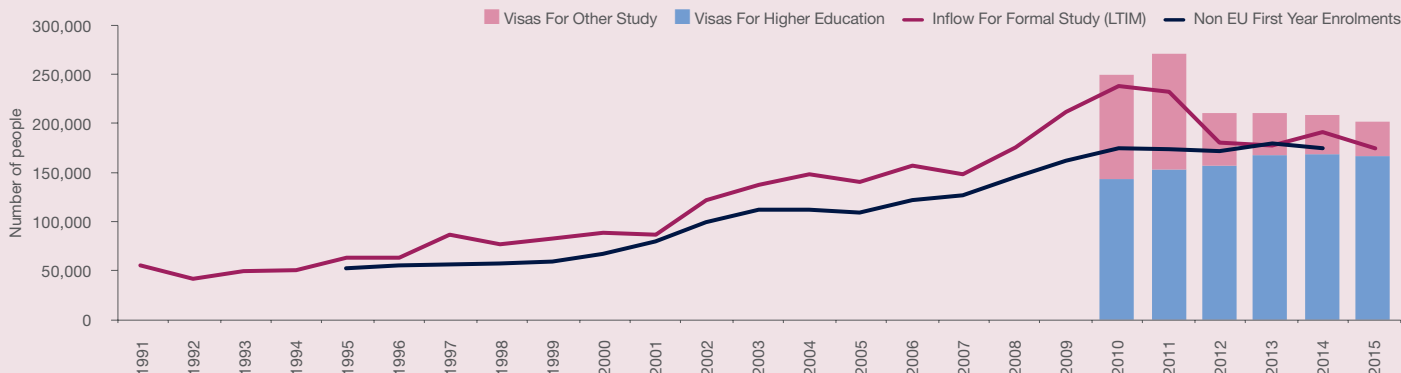
Source: HESA

FIGURE 13
Top EU Domiciles by Student Enrolments

Country of Domicile	2014/15 Students
Germany	13,675
France	11,955
Ireland	10,905
Italy	10,525
Greece	10,130

Source: HESA

FIGURE 12
International Student Numbers



Source: ONS, Home Office, HESA

Words:
Andrew Smith

DEVELOPMENT CHALLENGES

The supply of purpose built student accommodation has increased in recent years, as both student and investment demand have been strong. The sector now houses a third of all full-time students in over 550,000 purpose built beds.

However, despite the recent growth in the sector, supply in many towns and cities across the UK is still failing to meet demand.

The demand to supply ratio can be useful as a headline indicator, as shown by the map below, but it is not perfect. The optimum ratio for each town or city will depend on the characteristics of the local market including the demographic profile

of the students, the provision of university residences, and the size and strength of supply and wider demand in the private rented sector.

These differences extend to development where it's even more important to assess the overall quality, mix and location of competing stock to ensure that the product is appropriate for the micro and macro location of the site. ■

FIGURE 14
Student Demand Across the Country



Source: Savills Research, HESA

FIGURE 15
Development Examples



Green Park, Bath is one of the few successful examples of PBSA of scale being delivered in the city. The highly specified redevelopment of two buildings in a prime location will offer 461 beds for use by Bath Spa students from September 2016.



Tara House & Leece Street, Liverpool are two adjoining development sites bought by a leading student developer and operator. A 790 bed scheme is under construction which will target a range of rental price points.



Stapleton House, London is a successful example of when student developers were able to compete for land in a strong zone 2, central London location. The 862 bed scheme will complete for the 2016-17 academic year.

CLIENT VIEW – Unite Students

Managing build cost inflation is a key challenge for Unite. Build costs tend to account for between 60% and 90% of total development costs so, if inflation is not managed, margins can be eroded. Unite leverage their 8,000-bed development pipeline to help offset some of this risk by partnering with a small number of contractors who value the steady and consistent workload. These long-term relationships enable Unite to involve contractors at the beginning of projects where they can add valuable input into the design stage.

Unite are keen to invest in London, but cluster led development is unviable due to higher competing use values. The situation is made more difficult by local Boroughs and the GLA penalising student accommodation with high CIL rates and affordable housing or bursary contributions. These burdens reduce student accommodation development in London and will contribute to continued upwards pressure on rents as student numbers grow. **Nick Hayes, Development Director**

City Case Studies

BATH

Bath's supply of purpose built accommodation has increased in recent years but, with a demand to supply ratio of **2.5**, around **60%** of the **19,600** full-time students who attend the city's two universities have to find a bed elsewhere.

With only **2,000** beds in the pipeline, there are opportunities for development. However, the biggest challenge for developers is the high Community Infrastructure Levy (CIL). At £200 per square metre, this is the highest rate for student accommodation outside of London and double the local residential CIL rate. This rate has a negative impact on viability and makes achieving a competitive land value more difficult.

