CURIOSITY IS KEYS

The co-living market: contexts, expectations and opportunities

The housing market is not stagnant

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SECOND TRIMESTER 2020

No, the housing market is not stagnant.

Rather, rampant urbanization is forcing it to constantly grow, move and adapt.

Across the planet, the historic global cities continue to record population growth while new global cities grow even further :

- In Asia, the population of Shanghai rose from 14.25 million in 2000 to 25.58 million in 2018. During the same period, the Tokyo metropolitan area experienced a population growth from 34.45 million to 37,47 million, while Delhi went from 15.69 million inhabitants to 28.61 million. In Africa, the population of the Lagos metropolitan area in Nigeria has followed a similar trajectory, from 7.28 million to 13.46 million. In Europe, the Greater London area experienced a bump from 7.27 million inhabitants to 9.04 million, Madrid from 5 million to 6.5 million, and in the Paris metropolitan area, the population grew from 9.74 to 10.9 million. (UN The World Cities in 2018: p.10 to 29).
- And this global phenomenon is set to continue: according to the UN, 68% of the world population will be urban in 2050. "At the turn of the century in 2000, there were 371 cities with 1 million inhabitants or more worldwide. By 2018, the number of cities with at least 1 million inhabitants had grown to 548* and in 2030, a projected 706 cities will have at least 1 million residents. The report goes on to say that "globally, the number of megacities [editor's note: more than 10 million inhabitants] is projected to rise from 33 in 2018 to 43 in 2030. (UN The World Cities in 2018: p.2)

In light of this, it is important to reckon that in-depth social and economic changes in our everyday lives - particularly in the context of mobility and digitalization - particularly in regards to mobility and tech- are disrupting various real estate asset classes :

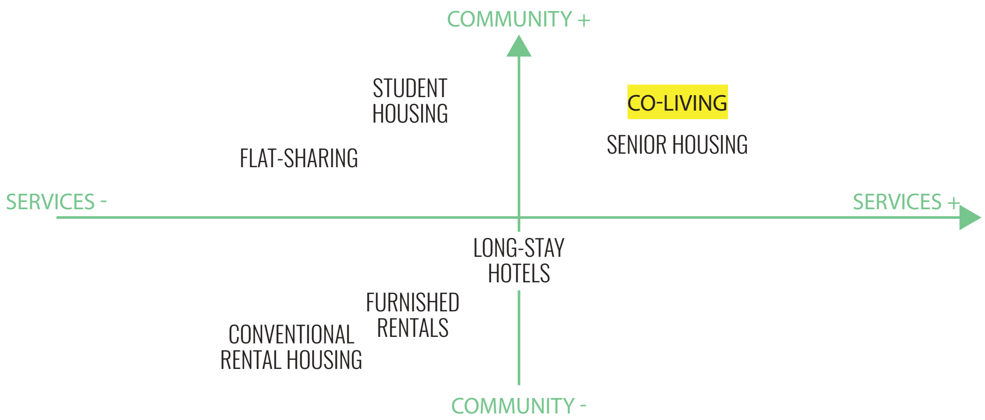
- Co-working has shaken up commercial real estate by providing flexibility and new services.
- Warehouses are moving closer to city centers with urban logistics solutions and a strong focus on last-mile delivery strategies.
- In the face of the e-commerce boom, traditional trade has begun to reinvent itself by digitization and broadened in-shop service offering.
- The emergence of Airbnb has forced the hotel industry to rapidly evolve through adaptation to new trends and demand for lifestyle products.

