European Commercial – December 2021

SPOTLIGHT
Savills Research

European Student Housing: Forever Young

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● The pandemic paradox effect ● Reversal demographic trends ● Strong investment activity

Positive counter-effect of the pandemic on student numbers

Student numbers increased significantly last year (2020-2021) in most European countries. On average across the countries shown in graph 1, student numbers increased by 2.4% compared to the previous academic year (pre-Covid), whilst they decreased by 1.2% between 2018-19 and 2019-20. In some cities, student numbers evolved particularly sharply and in opposite directions, ranging from 9% in Gothenburg and 7% in Malmo to -10% in Rome, -4.4% in Barcelona.

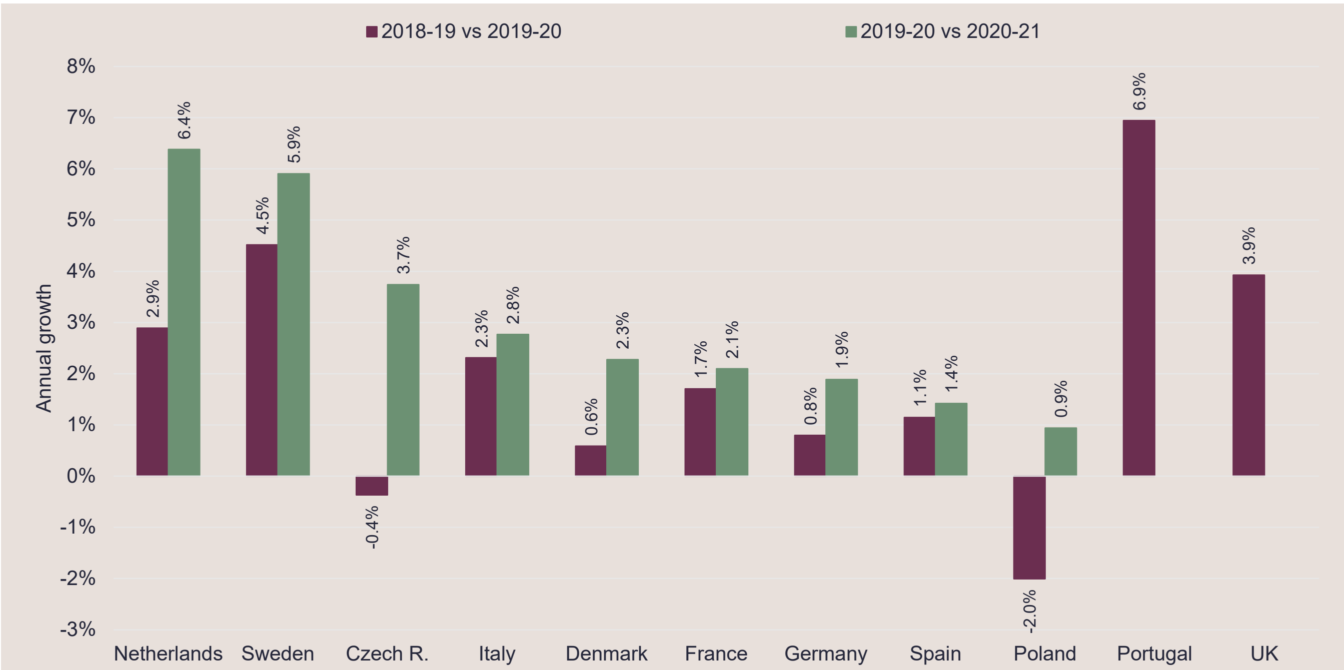
Paradoxically, part of this increase can be linked to the pandemic, for three reasons. Firstly, because in some countries (e.g. France, Denmark, Netherlands), there was greater leniency than usual in respect of higher education entry tests and grading of exams. Given the difficulty to attend classes or exams during lockdowns, some ministries of education decided to lower the grade which grants access to universities. Secondly, due to the tight labour market, scarce job opportunities, especially amongst young people, did not provide the usual alternative to the education path. Indeed, historical data shows a strong correlation between rising student numbers and falling employment rates. Finally, sabbatical plans were limited due to travel restrictions.

