Co-living in Costly Cities – Asia Pacific

How the rise of the shared economy is propelling a new way of living, and the impacts on the real estate market.

JLL | *Achieve Ambitions*

Co-living is a broad concept and not one that is easily defined. But, according to co-living.org, the concept can be best defined as:

Co-living / noun

1. Shared housing designed to support a purpose-driven life.

2. A modern, urban lifestyle that values openness, sharing, and collaboration.

While the concept of shared living spaces is nothing new, this evolution of a more organised system is new. There is an emphasis on collaboration, convenience, cost and community that make it unique. And, as the way we live, work and play evolves, so do our preferences for where and how we live.

The demand drivers that support the development of the co-living sector stem from changing demographics, financial considerations and tech advancements. The flexible co-living model is filling-in the gaps of a residential market that's been under-served for too many years.

"Disruption and the rise of the sharing economy is leading to the rationalisation of all things underutilised. That now includes residential real estate."

The 4C's of Co-living: What it's all About.

Convenience –Long lease contracts with prohibitive lease break clauses aren't geared towards the uptick of global mobility and international assignments. Co-living on the other hand, offers flexible and shorter lease terms, and often monthly lease options making it highly attractive in today's more transient world. It's a simple solution that provides a ready-to-move-in product that's hassle free for residents. Co-living contracts generally cover all services and move-in requirements. The spaces are fully furnished, utilities are set-up, and cleaning and maintenance services taken care of. The spaces are professionally managed often by an on-site team that handles maintenance and repair requests, with most of the communication and service requests done seamlessly through technology and mobile apps.

Cost – Housing affordability is becoming problematic in major gateway cities around the world. Dwelling prices have increased considerably faster than both rental prices and wages, leaving home ownership out of reach for many. Co-living operators are using the space better and reducing underutilised space. Economies of scale for things like utilities, Wi-Fi, cleaning and furniture are also creating cost efficiencies for all parties involved. While, a co-living space may cost more than a room in a shared apartment at first glance, once all the additional costs like move-in and move-out, agent fees, utilities, maintenance and furniture depreciation are factored in, the pricing is relatively similar – with the added benefit on having flexible lease terms.

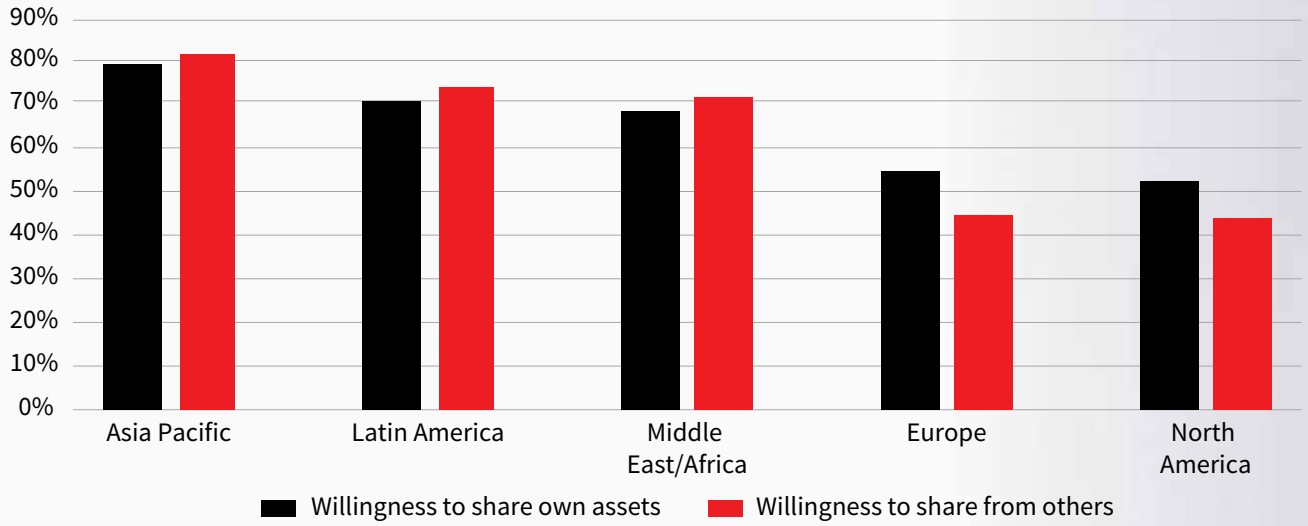
Community- The biggest differentiator for co-living compared to traditional shared residences is the emphasis on community. Loneliness and social isolation are one of the fastest growing health concerns in much of the developed world, and co-living operators are cultivating communities that fight that through organised social activities, events, workshops and classes. They also tend to match residents with other like-minded people though personality profiling. There is a hidden element of demand for this community aspect as well.