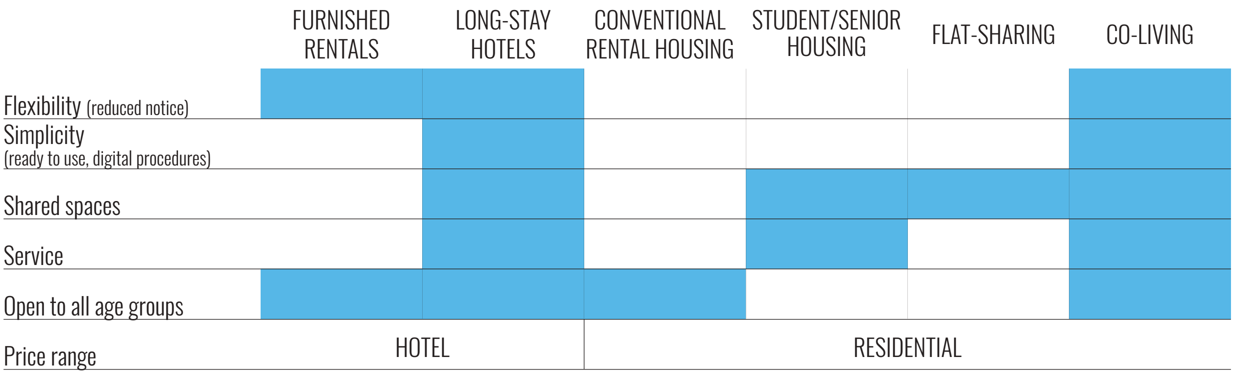
It's now time for the housing market to change and to adapt to the evolving needs and lifestyles of residents. They are demanding flexibility, simplicity and a sense of community. For us professionals, the time has come to listen, to innovate and to take action. Co-living seems to be a solution among others, a first response to this evolved demand.

PART I : Co-living, the basics

1. What is Co-living?

As established by the think- and do-tank Co-liv, co-living is a form of housing managed by a professional third party, in which residents share spaces and / or services in order to access better quality of life.
The concept differs from flat-sharing, student housing, conventional rental housing (furnished or unfurnished) or long-stay hotels, as it integrates services into communal living.





2. Why co-living?

Because it provides an answer to part of the current demand for housing in that it better meets (some) residents' expectations than the conventional sector.

2.1. Evolution of needs

Over the past three decades, our lifestyles have changed significantly, leading to a shift in housing needs for a growing portion of cities' population. And yet: this is scarcely -- or sometimes not at all -- taken into account by the developers and designers in the housing market.

The most visible change relates to the composition of households.. Single-parent families, young single workers, and a growing number of seniors are adding to the classic household model of couples with children. As a result, between 1999 and 2015, the number of households increased by 4.7 million, according to INSEE. Only half of the increase is due to population growth while the rest stems from a reduction in household size. In 2015, the average household size was 2.2 residents compared to 2.4 in 1999. And more than a third of these were single parents (and as many as 56% in Paris), reports Terra Nova in its 2019 study "Habiter dans 20 ans."

NEW NEED > Today's residents expect not only more diversity in available housing models, but also more spatial modularity to adapt to all profiles and ways of life.

Beyond the composition of households, the pace of our lives has accelerated and the number of life phases has multiplied. Life events such as births, separations, divorces or deaths, but also college education and greater job mobility has entailed more frequent relocations, notes Terra Nova. And in spite of this need for flexibility, entering into a rental agreement remains a cumbersome process: security deposits, proof of income, «competion» between prospective tenants in large cities ...

NEW NEED > People, and city dwellers in particular, are therefore looking for more flexibility in housing offering. They want to move in and out of homes faster, especially when the next phase in their lives in on the horizon.

More than ever before, affordability has become a priority. In large cities particularly, housing is increasingly scarce and expensive: in Paris, only when INSEE assesses a need for 13,000 homes in order to offset the demand and thus achieve a 2% decrease in pricing.

And as pricing continue to rise, flat-sharing attracts more and more city dwellers, young and older.

In recent years, the share of employees who share their apartment make up for nearly half the tenants (45%) in 2019. Still, it has not been addressed by investors..

NEW NEED > Residents expect not to have to trade quality of life for housing affordability.
Sharing is a way to lower the global cost of living in the city.

And at last, people need people. We're social animals. If further proof is needed, sharing is a defining feature of our society (car pooling, open-innovation, fablab, shared gardens). And housing is no exception. Especially as loneliness is an increasingly familiar feeling among urban dwellers: in France, around 36% of urban residents experience feelings of loneliness. According to a survey by the Fondation de France, more than 5 million French people are considered isolated, or one in ten people aged 15 and above.In the UK, it is one out of 10 people who reports to have no close friend whatsoever. in the United States, that number is one in four. And the social distancing imposed during the Covid-19 crisis might further exacerbate the need for socializing.

