

MarketUpdate

European student housing market

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Summary

- When conditions are tough in traditional real estate investment markets, investors tend to look for 'attractive' alternative real estate sectors. One of these is student housing. However, European student housing has not yet been 'discovered' as a new and interesting opportunity. One of the causes might be its under-researched market characteristics.
- Knowledge is the key to prosperity and generally people are driven to invest in their own future. More than ever, students are willing to travel to search for the best university in their field. Even in the current economic downturn students are able to afford tertiary education, often supported by their parents.
- According to our analysis, the European student housing market is an attractive investment market. The student housing market is characterised by continuing strong demand and a clear lack of supply. Additionally, it is anti-cyclical, delivers secure rental income and often has an alternative use.
- Remarkably, yields on student housing are substantially higher than those on traditional housing. The additional risk premium is 1.5% on average.
- We believe that the inclusion of an additional premium is primarily due to the absence of a databank and the under-researched market characteristics. However, we expect the market to become more mature in time, which should diminish the premium. This might therefore be an interesting time to enter the student housing market.
- Due to the shift towards a modern, open and knowledge-based economy, the number of students worldwide has increased substantially over the last 30 years. This growth is expected to continue in the next decade.
- The total number of students in Europe will increase slightly, despite the ageing trend. The reason for this is the increasing number of foreign students, mainly from Asia. European cities that offer a good quality of life, have top universities with English language courses and relatively low tuition fees will especially enjoy continuous growth.
- Housing is a basic need for all students and in most European university cities there is a clear shortage of modern and affordable student rooms. In the coming years, new purpose-built student accommodation will come onto the market in response to strong demand. This can be seen as an opportunity to participate in a new and attractive investment category.
- Our top-down analysis demonstrates that attractive cities to invest in are cities that host top universities combined with generally tight residential market conditions. Examples are: Edinburgh, Munich, Mannheim, Paris and Utrecht.

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Student housing, an upcoming investment class?

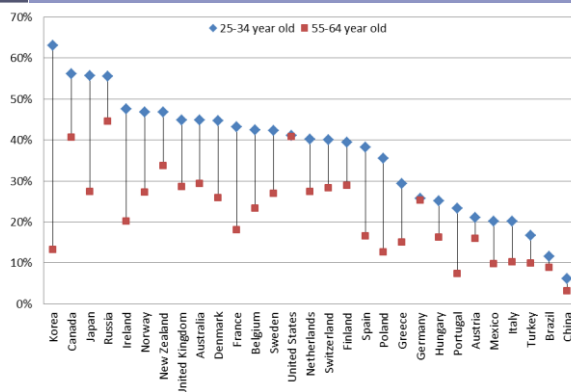
When conditions are tough in traditional real estate investment markets, investors tend to look for 'attractive' alternative real estate sectors. New and cash flow-oriented investment classes are clearly gaining the interest of institutional investors. According to INREV, institutional investors have substantially enlarged their new allocation to less traditional real estate sectors such as leisure, parking and healthcare. However, investments in European student housing, which can also be seen as one of these new sectors, remain rather underexposed, with the exception of the UK. One explanation might be that the investment market for student housing is rather opaque and under-researched. As we believe that investing in student housing has an attractive risk return profile, we are putting the spotlight on this 'new' real estate investment category in this update.

Increasing number of students

Worldwide, the number of students is increasing at a rapid pace. Over the last 30 years, more and more people have attained a tertiary education. This is not only the case in Europe, but also in Asia. As such countries as Korea and Japan are fast reducing their backlog (see Figure 1). The growth in student numbers is mainly caused by the worldwide shift towards an open knowledge economy. Generally, higher education improves people's prosperity (see Figure 2). Manual labour and basic skills can be outsourced to cheap labour countries or replicated by computers. Furthermore, the number of students has grown quickly because of ever-improving access to education in general. And finally, more women have been entering higher education throughout the past decade. In times of economic downturn, there is often a short-term rise in the number of students. This is caused by the anti-cyclical nature of student numbers. Students choose to study longer when job prospects are poor. During the economic downturn between 2009 and 2011, student numbers in the Netherlands increased by 5.5%. Changes to the regulatory system have also had an impact on student numbers. For example, in Germany the length of time pupils stay in high school has changed from nine to eight school years and as a consequence students start tertiary education one year earlier. This has had a one-off positive effect on the total number of students. The total number of students in Germany increased by 9.5% between 2009 and 2011.