Collaboration - Catering to a young, aspirational demographic, often residents within co-living spaces enjoy the collaborative benefits that the community provides. Some co-living models cater entirely towards a certain profile or profession, with co-living operations that specifically house 'digital nomads', Blockchain communities or tech start-ups etc.

The fundamentals driving co-living

People in Asia Pacific are the most willing to share their own assets, and receive shared assets from others according to Statista. It's likely that the region's younger demographics and the higher densities of its major cities are the reason for this. The sharing economy can be applied to everything from underused cars, homes, bicycles and even music. Much of the modern home remains vacant or underused, and the excessive size of dwellings exacerbates housing affordability.

Figure1: Willingness to participate in sharing communities



Source: Statista

Urbanisation

Urbanisation rates and urban population rates across Asia Pacific continue to rise, with an expected 565 million more people living in Asia Pacific in the next 15 years. That's equivalent to the size of a new Singapore every 8 weeks. The three biggest areas of growth in urban population over the next 15 years are China at 235 million, India at 150 million and Indonesia at 50 million. For this reason, co-living operators in these markets are focusing on inter-country migration. Professionals or students moving into cities for jobs or education opportunities, or from one city to another are a strong candidate for co-living in markets like India.

Immigration

Inbound immigration is driving demand for co-living spaces in large, developed cities like Singapore, Hong Kong and Tokyo. The transient nature of these expat populations makes them right for co-living – they value flexibility and convenience. Typically, they don't have permanence or family ties holding them to their current place of residence. The ongoing evolution of global assignments is shifting away from traditional long-term engagements to more short-term projects – making co-living by far the most suitable option for many assignees. In cities like Tokyo, getting a residential lease as a foreigner presents challenges. The upfront costs in Japan are very high – upwards of 4-6 months of rent required before moving in – making co-living a much more desirable option.

The three biggest areas of growth in urban population over the next 15 years:

China
235 million

India
150 million

Indonesia
50 million

Housing Affordability

The cost of housing remains a challenge for millennials in almost all gateway cities worldwide. House and condominium prices grew significantly faster than wages and rental costs. And, as a result, the financial decision made between renting or buying real estate is now more than ever skewed towards renting. Co-living is making renting more attractive, as people can live in better quality and better located dwellings, while keeping costs under control.