NEW NEED > In their homes and buildings too, residents need to bond with one another. While they need the appropriate amount of private space for their specific lifestyle, they also need to feel that they are part of a community, inside and outside of their residential building.

These four major trends and their ensuing needs highlight the mismatch between the offerings of the current housing market and the expectations of residents.
They urge a transformation in all segments of the housing sector to invent new forms of living -- flexible enough to bring real solutions to the residents of today, as well as to the still-unknown demands of the residents of tomorrow.

2.2. Co-living offers answers

Co-living precisely addresses these new economic and social demands.

It constitutes a new form of housing, which provides:

- The modularity needed to grow a home in pace with the evolution of your household.
- The flexibility residents need, by way ofsimplified move-in and move-out processes (shorter notice), reduced administrative work 100% online management, and ready-to-use furnished accommodations enabling nomadism and/or unexpected life changes.
- High quality shared common areas such as family-size kitchens, terraces and backyards, laundry rooms or even fitness facilities to meet residents' expectations of modern comfort while reducing monthly expenses.
- Community living and a social safety net for whoever needs it at any moment in time.

3. Co-living models

3.1. Two models stand out:

Residential co-living

which becomes the tenant's primary home address, whether it is for the medium- or long-term.

And the hotel co-living

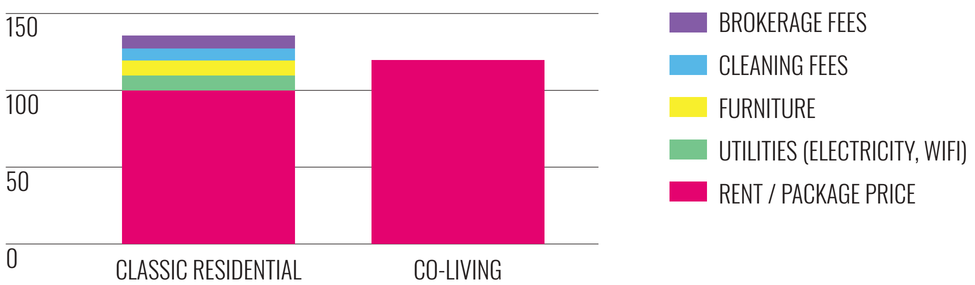
houses remote workers and mobile users, in need for short- to medium-term accommodation for occasional or regular.

3.1. Five factors to consider when choosing a co-living model:

Pricing

While it may appear more expensive than conventional housing at first sight, co-living incurs a number of hidden costs (internet, cleaning, maintenance, etc.). The price must therefore be considered as a whole. In order to compare the rent of a traditional apartment to the price of a co-living space, you must add up all expenses included in the co-living «package." Co-living generally has a more attractive overall cost than traditional housing, since it divides the common operational expenses between all co-tenants.

GLOBAL PRICE



Size

Several co-living formats exist, ranging from houses with fewer than five residents to a full building with 400 rooms with shared common areas.

Offered services

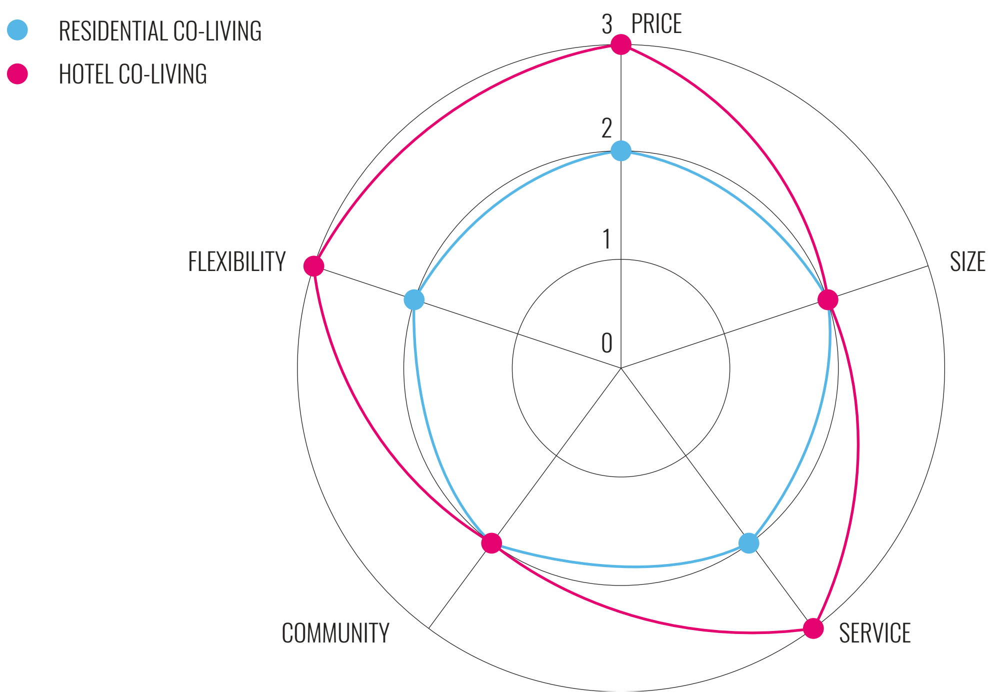
Basic services such as rental management, cleaning, community event, included in the packaged pricing sets co-living apart from other shared accommodation models. Each operator and brand crafts its unique service offering to best serve its residents needs.

