

# The Rise of Co-living in New York City



**Author: Parth Patel**

Parth Patel is a Master's candidate in the Baker Program in Real Estate at Cornell University's SC Johnson College of Business. Prior to attending Cornell, Parth completed an internship at The Habitat Company in which he assisted in a distressed workout of a 950+ unit multifamily portfolio. Parth has also helped assemble single family home REITs for institutional clients—including Blackstone's Invitation Homes, and developed luxury residential real estate on his own account. Parth is a graduate of Hope College in Holland, Michigan, where he studied Economics and Mathematics.





## EXECUTIVE SUMMARY

Co-living has taken off in the last year as a brand-new phenomenon within the multifamily real estate sector. Not only is it a new asset type for the general public but it is also the new niche asset type receiving a considerable amount of attention from institutional investors. So, what exactly is co-living? Is it something completely new as it is often talked about in many conversations in the real estate industry or is it rather a simple, modified version of a real estate asset type that we have grown to know incredibly well?

In this article I will begin with introductory remarks on what the co-living asset type actually is, and what it is not. I will then (1) briefly discuss the demographic that co-living operators are hoping to serve and whether or not the demand is sustainable, (2) illustrate a geographical overview of the current state of co-living in New York City, (3) provide insight into the link between affordability and the rise of co-living in those neighborhoods, (4) discuss the regulatory hurdles that co-living faces and the efforts that are being made by the real estate industry to overcome those hurdles, and (5) discuss how the institutional world views the rise of this niche asset type and what trends investors may look for as they seek to confirm the viability of their investment. Finally, summary remarks are at the end.

## INTRODUCTION

In a traditional multifamily business model, a group of non-familial individuals will form a household to rent a multifamily unit of two bedrooms or more to save money. This is a fairly common phenomenon in America. When this occurs each member of the group is liable for the whole lease if any of their counterparts fails to uphold their contractual obligations. This group will generally have a loose verbal agreement for how they will divide monthly rent, utilities, and upkeep of the common area. Furthermore, each member of the group will be subject to the same start and end date of the lease as well as high start-up costs that come from the time and resources spent on furnishing the common areas and setting up utilities.

Some industry leaders have come to recognize that not only do each of these issues represent a major source of potential conflict among roommates, but also that the high start-up costs represent a significant burden on the tenants. In order to overcome these hurdles and improve the experience for their tenant base, some multifamily operators are increasingly allocating a portion of

their portfolios to a different lease structure that has now widely come to be recognized as co-living.

Under the co-living lease structure each tenant signs a lease directly with the building owner to rent one of the bedrooms in a unit that otherwise feels similar to a traditional apartment or luxury student housing, removing the financial liability that would result if their roommates did not uphold their lease obligations. Each person will also have an individual start



Figure 1: An example floor plan of a co-living unit from WeLive property located in the financial district at the southern tip of Manhattan.

and end date, providing greater flexibility. Furthermore, these co-living operators are furnishing common areas, billing utilities directly to each tenant, and offering general cleaning and maintenance, creating a turn-key solution that makes it simple and easy for anyone to move into an apartment without having to invest significant time and resources. In fact, this ease and convenience cause some to opt for a co-living solution who would have otherwise opted for a studio, and do so at net savings compared to what a studio may have cost them. (Lee, Levine, Koles, & Dominguez, 2019)

The result is a living arrangement that looks and feels very similar to luxury student housing for adults. In fact, a typical floor plan of a co-living unit is very similar to a luxury student housing floor plan and includes a kitchen and a family room. Generally, there are two to four bedrooms that are private for each tenant with a private or shared bathroom. While slight variations exist, this is generally how co-living is organized across the industry.

There is also a misconception of what co-living is as a result of the narrative being used by industry leaders to describe it. While describing co-living, there is an emphasis on “experience” rather than the fundamental problem that the co-living operators are solving for their tenants: lack of flexibility, high start-up costs, and ongoing common area maintenance synonymous with traditional leases. For example, Rebekah Neumann, a former executive of WeLive, a co-living operator that is an offshoot of its better-known shared office platform, WeWork, remarked while introducing WeLive’s flagship property in New York City’s financial district that co-living “[i]s a new way of living, centered on community, and the belief that we are basically as good as the people we surround ourselves with” (Neumann, 2016). While WeLive could have created a multifamily building anywhere, it chose to do so in one of the least affordable neighborhoods in the country, which is not accidental as will be shown later in this article.

