NOTE RAPIDE
L'INSTITUT PARIS REGION #42

SOCIETY AND HOUSING
February 2021 • www.institutparisregion.fr/en

PRIVATE INVESTMENT IN RENTAL HOUSING: INSPIRING INTERNATIONAL EXAMPLES?

IN THE CONTEXT OF THE CURRENT HOUSING CRISIS IN THE PARIS REGION, WHICH HAS BEEN WORSENED BY THE PANDEMIC AND ITS ECONOMIC CONSEQUENCES, CAN PRIVATE INSTITUTIONAL INVESTORS CONTRIBUTE SIGNIFICANTLY TO MAINTAINING AND PRODUCING RENTAL HOUSING STOCK? ANALYSIS OF FOUR CASES FROM AROUND THE WORLD SHEDS LIGHT ON THE PRACTICES ADOPTED BY THESE ACTORS, WHICH COULD, UNDER CERTAIN CONDITIONS, REVITALISE THE HOUSING MARKET.

Private rental housing is financed by two types of investors (cf. infographic n° 1 p. 5): on the one hand there are household investors; on the other hand there are "financialised" private institutional investors such as banks, insurance companies, mutuelles [French supplementary health insurance providers], pension funds, sovereign funds, etc. The latter either directly acquire properties or, more and more often, use investment trusts specialising in the management of property portfolios on behalf of others (such as SIICs in France or REITs in the USA[1]).

WILL INSTITUTIONAL INVESTORS INVEST IN RENTAL HOUSING AGAIN?

In France, institutional investors are currently in the minority on the housing market (about 200,000 homes in 2016: 3% of private rental housing stock[2]). They turned away from rental housing in the 1990s and focused instead on tertiary real estate: offices and, more recently, shops, warehouse space, etc. However professionals in the sector are reporting renewed interest in housing from institutional investors[3], while public authorities are implementing new tools to encourage these actors to invest in so-called "intermediate" rental housing[4].

In response to this observation, the Institut Paris Region asked students following the "Governing the Large Metropolis (GLM)" Master's degree programme at the Ecole Urbaine of Sciences Po Paris to carry out a survey of the distribution and practices of institutional investors in different national and metropolitan settings (in Germany, the UK, Canada and Japan), in order to gain insights that might be applied to the Paris region.

METHODOLOGY

The countries and cities selected for the survey were chosen according to how comparable they are to the context of the Paris region. With this in mind, the following prerequisites were established:
- a democratic political system;
- a relatively high level of economic growth comparable to that of France.

Once a broad initial selection had been made, the following criteria were also taken into consideration:
- the existence of a well-developed private rental sector likely to attract private institutional investors, especially in large cities;
- how well-established institutional investment is in the country in question;
- the history of social / affordable housing in the country and the current situation.

For the final selection of case studies, geographical diversity was also a determining factor: there are two from Europe, two from Asia and one from North America.

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Germany (Berlin): rumblings of discontent

The strong presence of institutional investors in the German residential property market[5] is partly due to a long-standing culture of renting and partly due to the sale of much of the country's historically large public housing stock in the 1990s. In West Germany, local housing organisations significantly increased their social housing stock after World War II, while steps were taken in support of private tenants (1971 Housing Employment Protection Act). In East Germany, rental housing stock (held until then by state bodies) was mostly given over to municipal housing companies after reunification in 1989. Faced with serious economic challenges in the 1990s, the federal government reduced its involvement in the social housing sector and authorised the widespread sale of social housing. Due to lack of resources, the municipal housing companies were then forced to sell off their assets at low prices, attracting an initial type of institutional investor: speculative investment funds and mainly American private equity firms (Blackstone, Cerberus, Fortress, etc.), with short-term strategies focusing on generating resale profits. After the crisis of 2008, a second wave of financialisation saw the arrival on the residential market of listed property companies whose strategies were based more on achieving stable returns from rents.

In Berlin, where 85% of households are tenants and where rents are traditionally affordable (cf. infographic n° 2 p. 5), institutional investors now occupy a dominant position in the private market. Of 1.6 million rented homes, 830,000 are shared between 180 property companies, the best known of which are Deutsche Wohnen and Vonovia. In less profitable residential blocks on the outskirts of the city, investors opt for disinvestment strategies (closing their local offices, downgrading management services, digitalising services for tenants, etc.). In more attractive city-centre areas, they implement gentrification strategies and systematically seek to get around rental controls, especially via energy retrofitting (cf. table n° 1, p. 4). This means that the median rent in Berlin has doubled since 2010, sparking significant protest movements, some going as far as to demand that investment firms should be expropriated. This situation led the Berlin authorities to vote for a partial rent freeze in 2019.

