UK Student Housing
MarketView

Q3 2013

CBRE Global Research and Consulting

Q3 STUDENT TRANSACTIONS £607.7m | INVESTMENT £602.7m | DEVELOPMENT £5m | REGIONS £497.7m | LONDON £110m

MANY HAPPY TOTAL RETURNS: SIGNS OF A MATURING MARKET?

Q3 Highlights:

- Sales agreed on 12,800 Opal bedspaces, with portfolios going to overseas buyers

- CBRE Student Housing Index shows national rental growth of 3.24% and total returns of 9.95%

- Total returns for student property outperforms the IPD all property index for third year running

- October UCAS figures suggest that nationally applications are back above 2010 levels

"During 2013, the government has shown strong support for Higher Education by introducing several key policy initiatives. Applications have recovered this year, and the sector has once again shown strong total returns, buoyed by continued rental growth and improved investor sentiment in key towns." Paul Savitz, CBRE

"The depth of demand for the Opal properties has surprised the market, and indicates the desire from investors to enter the market at scale. In spite of some risk factors, liquidity seems much improved in the student housing market. Now is an excellent climate in which to bring portfolios or single assets to the market, or for long term investors to benefit from further growth potential." Jo Winchester, CBRE

What is the government doing in support of Higher Education?

A combination of higher tuition fees being introduced in England and Wales, issues in A-level marking, a reduction in the deferral rate and confusion over visas, led to a reduced intake of students into Higher Education in 2012.

However, the government acknowledges the importance of the sector. Total UK education exports were estimated to be £17.5bn in 2011, making education the fifth largest services export sector in the UK, ahead of insurance services. In 2011/12, overseas students paid an estimated £3.9bn (net of scholarships) in tuition fees, and a further £6.3bn in living expenses, and it is anticipated that numbers of international students in UK higher education could grow by 15-20% in the next five years.

In 2013, the government has shown their support of the Higher Education sector with some key policy initiatives. To ensure the UK captures this growing demand, the government has reformed the visa system, and confirmed that there is no intention to impose any cap on the number of students who can come to study in the UK.

Other policies included:

• No restrictions on ABB students. Last year the cut off was AAB, but due to harsher A-Level marking the pool of these was reduced leading to a reduced intake.

• Penalties for over-recruitment have been relaxed. Universities will now be permitted to over-recruit by 3% without financial penalty.

• Up to 5,000 additional places to be made available nationally, to be allocated flexibly.

There is strong government support of the sector in policy, if perhaps not financial, form. With intensifying competition from other countries for English-taught degrees, this will help to maintain the UK's status on the world higher education stage.

All Property Update

Q3 2013		Trending
Total Return	7.40%	Stronger
Initial Yield	6.00%	Stronger
Capital Growth	0.90%	Stronger
E.R.V.	0.40%	Stronger
CBRE Index	6.60%	Stable

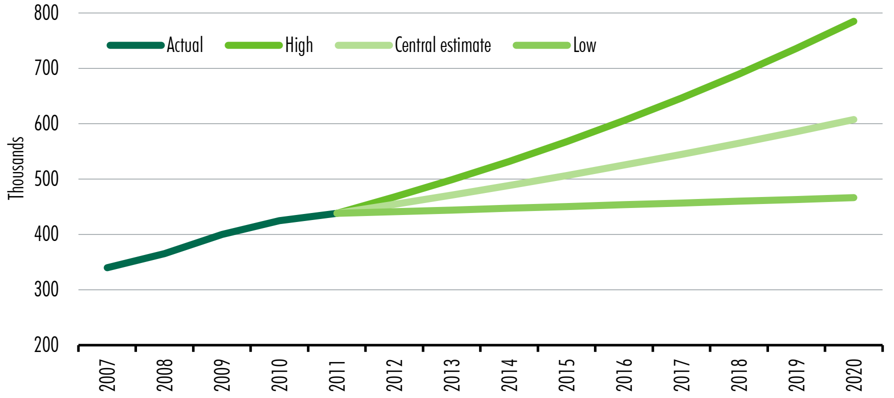
Student Housing Yields

Q3 2013 - Direct Let		Trending
London Zone 1	6.00%	Stronger
London Zones 2-4	6.25%	Stronger
Super Prime Regional	6.25%	Stronger
Prime Regional	6.50%	Stronger
Secondary Regional	7.25%	Stable

Q3 2013 – Uni Lease		Trending
London Zone 1	5.00%	Stronger
London Zones 2-4	5.25%	Stronger
Super Prime Regional	5.00%	Stronger
Prime Regional	5.25%	Stronger
Secondary Regional	5.75%	Stronger

Source: CBRE

Chart 1. Projected growth in international student enrolment in the UK



Source: HESA, BIS calculations 2013

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HOW HAS THE SECTOR PERFORMED IN 2013?

