



Investors for Affordable Cities

Responsible investment and affordable rental housing in Canada

DISCUSSION PAPER

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Executive Summary

Housing unaffordability is exacerbating economic inequality in Canada, with research indicating that renters are experiencing among the highest levels of hardship and poverty in the country.¹ The rising cost of housing is accompanied by the growing presence of institutional investors in the residential real estate market – a phenomenon known as the financialization of housing.

Residential real estate is an attractive asset class for institutional investors because it provides steady income and is considered to be resilient in economic downturns. At the same time, investors see occasions to increase the income generating potential of these assets through value-add and opportunistic strategies. For example, investors might purchase older rental buildings in disrepair, displace existing tenants, renovate and then recover the costs in the short term through substantial rent increases for new tenants.

There is a relationship between the growing participation of institutional investors in residential real estate and the housing crisis. The federal government's shift away from providing non-market housing, the rise of a secondary market where individuals are purchasing condos to rent for income, deregulated rent control and low vacancy rates are among the reasons why rental housing is less affordable for renters and more rewarding for investors.

While the potential for strong financial returns from residential real estate is clear, there are risks associated with this asset class that investors need to be aware of. Increasing levels of inequality and a shrinking middle class can create systemic risks for investment portfolios stemming from stagnating economic growth, declining consumer demand, and increasing economic and social instability. At the same time, institutional investor participation in the housing market in Canada has been met with scrutiny, generating reputational – and even operational – risks for investors.

Most Canadian institutional investors have responsible investment policies that commit to incorporating environmental, social and governance (ESG) considerations into their investment decision-making as a way to better manage risk, generate sustainable long-term returns and align their investments with the broader objectives of society. Yet ESG policies have not translated into an adequate consideration of affordability in residential real estate investments. In order to effectively manage the risks that investors face when they invest in residential real estate, it is critical for funds to understand and integrate housing affordability into their asset allocation, investment stewardship and policy advocacy efforts.

Our preliminary analysis indicates that there are opportunities for institutional investors to incorporate affordability into their approaches to responsible investing policies and practices. For example, investors can allocate assets to affordable housing initiatives, and, as part of their investment stewardship, engage with Real Estate Investment Trusts (REITs) on the impacts of their policies and practices on housing affordability. Institutional investors can also add an important voice to policy discussions in support of meaningful measures to advance housing affordability in Canada.

Introduction

Housing affordability is at a crisis point in Canadian cities. The Canada Mortgage and Housing Corporation (CMHC) considers housing to be “affordable” if it costs less than 30% of a household’s before-tax income.² In June 2021, the average Canadian buyer spent 52% of their income to cover the costs of a typical home in Canada.³

The latest Canadian Housing Survey concluded that 23% of renting households were in core housing need.⁴ This level of core housing need among renting households is over three times higher than among homeowners.⁵ The problem is most pronounced in the Greater Toronto Area and Metro Vancouver, where there are no neighbourhoods where a full-time minimum wage worker can afford to rent a one- or two-bedroom apartment.⁶

As housing costs have risen, so too has the presence of institutional investors in the rental market. Pension funds, asset managers, private equity firms and Real Estate Investment Trusts (REITs) are acquiring aging rental housing assets and developing new purpose-built rentals. Some argue that in the

absence of sufficient public investment, private capital is required to maintain existing buildings and build more housing stock. Others point to evidence that the financialization of housing is driving up rents and deepening unaffordability.

This paper is intended to stimulate a discussion among institutional investors about how their residential real estate portfolios may impact housing affordability and what actions they can take to address these impacts. It is divided in four sections that address the following questions:

- Why is housing affordability an issue of concern for investors?
- How is the financialization of housing related to affordability?
- How do Canadian investors participate in the residential real estate market in Canada?
- How can investors contribute to housing affordability?

Two general categories of investors are present in the real estate sector: retail and institutional investors. Though their trajectories are interrelated, this discussion paper focusses on institutional investors – entities such as pension funds, asset managers and REITs that pool other peoples’ money into collective vehicles and invest it on their behalf.



01

Why is housing affordability an issue of concern for investors?

Housing is a human right. The Universal Declaration of Human Rights and the International Covenant on Economic, Social and Cultural Rights recognize the right to adequate housing as a component of the right to an adequate standard of living.⁷

Investor responsibilities to respect human rights in their operations and value chains are articulated in international frameworks, including the OECD Guidelines for Multinational Enterprises, the UN Guiding Principles on Business and Human Rights and the UN Global Compact. A growing number of institutional investors are orienting their investment allocations and processes towards the Sustainable Development Goals (SDGs), which contain a target of ensuring access for all to adequate, safe and affordable housing by 2030.⁸

Most institutional investors incorporate environmental, social and governance (ESG) considerations into their investment decision-making as a way to better manage risk, generate sustainable long-term returns and align their investments with the broader objectives of society. Typically, ESG considerations have been used as part of investment analysis at company and portfolio levels. Increasingly, however, investors are looking at the implications that ESG factors can have at a systemic level. For example, investors have come to understand that climate change poses risks to the systems that sustain markets and portfolios. More recently, the COVID-19 pandemic and racial justice movements have highlighted the systemic risk that inequality poses to investors' portfolios.