In another example, Brian Koles, Brand & Marketing Director of PMG, a Chicago-based operator with a nationwide real estate portfolio, said the following in his opening remarks at a millennial housing and co-living panel hosted by *The Real Deal*: “I think what we are seeing is a shift from just trying to find the biggest space for my budget to finding the best lifestyle, the best experience for my budget and that’s a lot of what we have built our platform around; don’t just build a regular boring apartment building, instead tell a

story that makes them feel like they are going to live their best life in that building, which has been very different from [the] institutional multifamily world” (Lee, Levine, Koles, & Dominguez, 2019).

Andy Levine, Director of Real Estate Partnership at Ollie, a co-living platform that proclaims to provide fully furnished units with hotel style amenities, immediately followed Koles’ comment by suggesting that while experience is important, the number one pain point is affordability for their cash strapped consumers (Lee, Levine, Koles, & Dominguez, 2019). Brian Lee, Senior Director of Real Estate at Common, a leading co-living operator, continued that millennials want the convenience and flexibility that they have become accustomed to with other shared economy solutions such as Uber (Lee, Levine, Koles, & Dominguez, 2019).

### **DESCRIPTION OF CO-LIVING’S TARGET DEMOGRAPHIC AND IS IT SUSTAINABLE?**

In 2019, Cushman & Wakefield completed a research assignment on behalf of Common that identified the underlying demand drivers for co-living. This study found that millennials are burdened by high student debt, have delayed family formation, and prefer to live in urban cores that are associated with a higher cost of living (Cushman & Wakefield, 2019). This report does an excellent job at providing insight into the current demand for co-living.

But what about the future of co-living? Is there sustained demand for this product type? In short, the answer is likely to be “yes” even if millennials’ lifestyle preferences change over time. As millennials age, a large portion of them may delay family formation as there is evidence of a link between feeling ready for marriage and feeling secure financially, including an ability to buy and own a home (Gurrentz, 2018). This, coupled with the fact that a larger share of young adults graduating from college is riddled with student debt, suggests many millennials will likely not be ready to become homeowners any time soon (Noguchi, 2019).

Further, there is little evidence to suggest a reversal of the current urbanization trends. One authority on cities, Edward Glaeser, Professor of Economics at Harvard University, stated that, “The rise and fall and rise of New York introduces us to the central paradox of the modern metropolis – proximity has become ever more valuable as the cost of connecting across long distance has fallen” (Glaeser, 2011). As new college graduates continue to enter the workforce with increasingly high student debt,

there are higher and higher economic incentives for them to pursue the best opportunities in gateway cities and continue to work and live there for longer periods of time. As long as these relationships continue to hold true, a large proportion of millennials may likely delay their plans for settling down for the foreseeable future, creating a sustained demand for co-living.

In addition, there may be additional demand from other groups on the horizon. The share of young adults (ages 23-37) who have been living with their parents has increased considerably in the last decade (Rental Housing Journal, 2019). In 2005, only 13.0% of young adults in the United States lived with their parents, but by 2017 that number had increased to 21.9% (Rental Housing Journal, 2019). Many young adults chose to reside at home as they struggled to find meaningful employment during the Great Recession. Meanwhile, the unemployment rate of those living with their parents is now only 10.3%, down from 19.5% in 2010 (Rental Housing Journal, 2019). As the number of unemployed young adults from the cohort that is currently living with their parents continues to shrink, a large number of them will become fiscally stable and likely provide fresh demand for multifamily markets, including co-living. It is reasonable to assume that many young adults searching for apartments with roommates for the first time in their early 30's would rather opt for co-living solution instead of, for example, an apartment they would find on Craigslist.

