TORONTO STAR



BUSINESS

# Already controversial for its ownership of Revera, one of Canada's largest pension plans has just announced a $700-million joint venture with an architect of 'the big short'

The Pretium partnership represents a jump into the contentious single-family home rental business in the U.S., at a time when the Public Sector Pension Investment Board is already under unprecedented scrutiny.

By Richard Warnica Business Feature Writer
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READ THE CONVERSATION

Maya Abood grew up in Stockton, California, a historically poor community just far enough outside San Francisco to have only caught the tail end of the 2000s tech boom. For a brief, wild moment in those years, Stockton, which has been called America's most diverse city, rebranded as a commuter town. "It's like, a very far exurb," Abood said — a distant hub for affordable(ish) housing on the far edge of the hottest market in the world.

Of course it didn't last. Abood was in college when the economy collapsed in 2008. The housing market fell everywhere that year, but in Stockton, it cratered. Prices in some neighbourhoods dropped by as much as 75 per cent. Foreclosures piled up at the fastest rate in the nation. "Most people I knew were losing their homes," Abood said. In 2012, Reuters called Stockton "the town the housing boom broke."

The foreclosure crisis had a profound impact on Abood. After college, she took a job organizing tenants in South Los Angeles, the area that used to be known as South-Central. She was working with people who had, in many cases, already lost the homes they owned and were now facing eviction from the ones they rented. "That was the time of Occupy Wall Street and a lot of critical thought about the role of the financial markets in communities and in achieving housing stability," she said. "They had a very personal connection to that moment in time."

Eventually, Abood decide to go back to grad school at MIT. She wanted to find out what had happened to all those foreclosed homes, in Stockton and Los Angeles and all over California. She wanted to know what the long-term impacts of the crisis had been on things like community ownership and wealth creation. What she found, to her surprise, was a whole new industry that had sprouted up to take advantage of the crash.

"Millions of homeowners were stripped of wealth and that wealth was primarily redistributed," she said, not to other homeowners, but to the same industry that caused the crash in the first place. "Not every foreclosed home ended up in the hands of these Wall Street firms," Abood said, "but many did."

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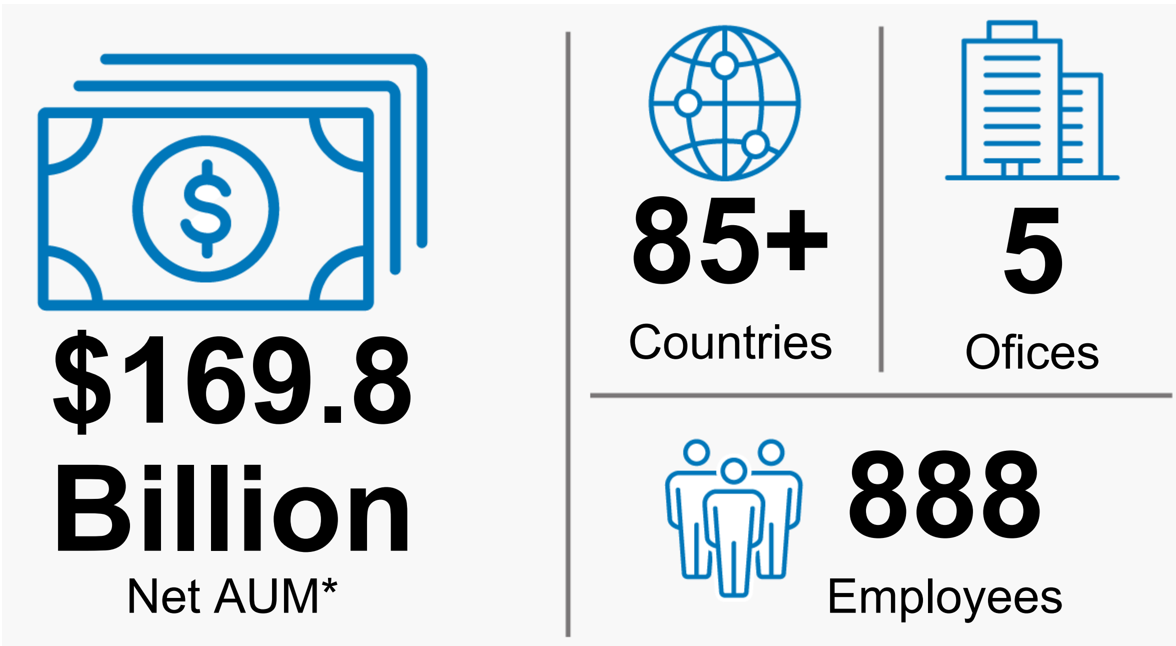
## PSP by the numbers