Overall, the growth of domestic students is attributable to both an increased number of first time students and longer courses. Nevertheless, in some countries such as Germany, the number of first-year students slightly decreased. This means that the rising total student number is strictly linked to existing students deciding to prolong their time at university and to delay their entry into the labour market.

With international student mobility particularly impacted by the pandemic, the real surprise came from foreign applications. In several countries, the number of international students increased last year, including in the Netherlands, (+11%), Czech Republic (+8.1%), Italy (+5.5%), Poland (+3%) and Germany (+1.1%). In total across the seven countries which have released their 2020-21 student figures, the number of international students rose by 2%.

Following the first wave of lockdowns, some surveys suggested students were reconsidering their study plans abroad. Yet, with the massive adoption of e-learning, many

Graph 1: Total student numbers



Source: Savills Research

European Student Housing: Forever Young

European universities, have been able to retain their international appeal. Since students could not attend classes even in their home countries, it did not make sense for them to change their long term university plans.

Online education has come a long way in a short space of time and has proven to be extremely useful. We expect to see the continued proliferation of e-learning solutions in the future, which will provide universities with some competitive advantage to attract international audiences. Yet, we do not see this trend as a threat to the PBSA market. From a student perspective, distance learning turned out to be a poor substitute for the sociable, in-person learning experience. For many international students, acquiring foreign language skills is part of their study plan abroad, which can only really be achieved by living and studying in the chosen country. We believe virtual learning will complement the in-person class experience and offer students who cannot leave their homes the ability to graduate from their chosen university.

Overall, we expect international student growth to be back to pre-pandemic levels from next year. According to UNESCO, in 2020, Europe contained five of the top 10 student destinations in the world. (UK, France, Russia, Germany and Spain). Additionally, Europe has benefited from an effective vaccine roll out, resulting in borders being reopened and quarantine restrictions largely ending. However, within Europe, the distribution of international students is expected to change in the coming years due to Brexit and the consequent Erasmus+ exit by the UK (Europe and Erasmus+ program)

Europe and the Erasmus+ programme

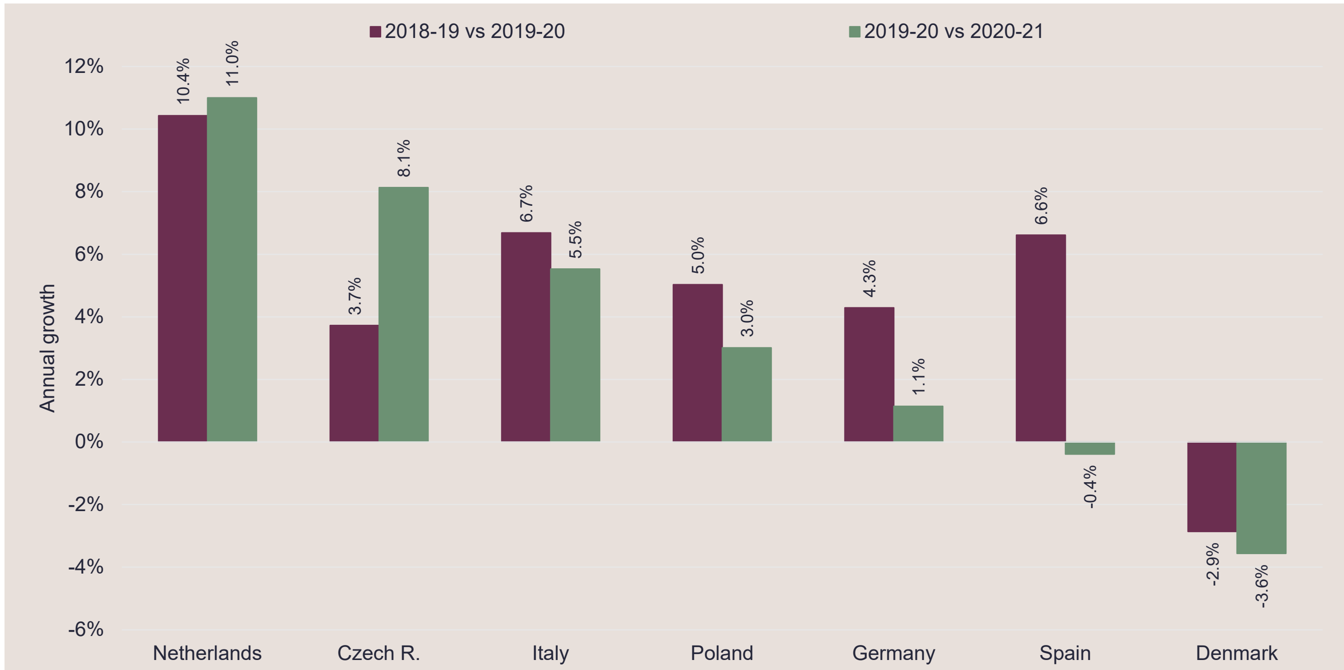
A significant driver of student mobility in Europe is the Erasmus+ programme. About 10 million individuals, including students, professors, and trainers in all sectors, are expected to participate in mobility activities abroad between 2021 and 2027, according to the European Commission.

