

Educating investors on a new asset class

Gerald Eve partners, in previous AF articles, have documented the willingness of investors to consider 'non-traditional' property investment classes as a result of the competitive investment environment. The continuing strength of the independent schools sector has led to its identification as a further specialist asset class that is set to continue to mature. Simon Chalwin, specialist property partner at Gerald Eve, charts the emerging opportunities in this property sector and assesses its prospects for further development.

The independent schools market is highly fragmented, much more so than many other business sectors, and has historically been characterised by few transactions. The majority of operators are charities and most operators only hold single assets. School properties that have come to the market have generally been sold with vacant possession and, in many cases, these have been purchased for alternative, commonly residential, use.

Venture capitalists and other financial institutions have recognised opportunities for investment in independent schools through either acquisition of the business or sale and leaseback and, in the public sector, through participation in public private partnerships as a result of the government's Building Schools for the Future (BSF) programme.

The education sector provides investors with the chance to purchase long-term cash flows generated by the school's business, secured on good, often freehold, properties. It additionally provides economies of scale by enabling investors to buy and develop groups of schools, particularly in geographic clusters.

Early investors

Prior to 2000, there were very few 'for-profit' groups of schools, with Asquith Court being one of the first to build up an independent schools group. A significant move in the market occurred in June 2002 when Alpha

Plus, backed by Sovereign Capital, acquired the former privately owned schools group Davies Laing & Dick.

Subsequently, in early 2004, a major international schools group, Global Education Management Systems (GEMS), entered the UK market with the acquisition of the former North Foreland Lodge School near Basingstoke. It followed this by buying the UK schools portfolio of Nord Anglia Plc in June that year. Four months later, Englefield Capital formed a new schools group, Cognita, which has quickly established itself as a leading provider of independent education with over 30 schools. Its most significant transaction involved the acquisition of Asquith Court's portfolio of 17 schools.

We believe that these relatively new entrants and their activities in the market have brought about a greater realisation of the potential value of school businesses and assets. This, together with the attractive characteristics referred to earlier, has resulted in a rising trend in school rental and capital values, and a growing number of sale and leaseback transactions.

Chalking up further purchases

Both existing schools groups and an increasing number of UK and foreign investors are now seeking to grow their portfolios in this sector. The Girls Day School Trust, Cognita and Alpha Plus are among those to have completed school purchases in the last few years.

Gerald Eve has recently agreed a letting of two charity schools in Swansea, South Wales, to Cognita, together with a transfer to them of the business, and the sale of two freehold interests, one in South Wales and one in North London, also to Cognita. All transactions were completed off market and in confidence.

For LaSalle Investment Management, we have recently provided property due diligence, consultancy and valuation advice on the acquisition of two schools in London, subject to new long-term leasebacks to the operator. The price reflected a sub 6% initial yield. We have also advised Alpha Plus on a recent acquisition.

This appetite for investment in the for-profit education sector was recently further demonstrated by the huge interest shown in the first private school to be purpose-built in London for generations. The school, part of a scheme by developer Ballymore on the Leamouth

“The focus on the independent sector has come at a time when independent pupil numbers are steadily growing. The 2007 Independent Schools Council (ISC) annual census revealed that pupil numbers in member schools had risen uninterrupted since 1995/96, with the exception of a slight decline in 2005. Numbers rose slightly, by 0.1%, between 2006 and 2007, with increases at nursery level and sixth form.”

Simon Chalwin

peninsula, opposite the former Millennium Dome, attracted 29 would-be operators. Ballymore is now considering including more new schools at its schemes.

The focus on the independent sector has come at a time when independent pupil numbers are steadily growing. The 2007 Independent Schools Council (ISC) annual census revealed that pupil numbers in member schools had risen uninterrupted since 1995/96, with the exception of a slight decline in 2005. Numbers rose slightly, by 0.1%, between 2006 and 2007, with increases at nursery level and sixth form.

Source: ISC 2007 Survey

Fee increases in 2006/07 averaged 5.9% which is close to the lowest average rise recorded by the ISC Census since 1999 and is probably a reaction to the very high fee increases in the last five or six years. This relatively buoyant performance needs to be viewed against parents' higher expectations, which are partially reflected in greater levels of capital investment by schools, and a reduction in teacher to pupil ratios, both of which can impact upon profitability. Fee concessions in charitable schools are also increasing and we would expect this trend to continue in the light of the new Charities Act.

A new school of thought

The government is also offering opportunities for public private partnerships through its BSF programme, which seeks to rebuild and renew virtually all of England's 3,500 secondary schools. This is being done through Local Education Partnerships (LEPs), bringing together a private sector partner (often a consortium including a contractor), the local authority and government body Partnerships for Schools.

The LEP enters into a strategic partnering agreement that gives it exclusive rights to deliver projects for a fixed period, likely to be 10 years. Schools are grouped together into large, high-value packages that provide greater economies of scale and streamline the procurement process. Roughly half of the schools will be procured through PFI contracts. Not surprisingly, many of the larger UK construction companies have signed up for the first in a series of 15 waves of schools between 2004 and 2016.

In the state sector, reference should also be made to the new Academies, which are primarily public-funded independent schools. There are expected to be 83 Academies open by September 2007 with a further 50 projected to open in September 2008. In return for a donation, private sponsors are able to participate in the

process of establishing the school, including its curriculum, ethos, specialism and building (if a new one is being built). Sponsors can be drawn from business, faith or voluntary groups working in partnership with central government and local education partners.

Timetable for growth

While opportunities for investment in the schools sector are currently limited by its ownership composition, the situation is improving as the market evolves and private sector owners increasingly recognise the advantages of releasing capital from their assets. For the private investor, schools provide the potential for solid returns, albeit they are more suited to the longer-term player seeking a steady performance and lower risk.

Over the next five years, we expect to see further consolidation, opportunities for sale and leaseback transactions and potential new entrants carrying on the evolution through secondary buyouts. **ACQ**



Simon Chalwin

DETAILS

Simon Chalwin
Partner, specialist property
Gerald Eve, London
www.geraldeve.com
schalwin@geraldeve.com
+44 (0)20 7333 6314