There is a need for more affordably priced family housing in the city and the high CIL rate may shift development towards residential. However, there may be unintended consequences as high-density residential schemes risk becoming student accommodation via the private rented sector. A more balanced approach is required.

LIVERPOOL

Liverpool has a relatively large supply of purpose built student accommodation, with over **20,000** beds available in university and private schemes. However, with **2.1** full time students for every bed, there are still opportunities for development in the right locations in the city, especially given the generally lower quality offering in the private rented sector and limited supply of this stock.

The challenge for developers and operators in Liverpool is creating a product that delivers a positive land value after construction costs while meeting their target returns. With affordability constraints and plenty of competition, there is a ceiling on rents in the market.

Successful schemes are therefore reliant on maximising the rent generated per developable area and creating economies of scale in management. A typical solution includes increasing densities by developing smaller cluster flats, while most schemes are held for long term income streams rather than capital uplift.

LONDON

The issues facing developers of student housing in London reflect the broader challenges facing all real estate developers. The capital has a massive need for more homes, more commercial space, and more student housing but a continuing scarcity of developable land. London currently has around **3.2** full-time students for every bed and, although there are **17,000** beds in the development pipeline, this would only improve the ratio to **2.6**.

With a constrained supply of land, the challenge is achieving a land value that is competitive with other use classes. In recent years there has been a drive towards premium student housing in central London and outwards into lower value markets.

However, it is increasingly difficult to compete in Zones **3-4** as high house prices spread outwards and residential developers outbid student developers for land. This will continue while the residential development market remains strong and so student developers will push further out along transport routes and towards higher densities.

Words:
Andrew Smith

DEVELOPMENT OPPORTUNITIES

Our 2016 league table of university towns and cities across the country provides a more appropriate benchmark of the development potential than any single indicator or ratio. The league table is specifically designed to consider the potential for future development of direct let purpose built student accommodation.

The rankings are based on a number of factors covering current and future supply, demand, affordability and rental growth alongside our in-house knowledge of local student development markets.

London and Bath are both in the First tier, reflecting the strength of demand in those markets despite

the challenges they face (page 09). Birmingham is the only promotion to the top tier where demand by the University at Selly Oak and Birmingham City University's Eastside campus show that there are opportunities for development.

Meanwhile, the Upper Second tier has seen the most change, with Guildford, Norwich and Nottingham all promoted and offering greater potential for development in the right location and with an appropriate product.

Unlike its successful football team, Leicester is a non-mover still stuck in the Lower Second tier. It is joined by six relegations including Aberdeen due to the oil price crash and potential supply pipeline.

Falmouth continues its rise from last year while Swansea also moves up into the Lower Second tier. Swansea

is arguably a better opportunity than Liverpool with a bigger supply-demand imbalance. However, it is constrained by the same challenges as faced by Liverpool but to a greater extent. Local rental affordability constraints mean it can be very difficult to develop a product that delivers a positive land value in the Swansea market.

The need for more supply in the Third tier is limited, and development should only be undertaken on the very best sites in these towns and cities. The Pass tier has seen four relegations, and speculative development remains very risky in these 21 towns and cities.

However, it is worth noting that a lower ranked town or city may still be attractive for investment (rather than development) if existing supply and demand are balanced and the potential investment returns are appropriate for the risks involved. ■

FIGURE 16
Development League Table

FIRST	UPPER SECOND	LOWER SECOND	THIRD	PASS
Bath ➡	Belfast ➡	Aberdeen ⬇	Aberystwyth ➡	Bolton ➡
Birmingham ⬆	Cambridge ➡	Bangor ➡	Chelmsford ➡	Bradford ➡
Brighton ➡	Canterbury ➡	Bournemouth ⬇	Cheltenham ➡	Carlisle ➡
Bristol ➡	Chester ➡	Buckingham ➡	Colchester ➡	Chislehurst ➡
Edinburgh ➡	Chichester ➡	Cardiff ⬇	Derby ➡	Cirencester ➡
Kingston upon Thames ➡	Coventry ➡	Durham ⬇	Dundee ➡	Coleraine ➡
London ➡	Exeter ➡	Egham ➡	Farnham ➡	Cranfield ➡
Manchester ➡	Guildford ⬆	Falmouth ⬆	High Wycombe ➡	Hull ➡
Oxford ➡	Leeds ➡	Glasgow ⬇	Inverness ➡	Ipswich ➡
St Andrews ➡	Norwich ⬆	Hatfield ➡	Lampeter ➡	Luton ⬇
	Nottingham ⬆	Huddersfield ➡	Lancaster ➡	Middlesbrough ➡
	Plymouth ➡	Leicester ➡	Lincoln ➡	Newport ➡
	Portsmouth ➡	Liverpool ➡	Loughborough ➡	Paisley ➡
	Sheffield ➡	Newcastle upon Tyne ➡	Ormskirk ➡	Pontypridd ⬇
	Winchester ➡	Northampton ➡	Salford ➡	Preston ➡
		Reading ➡	Sidcup ➡	Stoke-on-Trent ⬇
		Southampton ➡	Telford ➡	Sunderland ➡
		Stirling ➡		Uxbridge ➡
		Swansea ⬆		Wolverhampton ➡
		Twickenham ➡		Worcester ⬇
		York ⬇		Wrexham ➡