*Assets under management

SOURCE: PUBLIC SECTOR PENSION INVESTMENT BOARD—2020 ANNUAL REPORT

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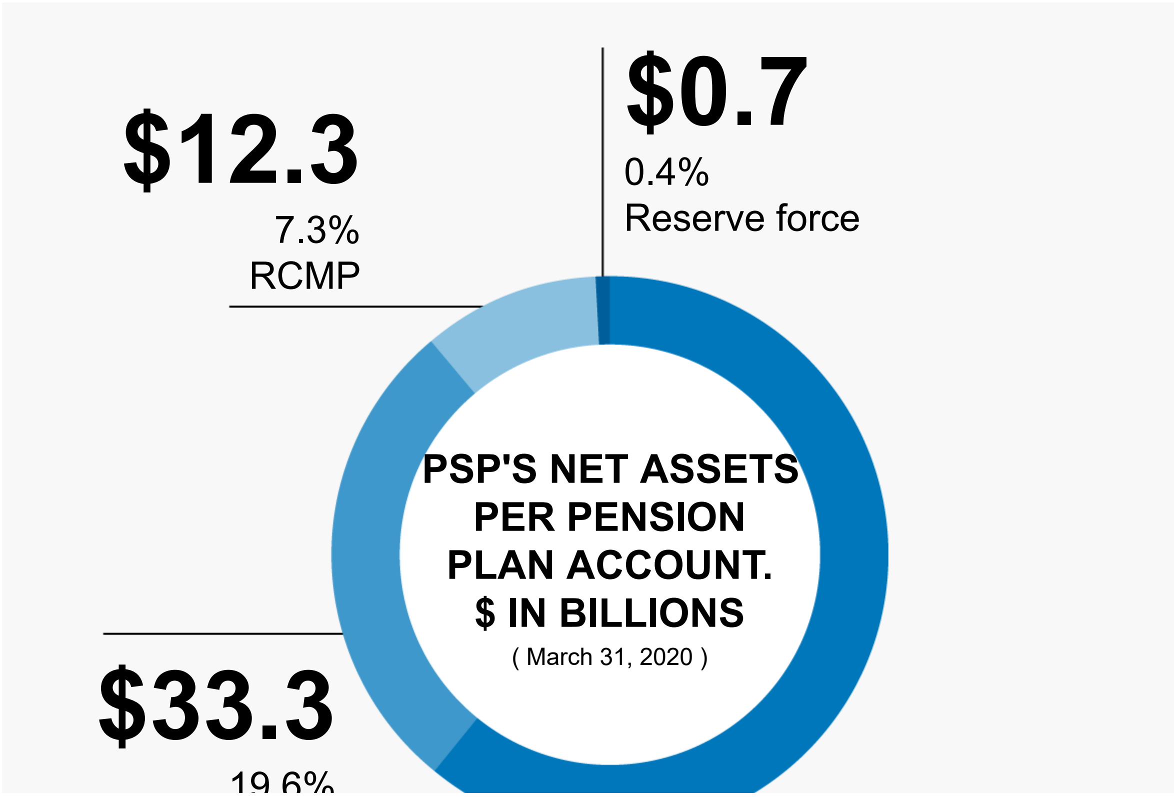



More than a decade after the crash, on the other side of the continent, across the border in a business world mired in a pandemic fugue, a Canadian Crown corporation signed a massive partnership with a hedge fund called Pretium Partners. The deal, a joint venture worth $700 million (U.S.), dropped the Public Sector Pension Investment Board, or PSP, into the world Abood had spent all those years studying. If the housing crash made a sound, Pretium's business is the echo, and now PSP, which manages the pension funds of federal employees, the RCMP and the military, was right in the heart of it.

From the outside, the timing seemed curious. The last year had been something of an annus horribilis for PSP. Before the pandemic, it was not a particularly prominent institution. But COVID-19 had shone a new, less than flattering, light on the fund.

PSP owns one of Canada's largest for-profit operators of long-term-care homes, a company called Revera. Since last spring, the fund has been inundated with calls to sell the company or even make it public. "We want our pension investments made in the best interest of our members, but also in the public interest as well," said Chris Aylward, the national president of the Public Service Alliance of Canada, the union that represents most federal employees. "And what Revera is doing is anything but in the public interest."