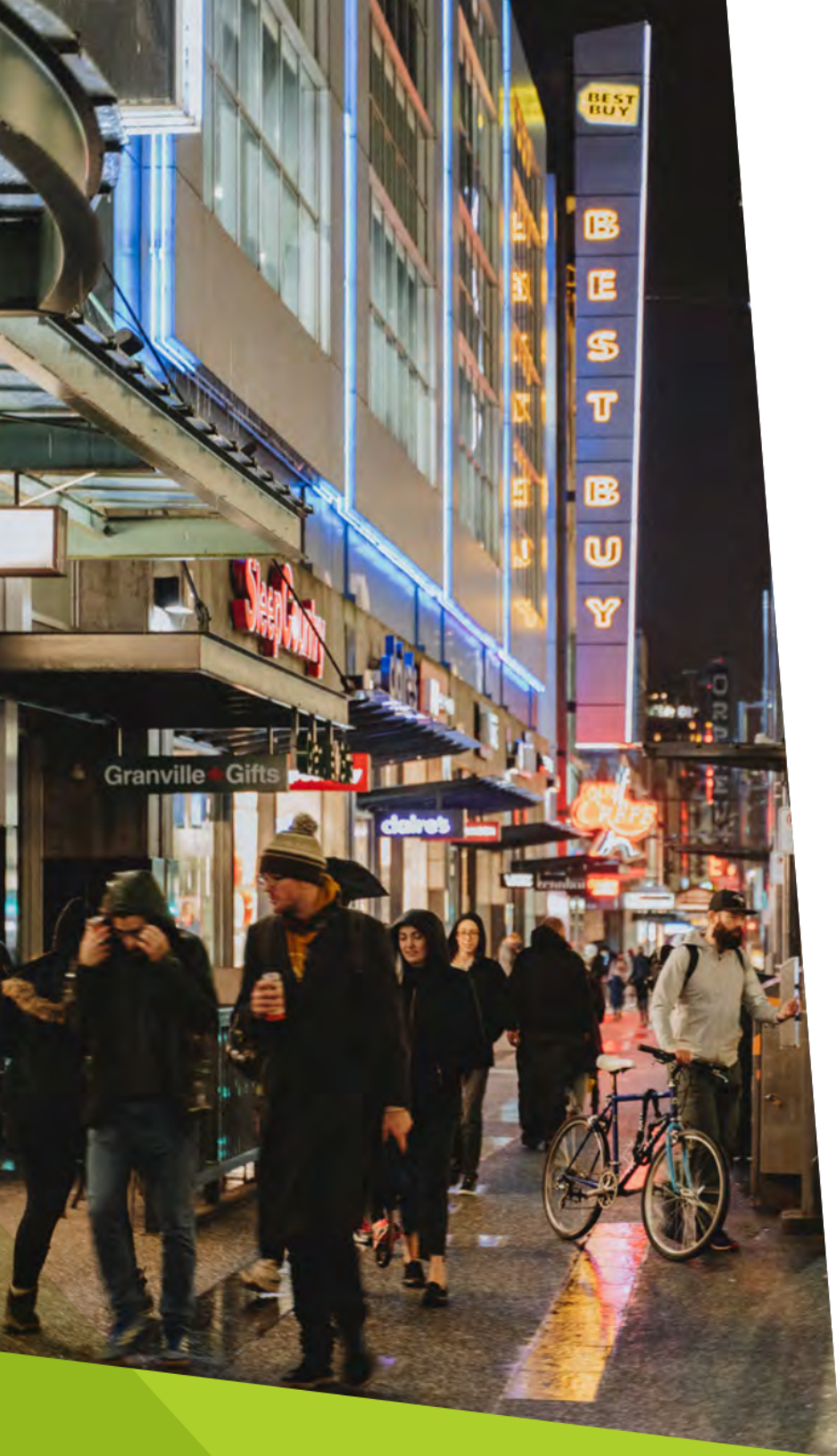
The social and financial instability that comes with a widening gap in income and wealth can destabilize investors' portfolios. A Principles for Responsible Investment (PRI) study on systemic risk and inequality found that deepening inequality "has the potential to negatively impact institutional investors' portfolios as a whole; increase financial and social system-level instability; damage output and slow economic growth; and contribute to the rise of nationalistic populism and tendencies toward isolationism and protectionism."⁹ The risks to investors include negative impacts on long-term investment performance, the universe of investment opportunities and the financial and social systems upon which investors depend.¹⁰

In 2018, Evan Siddall, then-President and Chief Executive Officer of the Canada Mortgage and Housing Corporation (CMHC), said: "Housing is unfortunately widening the inequality gap in Canada."¹¹ He explained how housing value gains over the past decades have benefited the wealthy disproportionately and that rising prices would lead to higher household debt, diminishing affordability and deepening wealth inequality. This inequality has intensified during the COVID 19 pandemic housing boom: The average home-owner household saw its net worth increase by approximately \$73,000 in the first quarter of 2021 while the average renter household's net worth rose by \$8,000.¹² CMCH research has found that renters have higher levels of hardship, housing-induced poverty and socio-economic inequality than homeowners, with the most severe impacts experienced by seniors living alone, women, immigrants and urban residents.¹³

In addition to the systemic risks associated with inequality, investors face reputational risks for housing investments associated with inequality and unaffordability. As will be described in this brief, tenants in Toronto's Parkdale neighbourhood declared a rent strike to object to above-guideline rent increases and demand necessary repairs to their units in 2017. They specifically targeted the Alberta Investment Management Corporation (AIMCo), which owned six of the buildings in question.¹⁴ In 2021, the Public Sector Pension Plan Investment Board (PSP) was in the spotlight for its \$870 million partnership with Pretium Partners, a US private equity firm. Pretium Partners is under investigation for seeking to evict over 1,700 renters during a federal moratorium on evictions at the height of the pandemic, including a disproportionately large number in majority Black counties in the US.¹⁵ In both cases, the funds were forced to respond to allegations that they were exploiting low-income and predominantly racialized tenants.

For some asset owners such as pension funds, housing inequality can also have deep implications for beneficiaries who are priced out of the markets in which they work. For example, spurred by the challenges posed by housing inequality and unaffordability by their membership, two BC Teachers' Federation union locals – whose members are public sector pension fund beneficiaries – submitted a successful redevelopment proposal to the Vancouver City Council to build non-market housing for teachers who cannot afford to live in the city.¹⁶





02

How is the financialization of housing related to affordability?

Financialization refers to the expanding role of finance in the economy. In her 2017 report on the financialization of housing, the UN Special Rapporteur on adequate housing (from 2017-2020) Leilani Farha describes the financialization of housing as the “expanding role and unprecedented dominance of financial markets and corporations in the housing sector.”¹⁷

Financialization transforms housing from serving an essential social purpose and human right into an asset that serves the financial purpose of generating income for investors. The value of housing is therefore responsive to the market rather than to peoples' housing needs.

This next section summarizes research on how housing financialization developed in Canada and what the implications have been for affordability. Understanding this context is important for institutional investors who wish to design investment policies and practices that consider housing affordability.



2.1

What gave rise to the financialization of housing in Canada?

DECLINING AFFORDABLE RENTAL STOCK AND STOCK RENTING AFFORDABLY

The entry of institutional investors into the Canadian rental housing market is correlated to the federal government's divestment from developing and operating affordable rental housing. From 1965 to 1990, the Canadian government invested significantly in building affordable housing – over 10 percent of new builds were non-profit, public or co-operative housing.¹⁸ In 1993, however, the federal government terminated all new funding for off-reserve social housing and oriented the CMHC away from providing non-market housing, resulting in dramatic reductions in affordable rental and non-market stock.¹⁹ Although almost one-third of households in Canada are now renters, fewer than one in ten homes built in the last 20 years were purpose-built rentals.²⁰

As affordable purpose-built rentals deteriorated and/or were demolished, rents in remaining rental stock began to rise dramatically. The issue, however, is not simply a lack of supply.