The UK was historically the fourth most popular destination for Erasmus+ students; however, the UK was only the seventh biggest source of Erasmus+ students (see chart below), so for European universities, the loss of UK students will likely be less than the number of European students they will gain.

For those who would have gone to the UK to study, they may now be looking for programmes taught in English elsewhere to replace the experiences and language exposure they would have had in the UK. European countries with the highest number of English-taught bachelor's (ETB) programmes that look set to benefit the most from the UK's withdrawal from the Erasmus programme are The Netherlands, Spain, and Germany, each with over 200 ETBs. This in turn will further underpin demand for student accommodation in these destinations.

Extract from the Savills Global Living Report - October 2021

Graph 2: International students



Source: Savills Research

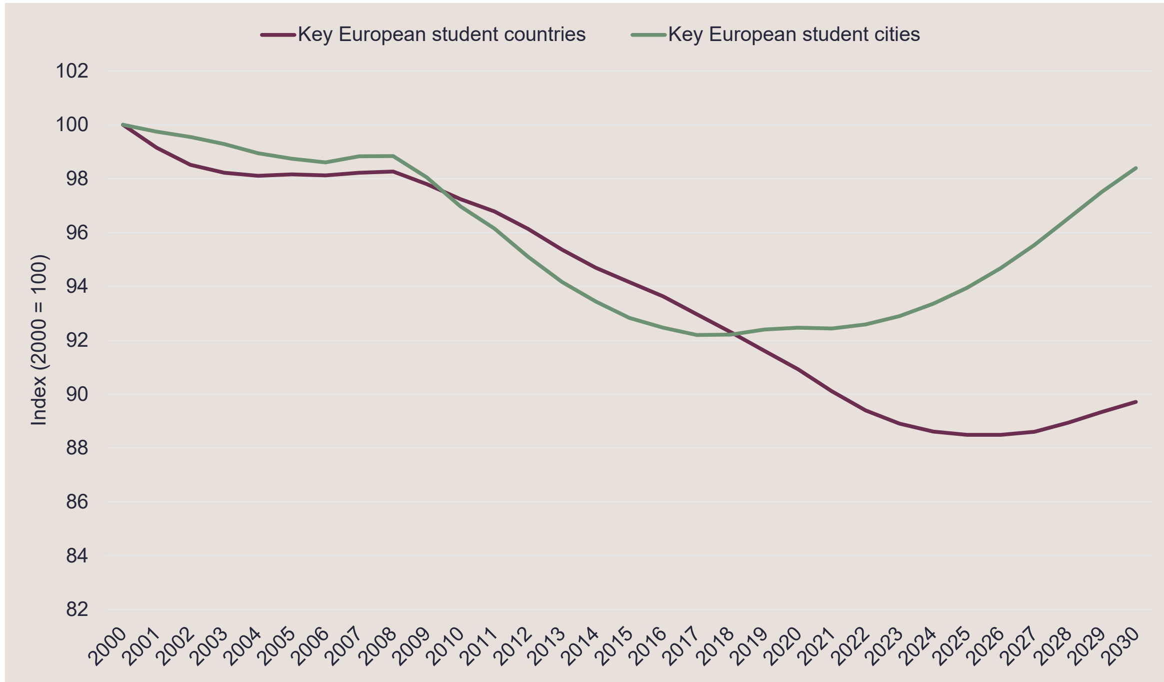
The European population to rejuvenate from 2022