The latest October 2013 UCAS data suggests that nationally applications are back above 2010 levels, and that the system is still heavily oversubscribed, irrespective of a falling younger population. Encouragingly for universities and student housing operators alike, the number of international applicants is up by 10% on the previous year's cycle.

However, UCAS have not yet published application data per university so the impact on the student population, and hence the distribution between individual towns is not yet clear.

Following the two abnormal years (high intake in 2011 and abnormally low in 2012) the main operators are now all reporting high occupancy levels in core towns.

According to the CBRE Student Housing Index, which measures performance for the year to September annually, regional towns have shown average rental growth of 3.51% for 2012/13. This is compared with a 3 year average of 3.36%, albeit with quite wide variations between towns.

London's rental growth was flat this year, at 0.61%. This was to be expected after an increase in stock and end of cycle rental reductions in 2012. However, London has shown 3 year rental growth of over 20%.

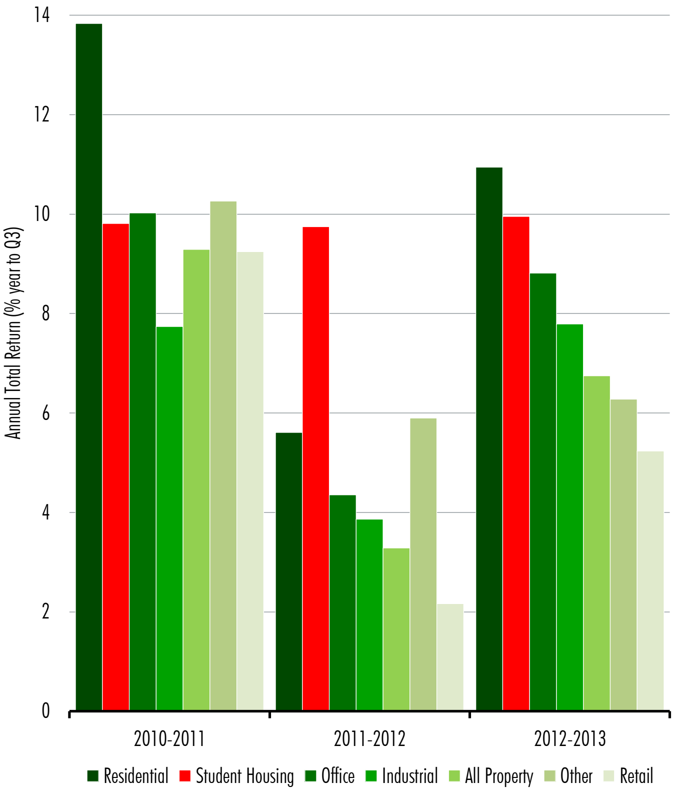
London continues to attract the most overseas students. However, after the completion of those beds already under construction, the London supply pipeline will be more restricted going forward. The introduction of CIL, tighter planning policies, a selective funding climate, the tendency for universities to seek to transfer risk onto the private sector and the recovery of other property sectors, are all pipeline inhibiting factors. The combined effect is likely to be that rental growth and values of existing stock holds up.

The CBRE Student Housing Index has shown total returns of 9.95% between September 2012 and September 2013, outperforming the IPD All Property Index for the 3rd year running. This has been the effect of rental growth and some yield compression in better towns.

Total returns have been supported by strong capital value growth, especially in regional towns and cities. The CBRE Student Housing Index shows the average value per bed has increased from £50,700 in 2009/10 to £56,600 in 2012/13, an increase of nearly 12%.