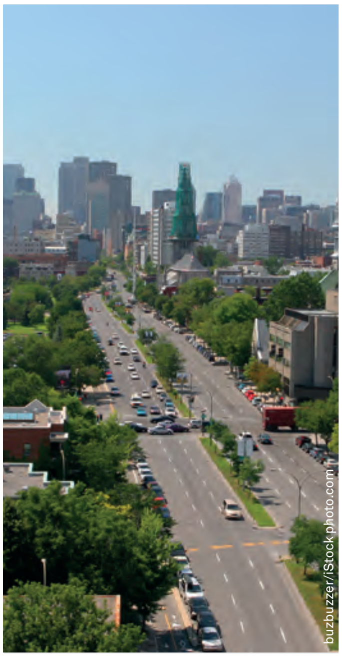
United Kingdom (London): Banking on institutional investors to help tackle the housing crisis

The UK government and local authorities have long been highly involved in the production of social housing, which still accounted for 31% of housing stock in 1981 (compared to 16% in 2018). The arrival in power of Margaret Thatcher marked the beginning of state retrenchment and widespread privatisation of housing stock, with the Right to Buy policy allowing council tenants to buy their homes (1.8 million homes purchased since 1980). Property ownership thus increased, and now stands at 66% of total housing stock. Private rentals, initially relatively uncommon, have also become more widespread, accounting for 18% of total stock in 2018, with 83% of rental stock owned by private householders. From the landlords' perspective this evolution has been driven by the downgrading of tenancy rights (1988 Housing Act), and from the tenants' perspective it has been fuelled by rising prices making it increasingly hard to own property. These trends have been sharpest in London, where the housing crisis is particularly acute.

The presence of institutional investors in the UK housing market remains relatively limited[6], although they have shown growing interest over recent decades. They first entered the student rental market in the 2000s, a time when student rents almost doubled in London. Taking inspiration from this model, the Build to Rent Fund was set up in 2012 (and continued in 2016 through the House Building Fund) with a view to stimulating the construction of new rental housing stock financed by institutional investors, in particular via assisted loans.

Although this policy has so far resulted in the construction of only about 43,000 homes (20,800 in Greater London), it now seems to have reached its cruising speed, with 110,000 homes either authorised or under construction (54,000 in Greater London). Rents for this type of development are nevertheless higher than market prices, with the exception of a mandatory proportion of "affordable" tenancies with prices capped at 80% of market rents. These have to account for at least 20% of homes built (35% in London). However, whereas initially the management of this affordable housing stock was entrusted to social landlords, investors have recently been allowed to manage it themselves.

Canada (Montreal – Toronto): two provinces, two models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In Canada, the provinces are in charge of drafting their own housing policy, although the federal government strives to create the enabling conditions for middle-class households to qualify for property loans. Alongside the provinces and social landlords, it also takes part in financing and managing "residual" social housing stock (4% of total Canadian housing stock), which mainly caters for the most vulnerable households. However in 1993, the federal government stopped subsidising the expansion of this social housing stock, and broadly delegated its management to the provinces and municipalities. In the same year, federal legislation authorised the creation of listed Real Estate Investment Trusts (REITs). In less than three decades—during which the private rental sector has grown—, institutional investors acquired almost 20% of Canadian rented apartment stock[7]. Toronto and Montreal, the two largest cities in Canada, have been affected by these changes in different ways.

In 2020, REITs own 10% of the apartments in Ontario. However the private rental market in Toronto is still mainly driven by the construction of condominiums sold to individual private buyers (about 51,000 apartments built between 1990 and 2017, of which one third are rented out). The sale of entire residential buildings to institutional investors (Purpose-Built Rental) remains more limited, with 12,500 units constructed over the same period. But the production of rental housing remains insufficient to satisfy demand. This imbalance is exploited by institutional investors and asset managers, who mainly invest in old rental stock which they operate using gentrification or disinvestment strategies.