Beyond the knock-on effects of the pandemic, which turned out to be far less negative than initially predicted, an underlying demographic reversal is also impacting student numbers and will continue in the long term. While the overall European number of young people (aged 20-29) had been declining gradually for a decade until 2017, it has since started to stabilise in the major European student cities and it is expected to increase from 2022, according to Oxford Economics data. Starting from 2026, it will slowly normalise at country levels.

The timing of this shift is uneven across different European cities. Over the next five years, the most significant growth is anticipated in Barcelona (+2.2%), Madrid (+1.9%), Dublin (+1.4%), Milan (+1.%) and Malaga (+1%). At the other end of the spectrum, Łódź (-3.5%), Krakow (-2.7%), Warsaw (-2.1%), Gothenburg (-1.2%) and Prague (-1.1%) are expected to show the largest falls.

European Student Housing: Forever Young

Graph 3: European young population growth indexed

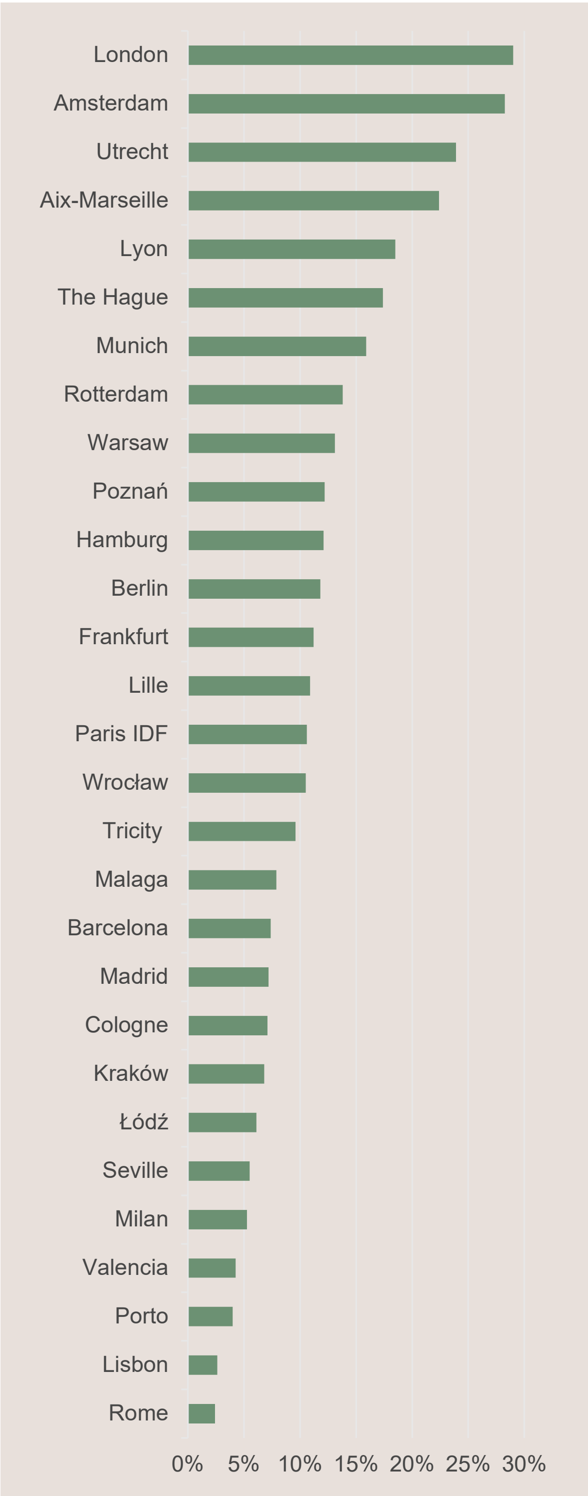


Source: Savills based on Oxford Economics

Graph 4: Young population growth forecast in key European cities

Source: Oxford Economics

Graph 5: Student housing provision rate*



Source: Savills / *Total number of beds divided by the total number of students

Demand & supply imbalance to further exacerbate

We expect the growth in student numbers to gather pace over the next five years in all large European university hubs, most particularly in the major Spanish and Italian student cities. In turn, this will create a growing demand for student accommodation.