THE SECURITIZATION OF MORTGAGES AND THE RENTAL MARKET

The federal government's withdrawal from providing affordable housing was accompanied by a series of policies and programs that transformed housing into an asset. One of these was the securitization of mortgages, which entailed pooling leases, loans and mortgages into a liquid financial product – asset-backed securities – to be sold to investors.²¹ Importantly, mortgage securitization programs that came into effect between 1987 and 2001 instituted government guarantees of principals and interest payments for mortgages from qualified lenders.²²

Securitization made credit more accessible and – when combined with tax programs and declining interest rates – incentivized individuals to purchase condominiums as “investment properties” with the intention of renting them to others, effectively creating a secondary rental market.²³ By all accounts, condominiums represent a significant proportion of rental units in Canadian Census Metropolitan Areas (CMAs). In 2019, 28% of all condominiums in Vancouver and 33% in the Greater Toronto Area (GTA) were rented out.²⁴

The implications of the secondary rental market for housing affordability are two-fold. On one hand, condos are significantly more expensive to rent than purpose-built rentals.²⁵ For example, the average condominium rented for 49% more than a purpose-built rental in Toronto and 15% more in Vancouver in 2020.²⁶ On the other hand, due to the deregulation of rent control, condominium investors can sell or repurpose units easily, contributing to the erosion of the security of tenure for tenants.

RENT CONTROL DEREGULATION

Rent control deregulation further fuels rising rents across the rental market. In most Canadian jurisdictions, landlords can only raise rents by legislated increments during tenancies but have no ceiling on rent increases between tenancies.²⁷ As a result, following the eviction of an existing tenant, the landlord can raise the rent for new tenants as much as the market permits. In provinces such as British Columbia and Ontario, landlords may evict tenants for certain “no-fault” reasons, such as “personal use” or renovations.²⁸

Tenant advocates have long argued that rent control legislation does not protect renters from being evicted on false or questionable grounds for the sole purpose of turning over a unit to new tenants who are willing and able to pay higher rents. In British Columbia and Ontario, “personal use” evictions are permitted when a landlord or their family claims they will move into a unit they are renting. “Personal use” evictions are most common in secondary rental market stock such as condominiums, which are considered volatile rental stock.²⁹ Evictions for renovations may occur in secondary rentals and purpose-built rentals.

In Ontario, the number of tenants seeking the support of a Tenant Duty Counsel in contesting no fault evictions has nearly doubled since 2015. While most cases are “no-fault” evictions for personal use, requests for advocate support in contesting evictions for renovations have risen steadily.³⁰ In British Columbia, information on causes of evictions is not available, but a recent report by the University of British Columbia calculated that Vancouver had the highest eviction rate in the country.³¹ Changes to the Residential Tenancy Act in British Columbia intended to better regulate “renovictions” – or evictions due to renovations – came into effect in 2021.³²

VACANCY RATES

Most discussions of rental housing affordability point to declining vacancy rates, which add competition to the rental market. Vacancy rates are sensitive to demographics and rising homeownership costs, declining as more people are priced out of homeownership.

Vancouver’s vacancy rate in purpose-built rentals was close to 1% from 2004 to 2020 and Toronto’s was well under 2% from 2010 to 2020.³³ It is important to note that vacancy rates alone do not set rents. Although vacancy rates in both cities rose in 2020, rents for vacant units also rose by approximately 20%.³⁴

Taken together, the government’s shift away from non-market housing, the rise of a private secondary rental market, deregulated rent control and low vacancy rates – in a context of low interest rates – produced favourable conditions for institutional investment in housing. Against this backdrop, REITs were given legislative status under the Canadian Income Tax Act in 2007 that exempted them from paying corporate taxes if they distributed their taxable income to their unitholders.³⁵ As will be further discussed, REITs play a key role in facilitating large-scale institutional and retail investment in real estate.



2.2

How does the financialization of housing contribute to unaffordability?

Although it is difficult to quantify the housing affordability implications of financialization across Canada's market, housing advocates, academic research and media reports document how specific practices embedded in some business models adopted by institutional investors contribute to rising rents.

Institutional investors' real estate portfolios include office, commercial/retail, residential, warehouse and cold storage properties. Residential assets are countercyclical and considered to be resilient in economic downturns while providing opportunities for a steady income and capital appreciation.

Institutional investors generally pursue core, opportunistic or value-add strategies in their residential portfolios, seeking returns through two components: 1) steady revenue streams with inflation hedging potential (rents, and adjustments to inflation); and 2) capital appreciation on the price of an asset between purchase and sale dates. Core investments are defensive and bring consistent returns to a portfolio through rental income generated from high-quality, stabilized assets. Value-added strategies are riskier and involve repositioning or enhancing assets to generate value through both income and capital appreciation. Opportunistic strategies are riskiest and entail acquiring properties and increasing value through modifications, usually using leverage (debt).³⁶

In all residential real estate investment strategies, the value of a building rises as rental income paid to owners increases. The capital appreciation that value-added and opportunistic strategies seek entails making enhancements and improvements to buildings so that they are able to attract different tenants that will pay more rental income to investors.³⁷

INSTITUTIONAL INVESTORS PARTICIPATING IN THE RESIDENTIAL REAL ESTATE INVESTMENT CHAIN

For the purpose of this discussion paper, we provide simplified working definitions of institutional investors in the real estate investment chain. These actors will be further described in section 3.1

Pension fund: Defined benefit and defined contribution pension funds pool workers' and employers' contributions and invest them across asset classes. Some public sector pension funds are required by legislation to use a crown corporation for their investment management services, such as BCI and AIMCo. Several large Canadian pension funds have their own real estate subsidiaries to manage their direct real estate investments.

Asset manager: Asset managers are financial firms contracted by asset owners to increase returns on a portfolio via the provision of financial products and services. Specialized real estate managers may provide a suite of investment management and real estate management services ranging from managing unlisted real estate funds to managing and leasing the buildings themselves.

REITs: REITs are publicly listed real estate companies that invest in and manage diversified real estate portfolios on behalf of their unitholders. REITs are themselves institutional investors in that they pool capital to acquire assets. Their unitholders include other institutional investors, such as pension funds and asset managers.

Real Estate Operating Company (REOC): REOCs are publicly-listed real estate companies that invest in and manage diversified real estate portfolios on behalf of their shareholders. While REITs pay taxable income to unitholders – who assume tax obligations – REOCs may reinvest earnings into the company and are therefore subject to corporate taxes.