In Quebec, the presence of institutional investors in the residential rental market is a more recent and less significant phenomenon. REITs own only 3% of the apartments in Quebec, mainly in Montreal. This is explained by several factors: although tenants are in the majority in Montreal (53% of all households, compared to less than 30% in Toronto), their status is less precarious thanks to more tightly controlled rent increases. Moreover, Montreal's zoning laws, which are less hostile to urban consolidation, have facilitated the construction of homes for rent, thus better meeting local demand. Last but not least, the fact that Quebec is a French-speaking province is another obstacle to the penetration of Canadian REITs, most of which are English-speaking organisations.

Japan (Tokyo): J-REITs: post-crisis drivers of urban development

Jean-Frédéric Lassara/L'Institut Paris Region

After the Second World War, the Japanese government strongly encouraged property ownership (63% home ownership rate). The rest of the residential stock is mostly given over to private rented housing, with social and subsidised housing playing a residual role (5%). Another specifically Japanese trait arises from the development of tied accommodation owned and managed directly by conglomerates, with the labour market favouring long careers within the same organisation. When the financial bubble burst in the early 1990s, Japan was plunged into a decade-long economic crisis and its model of urban development was called into question. In the centre of Tokyo, new skyscrapers and shopping centres appeared, while former office buildings were converted into flats. In addition to this, condominiums located near stations began to compete with the hitherto prevalent model of the detached suburban house. These changes were driven by institutional investors and the emergence in 2001 of "J(apan)-REITs", which made the country into the second largest market in the world (after the United States) in terms of property holdings. Currently, no less than 22 of these investment organisations own about 1,700 residential complexes, 1,400 of which are in Greater Tokyo (often high-end buildings near train stations). While the presence of institutional investors in the residential sector remains limited[8], the crisis and the new-found attractiveness of central neighbourhoods have nonetheless led to renewed interest in residential investments, which offer particularly stable financial yields. Japanese companies also use J-REITs to provide homes for their executive staff by directly meeting part of the rental costs, which are especially high in the most sought-after areas. Housing has become an argument to attract qualified employees in a society characterised by a sharply ageing population. The standard Japanese lease (which is very favourable to the landlord and requires a large deposit, a "thirteenth month" of rent and a Japanese guarantor) is also a significant obstacle to immigrant populations, which have thus become a prime target for institutional investment organisations. With this in mind, J-REITs are investing in student housing or renovated former state-owned homes, often on the outskirts of Tokyo.

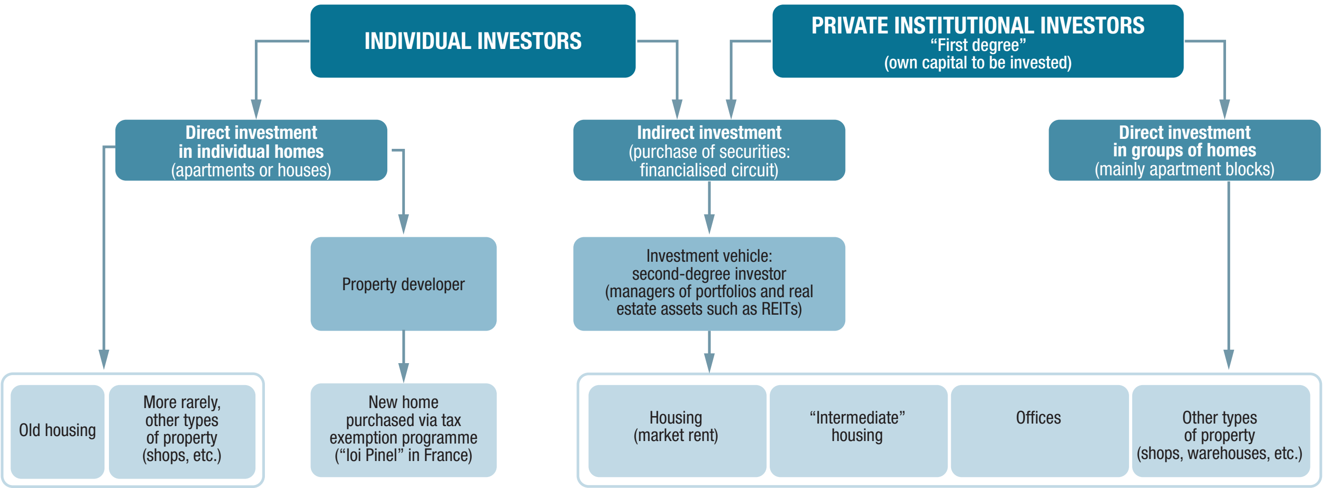
1. Three institutional investor strategies in metropolitan rental housing markets