The comunity factor

The higher the quality of shared spaces and community activities, the warmer and more inviting will your co-living be. Each operator and brand designs communal areas and community events to reflect their set of core values and provide an opportunity for social interaction. Co-livers are free to participate or not. The sense of belonging than many look for in this type of living scheme can only be inspired by the manager to residents.

Flexibility

In general, the co-living option is more flexible than conventional housing (simplified selection of housing, signing of lease and moving-out process). Within the co-living models, the hotel co-living, specializing in shorter-term stays, offers more flexibility than residential co-living.



PART II : Current offering

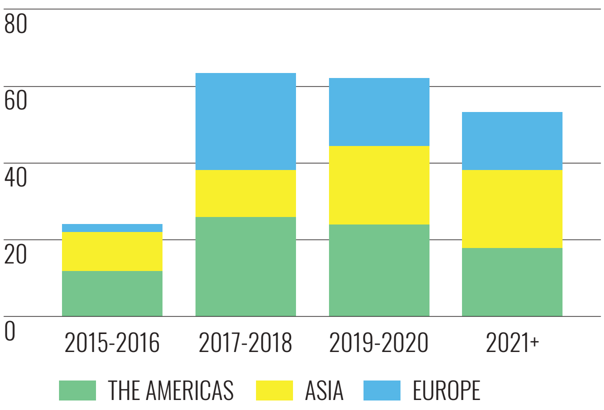
4. Competitive landscape

4.1. Market depth

23,150 co-living beds were available or underway in Europe at the end of 2019 (Source: JLL), and managed by a dozen operators.
But since 2015 and the worldwide emergence of co-living opportunities, the landscape has progressed very quickly. It seems easy to enter the market but difficult to establish a foothold and grow your business. The number of operators therefore increased significantly in the years 2017-2018.

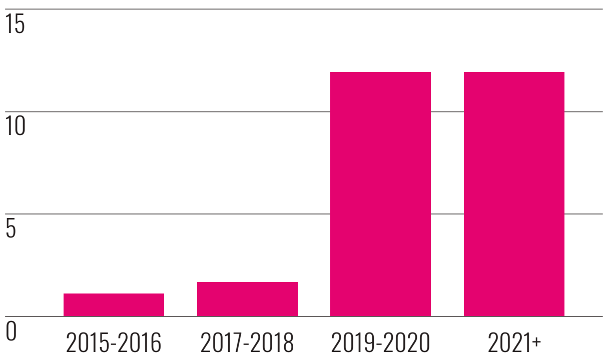
It is likely that the number of operators will now stabilize, while the overall number of beds will continue to grow exponentially, allowing operators to build track record and gain speed in their development. According to Richard Lustigman, head of co-living at JLL, 79% of construction projects in Europe will comprise of over 200 beds -- sizeable enough to attract traditional investors to co-living.

