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IDENTIFICATION OF RISKS OF INVESTMENTS INTO RESIDENTIAL PREMISES FOR RENT IN POLAND

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While looking for investment opportunities, investors analyse whether a potential investment will bring satisfactory returns, the level of which depends on many risk factors. That is why it is necessary to analyse the potential risks in the process of investment management. Investors need to possess knowledge of such risks, their influence on the investment, and the methods of avoiding risk. Given the scale of investments into residential property, the focus has been on the risk factors determining the return on investment, which is crucial for a large number of small investors. Identification of different kinds of risks associated with residential premises is crucial for the management of such investments and translates directly into the level of return on the investment. The increase of the investments into residential property is caused by some small investors who are looking for an alternative method of investing. Their funds do not bring a satisfactory level of returns while in bank deposits. Those investors recognise the opportunity which arises from renting flats. The temptation of high returns compensates for the level of risk.

Keywords: *risks, investments, real estate investment management, investment properties*

1. Introduction

In today's turbulent economies and dynamically changing real estate market conditions, making effective and strategically viable property investment decisions has become very difficult [26]. The last few decades have witnessed the integration of global capital and real estate markets across the world. Global cross-border capital flows in direct real estate are expected to reach near USD 500 billion by 2020. Fundraising the world by

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private closed-end real estate funds stands at its highest first-half level with 80.3 billion US $ raised through the first two quarters. LPs continue to flock to mega-funds as they seek to consolidate their real estate investments [29]. Low-interest rates in today's developed economies encourage small investors to look for alternative investment opportunities that can yield more satisfactory returns. Taking into account the relatively small level of the necessary capital commitment and the material nature of the investment, investment purchases of residential units have become very popular among small investors. Investors investing in real property of this type of estate consider it to be similar to a bank deposit, believing the investment risk to be quite low.

Risk is one of the most important limits that define the scope of the financial decision-making. Special attention should be paid to the risk of long-term financial decisions. Risk is the chance to achieve an above-average return on investment [18]. Given the current situation in the real estate market, they estimate the risk of renting to be minimal. However, due to an increased interest in such investments, it was considered necessary to identify the related risk factors that investors should analyse on an individual basis while making investment decisions. Risks factors have an impact on the future benefit time and how these impacts occur. They are different for factors attributed to diverse risk types [32]. The growing list of macroeconomic factors naturally raises some questions. What are the relationships between different factors? How can the relative importance of different factors be evaluated? Their joint characteristics are more important than individual separate effects [25].

This study should contribute to reducing the risk of misguided choices, which, however, takes place on the market of investment properties regardless of a high level of optimism among investors. The tools that help in investment choices turn out to be very necessary given the volume of such investments and expected development. According to the report, *How the rental market looks like in Poland 2018*[1], the people of Europe have long protested against short-term renting and the legal regulation behind it. Authorities of many European countries decided to limit its expansion. As economic practice shows, rising rental prices and the conversion of entire buildings into quasi-hotels have become a problem for the economies of individual countries. In Poland, rents are still at a relatively low level of 4.2% compared to the EU average of 19% but it should be noted that they are on an increasing upward trend in Poland. As follows from the report, over the next ten years the rental market in Poland may even double, i.e., increase by 800–900 thousand flats for rent. The expected changes may be supported in particular as a result of limitations of access to mortgage loans and progressing social changes – there will be more and more one-person households, divorced people, and economic immigrants from Eastern Europe. In addition, there will be changes in mentality and a growing willingness to share, including the place

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[1]https://www.nbp.pl/publikacje/rynek_nieruchomosci/raport_2018.pdf

of residence [39]. As said by Jud, Roulac and Winkler [23], several past studies have examined the risks and returns of housing market investment [9, 1, 17, 40, 46, 36, 7, 13].

The interest in investing in apartments for rent results from a satisfactory profit-risk profile, which is associated with a drop in bank deposit income to such a low level that it does not even guarantee protection against inflation – according to Eurostat, inflation in Poland for 2020 was 3.7%. With the tools that are now available for fixed-income investors, it is time for sustainable investments and the integration of environmental, social, and governance factors into their strategies [47]. The impressive popularity of a residential unit as a profitable investment can be attributed to three factors. First of all, the Polish national mentality connected with the tangible nature of its object is important. The second factor stems from a well-established, but not necessarily an entirely correct belief that there is no investment risk or the need to have specific knowledge and experience as a necessary condition for earning effective profits on real estate. Thirdly and finally, it is connected with the lack of competitive forms of capital investment given the record low-interest rates. The rental market in Poland is growing at a rate of about 25–30 thousand new flats per year, which, contrary to what one might think, is not a significant number given the current conditions that prevail in Poland. The interest rates established by the National Bank of Poland are likely to remain at the current record low levels. These are good, if not optimal, prospects for the continuation of the investment boom in the domestic residential real estate market [41].