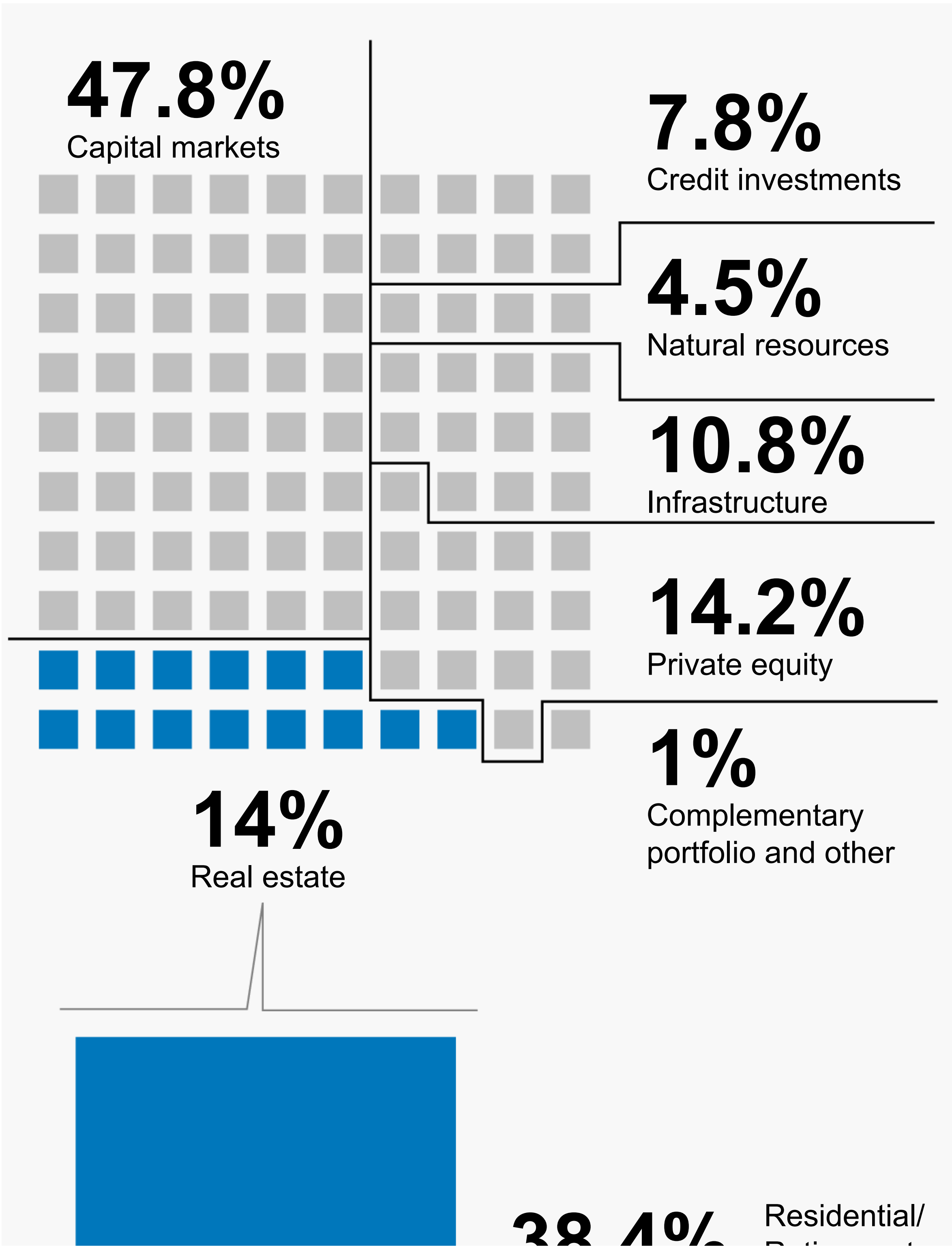
The Pretium partnership, announced Jan. 28, represents another jump into another controversial sector, at a time when PSP is already under unprecedented scrutiny. It underlines questions, italicized by Revera, about how exactly a pension fund should behave. For PSP, those questions are existential. They get to the heart of how it operates and why. They raise issues of governance and ethics and what exactly it means to succeed as a public body charged with making gains on the private markets.




WAR IN
UKRAINE
UKRAINE, RUSSIA BATTLE OVER GAS SUPPLIES

## Breakdown of PSP's net assets per asset class

As of March 31, 2020




For now, for PSP, the main question might be this: Should it be investing for the public good, or just for good returns?