NUMBER OF CO-LIVING OPERATORS INTERNATIONALLY



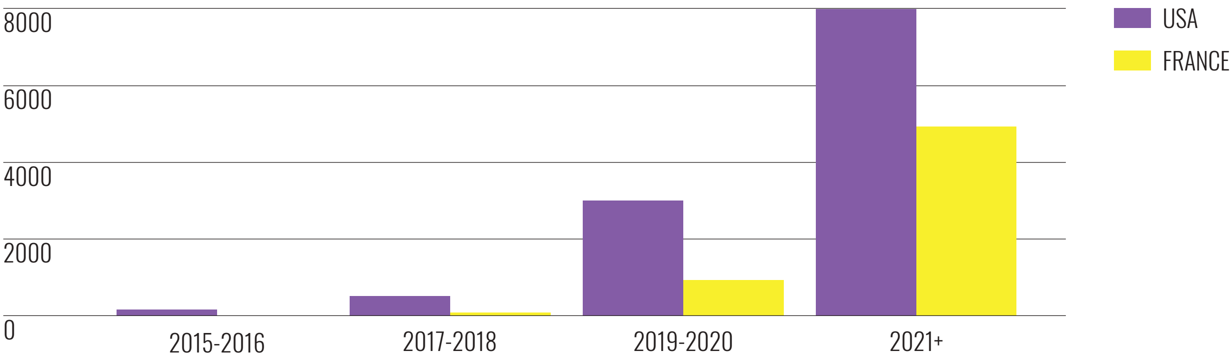
Source: Who's Who in co-living; Coliv + Co-living Bible by Gui Perdrix
* does not include co-housing, and scandinavian models

NUMBER OF CO-LIVING OPERATORS IN FRANCE



Source: Co-Liv, internal

NUMBER OF CO-LIVING BEDS IN FRANCE AND IN THE US



Source: Co-Liv, interne

Several methods can be used to assess and measure the depth of the market in a given area. We recommend taking into account the number of households without children, the proportion of employed individuals and mobile professions, as well as the attractiveness of the area -- based on factors like local employment and ridership at national train stations.

4.2. Examples of operators and their value propositions

Pure operators

PRICE SIZE FLEXIBILITY

SHARIES

Launched in 2017 in France, the company has two locations in Marseille and Nancy and plans to open 4 new addresses in Paris and Strasbourg by 2022. The target clientele is young adults (working or students) for stays longer than 6 months.

News: in 2019, sharies, together with their investment partner Audacia, launched a co-living fund aiming for an investment capacity of capacity of €50 million.

OUTSITE

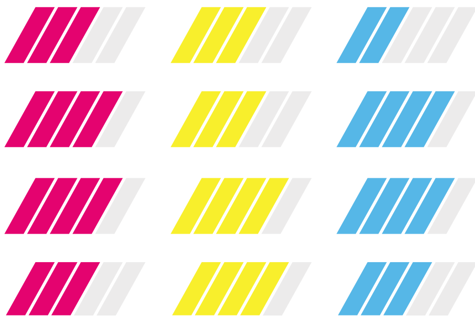
Founded in 2015 on the West Coast of the United States, the company operated 28 co-living spaces around the world at the end of 2019, mainly in the US. Outsite primarily targets mobile professionals and digital nomads. Since 2018, the company has entered the European market with two locations in Portugal and one in Biarritz.

News: In 2020, Outsite will open a second location in Midtown Manhattan, New York. The space will have 8 bedrooms, 5 bathrooms and a separate studio, spread across 5 floors.

THE BABEL COMMUNITY

Launched by Axis in 2017, the company opened its first location in Marseille, offering 80 accommodations, 170 coworking spaces, a bar and a restaurant. It expanded to Montpellier in November 2019.News: The Babel Community will open a new location in Marseille in 2021, and plans are underway for Grenoble in 2022, Bordeaux in 2023, Lille and Paris in 2024.

