Hines

Hines

The living sector is a global opportunity

Chase McWhorter, Institutional Real Estate, Inc.'s managing director, Americas, recently spoke with **Michael C. Hudgins,** senior managing director of research with Hines, about the overall attractiveness of the living sector. Following is an excerpt of that conversation.

What is your strategic perspective on the overall attractiveness of the living sector?

One thing that is absolutely clear to us is that the living sector is a global play, a sector with opportunity across all three global regions – the Americas, Europe and Asia Pacific. Sitting here in the United States, we all hear a lot about the U.S. housing shortage and think we have a lot to do here. But it turns out, there is a lot to do everywhere.

And the key drivers are similarly global themes. One, we have a global shortfall or deficit in housing. Two, we have a global problem with home affordability, really a problem in any major metro. Consequently, we have our third global theme, which is an increased proclivity to rent across most major developed economies over the past 10 years or so. This shift toward renting is supporting demand for rentals across many subtypes of the living sector – not just traditional multifamily but also single-family rentals, student housing and lot development. There are factors, however, such as differences in demographic growth trends or the existing scale of institutional-quality product, that vary in those regional markets, and those disparities lend especially strong support for specific opportunities by region.

When you talk about a global housing shortage, do you have any idea of the scale? How widespread is it really?

It is difficult to get homeownership data and housing inventory consistently across all countries. But Hines Research was able to analyze 14 developed economies.[1] We looked at how supply/demand dynamics since 2007 compared with pre-2007 trends. We think the global housing shortfall or deficit for those 14 countries is at least 6.5 million homes, and that is likely conservative. The deficit in the United States and developed Europe, for instance, is approximately 3 million each, with the rest of the shortage number representing several major markets in Asia and Canada. The number is net, so it includes the sum of countries with shortfalls and some with surpluses, such as France and Italy. In France, the surplus may be the prevalence of second homes for both domestic and international vacation homeowners. In Italy, many rural villages have emptied out as younger people moved to cities, leaving an oversupply of housing in those rural villages. When we look at the cities themselves – at Paris or Milan, for instance – they each look undersupplied by roughly 150,000 homes. But, as we mentioned, the housing shortage isn't just a U.S. phenomenon, but a global problem – or, from our perspective, an opportunity.

You talked about how homes have become unaffordable and how that may be supporting renting over buying. How does that play out?

We analyzed metros across the globe to compare disposable income per capita with home prices to arrive at a ratio of how expensive or cheap home prices are compared with the income households actually have to spend. We then compared the current ratio with each market's history over time. It is a technique Hines' research team uses to make data comparable whenever there are differences in the data available across a wide range of regional, country and particularly metro markets. Then you can look at that ratio and compare it with the historic trend for that actual metro. To make it even more digestible, we create a score, zero to 100, where 100 generally means the market is as expensive as it's ever been, and greater than 70 is statistically where it's meaningfully expensive. For 40 major markets we've analyzed, the average was greater than 80, which means it is more expensive now than during more than 80 percent of history. There are only a handful of markets screening "less than expensive," or less than that 70. More than half of them were closer to 90 to 100. Meanwhile, none was close to what we consider "inexpensive," or less than 30.

Now, what has that done for the rental market? During the past decade or so, most of those developed economies we analyzed – and we use the same list of markets that we use for the homeownership shortfall – have seen their home ownership rates fall. In fact, about 340 million out of the total 407 million households in those economies sit in markets where the home ownership rate has fallen. That's more than an 80 percent share. That is evidence for the proclivity to rent. Another way to think about it is as momentum in favor of renting. During the period we studied, renter households grew at a rate of about 15.4 percent, versus 8.5 percent for home buyer households. That's almost double the growth rate. If homeowner rates had not fallen, we would have added almost 6 million fewer rental households over that period.[2]

It sounds as if there are specific opportunities by region that have especially strong tailwinds for one reason or another. Can you discuss that?

There are living sector subtypes that have stronger tailwinds by region. In the United States, we see an especially compelling opportunity in single-family rentals or SFR. Related to that is lot development. A trend in U.S. demographics that has implications for the traditional multifamily sector concerns the traditional renter cohort, which we would define as younger people between the ages of 20 and 34. That cohort historically has leaned to renting over owning. The growth of that cohort over several decades served as a tailwind for new development or rental growth in existing apartment properties. But that cohort isn't growing like it has for the past 20 years. Moving forward, the number of persons 20 to 34 will most likely remain flat. But what is happening is that "renter" cohort is aging into a group of households aged 35 to 54, which we call the "raising children" cohort. As this cohort enters their child-raising years, it means more people and belongings per household create demand for larger spaces. In an analysis of all our U.S. renters, we found our raising-children cohort generates the strongest demand for single-family rental – including attached homes or townhomes. Interestingly, an additional finding was that cohorts of people older than 55 aren't far behind in their demand for single-family rentals. Given that older Americans may be healthier for longer, we think there could be a period of 10 or even 20 years where these cohorts also help SFR demand.