Demographics

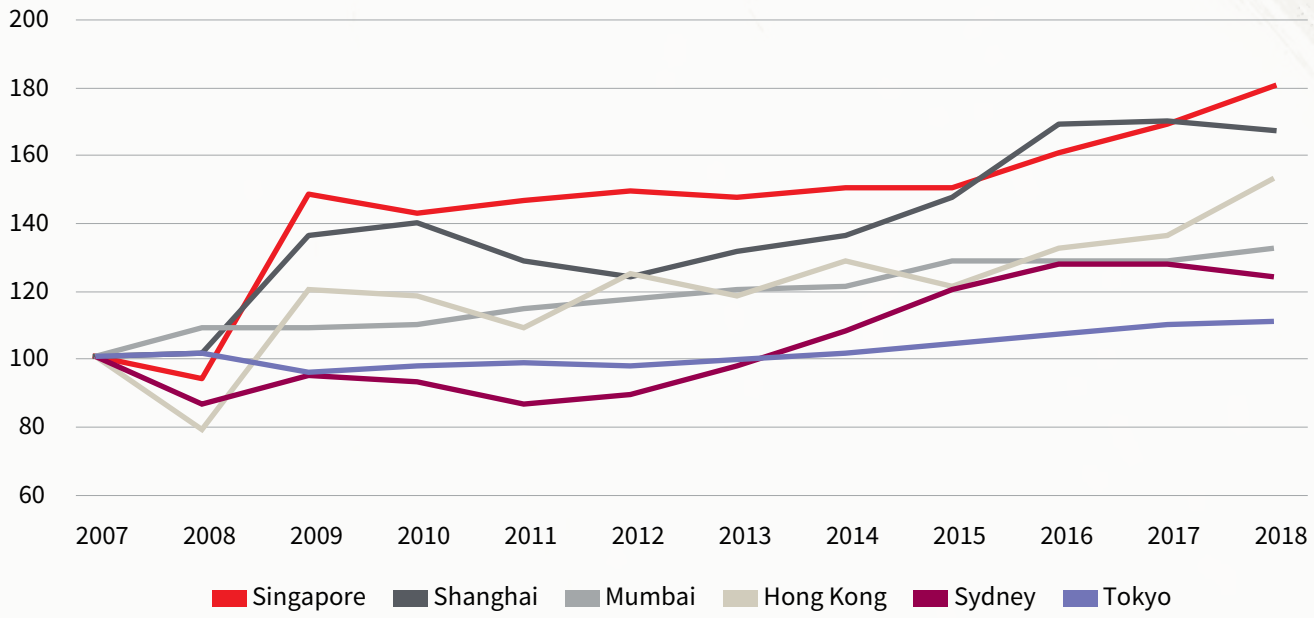
Delayed marriage and child rearing has shifted housing requirements for the entire age bracket of mid-20's to early 30's. The median age of marriage across the OECD* is now 32 years, up 5 years from 1990. This is reducing the requirement for traditional residential space and increasing the demand for flexible lifestyle-based housing. This trend is supporting the development of co-living in all markets, even those like India where people marry young (relative to other markets).

As lifestyles change, so do living requirements. It's been well documented that millennials value experiences over ownership of things. Co-living plays right into this reality because it makes housing a service and an experience, rather than a product. Millennials value access to this service over ownership of it.

Serviced based living is on the rise – from student housing to renters who prefer the serviced-based offering of multifamily over traditional condominiums. Hotel operators and developers are picking up on this trend, and focusing more time on "branded living", as demand for the service-based aspect of residential takes priority. Even senior care homes are becoming more about the extras and lifestyle, contributing to an evolving set of living categories across the life spectrum.

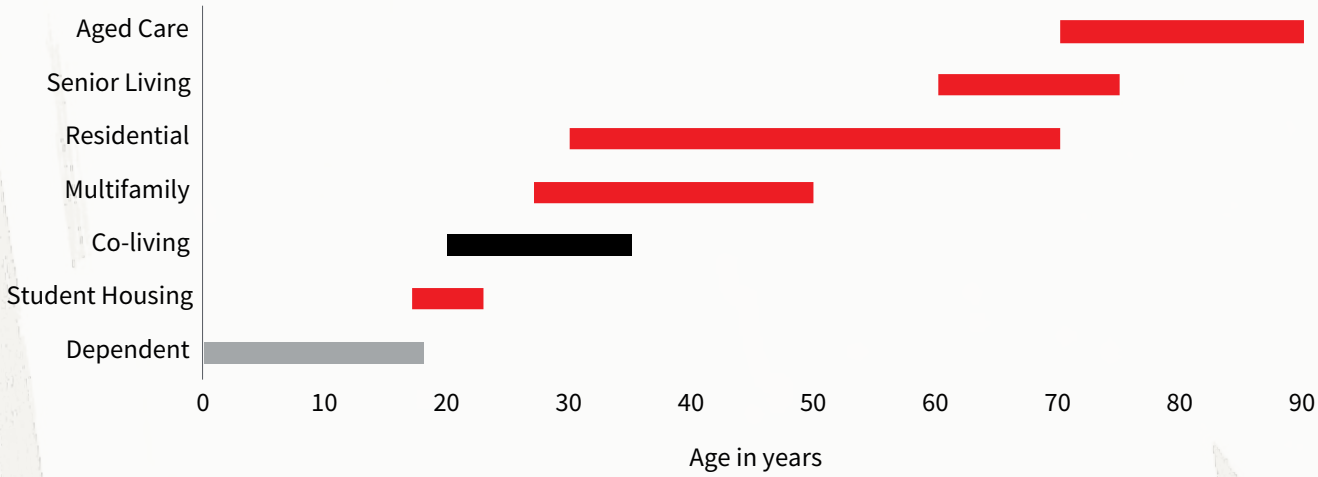
* The Organisation for Economic Co-operation and Development"