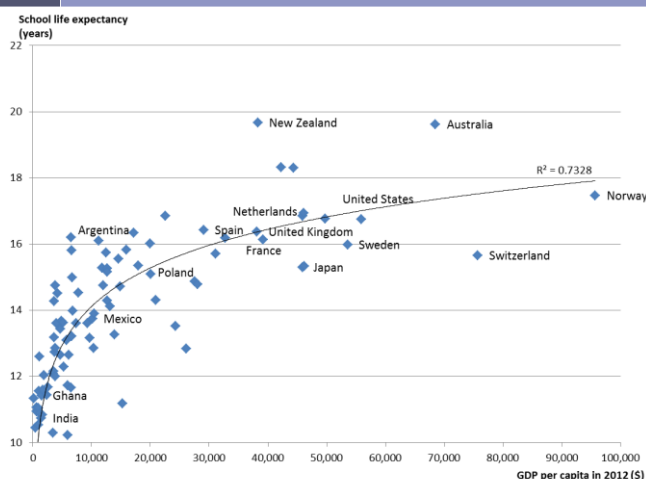
Students nowadays are also more willing to travel, since students with international experience are preferred by employers who see it as evidence of their self-reliance, entrepreneurship, etc. The number of students who choose to study outside their own country ('foreign students') more than quadrupled between 1975 and 2009. According to UNESCO data, 165 million students around the world participated in formal tertiary education in 2009, a growth of 65% since 2000. Figure 3 shows that the number of foreign students increased in the same period by 77% to 3.2 million and that Asian students represent almost 50% of foreign students enrolled worldwide. According to the OECD (Organisation for Economic Co-operation and Development), Europe received the most foreign students, around 40% of all foreign students worldwide studying in Europe in 2009. Within Europe, the United Kingdom (10%) received the most students followed by Germany (7%) and France (7%). The long-term trend of increased participation in tertiary education programmes and global mobility will continue. The OECD expects the global number of foreign students to double again from 3.2 million in 2009 to 7.6 million in 2025.