**GEOGRAPHICAL OVERVIEW OF THE CURRENT STATE OF CO-LIVING IN NEW YORK CITY**

This article relies on an examination of every co-living multifamily property in New York City that allowed its tenants to directly rent a bedroom from the landlord as of January 15, 2020. This list was then further refined to only

include those buildings that offered true turnkey solutions by including three important services: furnishings for common areas, direct billing of utilities without any burden on tenant for set-up, and general cleaning and upkeep for common areas. In total, there were 32 properties included in the study.

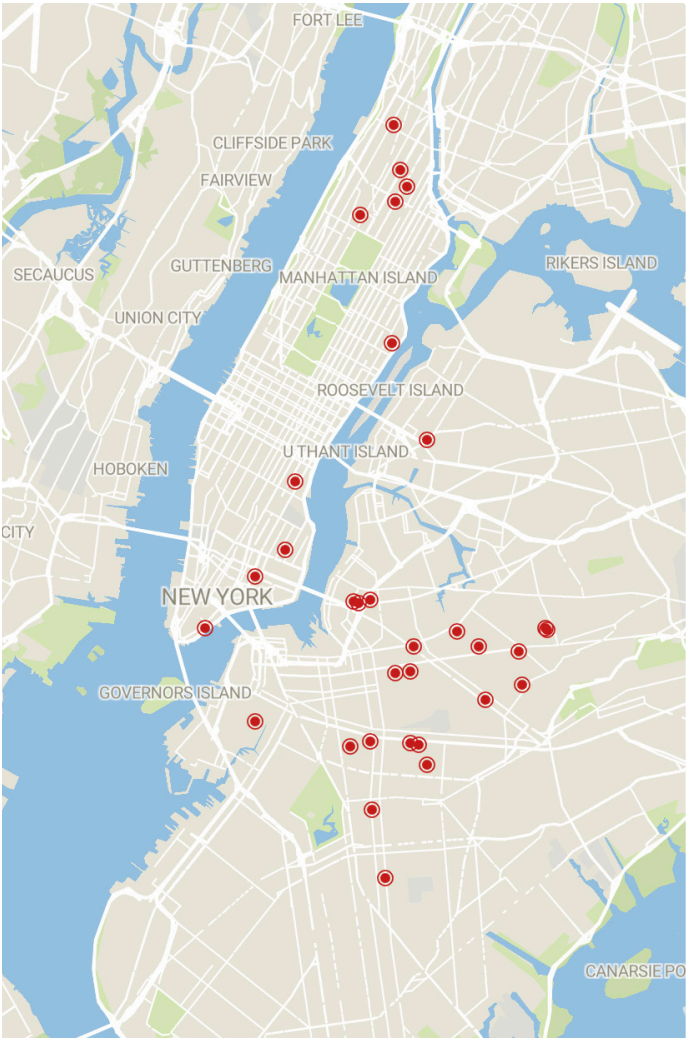


Figure 2: An illustration of co-living locations across the New York City.

| Group                            | Median Income per Capita | Median Household Income | Ratio (Annual Housing Costs / Median Income per Capita) | Ratio (Annual Housing Costs / Median Income per Household) | Ratio (Annual Housing Costs for Studio / Median Inome of Co-living) |
|----------------------------------|--------------------------|-------------------------|---|--|---|
| United States                    | 33,831                   | 61,937                  | 0.384   | 0.210  |   |
| New York State                   | 38,884                   | 67,844                  | 0.412   | 0.236  |   |
| Co-living Property Neighborhoods | 40,307                   | 64,233                  | 0.522   | 0.309  |   |
| Co-living Properties             | 75,000                   | 150,000 - 300,000       | 0.270   | 0.270  | 0.351   |

Table 1: Zip Code Level Analysis (Census Reporter, n.d.)

| Group                            | Median Income per Capita | Median Household Income | Ratio (Annual Housing Costs / Median Income per Capita) | Ratio (Annual Housing Costs / Median Income per Household) | Ratio (Annual Housing Costs for Studio / Median Inome of Co-living) |
|----------------------------------|--------------------------|-------------------------|---|--|---|
| United States                    | 33,831                   | 61,937                  | 0.384   | 0.210  |   |
| New York State                   | 38,884                   | 67,844                  | 0.412   | 0.236  |   |
| Co-living Property Neighborhoods | 74,911                   | 85,066                  | 0.535   | 0.301  |   |
| Co-living Properties             | 75,000                   | 150,000 - 300,000       | 0.270   | 0.270  | 0.351   |

Table 2: Census Tract Level Analysis (Census Reporter, n.d.)