If the housing market collapse was, for most of the world, a calamity of pain and hardship, for some on Wall Street, it was an opportunity. Beginning in the depths of the crash, Wall Street firms began buying up foreclosed or deeply discounted single-family homes, sprucing them up and renting them out on a massive scale. Across the sunbelt, in suburbs outside cities like Dallas, Phoenix,

and Atlanta, buyers for these new firms began appearing at courthouse auctions in droves. "They would literally be having these agents and auction participants with duffle bags full of millions of dollars in cashiers' cheques buying every house that fit their criteria of what they wanted," said Ryan Dezember, a Wall Street Journal reporter who wrote a book about the industry called "Underwater," which came out in July.

The new firms developed software to scour listings. They pioneered algorithms to predict revenues vs. costs. Soon, they were selling new securities backed, not by mortgage payments, but by rents. At first, the plan was to hold the assets and flip them when the market rebounded. But soon the business plan evolved. "They realized that there was money to be made," Abood said — big money, not in selling the homes, but in renting them out for good.

Twelve years ago, the financialized single-family rental business basically didn't exist in the United States. Today, it's worth billions. Some of the largest institutional investors in the world have a stake in the industry. Meanwhile, some familiar figures from the crash have become major players in the business.

In 2012, Donald Mullen Jr., a long-time senior partner at Goldman Sachs left the company to found Pretium Partners, a hedge fund dedicated initially to buying up and renting out single-family homes. To close followers of the financial crisis, Mullen was something of a celebrity. He ran the unit at Goldman that had bet heavily against the housing market — the trades that became known as "the big short." In 2007, as the housing market began to collapse, Mullen wrote to a colleague "sounds like we will make some serious money."

Mullen's entry into the new single-family rental market didn't go unnoticed. "A guy whose most famous trade was a successful bet on the full-scale implosion of the housing market is now swooping in to pick up the pieces on the other end," Kevin Roose wrote in New York Magazine. "Alas, such is the Wall Street circle of life."

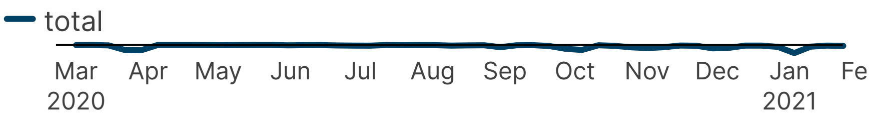
But the bad press didn't deter Mullen. Pretium raised an initial $1.2 billion in 2012 to sink into rental homes — which it operates under the name Progress Residential — across the southwestern and southeastern United States. The company raised another $900 million in 2014, according to Dezember's reporting, and another $1 billion in 2016. By the end of 2020, after swallowing up a rival company, Pretium was billing itself as the second largest owner and operator of single-family residential homes in the entire United States. "A big short," Dezember wrote in 2016, "is going long on the U.S. housing market."

The deal signed with PSP in January will allow Pretium to expand even further. The joint venture will invest an initial $700 million into single-family rental homes across the southwestern and southeastern United States, according to a press release. "We can think of no better partner to expand our presence in this increasingly attractive asset class and look forward to working with Pretium to deliver compelling results for our beneficiaries," Carole Guérin, PSP's managing director of real estate said in the release.

But if single-family rentals have a history of delivering solid returns, they've also proven, from the very beginning, to be incredibly controversial. The industry has been associated with a host of disturbing practices and trends, according to researchers, advocates and academics. "When you have these financial interests driving their strategies it puts a lot of people at harm," said Nemoy Lewis, the Provost's Postdoctoral Fellow in the department of geography and planning at the University of Toronto. For Lewis, an investment in the SFR industry is an inherently troubling one. "These types of investments are investments in the displacement of vulnerable people," he said.

## U.S. eviction applications during the pandemic by Pretium owned brands

Pretium operates homes under the name Progress Residential and Front Yard Residential




SOURCE: PRIVATE EQUITY STAKEHOLDER PROJECT TORONTO STAR

The core criticism of the finance backed SFR industry boils down to this: The companies have to deliver returns to their investors and to do that, they have to endlessly pull out more revenue on the one hand and push for lower costs on the other. "There's all these kind of disciplining structures in that system to make sure those investors get paid," Abood said. "They nickel and dime all the time." That can mean ever-higher rents, escalating fees, delayed maintenance and aggressive eviction policies. "People are actually being kicked out of their homes right now," said Pilar Sorensen, an investment analyst at the Private Equity Stakeholder Project.

Sorensen and her colleagues released a report in the fall showing that large corporate landlords had filed for almost 10,000 evictions in five states in the weeks after the CDC imposed an eviction moratorium in September. Not all of those are from single-family homes. But according to an updated database Sorensen provided, Progress and Front Yard Residential, a company Pretium acquired in January, have filed for nearly 1,000 evictions between them since the beginning of the pandemic.

