UK Student Market Update

Q1 2024

Knight Frank's quarterly review of the key development and investment themes in the UK student property market

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> Investment was robust in the first quarter of 2024. Activity will pick up further once interest rates start to come down and as cost inflation continues to ease, but politics and policy will be key this year

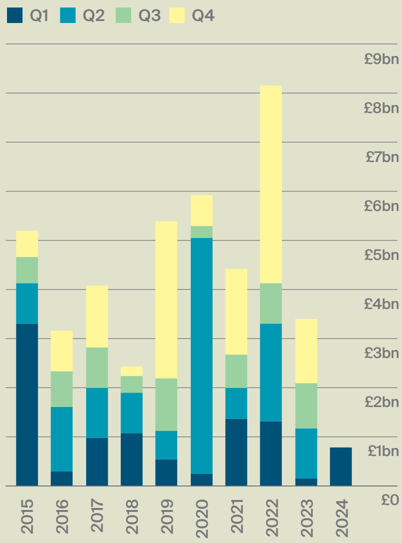
Investment volumes

Investment in UK purpose-built student accommodation (PBSA) was robust during the first quarter of 2024, following a flurry of transactions at the end of last year. In total, 21 deals completed with a combined value of nearly £750 million. While that figure was up substantially year-on-year (just £148 million transacted in Q1 2023), it was lower than in both 2022 and 2021. Nevertheless, investors continue to view the sector favourably, driven by strong fundamentals, counter-cyclical features and the prospect of good risk-adjusted returns. The transactional evidence suggests that yields were stable this quarter having shifted by approximately 50-75 basis points from peak pricing. Overall, yields have proven notably more resilient than in many other traditional real estate sectors.

Deal structures shifting

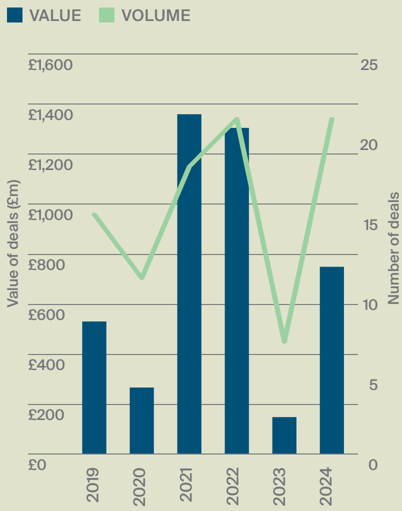
While investors continue to seek exposure to the market, the increased cost of debt continues to put pressure on deal structuring, particularly in the funding market. Consequently, we are seeing investors seeking alternative pathways to deploy capital as well as diversify their risk. While funding is available for prime assets in prime university towns and cities, for others - particularly those in more secondary locations – joint venture (JV) structures are proving more favourable.

Fig 1: PBSA investment volumes
Quarterly



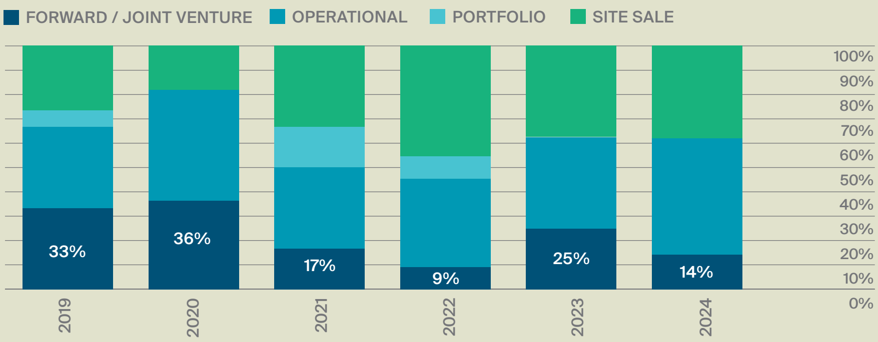
Source: Knight Frank Research

Fig 2: Q1 PBSA investment performance
Deal values vs deal volumes



Source: Knight Frank Research

Fig 3: Q1 PBSA investment by transaction type
By volume of deals



Source: Knight Frank Research

In total, funding deals and JVs accounted for 14% of total deal volumes in the first quarter, down from the comparable period in 2023 where they held a 25% share. While the proportion of funding deals has dropped, they remain an important component of overall investment, accounting for 42% of total spend in Q1. Larger deals such as the Torsion Portfolio (£147m) and Hallsville Quarter, Canning Town (£125m) bolstered their market share by value over the course of the quarter.