Figure 1: Percentage of people who have attained tertiary education



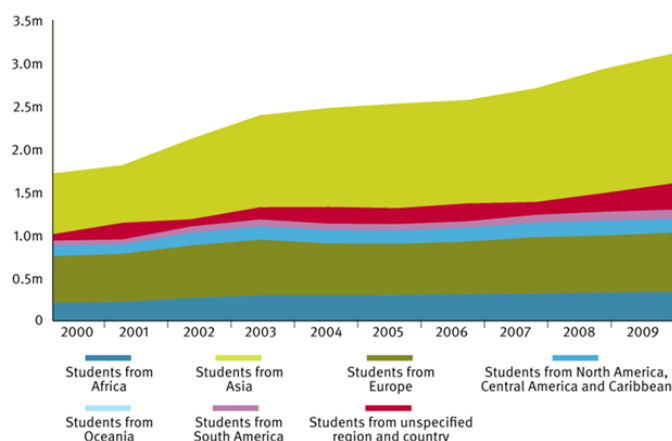
Source: OECD

Figure 2: Relation between education and prosperity



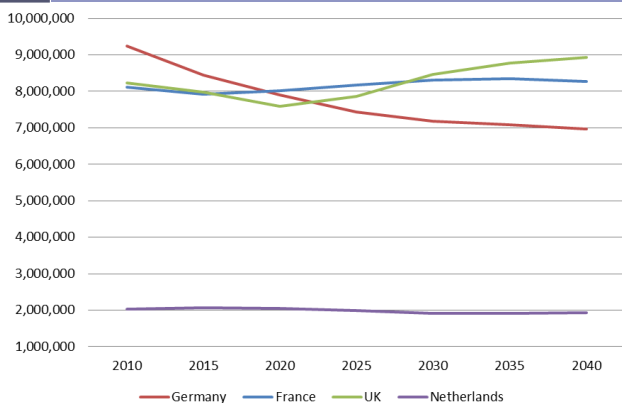
Source: Oxford Economics and UNESCO

Figure 3: Number of foreign students split by world region



Source: Knight Frank and UNESCO

Figure 4: Number of 15-25 year olds



Source: Eurostat

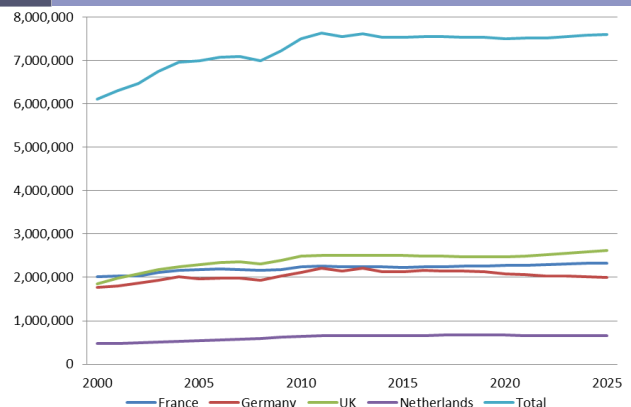
Domestic students in Europe

The total number of domestic students in European countries has grown rapidly since World War II. This trend is expected to level out in most countries, due to ageing and non-rejuvenation of the population. Looking at Germany, the UK, France and the Netherlands ('our researched countries') the number of 15-25 year olds will decrease the most in Germany in the next decade, followed by the UK and France. After 2020, the number of 15-25 year olds will further decline in Germany and the Netherlands, but increase in France and the UK.

The numbers in the figure above will undeniably have an impact on the number of domestic students. However, other aspects might compensate for these demographic changes. For example, Southern European students increasingly choose to study in Western Europe as a result of the uncertain economic outlook and unemployment in their home countries. This can be illustrated by recent figures of StudyPortals for the Netherlands: the interest shown by students from Greece, Spain and Italy in studying in the Netherlands has increased significantly in 2012. We also believe that more young people will opt for a tertiary education to secure their own future. Domestic and foreign students will, more than ever, be motivated to opt for the best universities at home or abroad to escape poverty and to improve their chances on the labour market.

Another factor is that the Bologna Process will make it easier for European students to study within Europe. At the start of this European reform programme in 1999, the aim was to create a single European Higher Education Area (EHEA) by 2010. The EHEA covers 47 European countries, in which students can choose from a wide range of high quality courses and profit from easy entry procedures. Ministers of the EHEA countries set the new agenda in 2009. One of the four main goals is to ensure that by 2020 at least 20% of those graduating in the EHEA have taken part in a study programme or training period abroad. At present, only 2% of EHEA students study abroad in the EHEA. However, there are variances between the different parts of Europe. According to Eurostat, Southern and Eastern European countries have more outbound students and Western European countries more inbound students. To illustrate this, almost 50% of EHEA students choose to study in the United Kingdom, Germany, France and the Netherlands.

Figure 5: Outlook in terms of total number of students



Source: Bouwfonds REIM Research

Foreign students in Europe

The total number of foreign students in Europe is expected to grow further. Germany and the UK will attract a lot of foreign students, especially from Asia. Given the uncertainties in Southern Europe, Germany in particular might be seen as the future 'banker of Europe' and attract more students than currently assumed. France will continue to benefit from French-speaking students, mainly from Africa. Overall, the number of foreign students in our researched countries will increase by 30% on average in the next decade.