I also mentioned lot development. Constructing and then leasing up bespoke SFR communities may lead to attractive returns. If you find the land at a good price, you can build a bespoke community that's designed to offer activated space. Rather than a group of unrelated homes, you are creating the infrastructure and spaces where people can meet — a concept of community. Lot development, however, is horizontal development of raw land rather than the vertical development of constructing the houses. For this strategy, a developer such as Hines will secure entitlements to build out the basic infrastructure on big parcels of land. Then we can sell that land to homebuilders, who then have the option to create for-sale housing or purpose-built single-family rental communities.

What about European and Asian markets?

In Europe, the tailwinds are behind student housing. People worry about the weaker demographics for Europe, and rightly so. But one of the cohorts that is forecast to grow is a proxy for the secondary school cohort. There are also other drivers. International students in Europe tend to flock to higher-quality schools. Roughly 60 percent of the international student population in Europe goes to schools within Europe that are in the top 200 schools ranked on quality across the globe. In fact, the top 100 schools enjoyed enrollment growth of about 10 percent between 2019 and 2024. And around the top schools, rents are approximately 15 percent higher than the metro average for privately run student accommodations.[3]

In Asia, diversifying your living exposure across the entire region makes the most sense. It's an undeveloped region in terms of institutional-quality rental residential product. Investors have recently been very focused on the potential for Australian build-to-rent housing. Our concept is to build product that is amenitized, professionally run, and that addresses the evolving needs of student populations, older populations and renters in general. Home prices have fallen in Australia, improving affordability. But by no means are its major metro markets inexpensive. Brisbane and Sydney are clearly expensive per our research.[4] While Melbourne is more affordable, it's not inexpensive. Moreover, the housing shortfall is still acute in Australia.

Japan has long been the most established rental market in Asia, with a well-developed rental apartment market. What's interesting, though, is that with the return of inflation and wage growth there after almost 30 years of flatlining for both measures, we finally see the prospects of significant rental growth coming through to drive investor returns.

We see a further opportunity to meet investor demand for greater Asian exposure to the living sector through participating in the for-rent residential market in South Korea. The South Korean living market looks similar to what we might have seen in Japan 10 years ago. There is strong demand for rentals in South Korea. While there is some concern about the demographics in South Korea, our research indicates population growth is still expected to be moderately positive for greater Seoul over the next 10 years. Maybe more importantly, household growth is still positive, in part because average household sizes are decreasing. In Seoul, that household growth is driven primarily by single-person households in the under-35 cohort — a cohort more likely to rent.

What about the argument for just plain old multifamily in the regional markets?

There is plenty to do in all three regional markets in traditional multifamily. We believe the sector is strategically very attractive for investors. We think demand will continue given the fairly predictable support from secular demographic trends. The reality is that people do need a place to live, to go to school and to retire. And last, but certainly not least, are the sector's performance attributes. While apartment values and rents may be the first to fall in periods of uncertainty, they're also the first to recover. Across the globe, the apartment sector has only experienced two years of consecutive rent declines 14 percent of the time.[5] That's about half the average for the other major sectors. Multifamily is typically very reliable in terms of cash flow. There are markets in Europe where rent control may limit upside, and that's a negative, but they may also protect investors from declines. These are markets that a global investor can buy as a complement to places where rents are driven primarily by market forces. Finally, while the sizes of the European and Asian for-rent markets are much smaller than the U.S. apartment market, both regions are seeing increasing investor demand. That opens up the opportunity for the development of institutional-quality product.

In the United States, it's never been more affordable to rent versus buy. We believe this will drive demand for multifamily in addition to single-family rentals in the near future. But developers may need to think about the mix, offering larger apartments over studios.

Notes:

[1] Developed economies analyzed include Australia, Canada, Denmark, France, Germany, Hong Kong, Italy, Japan, Netherlands, South Korea, Spain, Sweden, United Kingdom and the United States.

[2] Past performance cannot guarantee future results. Sources: Oxford Economics, Eurostat, U.S. Census Bureau, Statistics Canada, Australian Bureau of Statistic, Statistics Korea, Hong Kong Census and Statistics Department, Statistical Bureau of Japan, Hines Research, as of 4Q 2024.

[3] Times Higher Education, Bonard, Hines Research, as of Q3 2024

[4] JLL, CBRE, Moody's, Zillow, ONS, Bulwiengesa, Rightmove, Nomisma, Newsec, Oxford Economics, Hines Research, as of Q3 2024

[5] JLL, CBRE, CoStar, NCREIF, Oxford Economics, Hines Research, as of Q3 2024. The analysis covers the period from the end of 2000 to present as ex-U.S. data becomes more consistently available across a wider range of markets.

CONTRIBUTOR AND COMPANY OVERVIEW

Michael C. Hudgins

Senior Managing Director of Research, Hines

Hines is a leading global real estate investment manager. We own and operate $93 billion* of assets across property types and on behalf of a diverse group of institutional and private wealth clients. Every day, our 5,000 employees in 30 countries draw on our 65-year history to build the world forward by investing in, developing and managing some of the world's best real estate. To learn more, visit www.hines.com and follow @Hines on social media.

* Includes both the global Hines organization and RIA AUM as of June 30, 2024

CORPORATE CONTACT

John Faust | Americas Lead of Institutional Investor Solutions

Hines | +1 415-399-6210 | John.Faust@hines.com