Financialization of Purpose-Built Rental Housing

Written submission to the Review Panel on financialization of the National Housing Council / Conseil National du Logement (NHC-CNL)

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Housing connects local geographies of home, community and indebtedness to national and global geographies of mortgage funding, institutional investors and interlinked crises. Housing, like other forms of real estate, provides a critical outlet for investments, a place where capital can be invested in—"fixed"—and thereby locked into a place for a period of time.[1] The absorption of capital by real estate is one of the defining characteristics of the current **finance-led economic growth model**.[2]

The phrase "financialization of housing" suggests that housing is increasingly becoming more dependent on finance. It does not mean that housing is completely or only related to finance. The noun-suffix "-ation" denotes an action or process. The most basic **definition of "financialization"** would then be the process of becoming finance-like. A broader definition could be: "the increasing dominance of financial actors, markets, practices, measurements, and narratives, at various scales, resulting in a structural transformation of economies, firms (including financial institutions), states, and households."[3] This definition implies that financialization is made up of different processes, located at multiple scales.

At times, financialization is simply used as shorthand for the increasing reliance of mortgage lending, and therefore debt, to finance homeownership. Yet, there are many additional forms and expressions of the financialization of housing, some better studied than others. In many countries around the globe, we also see **a range of funds that have entered the rental housing market** in the past 20-25 years: private equity firms, hedge funds, Real Estate Investment Trusts (REITs) and publicly listed real estate firms.

[1] Harvey, D. (1985) *The Urbanization of Capital. Studies in the History and Theory of Capitalist Urbanization*. Oxford: Blackwell.

[2] Fernandez, R. and Aalbers, M.B. (2016) Financialization and housing: Between globalization and varieties of capitalism. *Competition and Change*, 20(2): 71-88.
Hofman, A., & Aalbers, M.B. (2019). A finance- and real estate-driven regime in the United Kingdom. *Geoforum*, *100: 89-100.*

[3] Aalbers, M.B. (2019) Financialization. In: D. Richardson, N. Castree, M.F. Goodchild, A.L. Kobayashi, W. Liu and R.A. Marston (Eds) The International Encyclopedia of Geography: People, the Earth, Environment, and Technology, DOI:10.1002/9781118786352.wbieg0598.pub2. Oxford: Wiley.

These different players may have different investment strategies and horizons. Generally (but not necessarily), **private equity and most hedge funds rely on short-term investment strategies** of "buying low and selling high."[4] They operate in a financial web of multiple actors, holding companies, loans and securitizations, which makes it difficult to conceptualize who really is the landlord and to whom tenants should address their grievances. Private equity firms have a short-term focus (3 to 5 years), are highly leveraged and typically invest little in maintenance. Some of their real estate acquisitions are so over-leveraged that the average rent per unit is lower than the cost of servicing the debt per unit, i.e. the rent does not even cover the interest on the loans that were taken out to acquire these properties in the first place.[5]

In cities like New York and Berlin the financial expectations of the private equity firms often did not materialize. Making money on subsidized rental housing turned out to be harder than expected. Some of these firms simply have collapsed, others had to readjust their strategies: both rents and sales brought in less money than expected and buy- hold- and sell-plans had to be adjusted accordingly. As a result of the crisis, accessing external finance, crucial for the business models of private equity and hedge funds, became so difficult that most were **forced to sell off their portfolios**. However, financialization did not stop or halt; many private equity funds were converted into REITs and listed real estate companies, and housing portfolios were sold directly to listed real estate funds. We refer to the take-over of housing portfolios by REITs and listed real estate funds as **the financialization of rental housing 2.0**.[6]

Unlike private equity and hedge funds, **REITs and listed real estate companies adopt a mid- to long-term investment strategy to create stable cash flows for their shareholders**. They seek to create a "rentier structure" to optimize cash flows, rental income and capital gains through the sale of individual housing units. While shareholders expect a maximization of shareholder value, listed real estate companies typically seek returns of 4-6% annually and are thus devoted to creating continuous cash flow and operating income by renting out housing units and selling individual units at profitable prices. Secondly, **they seek to enhance the net value of the portfolio, for instance by focusing on core investment strategies, stimulating gentrification effects through asset modernization and refurbishments, evicting tenants, and "gaming" rental regulations**.[7] Instead of the pure speculative strategies of "buying low and selling high", the new landlords focus on mid- to long-term real estate management. Nevertheless, REITs and listed real estate companies primarily aim to extract (potential) value from housing. The shift towards financialization 2.0 does not signify a radical break with financialization 1.0, but rather a continuation with different means and strategies. The table below provides a summary of the investment strategies of REITs and listed real estate companies compared to social/public housing companies as well as private equity and hedge funds.