Dwelling prices to rent ratio (Indexed)



Source: JLL, various national statistics sites

Cradle to Grave



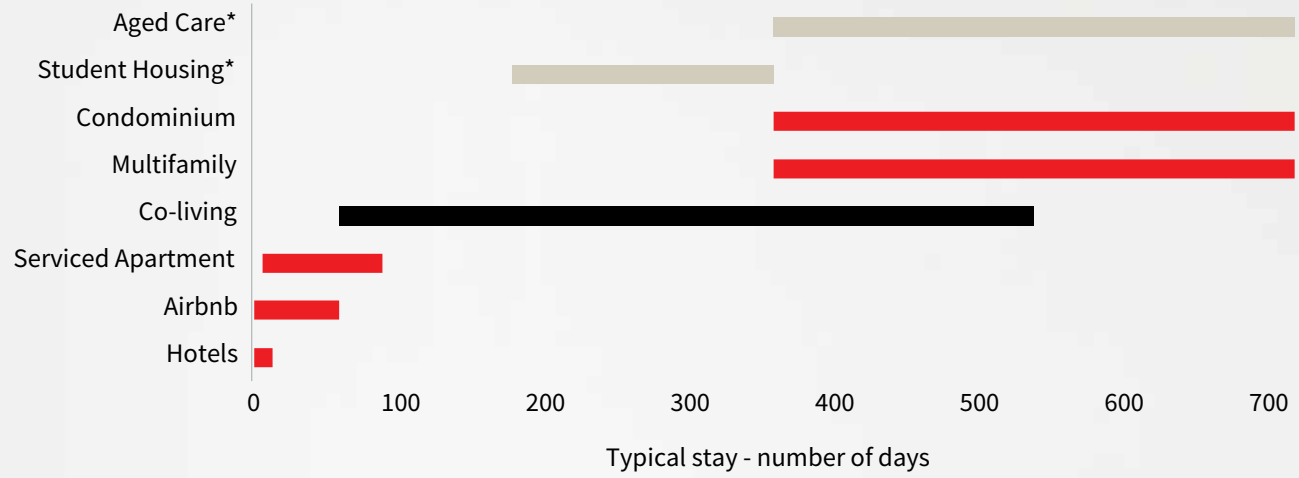
Source: JLL

Where co-living comes in.

The co-living sector is bridging the housing gap that isn't supported by any of the other living/accommodation categories. Most options tend to be easily defined by the typical length of stay of an occupant. Hotels for example have typical stays of a few days, with serviced apartments providing a solution for anywhere from a few weeks to a few months. Options for accommodation anywhere from a few months to a year, however, become less clear. Renting a condominium/multifamily unit for this timeframe is highly inefficient and costly given the move in/out cost, agent fees, lack of furnishings, requirement to set up utilities and the lack of willing landlords looking for shorter-term tenants. This is where co-living is filling a fast growing housing gap.

The corporate sector is also supporting demand for co-living, with more project-based relocations or short-term assignments that are 3 to 12 months. A length of stay that doesn't currently fall into any traditional sectors. This could also help to establish the next evolution of co-living, which will focus more towards older professionals in their 30's to 50's who value the community-based aspect of co-living while simultaneously wanting a higher level of privacy. This model could involve each member having a small private apartment, but also incorporate the community aspect and flexible lease terms, akin to co-living.

Living Tenure (Expected stay in days)



*Restricted Access
Source: JLL

Co-living: A tenant's perspective

There is a spectrum of rental costs for the varying co-living models in Asia Pacific. However, given the additional flexibility embedded in the lease contracts and the services provided to the tenants like cleaning and utilities, many question what the overall cost premium is compared to traditional residential.