Type of strategy:	Core market	Gentrification ("value-added")	Disinvestment ("squeezing")
Location of housing	The tightest and most expensive markets in large cities, which are the most stable and least risky for investors	Initially working class districts under redevelopment with a large number of old and/or dilapidated homes: rent-gaps may be "captured" through property investment	Less attractive areas, often on the outskirts and with low development potential, most of whose residents are not well off (and are thus "trapped" in the neighbourhood)
Methods used	- Maintaining or updating the quality of properties and services provided to tenants - Gradually increasing rents (according to market trends)	- Upgrading assets or building from scratch - Steep rent hikes (potentially with eviction of current tenants)	- Reducing tenant services and investments in properties to a minimum - Increasing rents to the maximum tenants are able to pay
Potential consequences	- Higher rents - Evicting less well-off tenants in city centres - Strengthening the hierarchy of property markets to the benefit of the core market	- Higher rents - Eviction of working-class households - Acceleration of gentrification processes on the margins of the core market	- Higher rents - Increased effort rate for tenants, with risk of pauperisation - Deterioration of properties, with potential risks for occupants

2. Comparative table

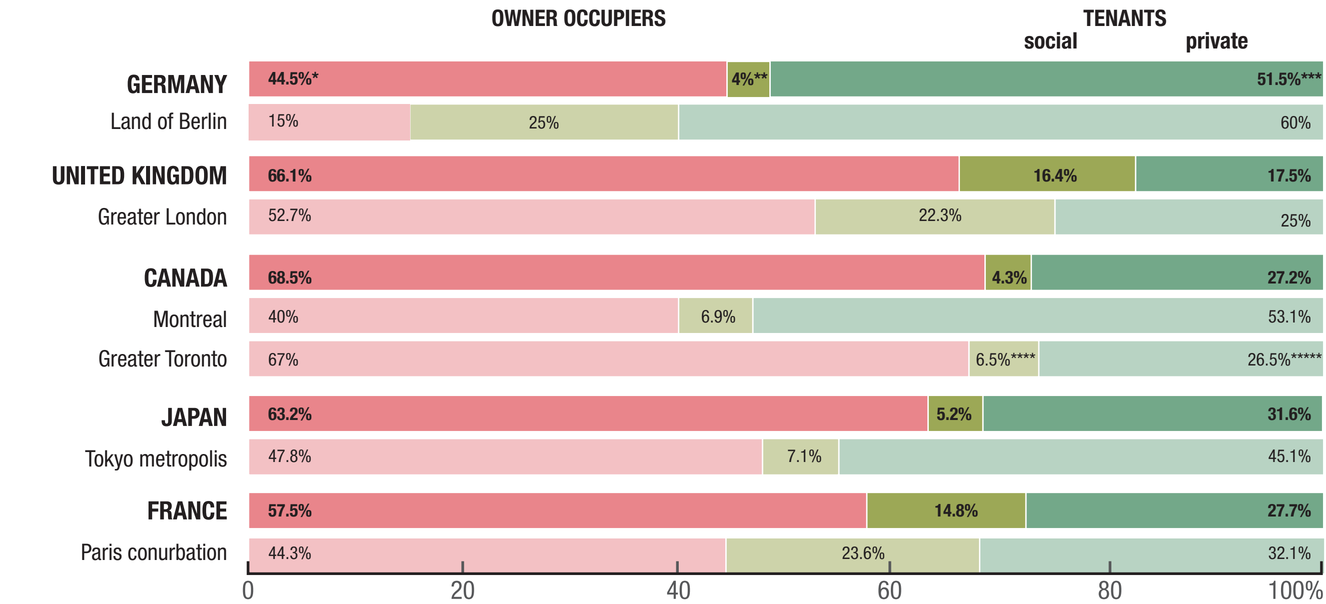
	France (Paris)	Germany (Berlin)	UK (London)	Canada (Toronto - Montreal)	Japan (Tokyo)
Political system	Centralised	Federal	Centralised	Federal	Centralised
Scale of definition of housing policy	National	*Länder*	National	Provinces/municipalities	National
Urban structure	Macrocephalous: 11 million inhabitants in Greater Paris	Polycephalous: 3.7 million inhabitants in the Land of Berlin (4.4 million in the metro area)	Macrocephalous: 9 million inhabitants in Greater London	Polycephalous: 6.4 million inhabitants in Greater Toronto. 2 million in the urban agglomeration of Montreal	Macrocephalous: 13,8 million inhabitants in Tokyo Metropolis
Characteristics of social housing	Historically strong, more dynamic since the SRU law of 2000 set social housing goals for local administrative areas (communes)	Social housing greatly reduced following the privatisation of stock belonging to municipal housing organisations from the mid-1990s onwards.	Sharp reduction in social housing since the 1980s, with the introduction of the Right to Buy scheme.	Historically residual, sluggish since the 1990s due to the cessation of federal subsidies.	Historically residual, suffered massive sell-offs when the speculative bubble burst in the 1990s.
Protection of tenants	Legislation on leases has been broadly stable for several decades and protects tenants; rents are tightly controlled in large cities.	High level of protection for tenants with unlimited leases and rent control system.	Low level of protection for tenants since the 1988 Housing Act. Recent political will to provide tenants with more protection.	Protection of tenants varies between provinces: less strong in Ontario than in Quebec, where rent control is stricter.	System highly favourable to landlords: no rent control; numerous additional charges for tenants (key money, early termination/lease renewal fees, etc.).
Presence of institutional investors in rental housing	Low (3% of private rental housing stock in 2016): institutional investors largely withdrew from the residential sector and focused on tertiary developments in 1980-1990. Sector professionals are, however, pointing to renewed interest in the residential market from institutional investors.	High (over 10% of rental stock in 2011, and growing presence since then): institutional investors have been present in major cities since social housing selloffs in the 1990s. In Berlin they occupy a predominant place in the private rental market.	Quite low (in 2018, 6.4% of private rental stock belonged to companies owning at least 25 homes), but growing: recent policies (Build to Rent) have been set up to encourage the construction of new rental stock by institutional investors, especially in London.	Quite high (the 25 largest private landlords own 9% of private rental stock): institutional investors have increased their presence since the 2000s, though it varies between provinces and cities: it is higher in Toronto (more populated, stock market, English-speaking) than in Montreal.	Very low (J-REITs account for less than 1% of private rental stock). However institutional investors have been more present in the residential rental market since the 2000s via J-REITs, especially in Tokyo.