LIFE X
SONDER
OLLIE
COMMON



In Europe, France has incurred some delays in the adoption of the co-living trend. However, one should note some recent moves into this space :

- Quartus: The property developer launched, in March 2018, two separate co-living brands: LIVINGHOMES by Quartus aimed at young workers, and THE OPENER, aimed at students and young travelers. To date, no space has yet been opened.
- Bouygues Immobilier: Created in 2017 by 4 intrapreneurs from Bouygues Immobilier, Koumkwat intends to open homes in France and Europe's major cities in order to promote community living, flexibility and mobility between cities.
- Vinci: The construction group launched its co-living brand Bikube in March 2019. The concept offers 2019, a concept that offers «a new residential experience centered on conviviality and services.» The first Bikube (Beehive in Danish) residenclocation is set for completion by 2021.
- Medici Living: The largest flat-share provider in Germany already operates co-living homes under the Quarters brand in Berlin, Munich, Frankfurt, Stuttgart, Amsterdam, New York and Chicago. The company raised €1 billion in January 2019.
- Nexity Urban Campus: The property owner and developer took a different route and decided to capitalize the existing brand and operator Urban Campus in 2018. Urban Campus operates co-living and co-working spaces as well as third places and currently manages 4 locations in Madrid, Spain. (source: Nexity 2018, p.69)

5. Arrangements and economic model

What are the risks? What should you pay attention to while running your valuation model?

5.1. Three models to consider :

	LEASE	HYBRID	MANAGEMENT CONTRACT
CHARACTERISTICS	**Master lease** between owner and operator. The operator is held accountable for the operations of the asset.		**Management contract** between owner and operator. The landlord is held accountable for the operations of the asset. However, s/he delegates.
REVENUE STRUCTURE	**The landlord** receives a fixed rent. **The operator** receives the entire profit generated by the operation, minus the rent.	**The landlord** received a fixed rent as well as a variable portion based on an agreed revenue-share model. Beyond a certain threshold based on gross revenue or EBITDA, the **operator** shares the profit margin?	**The landlord** receives the entire profit generated by the operation minus the management fees. The **operator** receives the management fees which are generally expressed as a percentage of turnover and / or EBITDA.
DURATION	Standard commercial lease		Typically 10 to 20 years, renewable
MAINTENANCE AND FF&E	Maintenance works and FFE costs are shared based on hotel standards (general CAPEX are generally paid by the landlord, FFE are covered by the operator), although subject to negotiation.		
PROS & CONS	FOR THE LANDLORD :		
	−	+	+
	Does not capitalize on operations	Capitalizes on operations	
	FOR THE OPERATOR:		
	−	−	+
	Higher investment: - Potential intangible business assets or "fonds de commerce" - Security deposit in France - FF&E		Low investment: Allows for accelerated development without having to mobilize cash to support security deposits and other lease-related expenses.

5.2. Four areas to pay attention to in the business model from least to most risky.

1. One can only inspire a sense of community: yet it is essential to the co-living model to properly invest in the design of shared spaces so it produces the right atmosphere for the target audience.
2. Market depth: while you generally need to reach a critical mass to cover your operational expenses, it is important to properly size the asset (the supply) to match local neeeds (demand). This is especially true of hotel co-living models.
3. Affordability and profitability: Striking the right rent balance is essential. Will you comparable be made of studios and one-bedrooms on the conventional market or else? How do you take services into account in the analysis? How will you optimize taxes (VAT for example) and what type of lease will residents be asked to sign?
4. Country-by-country specificities: housing and hotel regulations are often specific to each country, even in the EU. Investors should have a clear understanding of the local requirements in terms of tenant rights, provision of affordable housing, and taxes, before proceeding.

PART III
Valuation methodology

6. Third party valuation

6.1. Adjustment to the traditional approach

Our valuation approach for co-living is based on the three traditional valuation methodologies, with specific adjustments for the co-living typology. Thus, we first analyze the asset's geographical and urban context, its tenancy and the depth of its local market. These elements are then assessed through a SWOT analysis, highlighting the strengths, weaknesses, opportunities and risks of the asset, before proceeding to the final evaluation.

The diagram below presents each step of the analysis, with a focus on attention items for co-living transactions.

LOCATION

- **Proximity** to services, restaurants, shops, business districts (for hotel models especially)...
- **Connection** to transportation hubs (train station & airports particularly)

TENANCY

- **Lease or management contract**
- **If lease:** duration, signature quality (track-record)

MARKET ANALYSIS - ESTIMATED MARKET RENTAL VALUE

> GROSS REVENUE :

- **Residential :** market analysis, comparables (roomsharing, studios and one-bedrooms).
- **Hotel :** TO and PM analysis offered (tourism residences for medium-length stays, hotels for short-term stays).