In locations where the supply of purpose-built student accommodation is limited, this will eventually put upward pressure on rental levels. Whilst overall PBSA rental levels plateaued over the past 18 months due to the pandemic, next year, we expect rents to slowly start growing again, in line with the general residential market. We anticipate strong rental growth in cities such as Rome, Valencia, Milan and Seville, where the overall PBSA bed provision rate is low.

Despite a strong development pipeline across many European cities, we believe it will be insufficient to meet the expected pent-up demand. Hence, we anticipate the demand and supply imbalance to further accentuate in the next 12 months. Furthermore, development activity is currently facing the risks of delays due to major supply chain disruptions in the building industry, which follows a period of inactivity during lockdowns.

Eventually, new developments will improve the overall quality of PBSA available to the student population and have better ESG credentials which will be important criteria for institutional investors.

In most European cities, occupancy is back or close to pre-pandemic levels and is generally north of 90%. We expect it will rise further in the year to come.

Affordability... not at any price

Amongst many other things, the pandemic pinpointed the financial vulnerability of young people, who were particularly affected by the surging unemployment rate, particularly as short-time and part-time jobs have not always been included in furlough schemes. This implies that the need for affordable PBSA is high and likely to increase in the short term as rental growth prospects are strong.

On average across the major European university locations, the PBSA rental cost represents approximately 23% of the average household income. Considering that the large majority of students partially or fully depend on their parents' income, PBSA rental costs can significantly impact their monthly outgoings.

The affordable segment of the market has been historically covered by the public sector or non-profit enterprises. Yet, as the market is widening, local authorities' budgets are under increasing pressure, which leaves great potential opportunities for investors, developers and operators. In Spain, the offering of affordable student accommodation has been growing over the past five years. Over this period, Micampus and Camplus started focusing on this market segment with excellent results. More recently, the Belgium developer "LIFE ES" also made plans to enter this sub-sector with a seed portfolio of over 1,800 beds.

The success of these affordable PBSA operators lies in finding the right balance between operational, amenity and service cuts. As young people may not yet be ready to give up lesser amenities in exchange for cheaper rental rates, it is important to distinguish the must-have services from the good-to-have services. These can vary from country to country but generally, the necessities include high-speed WiFi, well-designed study/social spaces, 24hr security, a laundry, some car/bicycle parking spaces and an F&B offering.

Increasing investment activity

Student housing investment volumes have reached €5.8bn so far this year. This is 14% down compared to the first three quarters of 2020, which was particularly high due to Blackstone's acquisition of the iQ student housing portfolio in the UK for £4.7bn (€5.4bn). Investment activity in the sector remains buoyant, fuelled by portfolio and single property acquisitions in the most developed markets as well as forward funding deals, particularly in emerging markets. The UK remains the largest destination by volume, thanks to a few large portfolio transactions. Nevertheless, investors are increasingly looking beyond the core PBSA destinations (UK, Germany, Netherlands, France), notably in Spain, the Nordics (Denmark and Sweden), Italy and Poland.

