The Profitability of Converting Single Family Residences into Multi-Unit Student Rental Housing in San Luis Obispo

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This paper explains how a comparative case study was conducted to determine why some single-family homeowners in the San Luis Obispo area are converting their residences into multi-unit rental properties that can be rented out to several students rather than one family or couple. Through individual, semi-structured interviews, information was gathered on the homeowners’ thoughts and experiences regarding the process and results of construction, the rental market as a whole, and the newly realized convenience or difficulties associated with the change in client base. It is important to note that one of the properties is divided into two sections. One of these sections is dedicated to multiple student rental units while the second section is where the homeowner lives and manages the property. The second property is divided into four units that are occupied only by students while the homeowner lives and manages the property in a separate location. This distinction enables the comparative case study to identify what may contribute to the convenience or difficulties associated with coordinating these multi-unit rental properties. Both homeowners found the conversions to be profitable even with their different situations and levels of conversion.

Key Words: Rent, Property, Student Housing, College Town, Profitability

Introduction

The student housing market in San Luis Obispo, like any college town, is flooded with students who are looking to move off campus and create a home for themselves. Whether it’s apartment complexes, single-family homes, or multi-unit rental properties, property owners generally have little to no trouble finding tenants each year. The high demand for student housing is being viewed by some single-family homeowners as an opportunity to increase their monthly rental revenue. These single-family homeowners in the San Luis Obispo area are dividing their properties into multiple units that can be rented out by one or more students. By increasing the number of residents per property, the owners are able to increase the monthly rent while still providing affordable housing options for the students. While the increase in monthly revenue tends to be the driving force behind the decision to convert single-family residences into multi-unit student rental properties, this paper will also take a look at other added benefits and possible drawbacks of these conversions. The topics of resale value and maintenance costs should be looked at when considering the profitability of these conversions.

Market Research

At the beginning of the project, market research was conducted in order to find information relating to San Luis Obispo’s general population and housing market. The purpose of this research was to understand how heavily Cal Poly’s student body impacts the city as a whole, and how that younger demographic influences housing needs and prices. This market research serves as a foundation for the semi-structured interviews and really helps to provide an understanding of the student housing situation as a whole. It is also important to understand the effect that the student housing market has on the general population, and how an increase in multi-unit student rental housing options will amplify or mitigate those effects.

All of the information contained within this market research is pulled from the city of San Luis Obispo’s General Housing Plan Element for 2014-2019. The majority of the information that is used within the housing element is
taken from 2010. While this information may seem outdated, the city of San Luis Obispo states within the housing element that the general trends are expected to continue throughout 2020 and possibly even to 2030. This means that the numbers may not be exactly true to the current state of San Luis Obispo’s housing market but they are still relevant to the student housing situation that is covered by this project.

This chart shows the age distribution of San Luis Obispo. The graph clearly shows that the largest age group within San Luis Obispo is 20-24 years old. This is the group that consists of nearly all of Cal Poly’s students. According to the housing element, the 20-24 age group makes up approximately 35% of San Luis Obispo’s population. It is important to realize that these students are far less likely to own property within the San Luis Obispo area than the older age groups. This means that while the 20-24 age group makes up around 35% of the general population, they make up an even larger portion of the renting population. This creates an issue within the housing market where there is a greater number of low-income renters than there are affordable living spaces available.

<table>
<thead>
<tr>
<th>Approximate Income Categories</th>
<th>Income Limits</th>
<th>Number of Households</th>
<th>Percent of total households</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extremely Low</td>
<td>Income &lt; $24,999</td>
<td>6,288</td>
<td>33%</td>
</tr>
<tr>
<td>Very Low</td>
<td>Income $25,000 - $34,999</td>
<td>2,014</td>
<td>11%</td>
</tr>
<tr>
<td>Low</td>
<td>Income $35,000 - $49,999</td>
<td>2,285</td>
<td>12%</td>
</tr>
<tr>
<td>Moderate</td>
<td>Income $50,000 - $74,999</td>
<td>3,116</td>
<td>17%</td>
</tr>
<tr>
<td>Above Moderate</td>
<td>Income &gt; $75,000</td>
<td>5,228</td>
<td>27%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>18,931</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>
According to the housing element, approximately 56% of people or families that are renting in San Luis Obispo fall into the extremely low to low-income categories. The combination of the majority of San Luis Obispo residents having low levels of income and the increasing cost and demand for rent means that many people who work in San Luis Obispo cannot afford to live there. While students also technically fall into the extremely low to the low-income group, they generally have significant financial support from parents or family. Single-family homes can also legally house up to five adult students. This gives the students the ability to divide up the total cost of rent which allows them to pay higher than the average resident or family. This means the group that suffers significantly from this housing situation is the people and families in San Luis Obispo who are struggling to afford their rent. The housing element goes on to point out that the median renter in the city of San Luis Obispo was spending 48% of their income on housing. This is much higher than the statewide average of 33%.

### Methodology

The research for this paper was conducted through a comparative case study of two multi-unit rental properties in the San Luis Obispo area that were previously considered to be single-family residences. Semi-structured personal interviews with each of the homeowners or property managers are the sources for the qualitative data that is used in conjunction with market trend research to determine the profitability of these property conversions. The end goal of this paper is to present single-family homeowners in the San Luis Obispo area with new information regarding the process of converting their single-family homes into multi-unit student rental properties. Ideally, this new information will encourage more single-family homeowners to convert which will provide more available housing for students while simultaneously increasing rental profits for the property owners.