Past peak pain

Inflation dropped to 3.2% in March, the latest figures from the ONS show, down from 3.4% in February but slightly above market expectations of a fall to 3.1%. Despite inflation slowing by less than expected, a softening in the labour market should build a case for rate cuts. Private sector wage growth – the Bank of England's favoured measure – slowed to a 16-month low (+6.0) in February, while employment fell, and the unemployment rate rose. Money markets are betting on two cuts of 0.25% by December, with June looking more likely for the first cut than May. The SONIA forward curve confirms financial markets are expecting a sizable fall in the cost of debt through 2024 and 2025. As the cost of debt comes down, transactional activity will pick up and provide a boost to the funding market.

Construction costs ease

Build costs are still rising but over the last year the rate of inflation has eased, driven by a slowdown in construction demand and a fall in material costs. Build cost inflation stood at 3.1% in 2023, down from a peak of 15.5% in 2022, according to the BCIS. More stability is anticipated in 2024, which should help support viability for new and existing projects. Tender pricing is forecast to ease to 1.5% this year, from 3.5% in 2023. However, there are additional development costs for parties to manage, which include building safety requirements related to secondary staircases, as well as compliance with other regulations.

Green shoots for development

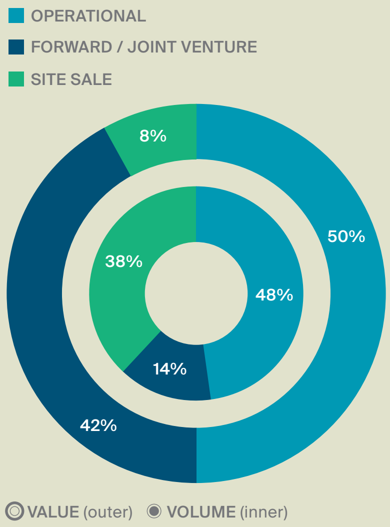
Rising build and site costs, skills and labour shortages, higher financing costs, and tricky-to-navigate planning policy have all been notable headwinds that have contributed to a slowdown in delivery of PBSA. Many of those headwinds remain but more stability around costs will provide a platform for a longer-term recovery in development volumes. Our analysis shows that London has the largest pipeline of student beds either under construction or with planning granted, at approximately 26,000 units. Other large markets include Manchester (10,500), Bristol (8,700) and Nottingham (7,600).

Appetite for land

Improving sentiment should support a more active land market in 2024. Land pricing was flat in the first quarter, Knight Frank data shows. Nearly a quarter of respondents to our quarterly survey of 50 volume and SME housebuilders across the UK, said student developers were the most active land buyers in their regions in the first quarter, second only to the PLC housebuilders, and up from 8% a year previously.

Fig 4: Q1 2024 PBSA investment volume v value

By transaction type



Source: Knight Frank Research

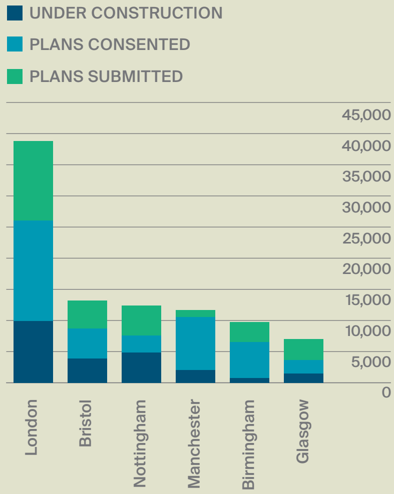
Fig 5: Financial markets expecting falls in debt costs

3-month compounded SONIA forward curve

Source: Chatham Financial (26th April 2024)

Fig 6: PBSA bed pipeline

Selection of large markets



Source: Knight Frank Research

Fig 7: Key deals in Q1 2024

Closed	Transaction Name	Transaction Type	City	Beds (approx.)	Price (approx.)	NIY (approx.)	Purchaser
Q1 2024	Torsion Portfolio	Forward / Joint Venture	Leeds, Warwick, Nottingham	817	£147,000,000	Confidential	Torsion & Zenzic
Q1 2024	Hallsville Quarter, Canning Town	Forward / Joint Venture	London	375	£125,000,000	4.75%	Link City & Crosstree
Q1 2024	Project Aqua	Operational	Exeter, Glasgow	711	£122,200,000	5.30%	LGIM
Q1 2024	The Mont	Operational	Edinburgh	324	£68,000,000	5.50%	Blackstone / iQ
Q1 2024	Gas Lane	Forward / Joint Venture	Bristol	240	£44,750,000	5.75%	Hines