While this premium or discount varies considerably across the various models, operators can create efficiencies in services and space. Through densification, operators can ensure there isn't a significant cost premium to traditional shared real estate.

We've broken down a cost comparison for a Singaporean co-living room compared to the cost of that same apartment under a traditional lease of 1 to 2 year lease. The headline rent in the co-living apartment under this scenario is 27% higher than the traditional rent model. However, after accounting for all expenses incurred by a tenant throughout a lease and considering things like the amortised lost value of furniture, exit cleaning costs and general maintenance, the real cost premium to live in a co-living (like-for-like) unit is around about 5% in this scenario.

In some cases, co-living can be cheaper than living in a traditional landlord-tenant model. There is no lease break costs or any applicable agent fees, not to mention the time saved on going through a traditional rental process. Managing the process of moving-in, moving-out and the ongoing logistics of living under a tenant-landlord model, that's intermediated by a property manager and an agent is highly inefficient and often frustrating. Dealing with a single company on all related issues, plus peace of mind regarding relocation or move-out creates huge upside for the tenant base.

Co-living - A Singapore example – Tenant costs for a room

	Standard shared lease (per room)	Co-living lease	Operator cost efficiencies created
Base rent (monthly)	1,500	1,900	
Utilities	60	0	✓
WiFi	20	0	✓
Cleaning	100	0	✓
A/C servicing (monthly amortised)	10	0	✓
Move in costs (amortised)	10		
Tenants share of maintenance amortised	20	0	✓
Amortised furniture cost	70	0	✓
Lease stamp duty amortised	5	0	✓
Exit cleaning costs amortised	15	0	✓
Value of your time to arrange all the above	Unquantifiable	0	
Value of the flexibility to leave when you like	Unquantifiable	0	
Total monthly cost	**$1,810**	**$1,900**	
Co-living cost premium	**$90**	**5.0%**	

Prices are based on a single room, sharing a 2BR unit, no ensuite, mid-end location, all prices in SGD

Co-living: An operator's perspective

The co-living profit model varies significantly due to lease structures and ownership models. Most co-living operators are asset light and try to work off a profit-sharing lease arrangement or management agreement, while others prefer fixed market based leases. Less common are co-living master-lease structures, however that structure may expand as the sector matures. Operators that are owned by developers or investors also create efficiencies on costs.

Co-living operator cost savings are driven by inefficiencies of a traditional residential building. Under a traditional residential model, there are three layers of fees. Firstly, a landlord pays a building manager to handle maintenance as and services of common space. Then a property manager is paid to collect rent and make sure the internal area of the apartment is maintained. Finally, you have a leasing agent who collect a lease fee upon successfully finding a tenant. When looking at co-living operators in whole buildings, they effectively act as all three (building manager, property manager and letting agent) without taking a fee from the landlord. In condominiums, a building manager will often already be in place however a co-living operator still takes the place of a property manager and a letting agent, again without cost to the landlord.

So using the same tenant and rental example as previously, co-living operators can remove outgoing line items for landlords, and in the process get potential rental discounts while still providing higher returns to landlords. Lease terms from co-living operators are often typically much longer than a traditional lease, often around 5 years plus extension options, and so landlords can also ensure limited downtime over a longer time horizon. The table shows an example of how these removal of fees even under a lower base rent can improve landlord net incomes.

Tenant vs Co-living operator (per room per month)

	Traditional Tenant	Co-living Operator	
Market Rent (monthly)	1,500	1,500	**Market rent (monthly)**
Occupancy rate	95%	10%	**Discount**
Average monthly rent	1,425	1,350	**Net monthly rent to Landlord**
Leasing/advertising cost (4% of rent)	71.25	0	**Leasing/advertising cost**
Management cost (6% of rent)	85.5	0	**Management cost**
Net to landlord	1,268	1,350	**Net to landlord**
Net annual (pre land tax)	15,219	16,200	**Net annual (pre land tax)**

Co-living model – gross margin per room

Base rental income
1,900

Occupancy
95%

Gross rental income
1,805

Rental payment to Landlord (as above)
1,350

Gross income to operator (monthly)
455

On a fixed rent basis, co-living operators can create a reasonable gross income by guaranteeing a fixed rent over a long lease term, which is favourable to the landlord. By assigning this responsibility to a co-living operator, a landlord's incentives are better aligned as the operating company has much stronger case to ensure that space is leased quickly. Most operators also now have waiting lists as demand is growing faster than demand in most major cities. Using the same example figures as above, we can see where co-living operators can etch out their revenue streams while providing potentially higher incomes to landlords and a service to tenants at no significant cost premium.

