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School Spirit:

Student housing makes the grade with investors

As college students across the nation head back to school this month, both anxious and eager over the challenges and adventures to come, student housing owners and operators are feeling confident about their business.

The student housing sector has performed better than all other commercial real estate sectors during this economic downturn. And that outstanding performance has enticed new investors to direct money into student housing. Both institutional and private investors have identified the sector as one in which they want to place capital.

For example, industry sources say New York City-based Cantor Fitzgerald has \$250 million to \$400 million to invest in the sector, while student housing REIT American Campus Communities Inc. (ACC) is eyeing roughly \$500 million in acquisitions for 2010.

“For this school year, leasing has gone well and rents are up,” says Kevin Larimer, national director of student housing for Hendricks & Partners in Birmingham, Mich., who brokered the largest deal so far this year. “The sector hasn’t missed a beat, and more and more people are taking notice of that. We are at an all-time high for capital to be looking for student housing opportunities.”

Outstanding performance

Although experts expect student housing to be more resilient during economic downturns than other commercial property types, particularly retail and office – parents make great sacrifices for their children, after all – this most recent recession was so deep that many people thought parents would not be able to send their children to four-year universities or they would choose community colleges in an effort to cut costs.

To the surprise of even the strongest supporters, the student housing sector has come through the recession with only a few scratches. Most owners and operators are reporting strong leasing activity. Even more impressive, they’re achieving rental rate increases, something that no one property type can claim, Larimer points out.

For example, the largest student housing owner and operator in the nation, ACC, reported during its second quarter earnings that it saw improved pre-leasing for its wholly owned portfolio for the upcoming academic year to 98.6 percent applied for and 95.1 percent leased as of July 23, 2010, compared to 95.4 percent applied for and 92.3 percent leased as of July 24, 2009. Rental rates for the upcoming academic year increased 1.9 percent over in-place rents.

“We’re at maximum capacity at almost all of our student housing properties,” says Julie Bonnin, chief operating officer of Asset Plus Cos., a Houston-based firm that manages 48 student housing properties across the nation. “We’re finding enrollment continues to

grow at a record pace, and parents continue to be committed to higher education.”

Investors aren't focusing solely on the sector's strong performance. Student housing offers a compelling growth story as well, which is just as attractive as its current fundamentals, says Al Rabil, managing partner at Kayne Anderson Real Estate Advisors, an Armonk, N.Y.-based private equity firm that recently began investing in student housing through its first fund, Kayne Anderson Real Estate Partners I. The fund, which closed in March 2009, raised \$136 million in commitments.

In Texas, for example, college and university enrollment is expected to grow by more than 10 percent over the next 10 years, according to the Texas Higher Education Coordinating Board.

Increasing investment activity

Although the student housing sector garnered plenty of attention in 2009, most investors didn't make any big moves despite their access to capital. To a large degree, the sector has been able to avoid the impact of the credit crunch because investors have been able to turn to Fannie Mae and Freddie Mac to finance their acquisitions.

Instead, investors held off making any commitments until 2010 because they were waiting to see how the sector would perform during the most recent leasing season, which runs from December to March for the following school year. Moreover, there was a dearth of student housing assets on the market.

“During the second quarter, we started to see some fairly high-profile transactions,” Larimer notes.

For example, during the second quarter, ACC acquired Sanctuary Lofts, a 487-bed student community within walking distance of Texas State University in San Marcos, for \$21.4 million.

“Now, the sector is getting pounded by the amount of capital looking for good core deals. We're going to see some very significant transaction activity during the fourth quarter of this year and the first quarter of 2011.”

This month, Larimer began marketing a portfolio of eight student housing communities totaling 2,461 units and 4,057 beds owned by a joint venture comprised of Chicago-based GEM Realty Capital Inc. and Schenk Realty Inc. The portfolio has been listed without an asking price, but industry sources say it is worth roughly \$250 million.

“It is a rare occasion that a national portfolio of institutional quality student housing becomes available,” Larimer says. “The student housing market is very competitive, and it is difficult to assemble eight luxury assets that are all within one mile of university campuses that average over 34,000 students.”

The properties included in the portfolio are: Hillside Ranch and Riverside Ranch at Texas State University; Logan Square at Auburn University; Heritage Apartments at The Ohio State University; Campus Court at Knollwood and Hunter's Ridge at Western Michigan University; Campus Court at Red Mile at University of Kentucky; and Campus Court at North Walnut at Indiana University.

While Larimer doesn't expect the portfolio to ignite a "feeding frenzy," he believes it will attract a large number of investors. "[Bidding] should get very aggressive," he says.

Partnering with operators

Sophisticated investors recognize the fact that student housing is unlike any other type of commercial real estate.

Even those who might compare student housing to traditional multifamily acknowledge that student housing properties are far more operationally intense than apartments. Because student housing assets are leased by the beds, the average property has in excess of 500 leases.

Moreover, student housing operators not only deal with the people who live in their buildings (students), but they also deal with parents who pay the bills. (And don't forget the challenges involved with handling hundreds of young adults who desire a plethora of amenities and activities to keep them happy.)

To that end, most investors who are new to the student housing space have chosen to partner with experienced operators. Whether they're investing in development projects or existing properties, most investors are choosing to contribute equity rather than hands-on expertise.

"Most investors are looking to marry up with the right operators," Larimer says.

According to Rabil, student housing joint ventures are more common today than in the past because of the capital markets. "We see a lot of opportunity because there are a fair number of players who need to re-equitize themselves or their projects," he explains. "We've gotten a lot of traction by acquiring from owner-operators and then partnering on new developments.'

In May, for example, Kayne Anderson's fund partnered with two companies to invest in an existing property and a new development project. By partnering with The Edwards Cos., the fund invested in The Province at Louisville near the University of Louisville in Louisville, Ky.

Developed in 2009 by Columbus, Ohio-based Edwards Cos., The Province is a garden-style community of 266 units and 858 beds. Larimer brokered the deal, which was the largest student housing transaction completed in nearly two years.

The fund also partnered with Asset Campus Housing, the development arm of Asset Plus Cos., to invest in 25Twenty, a new student housing community of 249 units and 562 beds. Located in Lubbock, Texas, near Texas Tech University, the project is already under construction and scheduled for completion in July 2011.

Similarly, Kayne Anderson again partnered with The Edwards Cos. to invest in the development of The Province at Greensboro, a 219-unit community with 696 beds. When completed in August 2011, it will be the closest student housing property to the University of North Carolina at Greensboro's academic buildings.