Total number of students in Europe

Based on the expected demographic changes and the OECD outlook for foreign students, we have estimated that the total number of students in Germany, France, the Netherlands and the United Kingdom will increase slightly in the years to come (Figure 5).

Attractive European Student Housing regions

Although the total number of students across Europe will continue to grow, it does not mean that every European city will be faced with an increasing number of students. Other factors that also play an important role are:

- Top universities
- Languages provided (English/French) by universities
- Relatively low tuition fees
- Good quality of life

Many European countries fall within the top 15 most favoured destinations for students. According to the OECD, the UK, Germany and France all rank in the top 5 destinations for foreign students. Europe is not only home to a large number of the top universities worldwide, but also many of those universities offer English-language programmes with relatively low tuition fees. The cultural and historical aspects of European cities also make them an attractive destination for many foreign students.

Affordability

In order for an investor to secure rental income, it is important to consider the user's affordability. To determine the affordability of student housing, one has to take a closer look at students' sources of income and expenditure pattern.

Student sources of income

Sources of student income are self-earned income, public sources and funding from families. Students' average income differs greatly per country, with the United Kingdom having the highest average income by far (€1,500 per month, see also Figure 6).

The proportion of self-earned income is relatively high in France, while in the other three countries it is almost the same, namely around 25%. Dutch and UK students rely on public sources for nearly half of their income. Changes in governmental regulations would have a great effect on the income of Dutch and British students. In Germany and France, such an amendment would not have a large effect on students' income as their dependency on public sources is relatively low.

Families are another important source of income. German students rely on their family for around 50% of their income. In the three other countries, this percentage varies between 20% and 30%. Due to higher tuition fees and the fact that governments are moving from scholarships to loans, we expect that European students will rely more on their families in the future. Generally, families will support their children's education as much as possible, as it will offer their children a better start in a labour market that is more competitive than ever. Most families will also be able to support their children financially. Recent research by Eurostat shows that the financial position of European households is fairly healthy. Saving rates have remained remarkably stable over the last two years. In other words, despite the current economic situation, the financial power of students will remain -on average- relatively good.

Student expenditure pattern

Apart from student income, the affordability of student housing also depends on the cost of living. These costs can be split up into:

- Tuition fees and other study costs
- Rent
- Living expenses

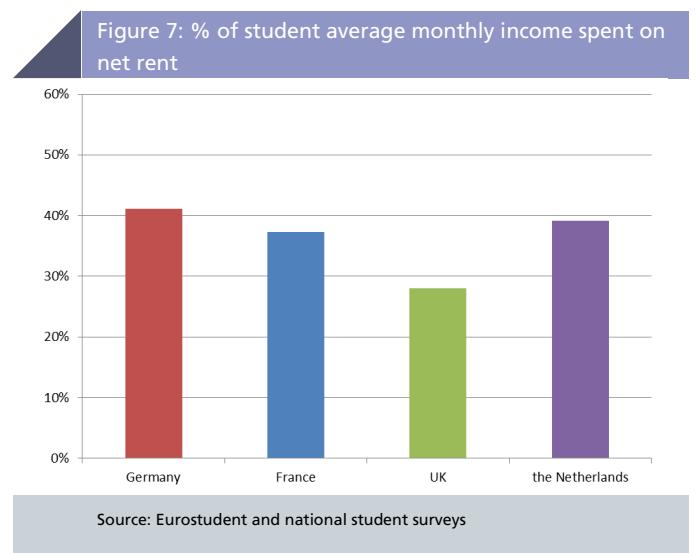
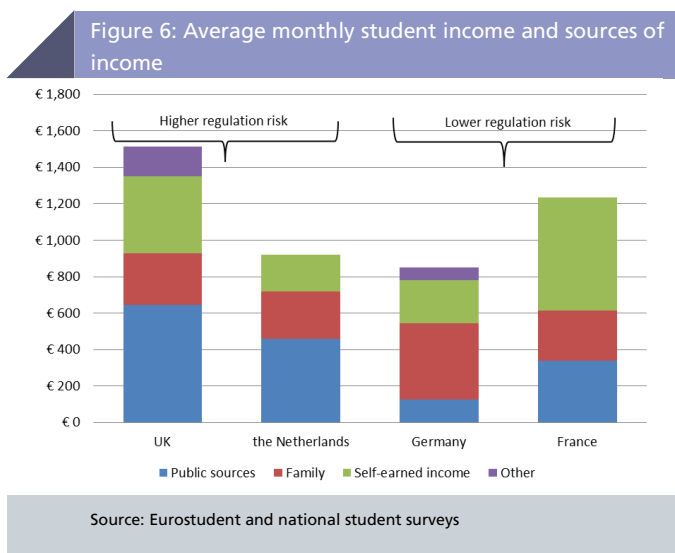
Tuition fees in Germany and France are the lowest. This offsets the lower student income from public sources in these countries. In the Netherlands and the United Kingdom, tuition fees are higher, ranging from 15% to 30% of monthly expenses. Tuition fees in the United Kingdom will rise significantly next year, but tuition fee loans will go up as well to cover these higher fees.