VALUE-ADDED AND OPPORTUNISTIC STRATEGIES: RENOVICATIONS, EVICTIONS AND RISING RENTS

Value-added and opportunistic strategies that are generally deployed by REITs have been the focus of most research into financialization and housing in Canada. Reports from housing justice organizers and the media have documented patterns where REITs acquire aging buildings in disrepair, displace existing tenants, make renovations of varying significance and then raise rents for incoming tenants.³⁹ Martine August's research on Canadian REITs involved a scan of public filings, which explicitly describe this strategy of "repositioning buildings" to attract higher-paying incoming tenants.³⁹ In addition to legal "no fault" evictions, nefarious tactics to drive existing tenants out by neglecting buildings, failing to address pest and mold issues, and engaging in direct harassment and intimidation in REIT-owned buildings have been widely documented.⁴⁰

In addition to evictions related to building repositioning, August's research suggests that institutional investors' drive to reduce building operating costs results in chronic maintenance issues, additional charges for tenants and higher tenant turnover.⁴¹ A 2021 CBC investigation alleges that Northview Apartment Real Estate Investment Trust, which holds a near-monopoly of rental housing in Canada's north, consistently fails to address ongoing and chronically deteriorating conditions in its assets.⁴² A Globe and Mail investigation in 2019 linked a significant number of landlord-initiated evictions in the Greater Toronto Area to financialization, suggesting that institutional investors are less forgiving than "mom and pop landlords" of short delays in paying rents and arrears.⁴³

In Ontario, financialized landlords have been associated with "above guideline rent increases" (AGIs), which allow landlords to raise rents for existing tenants above provincially mandated limits due to capital expenses. A study in Toronto from 2012 to 2019 found that financialized and corporate landlords filed 64% of all AGI requests, potentially impacting over 175,000 households.⁴⁴

CORE STRATEGIES: NEW PURPOSE-BUILT RENTALS AND FLEXIBLE INTERPRETATIONS OF "AFFORDABILITY"

While value-add and opportunistic business models that reposition aging rental buildings have received the most scrutiny, there are questions around the extent to which new purpose-built rentals contribute to – or detract from – affordability. In some markets, such as Vancouver, there has been a recent spike in new purpose-built rentals. The high costs associated with financing large constructions have meant that institutional investors such as pension funds – attracted by low-interest rates and a promise of steady returns – are joining traditional developers in the market.⁴⁵

At the top end, some institutional investors have built luxury rentals such as Tricon Residential's "The Selby," where rents are so high that they drove average rent levels in the neighbourhood up by 10% during 2020 when surrounding neighbourhoods posted rent declines of 8%-12%.⁴⁶

At the mid and lower ends of the market, governments at all levels have begun offering incentives to the private sector for much-needed new purpose-built rentals. In Vancouver and some parts of the Lower Mainland, for example, municipal governments may offer more density to housing development proposals as long as a modest proportion of units are earmarked as rentals or designated for "moderate incomes."⁴⁷ Quadreal, for instance, partnered with developer Westbank to redevelop the Oakridge Centre, a 28-acre mixed use site that boasted the most expensive condo pre-sales in Vancouver in 2019. In 2020, the developers asked the City to increase the project's overall residential density by 10% in exchange for building 319 additional market rental units, which have no affordability criteria, and 94 moderate income rentals for households earning between \$30,000 and \$80,000 per year.⁴⁸

The federal government, for its part, began offering financing to the private sector for affordable rental housing through the National Housing Strategy's Rental Construction Finance Initiative (RCFI). Announced in 2016, the RCFI provides financing for up to 100% of building costs provided buildings meet a set of criteria that includes designating at least 20% of the total units as "affordable" for ten years. Yet the affordability criteria are set according to area median family income rather than median rents in an area, resulting in rents that are more than double the median rent in most Canadian cities.⁴⁹

UNDERSTANDING AFFORDABILITY BENCHMARKS

Affordability benchmarks associated with government incentives for rental housing are contentious. The National Housing Strategy's Rental Construction Finance Initiative (RCFI)'s criteria of 30% of area median family income – based on a Statistics Canada data series – was a departure from earlier federal benchmarks that defined affordable rents according to local market median rents. In a context of generalized income and wealth inequality between homeowners and renters, a benchmark set to median income provides a distorted measure of what renters in a given area are able to afford.

Researcher Steve Pomeroy compared the RCFI benchmark to median rents in cities across Canada. He found that “in almost no city in Canada is the RCFI affordable rent benchmark less than \$2,000/month, nor is it remotely close to the median rent in any city.”⁵⁰ Pomeroy's calculations show that rents considered “affordable” under the RCFI benchmark are more than double the median rent in most cities.⁵¹

Some institutional investors – namely REITs – are obtaining RCFI financing to build new rentals.⁵² The financing terms led the CEO of RioCan REITs to comment that “the cheapest debt in town is CMHC-guaranteed debt.” RioCan obtained RCFI financing to replace a 120-unit affordable housing building with a mixed-use building containing 367 new condominium units, 183 market rental units and 50 “affordable” rental units in Toronto.⁵³ In these types of arrangements, the market rental units do not have affordability caps.

In cities across Canada, debates surrounding what is affordable in purpose-built rentals are casting a critical light on the development of much-needed new stock. Researchers Steve Pomeroy and Duncan MacLennan found that overall, new purpose-built rentals are renting at prices over 170% of average market rents. Paradoxically, they calculate that for every new affordable unit created under the National Housing Strategy, seven existing “modest” rental units were lost due, in part, to the financialization of housing.⁵⁴



03

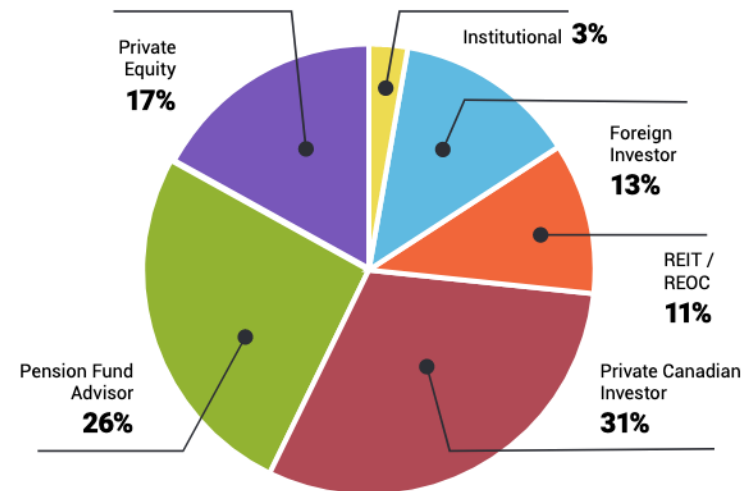
How do Canadian investors participate in the residential real estate market in Canada?