Operators can improve on the inefficiencies that would be created by a tenant if they were handling the general outgoings. Operators can create efficiencies of scale around things like utilities, WiFi and cleaning costs, as well as making huge savings on areas like furniture costs.

Using the same expenses as the earlier example, we estimate that the savings made by a co-living operator managing the operating expenses of residential property relative to an ordinary tenant is somewhere around about 25% of the total. The largest savings are made in areas like furniture (as the operator can source and buy wholesale), cleaning, and utilities due to their ability to scale operations. As the operators control the entire building, there are also opportunities to improve the utilities cost with certain technology currently being trailed, as well as through efficiencies of scale (WiFi) or installation of rooftop solar etc.

While not all costs are included in the above, like centralised staffing or technology costs, there are efficiencies made by the operator which can provide for a win-win-win basis for the tenant, operator and landlord. The tenants get the flexibility and the community aspect they are looking for, the operator can achieve a small rental premium on the tenant and boost their margin through alignment, and the landlord can remove the management intensity of the asset and potentially improve returns.

Tenant vs Co-living operator outgoings (per room per month)

	Traditional Tenant	Co-living Operator
Utilities	60	50
WiFi	20	15
Cleaning	100	70
A/C servicing (monthly amortised)	10	7
Move in costs (amortised)	10	5
Tenants share of maintenance amortised	20	20
Amortised furniture cost	70	50
Exit cleaning costs amortised	10	5
Total costs	**300**	**222**

Co-living model – gross margin per room

Gross income
455

Expenses
222

Operating income
1,350

Operating income per annum (per room)
2,796

"... there are efficiencies made by the operator which can provide for a win-win-win basis for the tenant, operator and landlord."

Co-living Around Asia Pacific

India is becoming the trailblazer of co-living in Asia Pacific. Younger generations, fast evolving consumer trends and the potential scalability of the market is a real drawcard for start-ups and developers looking to enter the market.

There are over 35 million tertiary students in India, with no significant purpose-built student accommodation (PBSA) operators in the market. Over 10 million of these students relocate to another city within India. As a result, some of the larger co-living operators like Stanza and Placio are targeting this student demographic and filling the void left by the lack of PBSA. This growing tertiary enrolment ratio and large number of students also means there is a large and rapidly growing base of young professional graduates. These young, well-educated professionals, particularly those from inter-state are one of the key demographics being targeted by co-living operators.

Most cities in India tend to have a fragmented traditional residential rental market, however there are various options at all ends of the budget scale. The co-living model is often focussed around convenience and community, rather than focussing on lower costs, however there are operators in that space. The process of moving inter-state and renting in the traditional sense has logistical hurdles in India. Those not yet married, or students without a stable income have traditionally been seen as a less attractive tenant option making the co-living product offering a readymade solution with a built in community is highly attractive to mobile professionals.

Institutional investors and venture capital firms have invested in the sector, with the likes of Sequoia (Stanza) Nexus Venture Partners (Zolo) and Goldman Sachs (Nest Away) already invested in the sector.

India

Co-living Around Asia Pacific

Japan's "gaijin" houses run a similar model to co-living, but they do vary. Gaijin is the word for foreigner in Japanese, and that's exactly the tenant profile these shared houses typically cater towards. These shared houses tend to cater to lower income earners, typically students or short-term English teachers and are often located away from the central areas.

More recently however, we have seen the emergence of more prime co-living products catering towards professionals – both foreign and domestic. Sharing apartments has not traditionally been common practice in Japan, instead dwelling sizes sit across a wide spectrum meaning those with low budgets tend to just rent smaller units. Renting units however, in Tokyo comes at a cost. Moving in expenses are typically 4-6 months of rent, making this option quite arduous to many – particularly those looking to move for less than two years. This is where co-living operators have a distinct advantage.