Students in Western Europe spend 30%-40% of their average monthly income on rent (see Figure 7 below). Those in the United Kingdom spend the lowest percentage. On average, students spend a higher percentage of their income on housing than conventional households do (25%-30%). This is explained by the fact that rent per square meter goes up when the rented unit becomes smaller.

Rents differ per city and within cities rents will also vary. In London, for example, rents are higher than in other parts of the United Kingdom. Students are compensated for this by being given higher loans and scholarships.

Tuition fees and rent can be seen as more 'fixed' costs, while living expenses are more 'variable' costs. If the first two rise, students could save money to a certain extent on their living expenses (such as sports, relaxation or communication costs). Living expenses in all countries make up the largest part of students' total expenses and range from 40% to 60%.

Overall, the average student studying in Europe seems to be able to pay their rent, often supported by their parents. Despite the fact that governments might cut back on scholarships, we expect this to hardly have an impact on affordability. Other sources of income (self-earned, parents, etc.) or loans are expected to compensate for this.



Supply of student housing

In a world of globalisation and mobilisation, housing remains a basic need for all students. In general, students can rent purpose-built student accommodation (owned by social housing corporations, universities or private/ institutional investors) or look for housing in the conventional housing market.

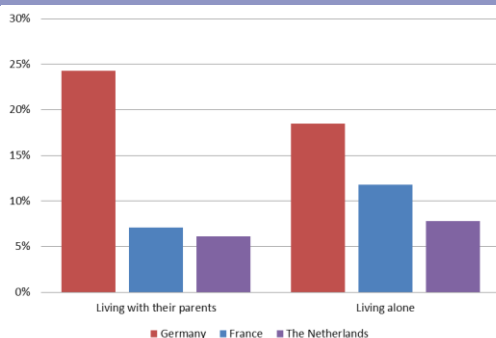
Many European university cities have huge shortages of high quality and affordable purpose-built student housing. Many top university cities have long waiting lists for suitable housing. It also appears that many domestic students live with their parents against their wishes. Their aim is to live independently, but they are unable to find suitable accommodation. According to Eurostudent, 24% of German students, 7% of French students and 6% of Dutch students live with their parents but would prefer to move out (see Figure 8).

Not only has quantitative demand for student housing increased in recent years, but so has qualitative demand. Most students want affordable accommodation within a short distance of the university, which is comfortable and reasonably close to leisure activities. There is a clear qualitative shortage of this in most university cities, especially in cities that offer a high quality of life combined with a tight residential market. Most of the existing student rooms in these cities are too small, too old and uncomfortable.

There is clearly a huge shortage of modern, high quality student housing. The gap between demand and supply occurs especially in the larger cities that are home to top universities where the residential market is tight. This implies that in these cities, the risk of vacancies in student housing is negligible.