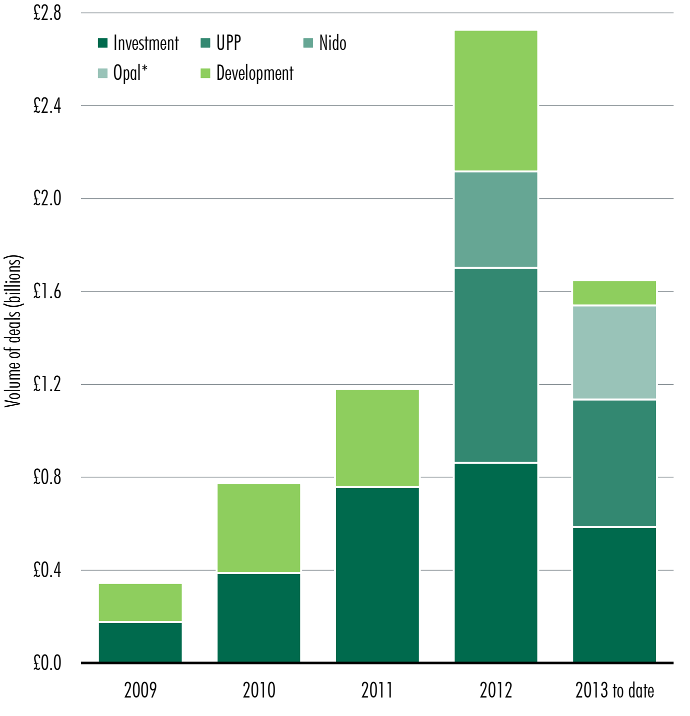
This has been partly a result of investment into, and the development of, higher quality purpose built accommodation in regional towns and cities. For the second year running, investment into the regions has reached £1.5bn, with developers, investors and operators seeing growth potential outside of London, where limited stock is available to purchase.

Chart 2. Total Returns (Direct Let)



Source: CBRE, IPD

Chart 3. Total Capital Investment



Source: CBRE (*Greystar and Avenue Capital deals only)

THE UK STUDENT INVESTMENT MARKET

What do the sales of Opal portfolios tell us about the investment market?

The biggest sector news of 2013 has undoubtedly been the agreed sales of over 12,800 beds owned by Opal. Previously the UK's 3rd largest operator, Opal was placed into administration in Q1 2013 due to well-documented debt issues.

After initial fears of surplus investment product and the potential for discounted prices, the depth of interest in these portfolios has surprised the market. The implications are far reaching.

Firstly, it is clear the UK student housing market is now viewed as a global haven for international capital. The first three portfolios have all gone to overseas buyers – Greystar (a US multi-family and student housing operator), Avenue Capital (New York Private Equity) and Campus Living (an Australian operator) who have overbid numerous UK operators and other investors. The attraction has been the opportunity to reposition some underinvested assets, to enter the market at scale and the scope for further rental growth. Another factor is the generally favourable commercial and regulatory climate in the UK, compared to other jurisdictions.

Secondly, the competitive tension around these deals, with numerous serious bidders, has meant that the pricing has been robust. Prices for the better regional towns can be analysed to show 6.75-7.00%, and 6.25% for a large London direct property, which bearing in mind the age, condition, scale and leasehold tenure of some of the assets tends to support our prime regional yield of 6.50% and 6.00% in London.

The strength of appetite confirms there is increased liquidity for some potentially difficult assets, such as regional schemes of nearly 1,000 beds, and large assets with sub-95 year leaseholds. There are also numerous unsatisfied bidders still looking to enter the market.

Thirdly, although it has taken portfolio opportunities to entice international investors in, the increased number of buyers should mean an improved market for single assets and portfolios. Avenue Capital have already purchased Trinity Square, Nottingham, the last of the Beach Fund properties, for example.

Arguably there has never been a better time to bring portfolios or single assets to the market, especially in London, where there are so few opportunities to buy.

What are the implications of fund suspensions?

Readers will be aware of the recent suspension of two student housing funds, which were reportedly due to regulatory and fund governance issues. Concerns over the outcome of Opal may also have been a factor, although in the event, the anticipated 'hangover' of property has not been an issue. The main point to note is that the suspensions were not primarily a result of the underlying letting business, or a reflection of the health of the sector in general. However, if properties from the funds do need to be sold, it would seem the market conditions are favourable.

This year has also seen the launch of the first dedicated student housing REIT, GCP Student Living Plc, on the London Stock Exchange, offering a possible alternative route to investment for smaller investors. REIT structures have very clear governance and reporting procedures.

Operators: Tomorrow's investment potential?

The growing scale of 3rd party operators such as CRM, Touchstone, Fresh Student Living and AC Collegiate, is a strong indication of a maturing market with new entrants requiring their services. The collapse of Opal into administration has been an additional factor.

The most important trend is that growing operational platforms, and existing investment portfolios, represent tomorrow's investment opportunities. This is especially so for platforms backed by a development pipeline offering the ability to add scale with brand new assets (page 4). It is relatively easy to obtain debt on operational portfolios, and operational branding and track record is increasingly important to investors and lenders.