> OPEX

> NOI :

- **Lease :** in addition to traditional metrics, focus on the sustainability of the rent level for the operating company...
- **Management contract:** focus on vacancy risks, projected turnover, and on-going opex.

> COMPETITIVE LANDSCAPE :

- **Residential :** existing and incoming housing stock (studios and one-bedrooms) in terms of vacancy, completion date, future pipeline etc..
- **Hotel :** long-stay hotels, corporate housing, etc.

SWOT / BENCHMARK

DCF VALUATION

FIXED RENT LEASE:

capitalization of a secure cash flow (long term)

MANAGEMENT CONTRACT:

Estimated cash flows under contract

FULL BACK UNIT-BY-UNIT SALES

Based on existing comparables.

CONCLUSION

6.2. Five key steps:

1. Location: based on the location's relevance as a residential or tourist destination (restaurants, shops, transport, neighborhoods (business, student, airports / stations, etc.).
2. Tenancy: situation propre au bail ou au contrat de management ? Durée ? Opérateur existant ou non ?
3. Market analysis, estimated market rental value: analysis of the market for residential co-living, and the prices charged in tourist residences and hotels for hotel co-living. Analysis of operating costs. In addition, there is the verification of rent sustainability within the framework of a lease, and of the fluctuations (holidays, turnover, maintenance cost, etc.) under a management contract. And of course, an analysis of existing competition is necessary to understand the supply and demand in a given sector.
4. SWOT/Benchmark: all of the above elements are then assessed in a SWOT, highlighting the strengths, weaknesses, opportunities and risks of a real estate asset, before proceeding with the valuation of the property.
5. Conclusion: they differ depending on the model.

   a. For residential co-living: in the absence of comparable references, we follow the methodology applied in Valuation by CBRE in the United Kingdom. And we estimate the capitalization rate used for residential co-living based on the return on the student and senior service residency market, as these are also managed assets.

In terms of cap rates, we would expect these to sit between the build to rent and PBSA sector for long stay income, depending on laction, design and tenant profile. Yields on short income would be higher than for long stay and more aligned to hotel cap rates.

YIELDS IN BED SECTORS Q4 2019 (CBRE published yield categories)

SECTOR	London zone 1	London zone 2	London zone 3-6	Outer London/ South East	Larger regional towns
Build to Rent	-	3.25%	3.5%	3.75%	4.25%
PBSA Direct Let	4.00%	-	-	-	5.00%
Hotels VP (upscale)	4.50%	-	-	-	6.25%
Hotels Management Contract	5.50%	-	-	-	7.50%
Hotel Lease - Prime Covenant	3.75%	-	4.00%	-	4.25%

Source - CBRE - Coliving : how is it valued *PBSA : purposed built student accomodation. (link)

REFERENCES AVERAGE RATE OBSERVED
Large metropolitan areas

VARIETY OF ASSETS	RECORDED AVERAGE RATE*
Residence Services, Seniors	4.00% - 4.50%
Hotels (walls)	4.50% - 5.00%
Student residences	4.00% - 4.50%

*pour des baux avec durée fermes longues (12 ans) et des opérateurs nationaux

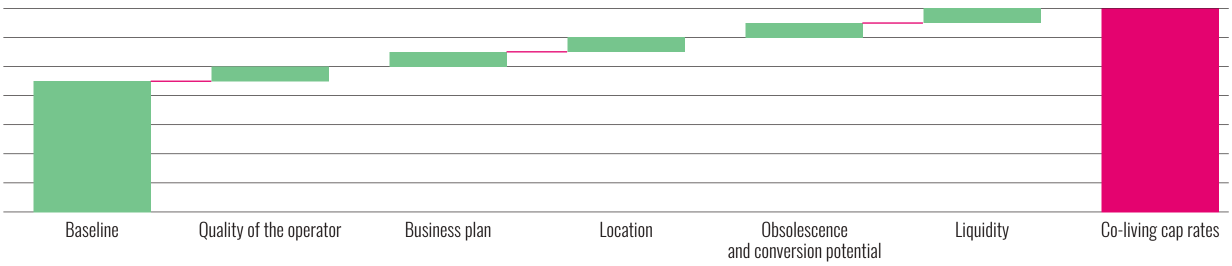
Ref: Expertises Keys Marseille Trinquet, Keystone Chartrons (CW, 2018)

The average rate for student housing in large metropolitan areas, for long-term leases with national operators ranges between 4 and 4.5%.