It is expected that in the coming years, new student housing supply will enter the market, mainly developed by non-governmental parties. Universities are more and more subject to benchmarking and are selected if they are considered to provide the best education. They need to focus more on their core business, and have less scope for paying attention to student housing.

Figure 8: Dissatisfied about their housing situation



Source: Eurostudent

Student Housing shortage

Germany

In Germany, around 225,000 subsidised student rooms are available for around 2.2 million students. There is only very limited purpose-built student accommodation developed by private owners. This means that almost 90% of all students have to rent on the conventional housing market if they cannot or do not wish to live with their parents. Only around 8% of the total housing stock comprises single or double room apartments, which is rather limited. Students have to compete with other single-person households and starters on the job market who are able to afford higher rents.

United Kingdom

UCAS data shows that the demand for university places has been about 20% higher than the number of accepted applicants in past years. Unite Group, the biggest market player for student housing, expects that this will also be the case in the coming years. According to Knight Frank, there is a structural undersupply of student rooms in the UK. Recent planning changes have made student housing development more difficult. The most attractive student cities to invest in have the most limited development pipeline.

France

Almost half of the two million domestic students live with their parents. This number is relatively large and may therefore indicate that there is a shortage in affordable student housing in France. This is confirmed by Savills, who estimates that there are only around 340,000 student rooms in France. In addition, around 1.5 million students wish to live independently. The current development pipeline contains around 25,000 rooms for the next five years. This is a significant increase, but insufficient to meet future demand. The government has plans to launch a Campus Plan, which has a target of 680,000 student rooms by 2020.

The Netherlands

Despite the growth in the number of students, waiting lists have stabilised. The percentage of students living away from home compared to the total number of students has also stabilised (at around 60%). This indicates that a growing percentage of students are able to find alternative accommodation outside regulated and/or specially constructed student housing or have given up hope. Waiting lists are still quite long. Waiting lists in Amsterdam, Utrecht and Leiden vary between 12 and 20 months. According to Savills, 80,000 new student rooms are needed to meet expected demand up to 2020.

The most attractive cities to invest in

The attractiveness of investing in European student housing depends on the regional residential market in which the property is located. Looking at the general European residential market, the regional differences in demand for housing will increase further. There will be ‘winning’ regions and ‘losing’ regions. In regions where the number of households will grow, demand for housing will remain high. In regions with a contracting number of households and an ageing population, demand for housing will decrease.

We have already analysed the more and less attractive European regions for investment in residential property for our existing residential funds. We conducted a top-down analysis based on demand factors for the next five years (2012-2017). Factors that were taken into account were growth in households, number of households, population density, ageing, size of the economy, growth in employment and regional clustering of important economic sectors. The outcome is an overview of European regions divided into seven categories, ranging from A1 regions (most attractive) to D2 regions (less attractive).