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[4] Fields, D. and Uffer, S. (2016) The financialisation of rental housing: A comparative analysis of New York City and Berlin. *Urban Studies*, 53(7): 1486-1502.

[5] See previous footnote.

[6] Wijburg, G., Aalbers, M.B. and Heeg, S. (2018) The Financialization of Rental Housing 2.0: Releasing Housing into the Privatized Mainstream of Capital Accumulation. *Antipode* 50(4): 1098-1119.

[7] Bernt, M., Colini, L. and Förste, D. (2017) Privatization, financialization and state restructuring in East Germany: The case of 'Am Südpark'. *International Journal of Urban and Regional Research* 41(4): 555-571.
Beswick J, Alexandri G, Byrne M, Fields D, Hodkinson S and Janoschka M (2016) Speculating on London's housing future. *City* 20(2) 321–341.

Investment strategies of different types of landlords (*Source: Wijburg et al., 2018 – footnote 6)*

Company structure (landlord) *Characteristics*	**Social and public housing company**	**Private equity and hedge funds (financialization 1.0)**	**Listed real estate companies/REITs (financialization 2.0)**
Principal activity	Providing affordable housing for low- and moderate-income households	Buying low and selling high	Managing and maintaining income-producing real estate assets
Debt structure	Fiscal and financial subsidies, bank loans	Low equity and high debt, often through offshore finance (highly leveraged)	Capital markets and offshore finance
Profit versus risks	Non-profit, long-term	High risks, high profits, short-term	Medium profits, low to medium risks, long-term
Tenants	Security of price and tenure	Insecurity of price and tenure	In/security of price and tenure

In **Canada** the rental housing that investors buy up is often referred to as "purpose-built rentals", but this is a bit of a misnomer since most of the rental housing was built previously and is acquired, as part of a real estate portfolio, by investors. This is an important distinction, as it also implies these **investors add little or no housing units to the overall stock**. It is commonly argued that investment in housing should be encouraged to solve housing shortages, but if investors acquire existing housing units, this will do little to solve housing shortages. In fact, in most cases investors will try to **raise rents** to make up for the higher price they paid for the housing units as well as to satisfy shareholders. In other words: if investors buy up existing housing units, the effect on the housing stock is neutral at best, and creating rent increases and displacement for tenants at worst.

Another important issue is that **investors have expanded from investing in middle- and upper middle-class single- and multi-family homes to student housing, care and nursing homes, RV sites, employee dormitories**, and so on, not only internationally[8] but also in Canada.[9] The situation of these new asset classes is a bit more complicated, as some investors buy up portfolios of existing affordable housing stock, whereas others focus on new

[8] Aalbers, M.B., Taylor, Z.J., Klinge, T.J. & Fernandez, R. (2023) In Real Estate Investment We Trust: State De-Risking and the Ownership of Listed US and German Residential Real Estate Investment Trusts. *Economic Geography*. 99, 3: 312-335.
Aveline-Dubach, N. (2022) Financializing nursing homes? The uneven development of health care REITs in France, the United Kingdom and Japan. *Environment and Planning A: Economy and Space*. 54, 5: 984–1004.
Horton, A. (2021) Liquid home? Financialisation of the built environment in the UK's "hotel-style" care homes. *Transactions of the Institute of British Geographers*. 46, 1: 179-192.

[9] August, M. (2020) The financialization of Canadian multi-family rental housing: From trailer to tower. *Journal of Urban Affairs*. 42, 7: 975-997.
August, M. (2022) Securitising Seniors Housing: The Financialisation of Real Estate and Social Reproduction in Retirement and Long-Term Care Homes. *Antipode*. 54, 3: 653-680.
Revington, N. & August, M. (2020) Making a market for itself: The emergent financialization of student housing in Canada. *Environment and Planning A*. 52, 5: 856-877.
Revington, N., & Benhocine, C. (2023) Financializing Through Crisis? Student Housing and Studentification During the Covid-19 Pandemic and Beyond. *Tijdschrift voor Economische en Sociale Geografie*. doi:10.1111/tesg.12549.

investment. In both cases, there is a tendency to drive of rental prices, which comes at the expense of current or future tenants.