Education vs immigration

Heightened by the lead up to a general election, the government agenda to "slash migration levels and curb abuse of the immigration system", saw restrictions to student visa routes come into effect. International students starting courses in 2024 will no longer be able to bring family members on all but postgraduate research courses, or those with government-funded scholarships. The changes, first voiced in mid-2023, have also prohibited people from using the student visa as a backdoor route to work in the UK. The restrictions have had an immediate effect. Survey data collected by Universities UK (UUK), from over 70 universities, suggests international student numbers are declining, especially postgraduates. Changes to immigration rules and the potential for further change were cited as the primary reasons for the decline, with a view that some students - particularly postgraduates - will re-consider study abroad plans or choose another destination.

Student visas; the reality

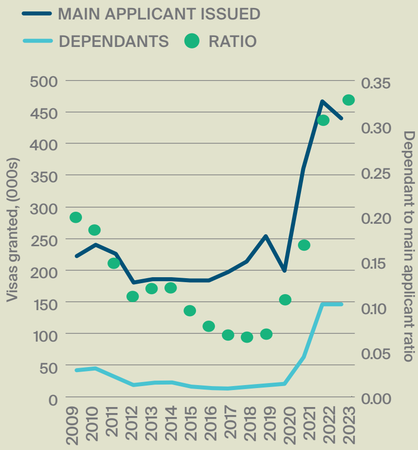
A total of 443,341 sponsored study visas were granted to main applicants in 2023, figures from the UK Home Office show, a 6% fall compared with 2022. Despite the year-on-year decline, the total number of sponsored study visas for main applicants was 73% higher than in 2019, highlighting the ongoing strong international demand for UK higher education. However, it is important not to conflate visas with actual student numbers. On average, three times as many visas are granted as there are postgraduate students, with many students securing visas for multiple countries because they want certainty over their education. Without a greater understanding of this from policymakers, there is a risk the student visa route could suffer as political parties' fish for populist votes in the lead up to a general election.

UK's productivity problem... how education can help the Levelling-Up agenda

The UK economy has a productivity problem having experienced significantly slower productivity growth than comparable countries over the decade and a half since the global financial crisis. Low productivity levels affect the resilience of the economy, making it more vulnerable to economic shocks, especially at a regional level. This, combined with NHS staffing issues, suggest that the UK needs to miss it arbitrary 'target' of 250,000 net migration to achieve long term growth, as widely reported by several economic Think Tanks. In this context, an over-correction on international students through visa restrictions presents a risk for the UK's economic outlook. Estimates from UUK, drawing on data from London Economics, suggest international students have "directly contributed" to a £60 billion economic boost over the past five years.

As the sector lobbies against moves to scale back the UK's graduate visa route, the regional productivity gap widens. Cities such as Birmingham, Glasgow and Manchester have recorded stalling productivity growth relative not just to London, but also against comparable cities in Europe. Universities are integral to the economic fabric of any city and building human capital is fundamental to the government's Levelling-Up agenda. For the PBSA sector, ensuring the availability and quality of accommodation is robust has a huge role to play in how the UK attracts and retains talent.

Fig 8: Issued student visas, main applicants vs dependants



Source: Office for National Statistics

Fig 9: Issued student visas, top 5 nationalities

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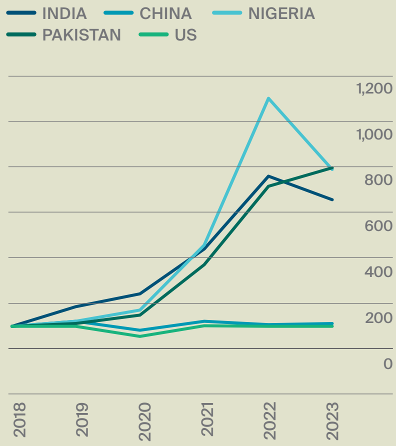

Source: Office for National Statistics

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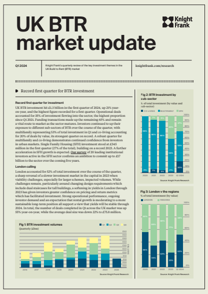

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