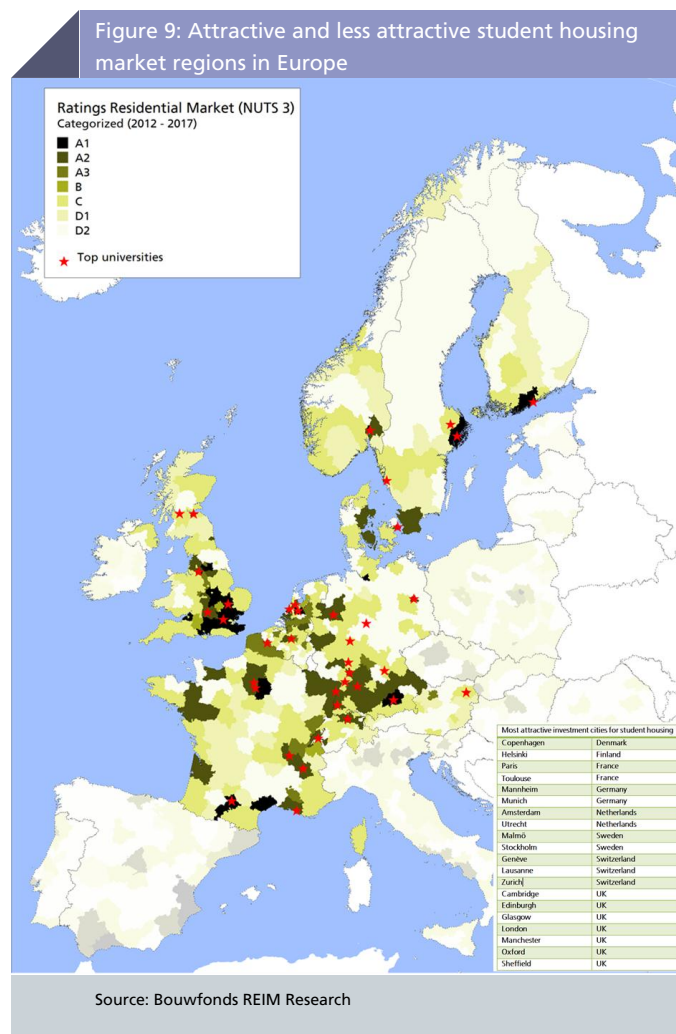
However, for student housing, not only will the factors mentioned above play an important role but also the differences between top and regional university areas. Cities that are home to top universities will attract more students (including foreign students) and will therefore be the winners of tomorrow. The most attractive cities in which to invest in student housing are therefore those regions with both an attractive residential investment market and those that host a top university.

For that reason, in addition to our existing residential top-down analysis, we created an European top university list based on the scaled rankings of:

- QS World University Ranking
- The Times Higher Education Ranking
- Academic Ranking of World Universities

The result of combining these two analyses is an initial list of global excellence cities with an attractive student housing investment market (see Figure 9). These cities not only host a top 50 university, they also rank A1 or A2. According to this list, European capital cities in particular offer good investment opportunities for student housing. Other examples are Edinburgh, Munich, Mannheim, Toulouse and Utrecht. There seem to be relatively many UK cities in the list, mainly because many UK universities are in the top 50 European rank.

We would like to emphasize that our attractiveness analysis is a demand analysis based on demographic and economic variables and university rankings. The supply side is not yet included because it is difficult to get hold of comparable data at local level. Data on student housing numbers, type and quality is not easy to find and the quality of the data is not always reliable. In general, an attractive region will offer more opportunities (with sufficient exit possibilities). Having said that, a bottom-up investment analysis has to be made of all regions on the basis of the local situation with regard to future demand and supply characteristics. Based on our own residential investment experience, additional cities, such as Marburg or Karlsruhe also appear to be interesting for investing in student housing. Consequently, this top-down analysis is only intended as a first step for determining which regions have the most and best investment opportunities for student housing.

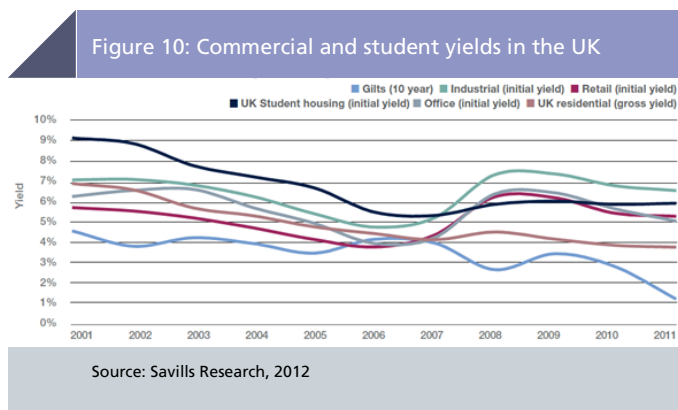


European student housing as a future asset class?

According to our analysis, market conditions for the Western European student housing market are relatively sound (increasing number of students, good affordability and a lack of supply). In this part, we take a closer look at investment characteristics such as market liquidity, cash flow and risk. In this context, we looked at the UK in particular, since UK student housing is already an established investment class.

