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FINANCE

Meet Wall Street's Rent Collector

Redwood Trust sells $376 million bond backed by rent payments, its first deal since buying CoreVest American Finance in October

Beth O'Brien, chief executive of CoreVest American Finance LLC. The company's recent bond deal was its 10th since hanging a shingle in 2014. PHOTO: KEVIN HAGEN FOR THE WALL STREET JOURNAL

By Ryan Dezember

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One of Wall Street's biggest bundlers of mortgage bonds has moved into rentals.

Redwood Trust Inc., which specializes in packaging jumbo home loans into securities, recently sold a $376 million bond backed by rent payments. The deal was its first since acquiring CoreVest American Finance LLC, a lender to landlords, in October.

Redwood's $490 million purchase of CoreVest—as well as a smaller deal in March for fix-and-flip lender 5 Arches—marks a concession to the rise of renters since last decade's housing crash and the growing slice of the housing market being bought by landlords and flippers. Purchases by such investors accounted for more than 11% of U.S. home sales in 2018, their highest share on record, according to CoreLogic Inc.

"We're no longer making a call or taking an ideological view on the direction of homeownership," Redwood Chief Executive Chris Abate said. "We can lend to home buyers; we can lend to investors."

With its acquisitions, Redwood could originate more than $3 billion of loans to landlords and house flippers in 2020, said Matthew Howlett, an analyst with Nomura Instinet. Doing so wouldn't only produce fees for bundling the bonds, but also more than $300 million of securities—the lowest-rated 10% segment of each deal—that produce high yields.

> "It expands them into new asset classes but more importantly takes them where the market is going," Mr. Howlett said.

CoreVest's recent bond deal was its 10th since hanging a shingle in 2014, under another name, when investors were buying foreclosed homes from the courthouse steps. The company was backed by real-estate tycoon Tom Barrack's Colony Capital Inc., which also started a company to buy foreclosed homes to turn into rentals.

Beth O'Brien, CoreVest's CEO, had worked for Goldman Sachs Group Inc. investing in distressed commercial properties around the world and then for Citigroup Inc. in its residential mortgage-backed-securities business before she launched the rental lender. The idea behind lending to landlords was born from the struggle of big investors like Colony to find financing for their own foreclosure gambits.

If investors with billions of dollars and strong ties to Wall Street were having trouble financing their house hunts, surely smaller investors vying for foreclosures couldn't borrow either, Ms. O'Brien said. "They realized that there wasn't any institutional debt available," she said.

Meanwhile, the biggest home buyers, such as Blackstone Group Inc. 's Invitation Homes Inc. and American Homes 4 Rent, had begun to sell bonds backed by rent payments for thousands of homes they bought and leased out. Doing so freed up cash so that they could prolong their home-buying binges.

Those rent-backed bonds provided a structure for lenders to pass along risk to investors. Lending against other investors' properties was attractive because it produced about the same yield as owning rentals outright, cushioned against a fall in home prices by someone else's equity, Ms. O'Brien said.

Other house-hunting investors, including Blackstone and Cerberus Capital Management, came to similar conclusions. But neither of the landlord-lenders they launched has sold a rental bond since 2016, despite strong demand from investors.

"We're extremely bullish," said Greg Parsons, CEO of Semper Capital Management, which manages about $3.8 billion. About 15% of Semper's main fund is invested in single-family rental bonds, including those bundled by CoreVest. "Single-family has been a meaningful focus of ours within the construct of where the world is going."

To date, rental bonds haven't caused any losses for investors, according to analysts with Kroll Bond Rating Agency. However, Kroll warns, "the asset class remains relatively new in the U.S. and has not been tested through a recessionary period."

Lately CoreVest has been lending at a clip of better than $100 million a month. Its deals are a mix of monthslong bridge loans made to investors buying, rehabbing and selling occupied rental homes to other investors and longer-term financing on pools of rental homes and small apartment buildings.

A 300-home built-to-rent development in Huntsville, Ala., that was financed by CoreVest. **PHOTO:** JCF RESIDENCES

In all, the firm has lent more than $4 billion, including against 3,102 properties that were bundled into its latest bond. They include brand-new houses in Texas that lease for between $1,250 and $2,150 a month, duplexes around Boston that were built in the 1800s and go for more than $3,000 and apartments in Shreveport, La., that cost less than $700.

That is a much wider variety of properties spread over a greater range of locations than the homes that have wound up in the nearly $30 billion worth of rental bonds sold by the big landlords, such as Invitation and American Homes. Those companies and their closely held rivals with tens of thousands of houses usually stick to homogenous tract homes around booming Sunbelt cities. Those landlords' bonds tend to carry slightly lower yields than those associated with CoreVest's bonds, especially on the riskier slices.

Combined, those big landlords own about 2% of the country's 16 million or so rental houses, according to Invitation.

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"The next 15% is the market I'm focused on," Ms. O'Brien said. CoreVest lends to landlords with holdings that range from a few hundred houses to 10,000 or so. "There is a lot of consolidation there."

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