## **AFFORDABILITY AND THE RISE OF CO-LIVING PROPERTIES IN NEW YORK CITY**

It is not a coincidence that co-living is focused in two boroughs of New York City – Manhattan and Brooklyn. As discussed in the introductory section of this article, it is certainly possible to create co-living properties with the primary focus on offering a “unique experience” to tenants anywhere in the country. In fact, it would be more cost effective to do that elsewhere if that was indeed the primary reason for co-living’s appeal among its tenant base as land prices are generally cheaper as you move away from the city core. Instead, co-living projects are heavily concentrated in the most cost-burdened neighborhoods in gateway cities across the country.

In order to assess how co-living’s affordability compares to its relative neighborhood, the ratio of gross income allocated to the housing costs for co-living was compared to the larger general neighborhood level data gathered from the U.S. Census Bureau. For co-living, the official monthly rates offered from owner-operators when the tenant chose to sign a twelve-month term were adopted – a length comparable to traditional multifamily leases and housing costs that a large majority of residents would be subject to during the census data collection.

In order to mitigate any bias, co-living’s affordability was compared to its respective neighborhood at both census tract level (a microscopic view) and zip code level (a macroscopic view). For co-living, a \$75,000 median income was used, based on comments made by Lee, the Senior Director of Common, in an interview (Lee B., 2019). A 30% cost savings from traditional (studio) housing was found based on an average calculated from the Cushman & Wakefield report and Levine’s comments during the previously referenced co-living panel.

As illustrated, both analyses show that co-living properties are located in neighborhoods that are significantly more cost-burdened and above the 30% threshold for the percent of gross income allocated to housing costs that is widely quoted in housing research. Furthermore, co-living properties are offering a reasonable entry point to tenants that would be priced out of a neighborhood otherwise.

## **REGULATORY HURDLES FOR CO-LIVING OPERATORS AND OPPORTUNITY FOR ZONING CODE REVISIONS**

When co-living first emerged a few years ago, it largely fell

in the regulatory gray zone. New York City did not officially offer a broad enough definition of multifamily buildings to classify co-living as a multifamily building. Most developers used provisions in the zoning code reserved for the hospitality industry to develop co-living properties, though they were subject to less favorable tax treatment as a result. While this was the case when co-living first emerged, it is fast changing with New York City’s Department of Housing Preservation and Development introducing a program called ShareNYC – a pilot program for affordable co-living developments.

An active effort is being made by more established co-living operators such as Common to work with New York City to broaden the definition of multifamily properties (Lee B., 2019). Even more surprising is that New York City has been receptive and views co-living as an opportunity to meet its Affordable Housing 2.0 agenda of creating and preserving 300,000 affordable housing units by 2026 (Warekar, 2018). While it is clear from earlier analysis in Section 3 of this article that co-living does indeed bring more people into a neighborhood who would have otherwise found it unaffordable, co-living now attracts a different demographic than does typical affordable housing. One striking number is that, in the study area, the median income per capita for a co-living resident is higher than the overall median income per capita of the co-living resident’s neighborhood’s traditional makeup at both the zip code and census tract level.

## **INSTITUTIONAL VIEW ON CO-LIVING AS AN INVESTABLE ASSET TYPE**

No official known survey exists summarizing the institutional viewpoint of co-living at this time. Most of the interviews held during the research process displayed a healthy level of skepticism that is reminiscent of the attitudes toward luxury student housing a little more than a decade ago. Some companies, however, are beginning to take positions on co-living. For example, Invesco has published a favorable viewpoint in its white paper for co-living investments (Unger & Tan, 2019). Cushman and Wakefield has also been actively raising a \$1.5 billion fund for Six Peak, a New York-based firm with the exclusive goal of investing in the debt and equity of co-living properties (Real Estate Weekly, 2019). These examples represent early enthusiasm for co-living from institutional firms.