When it comes to investment in operational platforms the experience of the Opal portfolio sales suggests that scale is the pre-requisite factor, followed by the ability to demonstrate consistent occupancy and returns. 100% prime asset quality does not appear to be a pre-requisite, provided that the letting story is good and the quality is reflected in appropriate pricing or valuation.

Student Housing Investment Vehicles	Beds (including pipeline)
UPP Ltd	29,967
USAF	22,475
Liberty Living	16,827
Knightsbridge/Oaktree	8,090
Greystar/Goldman Sachs	6,502
Mansion Student Accommodation Fund	5,500
IQ Fund (Wellcome Trust/Quintain)	5,172
The Cordea Savills Student Hall Fund	2,900
Round Hill/Nido	2,526
Avenue Capital	2,400
Carlyle/Generation Estates	2,196
The Ahli UK Student Housing Fund	1,608
LSAV	1,287
Gravis Capital Partners (Scape)	588
Mansion PAIF	477
Total	108,515

Source: CBRE

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OPERATORS, RISK FACTORS AND MARKET OUTLOOK

Operators league table:

Operator Brands	Beds	Pipeline
Unite Group Plc (including USAF)	42,000	4,794
UPP	27,317	2,650
CRM (includes Opal)	19,921	7,242
Liberty Living	16,827	0
Sanctuary Management Services	13,638	267
MSAF/Mansion	9,000	390
Victoria Halls (including third party)	7,291	0
Unipol (halls only)	6,431	0
IQ	5,172	0
Fresh Student Living	4,234	3,115
Touchstone	4,166	0
Derwent	4,000	0
Campus Living Villages (excludes Opal)	3,821	2,563
The Student Housing Co (as operator)	3,789	3,589
South Street	2,801	1,391
Nido	2,526	0
MCR	2,509	0
Viridian	2,312	0
AC Collegiate	2,000	2,800
Student Castle	1,773	0
Urbanest	1,066	1,400
Prime Student Living (Crosslane)	1,051	1,969
Pure Student Living	974	1,222
Downing Developments	785	4,239
Scape Student Living	740	1,081
Total	186,144	38,712

Source: CBRE

In a sector with such strong underlying dynamics and current sentiment, there are the following key risks. Within the context of a robust market the following trends could potentially impact on performance or demand.

Risk	Impact	Risk Level
Rising cost of a degree	The full impact of higher tuition fees on the distribution of students is not yet fully known. Students may choose to study in their home town avoiding the need for accommodation. Students may also choose to avoid higher cost towns and cities, such as London.	Moderate risk which could impact demand from domestic student cohort in some towns.
Disparities in running cost models are an issue in liquidity	• There is a lack of a standard model or industry benchmarks as to running costs. • There is a lack of clarity as to how longer term capex requirements, management charges and VAT in particular should be reflected. • There are disparities between the low cost base of larger operators, and the higher costs of 3rd party operators, upon whom some purchasers rely.	Different costs models are an increasingly common problem in transactions. Rising actual costs are also a risk to overall asset performance for longer term investors.
Rising energy prices	Energy prices can represent up to a 1/3 of asset level costs. Average household fuel bills are forecast by DECC to increase by around 18% in real terms between 2010 and 2020, 60% of the increase will be policy related.	Low to moderate impact on rental performance.

Market Outlook

- Portfolio sales can be analysed to confirm our opinion of prime regional yields at 6.5% and prime central London direct let properties at 6%. Other sales have shown that a handful of 'super-prime' regional towns could achieve 6.25%.
- With the increased number of buyers, there is scope for further yield compression in strong locations.
- Operational platforms and existing investment portfolios will be an increasingly attractive route to market, but decent operational scale and a consistent track record of high occupancy and returns, will be pre-requisites.
- Arguably, there has never been better sentiment in the UK student housing sector.

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INTO, Newcastle University Halls

UK Development and Investment Highlights

Athena Portfolio. Greystar (a US multi-family and student housing operator), purchased the RBS/E&Y led sale of 6,502 bedspaces across 15 student schemes in Manchester, Leeds, Liverpool, Huddersfield, Bradford, Wolverhampton, Leicester, London and Dundee. The former Opal portfolio deal also included six PRS schemes and two commercial units.

The portfolio is believed to have sold for circa £310m. The deal can be analysed to show an estimated yield of circa 7% for the 14 regional assets and c6.25% for the 704 bed (93 year leasehold) Tufnell Park scheme.