KEY

⬆ Up from last year

➡ Same as last year

⬇ Down from last year

Source: Savills Research

POSITIVE CONTRIBUTION

The higher education sector is an important contributor to the UK's economy and is world renowned for its research and education. Over the last few years, our reports have highlighted this contribution and how the growing purpose built accommodation sector is essential to house higher education students. Our reports have also identified how increasing the supply of purpose built accommodation can help ease the housing crisis by freeing up family homes in towns and cities. As such, the increased delivery of purpose built accommodation is welcome but there are increasing concerns about the type and affordability of both new and existing student accommodation.

Higher education and its students make a significant contribution to both national and local economies across the UK. The sector may only contribute around 3% of UK GDP but in some local authorities, the local economic contribution is over 10%. This also ignores any indirect additional impact on economic activity such as technology hubs or science parks. Meanwhile, as university participation rose and student numbers increased, the migration flows of young people across the country have had a considerable effect on local demographics and housing markets. Some local authorities might actually have seen declining populations during the 2000s if it weren't for their local higher education institutions.

As the number of students grew during the late 1990s and 2000s, it was the private, typically buy-to-let, landlords who housed them. In many towns and cities, students were (and are) a significant driver of the growing private rented sector. Converting family homes into houses of multiple occupancy was an attractive proposition when you could save on your children's rent while earning a nice income and benefiting from house price growth. Unfortunately this process led to areas of university towns and cities becoming highly concentrated with students while pricing out families looking to buy and increasingly to rent.

The purpose built and professionally managed student accommodation

sector can make a positive contribution to housing supply and ease the housing crisis in these markets. In 2014 we calculated that delivering an additional 300,000 student beds could free up 77,000 family homes in towns and cities across the UK. Although that only equates to half of one year's new build housing supply, many of these houses are in locations where developing family housing is unviable or requires a price that is unaffordable to most.

For this approach to be successful, the newly built accommodation needs to be competitive with the private rented market. That doesn't necessarily mean competing directly with HMOs on rents, but it does require accommodation that is affordable for the majority of students. There is growing concern about the type and affordability of accommodation from existing students and local residents.

Targeting overseas students paying high rents for en-suite studios may have proven a successful approach in recent years but there is inevitably a limit to demand for these premium products in any one market, especially given current trends on overseas student numbers.

There is clearly an opportunity for the sector to reach into the mass market by developing appropriate types of accommodation (e.g. cluster flats rather than studios) at affordable prices (e.g. competing on total living costs including bills and shorter tenancy periods). However, viability remains a barrier to increased development in many markets, and so local authorities need to recognise the opportunities offered by purpose built accommodation through appropriate planning policies that allow developers to deliver appropriate and affordable student accommodation. ■

Words:
Neal Hudson

▼ Victoria Point, Manchester



OUTLOOK

Purpose built student accommodation remains a highly attractive asset

■ The UK is globally recognised for its higher education, and attracts large numbers of students from the UK and across the world. Overall student numbers look set to be broadly static for the 2016/17 academic year, but this will hide substantial variation in city and institution level trends.

■ The purpose built student accommodation market saw record-breaking investment in 2015 and remains a highly attractive asset. Although

investment is unlikely to hit last year's highs (£5.9bn) and Brexit remains a risk, we expect total investment in 2016 to hit £4bn, well above 2013-14 levels.

■ The challenge for investors is obtaining stock at a sufficient scale. With the majority of purpose built beds owned in small portfolios, we are likely to see further consolidation in the sector.

■ Increased investment appetite brings the risks of a shift to speculative

development in weaker markets. We advise caution as it is essential to understand local market dynamics and be selective in this increasingly competitive development market.

■ Provision of purpose built accommodation remains low in most markets and many students are reliant on HMOs. However, there are risks in developing too many premium schemes and a more affordable product offers the greatest potential for growth.

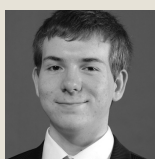
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