Institutional investors are exposed to residential real estate through direct investment, private market products (e.g., participation in unlisted real estate funds), as well as through holdings in REITs and Real Estate Operating Companies (REOCs) within their public equity portfolios.

A complex network of intermediaries seeking to attract asset owner clients offer services and pooled capital products to facilitate investment in private and public markets. Intermediaries include REITs and asset managers that specialize in real estate. They may finance, own and operate assets on behalf of their investors.

Institutional investment in residential real estate has been on the rise since 2010 in Canada and globally.⁵⁵ Allocations to residential real estate by Canadian institutional investors rose from \$5.5 billion in 2015 to \$11.0 billion in 2020.⁵⁶ As shown in Figure 1, a 2018 CBRE Research study of institutional residential buyers calculated that 26.2% of purchases were made by pension funds/advisors, 16.5% by private equity funds and 10.9% by REITs and REOCs.⁵⁷

FIGURE 1:
2018 Residential Real Estate Purchaser Profile



Source: Figure reproduced from CBRE Research's Canadian Multifamily Overview Demand Drivers & Market Fundamentals Mid-Year 2019.

Martine August calculates that institutional investors own nearly one fifth of privately-owned rental stock in Canada. Her research indicates that ownership concentration among large owners – ranked by number of suites owned – has risen dramatically in the last five years. The proportion of suites owned by the 20 biggest landlords rose by 27.8% from 2011 to 2017 while the number of suites available to rent grew by only 6.5%. REITs, in particular, have expanded from owning almost no rental units in 1996 to almost 165,000 suites between 1996 and 2017 – this constitutes almost 10% of Canada's private rental stock.⁵⁸

The COVID-19 pandemic has accelerated this trend, with institutional investors racing to acquire residential assets. Following an initial shock in the early stage of the pandemic, rental property values have remained at a cycle high and rates of return at record levels.⁵⁹ In Toronto, there were bidding wars in the fall of 2020 as institutional investors sought to acquire older rental buildings – an extension of a trend that began in 2019 when Starlight Investments bought a group of rental buildings for \$1.7 billion in one of the steepest valuations in Canadian commercial real estate.⁶⁰ Residential real estate was the second best performer out of 44 institutional real estate portfolios represented in the REALPAC/MSCI Canada Property Index in 2020.⁶¹

3.1

How is the residential housing investment chain organized?

A significant portion of residential real estate in Canada is still owned by relatively small developers, private companies and family-owned companies. This section looks specifically at institutional ownership.

DIRECT INVESTMENT BY CANADIAN PENSION FUND MANAGERS

In general, larger investors are most likely to directly invest in housing because they are able to pay the higher entry prices. Drawn from data collected by the Canadian Institutional Investment Network,⁶² Table 1 provides an overview of direct investment by plan size.

TABLE 1:

Plan Size and Direct Investment

Plan size	Direct investment (billions)	Invested in REITs (billions)
> \$25 million	\$1	\$0
\$25 million - \$249.9 million	\$296	\$7
\$250 million - \$ 9.9 billion	\$26,722	\$537
Over \$10 billion	\$159,416	\$718

Source: Table based on the Canadian Institutional Investment Network's 2020 Overview.

In line with the “Canadian Model” of direct pension plan investment in alternative assets,⁶³ four of Canada's largest defined benefit pension plans have created real estate subsidiaries to manage their direct real estate investments. Table 2 provides a snapshot of private investment in multifamily assets and broader real estate allocations for Canada's largest pension plans, indicating exposure to residential assets in cases where this data has been disclosed.

TABLE 2:
Canadian Pension Fund Real Estate/Residential Allocations

Pension Fund	(via) subsidiary	Real Estate allocation (private) \$CAD (billions)	Residential \$CAD (billions)
Ontario Municipal Employees Retirement System (OMERS)	Oxford Properties Group	\$70	Portfolio of 12,200 multi-residential units (no value disclosed)
British Columbia Investment Management Corporation (BCI)	QuadReal Property Group	\$61.2	\$18.9
Canadian Pension Plan Investment Board		\$46.5	n/a
Ontario Teachers' Pension Plan	Cadillac Fairview	\$36	n/a
Caisse de dépôt et placement du Québec	Ivanhoé Cambridge	\$35.5	\$5.6
Public Sector Pension Investment Board (PSP Investments)		\$26.8	\$9.9
Healthcare of Ontario Pension Plan (HOOPP)		\$15.5	n/a
AIMCo		\$ 14.8	\$2.4
Ontario Pension Board (OPB)		\$ 4.1	n/a
OP Trust		\$3.2	\$544 million

Source: List drawn from Benefits Canada's 2021 Top 100 Pension Funds Report's list of largest pension plan's real estate allocations.⁶⁴

Examples of recent direct investment include the Canadian Pension Plan Investment Board's (CPPIB) 60% stake in a multi-family rental property, alongside Minto Properties, in a Toronto apartment building in 2015 and Ivanhoé Cambridge's investment in the La Suite complex in Québec City.⁶⁵

Importantly, the bulk of direct investment in residential real estate among large Canadian institutional investors is abroad. A list of the CPPIB's direct real estate investments, for instance, contains one Canadian residential/multifamily asset on a list of 18⁶⁶ and Ivanhoé Cambridge's list of 58 residential investments contains but one Canadian asset.⁶⁷ Several large funds formed real estate joint ventures with private equity firms in the United States during the pandemic, including the CPPIB's joint-venture with Greystar Real Estate Partners, the Public Sector Pension Investment Board (PSP)'s \$870 million partnership with Pretium Partners and Ivanhoé Cambridge's joint venture with Walker & Dunlop Investment Partners Inc.

PRIVATE REAL ESTATE FUNDS

Real estate managers often package their real estate holdings into private funds and sell stakes into these vehicles to institutional investors. The general modus operandi in private market funds is that the real estate manager is the general partner and has responsibility for identifying, purchasing and operating assets; the institutional investor clients who buy into these funds are the limited partners. Private market real estate funds tend to be longer term investments that lock up the capital of limited partners. In general, these funds have a lifecycle of seven to ten years during which the general partner will return the capital invested by limited partners with a profit.