Returns

According to Savills, the initial yield for student housing in the UK is 6.3% on average versus around 4% for conventional residential properties (see Figure 10). Our own investment experience also suggests that yields for student housing are higher (1.5% on average) in comparison to residential yields in general. The question is whether this additional risk premium for student housing investments can be explained by the illiquidity of the market and/or a higher risk profile.



Size

Making some basic assumptions, it appears that around 5.6 million students are looking for a room in our researched countries. Based on recent transactions and the current supply of student accommodation in this area, the average value of each student room is around €45,000, which puts the estimated total investment volume at around €252 billion. Unfortunately there is insufficient data about ownership structures of student housing. The estimated total investment volume of €252 billion also includes social/public student housing and private student housing owned by private investors. The size of the European student housing market for institutional investors will therefore be smaller, but still quite sizeable.

Figure 11: Estimation of the investible student housing market

	Number of students looking for a room	Investment volume (€bn)
Germany	1.8 mln	81.0
France	1.5 mln	67.5
United Kingdom	1.8 mln	81.0
The Netherlands	0.5 mln	22.5
Total	5.6 mln	252.0

Source: Bouwfonds REIM Research

Cash Flow

Because students regularly rent for a shorter period there are more occasions when rents can be adjusted, in comparison to conventional residential accommodation. Because of the shortage in supply, this offers opportunities to frequently raise rents. Furthermore, the rent paid by a student is often supplemented up by the parents who act as financial guarantors. This reduces the risk of bad debts.

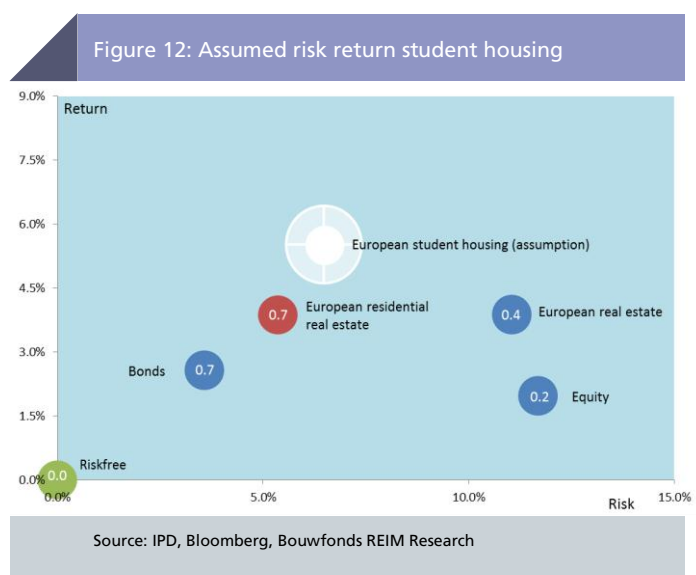
On the other hand, one could argue that investing in student housing implies additional and higher political risks which might partly offset the positive aspects above. However, conventional residential markets are also highly regulated by politics (as recently illustrated by the new government led by François Hollande in France). From that point of view, it does not explain the huge gap between conventional housing investments and investments in student housing.

Finally, most student buildings are located in the stronger residential markets. Often, there is redevelopment potential (into single family homes) which offers an alternative exit strategy. This will firm up capital value growth in the longer term.

Anti-cyclical

In times of economic downturn, there is often a short-term rise in the number of domestic students. This is caused by the anti-cyclical nature of student numbers. Students choose to study longer when job prospects are negative. The student housing market follows its own pattern and we therefore assume that investments in student housing are less volatile and have a relatively low correlation to other asset classes. Unfortunately, we do not have a databank to sufficiently test this assumption. This absence of data and the immaturity of this investment category could be the main explanation for the inclusion of the higher risk premium.

If, as we expect, the student housing market gains the interest of investors, we believe that the market will become mature and more transparent in time. And assuming this, downward pressure on required yields can be expected as well.



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