PBSA continues to benefit from structural undersupply, with continued investment despite a rising interest rate environment

Purpose Built Student Accommodation (PBSA) refers to accommodation with amenities and locations designed to suit tertiary education students. The student housing sector has continued to have a sustained undersupply of beds despite recent institutional investment in the UK. There is a 2.4:1 undersupply (reflecting 2.4 students for every 1 available bed) in the UK, and a 3.4:1 undersupply in London.

Sector with defensive characteristics

The PBSA market is a highly demanded real estate investment sector within the UK. Performance is underpinned by the strength of the UK's universities, home to 4 of the top 10 globally ranked universities and 17 in the top 100. The attractiveness of the UK as a study destination is highlighted by the Russell Group: 24 universities globally renowned for world class research and education.

In academic year 2022-2023, the total applicants were 5.0% above the pre-pandemic applicants. While European student numbers have fallen following Brexit, an increase in students from China, India, and Hong Kong has led to higher overall student numbers, and, accordingly, higher demand for PBSA beds. The overwhelming demand for PBSA is due to the appeal of the sector in offering elaborate amenities and modern living arrangements, with a focus on student wellbeing. The increase in cost of living expenses has also added to that appeal as students opt for more certainty of outgoings due to the all-inclusive rental payments.

According to Knight Frank, a record £7.2 billion was invested in PBSA in 2022, a 69% annual increase, across both developments and acquisitions. This comprised of £3.3bn in the acquisition of Student Roost by Greystar/GIC, along with new developments in London and regional cities. The high student demand together with the counter cyclical nature of tertiary education in a weakening global economy, is driving the continued investment in the sector.

Increasing institutional investment

Historically, student housing consisted of university student halls and low volume investment into HMO's (Houses in Multi Occupation). PBSA has brought to the industry an offering managed by institutional managers on behalf of pension and sovereign wealth funds, with professional operators.

Students are less willing to accept houses converted to student accommodation due to inferior safety, health and amenity provision. Parents also prefer sending students to live in professionally run accommodation, ensuring physical and mental support during a tumultuous period of their lives. As such, on-site security and support officers, along with premium amenities, such as gyms and lounges, have become common practice. Additionally, the PBSA sector benefits from the provision of a final price, paid in advance. Parents have certainty over energy costs and tenure.

Rising rate environment poses a challenge

As interest rates rise and portfolios continue to exhibit strong occupation and financial performance, lending markets have transitioned to lower ICR covenants and performance metrics. This has resulted in increased competition from debt funds relative to traditional clearing banks. However, investment and lending appetite remains high, with yields (around 4% in London, 5.00%+ in regional cities) remaining relatively stable in a rising interest rate environment.

The current construction market uncertainty does pose a challenge to the industry. PBSA development schemes are particularly sensitive to any delays in completion, as they need to complete prior to the commencement of the academic year to ensure they are ready for the arrival of the students. Established PBSA providers have responded well to construction delays, limiting the financial and operational impact.

Closing thoughts

Student demand for quality tertiary education is expected to continue to increase, as both overseas and domestic numbers grow. The overseas appetite for the UK, with its large number of globally recognised universities and a deep history in educational attainment, sees those with the financial ability keen to send their children here. UK demographics show the number of 18 year-olds increasing until 2030. The sector has proven resilient to the impact of COVID restrictions, and has successfully managed the costs associated with building cladding remediation following the Grenfell disaster. The rising interest rate environment makes interest coverage challenging and potentially higher yields resulting in a fall in values. However, at present, annual rent increases have mitigated any yield movements. Therefore for the right asset in the right location, the sector continues to demonstrate strong demand for equity and debt investment, supporting expectations of continuing stability and growth.

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