1. INVESTMENT CIRCUITS OF PRIVATE ACTORS ON THE PROPERTY MARKET



Sources: Ingrid Nappi-Choulet, "Les mécanismes de l'investissement immobilier", fiche du Certu 2010/79; Thierry Theurillat, "La ville négociée: entre financiarisation et durabilité" Géographie, Économie, Société, 2011/3 (vol.13); Ludovic Halbert, "Infrastructures financières et production urbaine: quatre circuits de financement de l'immobilier locatif en France métropolitaine", Espaces et sociétés, 2018/3 (174).

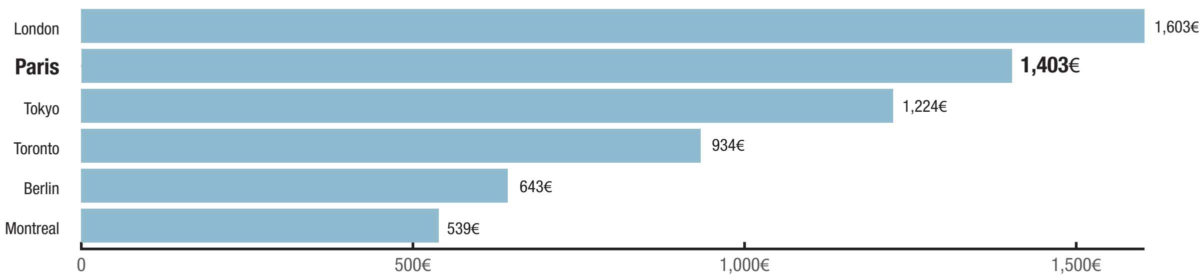
2. OCCUPATION STATUS IN COUNTRIES AND CITIES STUDIED



*For some data, values vary between sources: * Between 42% et 47%. ** Between 3% et 5%. *** Between 48% et 55%. **** Between 5% et 8%. ***** Between 25% et 28%.*