The Avenue Capital (1,796 beds) and Campus Living (4,539 beds) Opal portfolio purchases both fall within our Q4 sector analysis.

L&G. Legal & General Property has recently acquired two new student accommodation schemes, bringing the group's total commitment to the sector to nearly £750 million. The deals, one of which is backed by Aberystwyth University and another let to Newcastle University, are for a total consideration of £130 million. The two deals represent L&G's sixth and seventh major university-backed acquisitions.

The £86 million Newcastle purchase reflects a blended net initial yield of c.5% and is let to INTO Newcastle University on two 35-year leases from October 2012. The development comprises 534 student rooms in total, while the investment also includes 40,000 sq ft of bespoke, high specification teaching space.

The blocks occupy highly prominent locations at the front of the University of Newcastle's campus and currently represent its only on-campus accommodation. The highly sustainable properties were developed in 2011 and reached practical completion in July 2012.

The second in Aberystwyth is a new 1,000-bed, 23-block development, let to Aberystwyth University for 35 years from completion, for a total consideration of just over £43m, purchase reflects a NIY of c.5%.

Work on site commenced in March 2013 and is scheduled to complete by December 2014. The lease will have the benefit of annual rent reviews linked to RPI.

Unite, Holloway Road

UK Planning Highlights

Chester. Developer Watkin Jones gained planning permission early in July for the development of 394 student rooms on the former Chester City Transport bus depot in Crewe Street. The approved £20m scheme will comprise five blocks between three and six storeys in height. The Kelsey Design Associates-designed scheme is expected to complete for Summer 2015.

Bloomsbury. Permission has been granted for UPP's £120m development in Cartwright Gardens, WC1. The approved plans for the redevelopment of the existing 700 bed Garden Hall accommodation will be replaced by 1,200 beds and will be used by University of London students.

Norwich/Stratford. Alumno Developments have gained consent for a 228 bed scheme, of up to nine storeys, in Norwich city centre. The £16m Carson & Partners-designed All Saints Green development is adjacent to the city's bus station. The project is due for completion in September 2015. Alumno Developments have also lodged plans for a 26 storey tower comprising 431 beds in Stratford, to be managed by Derwent Living.

York. A £35m mixed-use redevelopment of the York Press offices has been given planning consent. The S Harrison Developments scheme, on 2 acres of brownfield land will include new offices, as well as 58 student beds and 303 studio flats. The flats will be owned by student housing group Student Castle and is expected to complete by September 2015.

Kings Cross. The Aga Khan Development Network has secured planning consent for a 198-bed scheme at King's Cross Central, N1. The Stanton Williams-designed 12-storey building on plot T5 at the 67-acre site, was backed unanimously by Camden council and is expected to be delivered in 2015.

Holloway/Wembley. Unite has submitted plans for a 991-bed scheme at 263-289 Holloway Road, which will range from six to 14 storeys. The PLB-designed scheme is scheduled to complete for the September 2016 academic year, subject to planning consent from Islington council. In addition, Unite have bought a 1 acre site in Wembley for £7.4m. Subject to planning consent for 700 beds, it has an estimated total development cost of £47m and is projected to deliver a 9% development yield and is targeted to open in 2016.

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This report was prepared by the CBRE UK Residential Research Team which forms part of CBRE Global Research and Consulting – a network of preeminent researchers and consultants who collaborate to provide real estate market research, econometric forecasting and consulting solutions to real estate investors and occupiers around the globe.

Yields

The Net Initial Yield, which is growth implicit, rather than the Equivalent Yield, is the key driver in this sector. Allowance for purchaser's costs of 5.8% is made in calculating the Net Initial Yield. All the yields assume properties completed within the last 5 years and stabilised, and ignore any forward funding discount. Yields assume a generic lot size of £35m.

Direct Let: Well located modern purpose built properties with a strong track record.

University Lease: Well located property on a Lease to a well regarded university, with a strong covenant strength and at least 20 years unexpired, with annual RPI uplifts on FRI basis.

Super Prime Regional: Mostly historic towns with restricted supply (Oxford and Cambridge)

Prime Regional: Mature markets with healthy supply / demand ratio and more than 1 university. Examples would include Newcastle, Aberdeen, Southampton

Secondary Regional: Towns with possible over-supply issues, newly formed universities etc.

CBRE's Student Housing Index is based on regular valuations carried out for clients by CBRE. 26,500 mostly direct let bedspaces are included in the index, with a total capital value of around £1.7 billion. 80% of the index is in regional towns, and 23 towns are represented. The index is calculated annually in September.

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