In response to questions about the SFR business model and its own practices, a spokesperson for Pretium wrote, in part, "Progress is committed to providing residents with high-quality homes and superior service." He said the company aims to respond to all work orders with 24 hours of being notified and that Progress is not currently evicting residents "if they file a declaration that meets the CDC's eviction moratorium criteria." He added, however, that Progress has a "fiduciary responsibility to take appropriate steps in accordance with the law to try and collect rent owed."

For Martine August, an associate professor of planning at the University of Waterloo, the idea that a Canadian public pension fund, and a Crown corporation at that, is investing in this kind of financialized, housing is deeply disturbing. "Companies are acquiring this housing because of what they can get from it, not what they can put into it," she said. "That money is not coming for free. And it's harming people. And so to me, that's out of step with what the objectives of public pension funds should be."

PSP did not respond to questions related to the Pretium investment. A spokesperson did point the Star to a recent joint statement PSP signed saying the organization is committed to strengthening disclosures on environmental, social and governance issues and to "allocating capital to investments best placed to deliver long-term sustainable value creation."

For PSP, the Pretium investment, like the one in Revera, is fundamentally about balancing value and values. And for pension managers, that isn't always an easy thing to do. On the one hand, some members of the plan might be uncomfortable investing in a deal with one of the architects of a trade that has become shorthand for how Wall Street always wins. On the other, the fund managers have a fiduciary, legal duty to make money, to grow the fund and to keep the plan solvent.

A move by the government to force PSP to divest itself of Revera or avoid Pretium or any other partner could have dire consequences, some pension-watchers believe. "We are contributing to the best pension funds in the world, precisely because they got the governance right. They operate like investment firms at arm's length from the government. And they have added tremendous value over public equities and bond benchmarks," said Leo Kolivakis, the publisher of Pension Pulse and a former senior analyst at PSP and senior economist at the Business Development Bank of Canada. "If they start messing with the governance model, they're going to destroy Canada's pensions."

But Pretium and Revera are far from the only controversial investments by a Canadian pension fund. And the issue of values in investing is one that almost every pension fund of any significant size is grappling with, said Mike Simutin, an associate professor of finance and the associate director of research at the International Centre for Pension Management at the Rotman School of Management at the University of Toronto. "I don't think there is a hard and fast rule that suggests this is the way we're supposed to approach these questions," Simutin said.

"One line of thought, is if I'm a pension manager ... I'm investing on behalf of my investors or shareholders or my future retirees, and I want to deliver the best long-term financial outcome for them. And if that means that I should invest in let's say, tobacco stocks, then I'm going to invest in tobacco stocks, because otherwise I'm violating my fiduciary duty. Of course the flip side to this argument is that investing in certain assets, like tobacco stocks is not in the long-term benefits of my constituents. And what I should be doing is divesting from them."

## Revera long-term-care homes across Canada

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For Toronto lawyer Randy Bauslaugh, who leads McCarthy Tétrault's pensions and benefits group, the legislation is clear. "The Income Tax Act says that a registered pension plan has to have as its primary purpose the provision of lifetime retirement income," he said. "So I would argue that is a financial purpose. So anything that's relevant to that purpose, fiduciaries can take into account." Beyond that, though, it starts to get fuzzy.

"The notion of fiduciary duty is a bit like Plasticine," said Benjamin Richardson, a professor of environmental law at the University of Tasmania who has studied the impact of fiduciary laws on environmental investing around the world. "It can be moulded and shaped in response to changing social value. It's a bit of an empty vessel. It doesn't say very much. Essentially, what it means is a duty to be loyal to your client or purpose."

So the question then is, what is PSP's purpose. Should it be maximizing returns at any cost? If not, where should it draw the line? Who decides, in other words, what values apply?

For his part, Lewis thinks PSP members, at the very least, should be disturbed by their pension plan's decision to get into bed with Pretium and Mullen, thereby helping a man who profited from the foreclosure crisis keep profiting after the crisis too. "I would say no, I don't think that they should feel good about it," he said. "They shouldn't be comfortable about these investments, because in order for their retirement to be secured, they're displacing others."

For Abood, who spent years studying the sector, it's a question of reckoning. At the very least, she believes, anyone who invests in the single-family rental home business, including, PSP, should have to face up to what the industry can be.

"You're investing in this extreme commodification of housing that is potentially putting tenants and communities at risk," she said. "It is not a model of housing ownership that is going to, in any way, create more equitable outcomes."

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**Richard Warnica** *is a Toronto-based business feature writer for the Star. Follow him on Twitter: @richardwarnica*

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