### Interviews

For each of the locations included in this project, a quick list of ten interview questions was created and presented to the managers of each property. However, the structure of the interviews was loose and did not follow a one-by-one question format. The interviews flowed in a more natural and conversational manner which allowed for all the important topics to be covered while still allowing the property managers to insert their own ideas and knowledge where they felt it was needed. The tenth and final question was also added to the list in order to ensure that they didn’t feel locked in by the list of questions that were being asked. The goal was to encourage the property managers to present any relevant information that didn’t come up during the interview even with the loose and free-flowing structure of the interview. Here is the list of ten main topic questions that was presented to the property managers:

- How many units are there?
- Are the units metered separately for gas/electric/water?
- What is the average rental price per unit?
- What is the average number of students per unit?
- What construction went into converting the home?
- Do you believe the total rent is higher now than if you would have rented to a family?
- Do you believe the increase in rent will make the cost of construction worthwhile?
- Are you concerned with resell value of house going down, or are you planning on selling in future?
- Are you happy overall with the choice to convert the home?
- Is there anything I haven’t asked about that you believe is important to consider?
The single-family residence at 125 Longview Lane was built in 1953 and is currently 3,224 square feet. That square footage is divided into six bedrooms and four bathrooms. Five of the six bedrooms are rentable rooms that are currently occupied by Cal Poly students. The rooms are small, bedroom-sized units that house one person each. The rooms are not metered separately which means that the property owner and the renters simply split the total utility expenses each month. Each student pays around $900 each month in rent which includes utility expenses. The only kitchen is accessible only by the sixth room where the property manager resides. The students essentially pay for a place to sleep and access to basic utilities. The only form of conversion that went into the home was the installation of dividing walls to form multiple bedrooms for students to rent out. Avoiding the installation of a second kitchen area for the renters to use helped to greatly decrease the construction costs associated with the single-family home’s conversion. While this minimalistic form of living may seem unattractive to many renters, there seems to be no issue with finding students to fill the rooms. This is most likely due to the home being located so close to Cal Poly’s campus.

The property owner explained that she definitely believes the rent is significantly higher with students than it would have been if she had rented out to a family. Part of the reason for this is because she believes that being located so close to campus is a benefit to students but not necessarily to a family. However, she explained that when she acquired the house, she planned to live there rather than rent it out to someone else. Including the student units was simply a way to capitalize on a large amount of space provided by the home. She stated that ultimately, she was happy with the way the conversion worked out. The process was apparently relatively quick and easy due to the simplicity of the project. When asked about the issue of resale value being affected by the now unusual layout of the house, she stated that she is not planning on selling the home anytime soon, but she believes that there are plenty of buyers in San Luis Obispo who are looking to buy rentable properties. She doesn't believe she will have an issue with finding a buyer for a fair price in the future. She said that there aren't any important factors that come to mind that weren't covered in the interview.

The multi-family residence at 526 Kentucky Street is a collection of two single-family style homes which were built in 1905. The two buildings consist of a total of 4,436 square feet and are divided into six units. The front house is made up of four units that each take up one corner of the building. The back house is split in half with each unit sharing a single wall. The property manager lives off the property, and he manages more than one of these multi-unit rental properties. The residents are currently all Cal Poly students. The rental units are metered separately which means that each portion of the house gets their own utilities charge. This utility expense is not included with their monthly rent which varies per unit. On average, there are 2-4 students per unit. This is because the units are larger than the size of a studio apartment. Each unit has its own kitchen and dining area and a bathroom. The two buildings also have a small shared parking lot and an outdoor area with a grill and space for a table. While all of these additions added to the cost of converting the two buildings into six different rentable units, having more than one student per space allows him to increase the cost of rent while still keeping rent affordable.

The manager stated that he knows the rent is much higher now than if the properties were rented out as two single-family residences. He also claimed that it is much easier to find students looking for housing than to rent to non-students. Often times when students move out, they will already have recommendations for friends of theirs who are looking to move in. The simplification of this process makes his job easier. Students are also more likely to be comfortable with less space and fitting more students per room. This allows him to increase the cost of rent which helps to cover the initial costs of construction. He is currently not concerned with the resale value of the house going down because he doesn't believe anyone looking for a single-family home would be interested in the property. It is possible that a person or company in his position would be looking to buy another house to manage, and he believes they will pay a good amount for an established property. He believes that the conversion process was worth the time and effort he put into it and considers it to be a profitable investment. He also informed me that the one thing I hadn't covered was the increase in maintenance costs associated with renting to students. According to him, students are far more destructive and less respectful of his property than non-students. The increase in costs of repairs and cleaning that goes into keeping the home clean is significant, but don't prevent the property from being a bad investment.
Conclusion

Based on both of the interviews, it is safe to say that each property owner considers the conversion to multi-unit student rental units to be worthwhile and profitable. Even though not every single-family homeowner is looking to go through the process of converting their home for students, the differences between the two properties covered by this project show that there are multiple scenarios that allow for a profitable conversion. This can most likely be attributed to a large number of factors that influence the cost of conversion and the price of rent. For example, the simple style of living for students at 125 Longview does not deter students from living there. This shows that a complete redesign of the home is not necessary in order to attract renters. At 526 Kentucky, the more complex conversion process is offset by the higher rent costs. Each of these properties has its advantages and disadvantages for the renters and owners. The key to making these conversion processes profitable is finding a balance between the two. Ultimately, it is up to the homeowner to decide how much time and effort they are willing to put into this type of project and determining if they can make a profit given their expected rent income.

Another important idea to take away from this project is the benefit that additional student rental units will have on the city of San Luis Obispo. The market research showed that the large number of students who are renting apartments and homes in the city of San Luis Obispo is making it difficult for San Luis Obispo's residents to find affordable housing. If more single-family homeowners in the area convert their properties to make room for more students, it may free up rental space that can be utilized by San Luis Obispo residents.
References