Co-living’s fate as an investable asset type will largely depend on the risk premium that the institutional world assigns to it compared to traditional multifamily property.

According to some in the industry, student housing is a great case study from which we can see that cap rates have followed traditional multifamily cap rates and that the spread between the two has narrowed over the years as more institutional capital continues to flow into the space. While no official data set of nationwide trends on co-living cap rates yet exists, reputable developers interviewed as part of the background research for this essay stated that they are underwriting potential investments at 40-60 basis point discount compared to traditional market rate multifamily development. This spread is very similar to luxury student housing even without an established track record, and there are number of explanations for this according to those in the industry:

1. The institutional world has deemed co-living investments as having a similar risk profile to student housing and therefore feels comfortable with a similar discount to multifamily cap rates.
2. There is an overenthusiasm for co-living and the institutional world is willing to deploy capital quickly though over time the spread may increase.
3. While the institutional world recognizes that there is significant risk associated with operating a new type of multifamily property, it is motivated to deploy capital in niche asset types due to excess dry powder.

## CONCLUSION

With strong demographic trends and a clear affordability crisis in gateway cities, co-living may serve as a solution if it is integrated thoughtfully. While it is helpful to continue to innovate and find solutions to underlying problems, developers must not lose sight of what it is that they are actually solving. Although it is helpful for co-living operators to improve the living experience of their residents, it should not come without a solution to the fundamental problems of affordability, flexibility, and convenience.

It is also important to acknowledge that this essay only serves as a starting point while empirically confirming the widely held belief that affordability is one of the principal driving forces behind the rise of co-living. Our research demonstrates that, while New York City's integration of co-living in its affordability initiative improves affordability for some, it does so at the expense of affordability for others. Further, some of the experts interviewed for this essay

widely cited that it is New York City's zoning regulations that have played a significant role in creating the affordability crisis in the first place.

Finally, in light of the COVID-19 outbreak, it is important to keep in mind that co-living operators face significantly higher operational challenges because their responsibility extends beyond the corridors of the building and into the shared family room and kitchen area of each apartment. With that, at least some of the properties that were previously financially feasible may face an uncertain future as they seek to provide safe living conditions for their residents.

## WORKS CITED

- Cushman & Wakefield. (2019). *Survey of Coliving Landscape*. Chicago.
- Glaeser, E. (2011). *Triumph of the City*. Penguin Press.
- Gurrentz, B. (2018). Millennial Marriage: How Much Does Economic Security Matter to Marriage Rates for Young Adults? *U.S. Census Bureau*.
- Lee, B. (2019, March 8). How will New York City zoning and housing regulations change to accommodate co-living? (L. Bujarski, Interviewer)
- Lee, B., Levine, A., Koles, B., & Dominguez, M. (2019, October 10). Millennial Housing & Co-Living. (D. W. Katherine Kallergis, Interviewer)
- Neumann, R. (2016, May 25). Office-sharing company WeWork expands to WeLive. (V. Duthiers, Interviewer)
- Noguchi, Y. (2019, February 1). Heavy Student Loan Debt Forces Many Millennials To Delay Buying Homes. *NPR*.
- Real Estate Weekly. (2019). Cushman & Wakefield tapped to raise \$1B for co-living investor. *Real Estate Weekly*.
- Rental Housing Journal. (2019, May 7). More Than One in Five Millennials Still Live With Parents. *Rental Housing Journal*.
- Unger, S., & Tan, J. (2019). *A case for co-living*.
- Warerkar, T. (2018, November 1). NYC launches pilot for affordable co-living developments. *Curbed New York*.
- WeLive. (n.d.). *WeLive 3-bedroom Floor Plan*. Retrieved from WeLive.com: <https://www.welive.com/new-york-city/>