Private real estate funds are generally categorized by investment strategy and location, with a range of core, value-add and opportunistic funds covering distinct regions and countries. Many funds will contain a range of real assets – residential is usually mixed with office, industrial and retail. In addition to funds that buy real assets, real estate debt and credit funds are common.

Private markets are more opaque than publicly-listed holdings. Private fund managers are not obligated to disclose their limited partner clients or performance in any public filings. While the larger pension plans tend to issue press releases to publicize significant joint ventures, information on which investor holds limited partnerships in private equity funds is less readily available in Canada. Specialized databases scrape property ownership registries, publicly accessible information and access to information requests in various jurisdictions, which provides some insight.⁶⁸ Some investors who participate in private equity funds alongside other limited partners list their real estate managers in their annual reports or press releases.⁶⁹ The general public can therefore piece together some information based on private market investments based on a mosaic of information, but this tends to lack timely details.

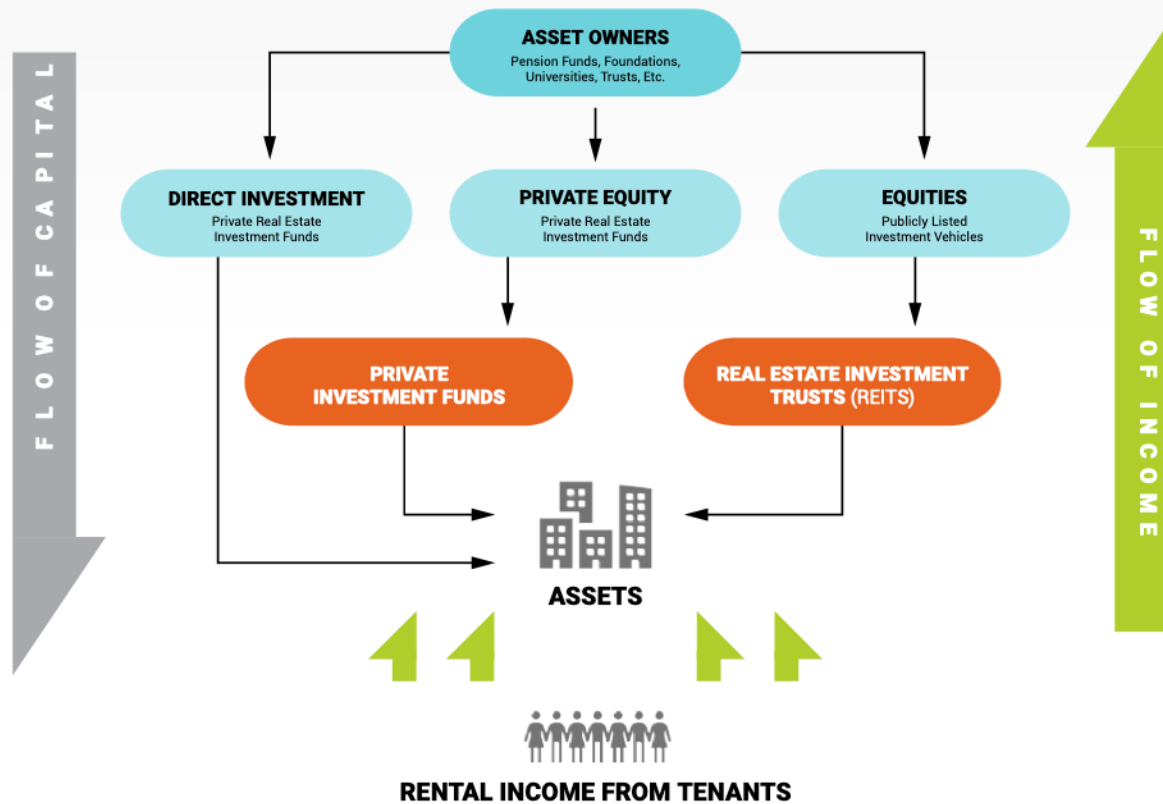


LISTED REAL ESTATE COMPANIES AND FUNDS

A third category of real estate investment is listed, public market equity holdings such as REITs and REOCs. REITs, such as Canadian Apartment Properties REIT (TSX: CAR.UN) and InterRent REIT (TSX: IIP.UN), purchase and operate real estate assets, passing rental incomes to unitholders, who may be both retail and institutional investors. REITs are attractive to institutional investors because they provide liquid exposure to real assets. While larger institutional investors own real estate directly and/or participate in private equity funds through their alternative investment divisions, listed real estate is part of a public equity portfolio. Large asset managers and pension funds are often at the top of the REIT investor list. Though less common, Mainstreet Equity Corp (TSX: MEQ) is an example of a Canadian REOC focused on residential assets. Some companies that own, operate and/or act as asset managers, such as Tricon Residential Inc. (TSX: TCN) and Morguard Corporation (TSX: MRC), are listed on stock exchanges.

FIGURE 2:

Simplified Residential Real Asset Value Chain



3.2

Case studies: Mapping the investment chain

One way investors generate returns is from the income that is derived when consumers purchase a given good or service. A distinctive feature of the residential real estate investment chain is that tenants are the consumers and income is generated through the rents tenants pay to secure a place to live. The capacity of a building to attract tenants who are able to pay higher rent adds value to an asset because it improves its earning potential. In the absence of government regulation that effectively protects the right to adequate housing, the result is that tenants with less purchasing power are most vulnerable to being displaced.

The following examples illustrate how financialization of housing has been met with resistance from tenants and local residents, generating immediate reputational and operational risks for investors.

REITS AND THE PARKDALE RENT STRIKE

Parkdale is a historically working-class, low-income and racialized neighbourhood near downtown Toronto where high-density rental housing has become increasingly financialized. One of the largest city landlords is MetCap,⁷⁰ a residential property management company that manages over 20,000 rental units and over \$2 billion in residential assets.⁷¹ AIMCo is a significant investor in MetCap and co-owns 14 buildings in Parkdale alongside MetCap.⁷²

In May 2017, 1200 tenants in six MetCap-managed – and AIMCo owned – apartment buildings organized a rent strike to oppose applications for above-guideline rent increases that the operator was justifying as building maintenance. The residents alleged that MetCap had failed to perform necessary maintenance for years while raising rents. As the rent strike progressed, residents allege that AIMCo began issuing eviction notices to those who refused to pay rent.⁷³