Here are **five key actions that governments can do to take action to curb the financialization of housing**:

1. The federal government should ask the question: it is fair to provide REITs with a tax advantage? Should it **create a level-playing field** where tax advantages are not selectively doled out to one set of actors?
2. Different levels of government should consider cooperating with not-for-profit, community, grassroots, and other **affordable housing providers**. They could also consider directly building or managing housing stock.
3. This one should be a no-brainer: governments should **regulate rental housing markets better, starting with regulating rent price increases and outlawing no-fault evictions**. Governments often fear that this will deter investors. But if investors are buying up existing housing stock with the main aim of increasing rents, deterring them would be a positive outcome for tenants and society at large. Existing landlords can continue to make a profit if rents follow inflation (or income/pension levels).
4. Local governments can use their **zoning and land use powers** to require inclusionary and affordable housing.
5. Finally, the government should **limit monopolies** when one landlord is dominant in one market segment, e.g. rental flats within a certain price range or units within a particular neighbourhood.[10]

Some of these solutions, along many others, are discussed in a range of reports and white papers that are highly recommended to anyone trying to improve housing markets through regulation and effective policies for affordable housing.[11]

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[10] Bernt et al. (2017): see footnote 7.
Charles, S.L. (2020a). The financialization of single-family rental housing: An examination of real estate investment trusts' ownership of single-family houses in the Atlanta metropolitan area. *Journal of Urban Affairs*. 42, 8: 1321-1341.

[11] Below are some recent examples of reports and papers discussing a wide range of policy solutions:
Farha, L. (2020). *Guidelines for the implementation of the right to adequate housing. Report of the Special Rapporteur on adequate housing as a component of the right to an adequate standard of living, and on the right to non-discrimination in this context*. Geneva: United Nations Human Rights Council. Available at: https://documents-dds-ny.un.org/doc/UNDOC/GEN/G19/353/90/PDF/G1935390.pdf?OpenElement
See also: https://make-the-shift.org.
Gabor, D., & Kohl, S. (2022). *"My home is an asset class": The financialization of housing in Europe*. Brussels: The Greens/EFA in the European Parliament. Available at: https://www.greens-efa.eu/en/article/document/my-home-is-an-asset-class.
Lawson, J., Norris, M., Wallbaum, H., Grimsley, K., Nasarre-Aznar, K., & Lambea Llop, N. (2021). *#Housing2030: Effective policies for affordable housing in the UNECE region*. New York: United Nations. Available at: https://unece.org/sites/default/files/2021-10/Housing2030%20study_E_web.pdf.
Wijburg, G. (2021). The de-financialization of housing: Towards a research agenda, *Housing Studies*, 36(8), 1276–1293. https://doi.org/10.1080/02673037.2020.1762847.
Other publications addressing the wider issue of rethinking housing policies include:
Aalbers, M.B. (2016) *The Financialization of Housing: A Political Economy Approach.* London: Routledge.
Ryan-Collins, J., Lloyd, T., & Macfarlane, L. (2017). *Rethinking the economics of land and housing*. London: Zed Books.
Wetzstein, S. (2022). Toward affordable cities? Critically exploring the market-based housing supply policy proposition. *Housing Policy Debate*, 32(3), 502–532.

Short Biography

Manuel B. Aalbers, a human geographer, sociologist and urban planner, is full professor of Economic and Urban Geography at KU Leuven, the University of Leuven (Belgium) where he leads a research group on the intersection of real estate, finance and states [http://ees.kuleuven.be/refcom], spearheaded by a grant from the European Research Council. Previously he was at the University of Amsterdam and Columbia University, and has been a guest researcher at New York University, City University of New York, University of Milan-Bicocca, and University of Urbino (Italy).

Prof. Aalbers is the world's leading academic expert on the financialization of housing, having coined the phrase in a 2008 paper that remains the most cited source on the topic. In 2016, Routledge published his book *The Financialization of Housing: A Political Economy Approach*. He has written numerous papers on the financialization of housing, often working with co-authors, and addressing these issues in several European countries, as well as in Brazil and the US. His is currently starting a new Europe-wide research project on housing inequality, coordinated together with Dr. Michelle Norris (University College Dublin) and funded by the European Commission's *Horizon Europe* scheme.

He has also published on corporate financialization, redlining, social and financial exclusion, neoliberalism, mortgage markets, the privatization of social housing, neighborhood decline, gentrification and the Anglo-American hegemony in academic research and writing. He is the author of *Place, Exclusion, and Mortgage Markets* (Wiley-Blackwell, 2011) and the editor of *Subprime Cities: The Political Economy of Mortgage Markets* (Wiley-Blackwell, 2012). He is also the associate editor of the *Encyclopedia of Urban Studies* (Sage, 2010), editor-in-chief of geography journal *TESG,* and has served as the guest editor for nine different journals. Most of his papers can be downloaded from https://kuleuven.academia.edu/ManuelAalbers.