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Institutional Investors Coming Around to Student Housing, Sector Seen as Recession-Resistant Alternative to Apts.

Rising College Enrollments, Limited Supply Drive US Student Housing Investment and Development

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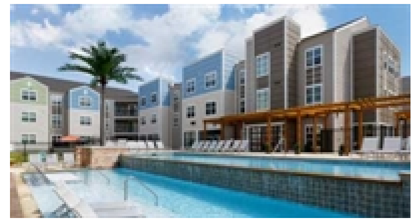

Institutional-grade properties like this new property at the University of Alabama is part of a $1.6 billion portfolio recently acquired by CPPIB, GIC and Scion Group in a series of transactions.

Once an overlooked niche, the student housing sector is attracting increased attention from major investors, who see the sector as offering less rental growth volatility and a recession-resistant hedge to conventional apartments.

Meanwhile, strong levels of US college enrollment and the diminished capacity for cash-strapped public universities to fund new dormitory development due to state budget cuts are creating more opportunities in the student housing sector for institutional investors and developers, which approached $10 billion in transaction volume in 2016, according to a new report by TH Real Estate.

Over the last three years, student housing has emerged as a leading property type in the preference of respondents to the Pension Real Estate Association's annual investor survey, according to Frederick W. Pierce, president and CEO of San Diego-based Pierce Education Properties, which had a portfolio of 12,500 beds valued at over $550 million in 2016

Christopher Merrill, co-founder, president, and CEO of Harrison Street Real Estate Capital, said student housing and other niche property sectors previously viewed as alternative asset classes were rarely if ever the targets of core funds four years ago, when Harrison Street launched its open-ended fund.

"Liquidity has increased tremendously, and investors are seeing the benefit in these asset classes," said Merrill.

Student housing demand is expected to remain healthy for years with another large demographic group, Generation Z, enters the college-age years, according to the TH Real Estate report, a real estate investment management holding company owned by Teachers Insurance and Annuity Association of America (TIAA).

In addition, the education plans of many Millennials include post-graduate schooling, which effectively extends the demand for student housing beyond the undergraduate years. An estimated 3 million students were enrolled in post-graduate programs in the fall 2016, up from 2.9 million in 2013 and 2.2 million in 2010, while applications for master’s and research doctoral programs surpassed 2 million in the fall 2015 for only the second time since 1986, the TH report notes.

With per-student spending during 2015 remaining below that of 2008 in 47 states, TH cited several factors piquing institutional interest in student housing, including favorable demographic trends, recession-resistant demand, and the limited and aging supply of under-funded on-campus housing as budget cuts in many states impact higher education funding.

"This presents an opportunity for investors to provide on-campus housing stock that universities are unable to provide themselves," according to the TH Real Estate report co-authored by Shannon Wright and Thomas Park, senior directors of strategy and research for TH Real Estate.

Foreign capital is also becoming more active in U.S. student housing. In one recent example, Chicago-based Scion Group, along with sovereign wealth fund partners GIC and Canada Public Pension Investment Board (CPPIB), acquired a portfolio of 11 U.S. student housing properties for $640 million, including nine properties owned by Harrison Street Real Estate.

The joint venture of Scion, CPPIB and GIC has completed $2.9 billion of investments since January of last year, including the $1.3 billion acquisition of the 19-property portfolio of University House Communities (UHC) in mid-2016.

Student housing portfolio sales such as the UHC deal drove transaction volume to $9.8 billion in 2016, $4.2 billion higher than the previous year and more than three times the 2014 total, according to CBRE's National Student Housing Group.

Hilary Spann, managing director and head of U.S. real estate investments for Toronto-based CPPIB, cited enrollment growth and limited new supply trends as reasons for the heightened level of investment in U.S. student housing, adding that achieving scale in the sector "is an important global investment objective."

For now, the U.S. student housing sector remains a highly fragmented market. REITs accounted for only 5% of acquisition volumes in 2016, with the two largest publicly traded REITs, American Campus Communities (NYSE: ACC) and Education Realty (NYSE: EdR), make up just a small fraction of total beds among institutional-quality properties.

Developers Getting In on the Action

Investor interest in student housing is matched by that of developers. Virginia Beach, VA-based Armada Hoffler Properties (NYSE: AHH) last week announced a $100 million project with Spandrel Development Partners to build two student housing apartment buildings totaling 600 beds near the College of Charleston in Charleston, SC.

While the broader apartment market is beginning to see slower rent growth from the ongoing wave of new supply, student housing rents have proven to be more stable, partially because the sector is less sensitive to changes in economic conditions and does not experience demand surges during boom times, noted Tom Park, senior director of strategy and research for TH Real Estate.

Investors are also attracted by generally higher capitalization rates in student housing transactions relative to the broader apartment sector, Park added.

To be sure, student housing has its own set of risks, such students skipping out on their rent, vandalizing property and pressures from the rising cost of tuition. However, those risks can me partially mitigated by having parents co-sign leases and provide security deposits, TH reports.