The Parkdale Rent strike drew residents from across the city to rallies and solidarity pickets. Some targeted AIMCo's Toronto office as part of a broader strategy to expose a contradiction between the pension manager's responsible investment policies and its treatment of low-income tenants living in its properties. At one rally, an organizer said, "AIMCo claims socially responsible investment practices. We fail



to see what is socially responsible about evicting low-income people from their homes in the middle of a housing crisis.”⁷⁴ The organizers launched a website named www.aimcoevictstenants.ca, which allowed supporters to click on a link and write to AIMCo executives to demand a halt to the evictions and negotiations with tenants. They engaged trade union activists in Alberta and brought the issue to the 2017 Canadian Labour Congress Convention, leading the Alberta Union of Provincial Employees (AUPE) – whose members’ pension assets are managed by AIMCo – to issue a statement in support of the tenants.⁷⁵ AIMCo, for its part, insisted that MetCap was managing its properties to the highest standards and, stated that as “a long-term investor, on behalf of our clients, and over the years, [we have] made considerable investments in these properties to address outstanding issues, for the benefit of all tenants.”⁷⁶

Ultimately, AIMCo and MetCap opted to negotiate with the tenants. In August 2017, the tenants secured an agreement that included a reduction of the rent increase, a commitment to complete maintenance and the creation of a new fund administered by MetCap and AIMCo that would allow tenants on income assistance to apply to reduce their rent further.⁷⁷

PURPOSE-BUILT RENTALS, AFFORDABILITY AND DENSITY IN VANCOUVER

In 1993, low-income residents of Vancouver’s Downtown Eastside began organizing against the conversion of the Woodward’s department store into a condominium project, arguing that the site should be redeveloped into social housing. Following years of protests and negotiations, the site was built in 2009 as a “social mix” development that included over 500 condos and 125 supportive housing units for low income people. Opponents argued that the condos would drive local rents up for low-income residents. Indeed, rents in surrounding privately-owned low-income housing buildings have risen systematically since, with many renovated into more luxurious rentals.⁷⁸

New “social mix” buildings that include a modest number of affordable units amid a mix of condo and market rental units have become a mainstay in Vancouver and surrounding municipalities. In the past years, however, local residents have been unwilling to accept added density and some have succeeded in blocking developments. Density is controversial because of residents’ perceptions of negative changes that large buildings bring to a community and the inadequate number of affordable units in the proposals.

For example, Developer Boffo Properties partnered with a local non-profit organization to submit a proposal to build up to 200 condos and 30 units of social housing in 2016. Local residents formed the “NO TOWER Coalition” and exerted pressure on Vancouver’s City Council to reject the proposal. Ultimately, the developer withdrew its proposal in response to the City’s demands for community amenity contributions.⁷⁹ In Burnaby, ACORN and other housing activists were successful in pushing the city, which had lost more rental units than any other Metro Vancouver municipality over 15 years, to adopt a Rental Use Zoning Policy requiring a one-for-one replacement of demolished purpose-built rental units.⁸⁰

Reflecting the shift towards institutional capital in residential real estate in Vancouver, a REIT is at the heart of the latest target of an anti-density campaign. The proposed “Broadway & Commercial” tower in East Vancouver is owned by Crombie REIT in partnership with local developer Westbank. The building would contain 415 purpose-built market rental homes, 235 condos and 37 rental units for moderate income earners.⁸¹ In response, local residents have launched a coalition called “No Megatowers at Safeway” and are actively campaigning against the project.⁸² A spokesperson from the Grandview Woodland Area Council, a local community group participating in the coalition, stated that the development would be a “massive bomb of market housing, be it market condo or market rental, onto a community that’s really suffering a housing crisis.”⁸³ The proposal is currently under review.





04

How can investors contribute to housing affordability?

The idea that income inequality poses systemic risks across investment portfolios is gaining traction with some institutional investors in the wake of COVID-19, racial justice uprisings and other recent events. Pressure on investors and other financial system actors to abandon business models that extract value at the expense of the needs and interests of impacted communities is building.

4.1

Changing the course of housing affordability: Paths for investors

Clear challenges remain in addressing systemic risks in the investment realm.⁸⁴ However, there are opportunities for institutional investors to align their investment processes and practices with the imperative of affordable housing (Table 3).

TABLE 3:

Opportunities for responsible investment in affordable housing

STRATEGY	DESCRIPTION
Fund governance frameworks	
Embed housing affordability into responsible investment policies	Most institutional investors incorporate responsible investment into their statement of investment policies and procedures (SIPP), and/or have standalone responsible investment policies. Investors can foster sound investment decision making on housing affordability in these key governance policies by acknowledging their duty to respect fundamental human rights enshrined in the UN Declaration on Human Rights, which includes the right to adequate housing.
Embed housing affordability in asset class-specific responsible investment policies	Many institutional investors have asset class-specific responsible investment policies. In real estate, these tend to encompass climate considerations, with some references to stakeholder considerations such as labour issues or community benefits. Investors could, for example, incorporate principles in these policies to exclude housing investments that embrace a business model based on tenant turnover and include those that contribute to affordability.
Asset allocation	
Allocate to affordable housing impact investment initiatives	Institutional investors can designate a portion of their funds to affordable housing impact investment initiatives. This could include allocating a percentage of a real estate portfolio's assets to affordable housing funds, having a clear approach to investments in genuinely affordable housing (e.g., a 30% allocation to affordable housing in direct real estate investments) and providing favourable financing to non-market housing developers.

Investment stewardship

Incorporate consideration of housing affordability into asset manager selection and oversight

Investors are incorporating ESG criteria in the selection and monitoring of asset managers. Adding criteria specific to affordability (and asset manager reputation with respect to affordability) in selection and monitoring can help investors avoid nefarious real estate investments while driving change across the financial services industry.

Incorporate housing affordability into engagement with companies

Investors engage with their managers and portfolio companies on ESG issues and may escalate their engagements through proxy voting on management and shareholder resolutions. REIT unitholders may engage REITs on the practices associated with their value add and opportunistic strategies, requesting reporting on tenant turnover, rent increases and other key indicators. Investors can also engage their private markets managers on affordability criteria in new housing developments and request information on social/community impacts.

Policy engagements

Support policy initiatives that are conducive to maintaining and building affordable housing

There are opportunities for investors to weigh in and comment on government initiatives and programs at the provincial, territorial and national levels related to investment in and the regulation of rental housing. An investor voice in support of government measures aimed at maintaining existing affordable rentals and building new genuinely affordable rental housing can be a powerful lever. Investor support for policy advocacy to encourage the government to reassess the preferential tax treatment given to REITs would also be powerful.