One can then apply a risk premium based on the identified weaknesses or risks identified in terms of :

- Quality of the operator (risk premium ranging from 0 to 0.5%)
- Consistency of the business plan: excessive charges or proposed rent (risk premium ranging from 0 to 0.5%),
- Quality of the location (risk premium ranging from 0 to 0.5%),
- Conversion potential and obsolescence (risk premium ranging from 0 to 0.5%),
- lquidity: number of units and market depth (risk premium ranging from 0 to 0.5%))

CAP RATES SPREADS



Source : interne

A quick and easy verification for traditional residential fall-back scenarii lies in comparing the sqm/unit ratio to the existing market.

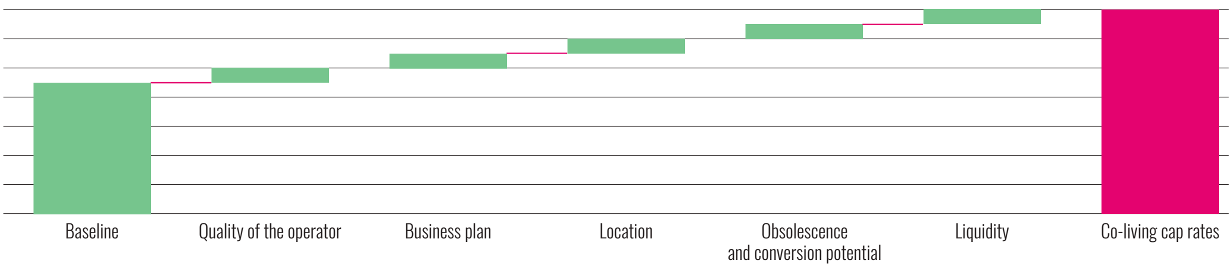
b. For the hotel co-living: given the turnover linked to short stays and the similarities to a hotel management model, we will use an average rate based on the hotel market.

The average rate for hotel activities in large metropolitan areas, for long-term leases with national operators ranges between 4.5% -5%.

Analysts will apply a risk premium as they see fit.

Student housing rate	4,00 % - 4,50 %
Quality of the operator	0% - 0,5 %
Business plan	0% - 0,5 %
Location	0% - 0,5 %
Obsolescence and conversion potential	0% - 0,5 %
Liquidity (volume 0-50 / 50-100 /> 100 lots)	0% - 0,5 %

CAP RATES SPREADS



Risk premiums to apply (subjective - to be refined)

Hotel rate	4,50 % - 5 %
Quality of the operator	0% - 0,5 %
Business plan	0% - 0,5 %
Location	0% - 0,5 %
Obsolescence and conversion potential	0% - 0,5 %
Liquidity	0% - 0,5 %

6.3. An example from France

Marseille, 70 rue de la République, 3832-m² building: Fully rented for a set period of 12 and 9 years for the restaurant at The Babel Community.

- Location: in the heart of Marseille on one of the city's main commercial strips, halfway between the Euromed business district and the old port.
- Mixed use: residential co-living, hotel, restaurant, coworking + fitness area and movie room.

Seller bares closing costs: € 5 228 /m²

"Prime" sector rent: € 230/m²

Estimated Initial Rate of Return (French AEM): 4,4 %

Source

CONCLUSION

It is safe to say that, in 2020, the co-living market is maturing. First developed on the American and Asian continents, the concept has rapidly conquered Europe in the last few years. The current socio-economic context in large European cities the diversification of such innovative housing schemes. As far as investment is concerned, the lack of data requires rigorous analysis of the local markets. Conventional analysis criteria such as occupancy rate, rent levels, location, etc. main relevant as long as they're analyzed in pair with the main co-living success factors, i.e. community management, quality of shared spaces, and service offering.

For broader, international insights on the co-living market, we recommend joining Co-Liv and access the Coliving Insights publication series.