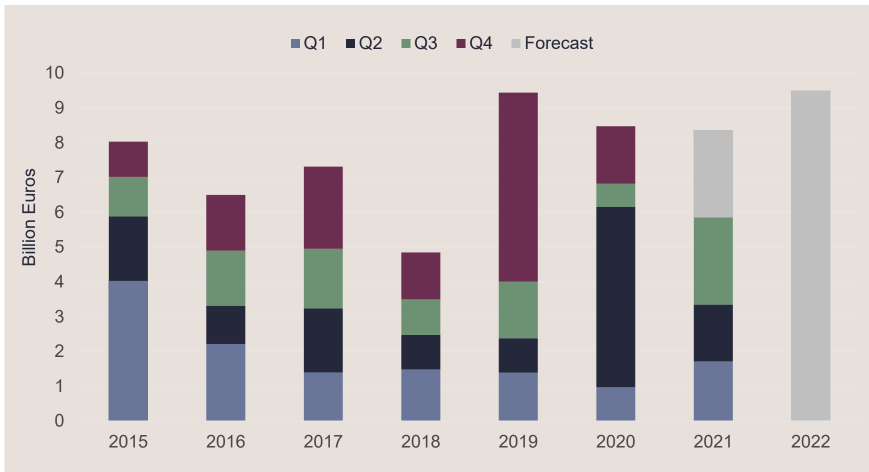
The PBSA sector, which is traditionally very exposed to cross border capital, is increasingly attracting foreign investments. Last year, cross border investment accounted for nearly 81% of the total volume. So far this year, the cross border share is approximately 74%, whereas on average, between 2005 and 2019, it was 61%. Traditionally, capital often originates from the US, UK, France, Sweden Germany and Belgium. However, over the past 18 months, Canadian, Malaysian and Qatari funds have show a growing interest in the European PBSA market.

Historically, investment has been split between private equity and core buyers, leaving a gap in the investment market. However, recently Core+ buyers have begun to shift their attention from the UK to the European PBSA market in order to take advantage of yield compression and rental increases.

Growing investor interest has put downward pressure on prime yields. The average prime student housing yield has moved in by 27 bps during the past 12 months, now standing at 4.1% in Q3 2021, though yields range from 3.3% in major German cities to 5.4% in Sevilla. However, the PBSA sector still offers better returns than multifamily. In Stockholm, Oslo and Lisbon, PBSA yields are the most competitive across the living asset classes.

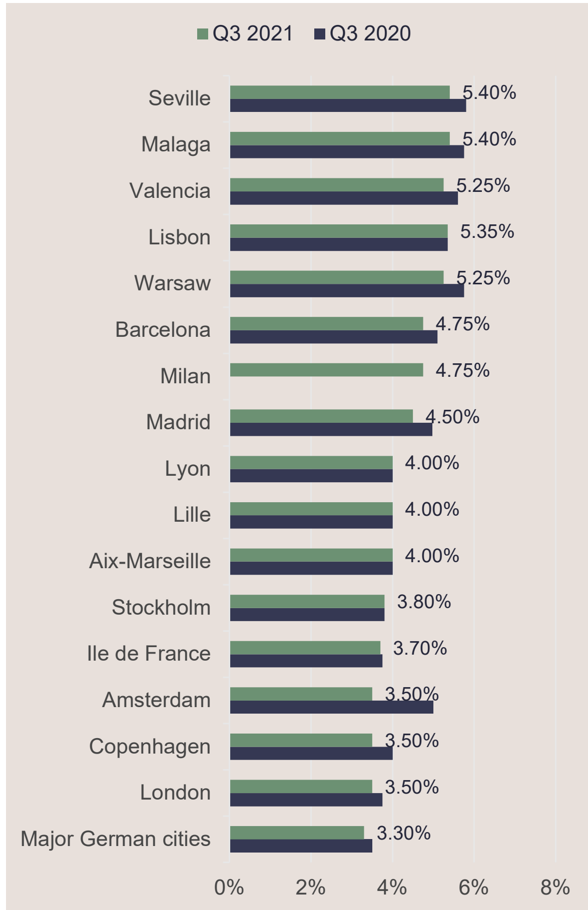
We anticipate that investment activity will intensify over the next 12 months as investors will continue to look for value in the living sectors and further consolidation in the PBSA sector is likely. We also expect to see a rising number of long-haul cross border acquisitions in the short term as well as a growing number of market players. Towards the end of 2022, we will start to see the next wave of portfolio transactions, as the first generation of developers and operators will be ready to sell their assets and exit. All in all, we expect 2021 end of year volumes to reach €8.4bn and 2022 volumes to be in line with the record level seen in 2019 (approx €9.5bn).

Graph 7: European student housing investment volumes



Source: Savills, RCA

Graph 6: Prime net student housing yields



Source: Savills

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