International frameworks and standards related to the human right to housing

Evaluate the alignment of real estate portfolios with commitments to the UN Sustainable Development Goals (SDGs)

Some institutional investors are aligning investment policies with the SDGs, incorporating this set of broader objectives for the global community into ESG risk frameworks and capital allocation strategies. A target of "Goal 11: Make cities inclusive, safe, resilient and sustainable" is ensuring, by 2030, access for all to adequate, safe and affordable housing.

Conduct investor due diligence under the OECD Guidelines for Multinational Enterprises (MNEs)

The OECD Guidelines for Multinational Enterprises (MNEs), which encompass human rights, which include the right to adequate housing, set out responsible business conduct expectations for companies and a mediation process. The OECD recommends that investors carry out due diligence in line with the OECD Guidelines for MNEs, with an expectation that minority shareholders use their leverage to encourage investee companies to prevent or mitigate adverse effects. This includes providing remedy and/or grievance mechanisms. The OECD Guidelines for MNEs are unique in that they are the only government-backed international instrument related responsible business conduct with a built-in grievance mechanism in cases of alleged contraventions. Cases have been raised against companies and investors under the OECD grievance mechanism for alleged human rights violations.



4.2

Case studies: Responsible investment in the housing investment chain

A series of case studies are presented below in order to further elucidate the opportunities for investors to align their investment processes and practices with the imperative of affordable housing, highlighting several examples and notable innovations.

FUND GOVERNANCE FRAMEWORKS: THE CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM (CALSTRS) REAL ESTATE INVESTMENT POLICY

The California State Teachers' Retirement System (CalSTRS) investment branch released a new Real Estate Policy in 2021. The policy includes criteria related to affordable housing in its list of investment prohibitions:



CalSTRS will not invest in strategies that are intended to capitalize on the displacement of low-income households. Any rent-regulated housing units that are demolished as such investment or project must be replaced with new rent-regulated housing units; and any persons lawfully residing in rent regulated housing that are displaced as a result of such strategies receive relocation benefits in accordance with relocation requirement as mandated by the local housing authority or by state or federal relocation laws, if applicable.”⁸⁵

The prohibition applies to all private real estate strategies in which CalSTRS has a controlling interest.

**ASSET ALLOCATION:
UNITED PROPERTY RESOURCE CORPORATION (UPRC)**

United Property Resource Corporation (UPRC) is a community-building developer established by the United Church of Canada in 2020 with the goal of creating mixed-income and affordable rental housing.⁸⁶ In 2020, CMHC provided UPRC with a \$20 million line of credit through the Affordable Housing Innovation Fund to reinvest in the (pre)development and (pre) construction of affordable housing across Canada.⁸⁷

UPRC committed to building a minimum of 5,000 new affordable housing units across the country over the next 15 years. In March 2021, the Toronto City Council voted to join UPRC in creating up to 500 affordable rental homes over the next five to seven years.⁸⁸ In Metro Vancouver, UPRC applied to the City of New Westminster in 2021 for a development permit to build a 12-storey residential building that's 100% rental, with 70% of the units being market rentals and 30% being below-market rentals.⁸⁹

**ASSET ALLOCATION:
NEW MARKET FUNDS INC.**

New Market Funds Inc. (NMFI) is a B Corp certified, for-profit impact investment firm that is 51% owned by a registered Canadian Charity and 49% owned by its team. As a specialized fund platform and manager, NMFI takes an integrated approach to delivering market competitive financial performance with lasting community benefit. NMFI currently manages over \$65 million of capital through its own proprietary funds and as a third-party fund manager. NMFI has practices in affordable housing and community lending that it services from its Vancouver and Toronto offices.

NMFI's affordable housing fund, NMF Rental Housing Fund I LP, aims to bring long-term affordable multi-family rental housing inventory to Canadian cities. Three main points distinguish NMF from other Canadian funds: first,

NMF seeks to fill community needs solely by working with community-based housing providers - non-profits and co-ops; second, NMF seeks to address the affordability gap by ensuring that the rental housing it provides is affordable to households earning, on average, 80% or less of the area median income; third, to best preserve long-term affordability NMF will only exit to community-based ownership – not for profits, co-ops or government.

The Fund provides post-construction equity as a means to secure construction financing. Structured exits through a sale to the non-profit partner on each investment are negotiated on the front-end, increasing certainty on returns while mitigating risk. The Fund is expected to earn risk-adjusted market rate returns. Investments in properties are made post-construction and are protected by priority of return and capital. The Fund targets a quarterly cash re-distribution of capital (4% annualized) as well as a lump sum upon exit. The target total investment return is 6% internal rate of return (IRR) net of fees.

**INVESTMENT STEWARDSHIP: MONITORING ASSET MANAGER
PERFORMANCE AGAINST GRESB BENCHMARKS**

GRESB, the global ESG benchmark for financial markets, assesses and benchmarks the ESG performance of US \$5.3 trillion in real estate and infrastructure assets, providing standardized and validated data to capital market actors. Investors use GRESB to monitor their investments and engage with their managers on ESG issues. The metrics include monitoring impact on community (TC6.2) on housing affordability and conducting community impact assessments (DSE5.1) that assess the potential socio-economic impact of its development projects on the community as part of planning and pre-construction.⁹⁰



Conclusion

The housing crisis is a crisis of inequality. There is a deepening disparity between those who cannot afford to rent adequate housing in Canada and those who are growing their wealth through homeownership. For investors, the inequality perpetuated by the housing crisis translates to portfolio- and systemic-level risks.

Canadian investors are exposed to the residential real estate market through investment vehicles across private and public markets. The growing participation of institutional investors in housing – often dubbed “the financialization of housing” – is associated with specific business practices that fuel unaffordability. These include displacing lower-paying tenants with those who are able to pay higher rents and reducing operating expenses by neglecting essential building maintenance. There is a critical need for new purpose-built rentals, but market conditions and the structure of government incentives cast doubt on whether the new wave of multifamily housing stock is affordable enough to address the housing crisis in a meaningful way.

There are broader questions around whether an institutional investor's imperative to generate returns through its residential portfolio is compatible with society's broader goals for housing affordability. In September 2021, 56.4% of people participating in a referendum in Berlin voted to expropriate apartments from corporate landlords. Though non-binding, the referendum result reflects the growing pressure to re-examine the financialization of housing.⁹¹

Many institutional investors have a sophisticated set of tools to incorporate ESG issues into their investment analysis and decision-making processes. There is an immediate need to fold housing affordability into these existing ESG tools and develop a coherent approach to responsible investment in residential real estate. The beneficiaries of a just and inclusive housing market are not only those whose right to adequate housing is protected, but all who ultimately benefit from a fairer and more equitable economy.

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