Upfront costs in leasing in Japan

Component	Component
Deposit	2 months
Key money	0-2 months
Agent fee	1 month
First months' rent	1 month
Insurance	0-1 month
Total	**4-6 months**

Japan (Tokyo)

Singapore and Hong Kong

Singapore and Hong Kong

Singapore and Hong Kong both have a small number of established operators, with many seeking rapid expansion. The target markets in Singapore are generally the transient expat population on the one hand, with another product looking to cater towards students. The continual churn of new expat arrivals and leavers provides a readymade base of demand, particularly for co-living products tailored towards lifestyle and convenience for a segment of the market with reasonable discretionary incomes.

While there is a growing number of Singaporeans moving into co-living spaces as well, the home ownership rate is high (over 90%) so the market is limited in that segment.

Hong Kong has a number of operators that seek to solve the affordability crisis. Many offer budget solutions with capsule style bedrooms or very small private offerings, while there are some newer operators now providing a more premium model.

The biggest challenge facing most co-living operators in both Singapore and Hong Kong is sourcing real estate. This is due to the lack of existing multifamily (en-bloc) property, meaning operators are looking at asset conversion strategies or built-to-suit development. Some operators also lease units in condominiums, which is providing an avenue for growth and placing emphasis on well-located properties and catering to a convenient living model for tenants seeking high quality residences. Also, the sector may start to receive more support from government, with the Singaporean government already having offered a land tender with a provision that the development must be a form of co-living.

China

China is among the most developed co-living markets in the world. The rapid evolution of the rental (multifamily) market is a key driver behind this trend, and is being strongly supported by government.

The rental market will be generally targeting the younger demographics as the home ownership rate is quite high among those over the age of 40. Several developers in China and are actively bidding on these land sites, earmarked for rental property and as a result have set up their own branded co-living operators. These operators therefore act as more of a subsidiary or management company, rather than a third-party operator. There are however more PE backed operators running an asset-light model entering the market.

Australia

Australia usually leads the Asia Pacific region in terms of its development of new or niche property classes. But, that's not been the case with co-living – Australia is playing catch-up to other markets. However, we've seen the announcement of several large operators with projects now underway more recently. Most operators are looking at built-to-suit product with some asset conversions underway. Due to the softer residential conditions, there is also an opportunity right now for investors to acquire multiple units in a development "in one line" at quite attractive discounts. The lack of multifamily build-to-rent (BTR) product makes accessing en-bloc scale difficult without undertaking development, however, similar sectors like student housing have developed quite quickly there.

Establishing the broader multifamily BTR sector remains a challenge. There remains a number of obstacles in place which also impact co-living from an investor standpoint – particularly around MIT tax status and the GST applicable on certain residential rental businesses. These problems are being looked at however, and co-living in Australia is expected to grow quite rapidly over the next few years.

What's *next?*

The co-living sector is still in the early stages of its potential development. It is likely that we will see the sector evolve further over the next few years to cater towards a broader tenant base. The general trend towards a more established multifamily market across most of Asia Pacific will also help in the establishment of the co-living sector.

In the next 12 to 18 months, JLL expects that in markets with under-developed student housing (PBSA), co-living will become an aggressive option to fill the gap for students. On the other end of the spectrum, it is likely that co-living will take more market share from the serviced apartment sector, as they can provide flexible leases on a more cost effective basis. We've already seen conversions of some underperforming serviced apartments into co-living buildings across Asia. Further to this, the added community aspect of co-living could allow the sector to draw a larger share of new arrivals to cities.

Over time we will also see more operators entering the market, each running a similar but somewhat differentiated business model. The co-living business model however needs scale to perform at the most efficient level. As a result, we expect that a number of the smaller operators or underperforming operators will be absorbed over time as many of the fast growing co-living operators have already rolled out M&A plans, particularly when looking to enter new markets.

Finally, a key challenge will continue to be around finding suitable real estate product. As a result, matching operators with investors and developers who have asset sourcing/development capabilities will be advantageous to all parties involved. Over time we're likely to see more build-to-suit product, however, developers will need to get more comfortable around the operating metrics of co-living.

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