Sources: **Germany:** *Destatis - Sample Survey of Income and Expenditure; Housing Europe 2018;* **Berlin:** *Senate Department for Urban Development and the Environment - Berlin Strategy 2030, 2014;* **United Kingdom:** *ONS - Annual Population Survey 2018;* **Canada:** *Statistique Canada - Enquête canadienne sur le logement 2018;* **Montreal:** *Service de l'habitation de Montréal - Profil des ménages et des logements 2020; Portrait des logements accessibles et adaptés;* **Toronto:** *Census 2016 ; AHO - Toronto Housing Market Analysis; G. Sutor, thèse 2014;* **Japan:** *e-Stat - Housing and land survey 2018;* **France:** *INSEE - RP 2017.*

3. AVERAGE PRIVATE PROPERTY RENTS IN CITIES STUDIED (2019 IN EUROS)



Sources: CBRE, Global Living 2020; Tokyo: numbeo.com (comparison Tokyo-Paris)

BERLIN, LONDON, MONTREAL, TORONTO, TOKYO: EXAMPLES TO BE FOLLOWED?

Three observations emerge from these international case studies (cf. table n° 2, p. 4). First, in the cities we studied, private rental housing stock remains mainly in the hands of individual household investors. It is not making its way back to the core of the institutional investors portfolio, even if there has been renewed interest in residential rental stock from such investors over recent years. Second, the presence of institutional investors in a market does not necessary mean the production of new homes: it can involve selling off public housing or purchasing existing buildings, including in less developed areas. Third, institutional investors are fundamentally market stakeholders. They are unlikely to step in spontaneously where social or intermediate housing is concerned. Without regulation, strategies of systematic rent hikes and/or cost-cutting seem to be the norm, which affects access to housing for low-income households.

The Paris conurbation has rent cap mechanisms in place, and has been able to develop significant social housing stock. The French model, mentioned in the introduction, aims to direct institutional investors towards new "intermediate" housing via investment companies jointly financed and managed by (para-)public bodies. Compared to the other cities we studied, could this be a win-win strategy? This question is discussed in another report[9]. ■

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- M. August and A. Walks, 2017, "Gentrification, suburban decline, and the financialization of multi-family rental housing: The case of Toronto", Geoforum, 89, pp. 124-136.

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ACKNOWLEDGMENTS

The students would like to thank the following for their help and advice as they prepared their report:
Cécile Asanuma-Brice (CNRS), Natacha Aveline-Dubach (CNRS), Sophie Buhnik (IFRJ-MFJ), Matthew D'Elia (Savills), Romain Desforges (Immobilière 3F), Ludovic Halbert (CNRS), Nordine Kireche (Sciences Po), Kristjana Lopston (SCHL), Jean-Pierre Schaefer (Soliha) and Manjo Shimahara (Lifull Home's).

1. SIIC: sociétés d'investissement immobilier cotées; REITs: Real Estate Investment Trusts.
2. In 1992, this proportion was still 13%. Cf. report from the Sénat (19 December 2017).
3. "Les investisseurs placent des sommes records dans le logement", Le Figaro, 30/09/19.
4. Intermediate housing fund managed by the Caisse des dépôts et consignations (CDC); real estate company Cronos by In'li, subsidiary of Action Logement; project for semi-public company by Paris City Council, etc.
5. Germany is currently the leading European market in terms of residential investments for institutional investors (JLL, European Multifamily Investment Market Update 2019). In 2011, private property firms and other companies accounted for over 13% of German rental housing stock; this percentage has likely grown since then.
6. In 2018, in the UK, "companies" (including institutional investors) supplied 13% of private rental properties, but landlords in this category owning at least 25 homes only accounted for 6.4% of private rental stock, and even as little as 2% if we only take into account landlords supplying more than 100 homes (English Private Landlord Survey 2018).
7. The 25 largest private landlords in Canada alone represent almost 9% of total private rental stock.
8. N. Aveline-Dubach (cf. Resources) has counted 1,680 residential buildings owned by J-REITs, with an average of 70 to 80 homes per property, which comes to a total of 118,000 to 135,000 homes. By comparison, this only represents 0.8-0.9% of private rental stock in Japan (15.3 million – not including staff accommodation).
9. Hélène Joinet and Philippe Pauquet, « Logement locatif intermédiaire : quel atterrissage en Île-de-France ? » *Note rapide* n° 876, L'Institut Paris Region, november 2020.

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ISSN 2728-526X
ISSN online
2497-126X

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