The literature identifies six key drivers that determine the attractiveness of real estate markets, in terms of their capital supply and demand conditions [33]:

- economic activity,
- real estate investment opportunities,
- depth and sophistication of capital markets,
- investor protection and legal framework,
- administrative burdens and regulatory limitations,
- socio-cultural and political environment.

The determinants vary between countries and in time. The current state of the housing market can be characterised by several key parameters: supply in the housing market, solvent demand, existing mechanisms for the purchase (sale) of housing, factors affecting the formation of market prices, the duration of the investment cycle, and legal support. In literature, there is a large number of works devoted to the study of the housing market, while the range of issues and problems under consideration is very wide. Conventionally, they can be divided into three groups. The first group of studies consists of works devoted to the analysis of the housing market in general and studying the dynamics of key indicators. The second group of works is aimed at studying demand. Finally, the third one is based on the study of the supply side. The main conclusion from the analysis and development of market relations in the field of residential real estate is that some progress has been made in the formation and development of the housing market. At the same time, the analysis made it possible to identify the characteristic features of the housing market sectors, the possibilities of their expansion and forecasting, as well as the creation of the market environment necessary to meet the housing needs of the population [43]. The purchase of a residential unit for rent is a popular solution among small investors. Such a step is taken by investors tempted by profits not only from rents but also by potential increases in the value of the real estate, which is particularly possible in the emerging markets. Investment in real estate is a slightly different opportunity for investing money than investment in securities or investment funds. The main features of a real estate investment include low flexibility and long-term efficiency [34]. lt is usually preferable for foreign investors to have investments in stocks and securities treated as ineffectively connected with trade or business. Unlike real estate investments, the allowance for deductions is seldom an important aspect of tax planning for these investments. While brokers' fees, transfer taxes, and similar expenses are often incurred, the amount of these expenses is usually insignificant. As real estate investments, capital appreciation is an important aspect of investments. If these investments were considered effectively connected with trade or business, then the capital appreciation would be subject to capital gains tax at the time of their sale or other disposition [5]. Whether it is worth investing in real estate or not is usually determined by the amount of capital available to an investor and the current market situation. The factors which distinguish real property investments from other tangible investments include [6]:

- the location of the property – one of the most important features which determines its value and usability,
- a non-transformable character which ensures a certain uniqueness of a given property,
- long-term nature which allows the owner to obtain financial benefits in the long term but at the same time, the owner may treat such property as a consumer good with additional value in use or as an investment generating regular income over time.

A clear objective of any investment is to achieve a measurable return which, expressed in numerical terms, can be compared to the profitability of alternative forms of capital investment. To calculate the annual rate of return of an investment into a residential unit, it is necessary to compare the sum of the annual rental income with the price paid by the owner to purchase it. The annual rental income should include the owner's costs, i.e., administrative rent, rental income tax, repair, and overhaul costs, or a period of one and a half months with no income due to a change of tenant. As follows from the E-VALUER Index 2018[2] report which presents the results of the research on the profitability of renting new flat, higher rates of return ranging from 5.3 to 5.5% are much easier to achieve in smaller cities. On the other hand, in the largest agglomerations, the rates range from 4.1

[2]https://www.emmerson-evaluation.pl/wp-content/uploads/2019/05/report-e-valuer-index-2018-english.pdf

to 5.4%. Overall, rates of return are relatively low, further emphasising the need for careful attention to risk factors, as low returns are not tolerant of mistakes and, as a result, an unidentified or misjudged risk factor can cause a property to begin producing a loss. This aspect is important because when comparing the E-VALUER Index report for 2018 with the report for 2021, one can see a decrease in the level of profitability, for example, for large cities from a ceiling of 4.1–5.4% they fell and were in the range of 3.0–4.8%. Real estate, considered as a long-term investment, effectively protects investors' capital against impairment in periods of adverse market changes and high inflation. Considering a real property in terms of stability of its value, a potential investor can also rest assured that the rate of increase in property prices in the market significantly exceeds the rate of loss of value due to technical wear and tear. In this respect, it should be noted that real estate investment has the potential to generate twofold income.

Real estate, considered a long-term investment, effectively protects investors' capital against impairment in periods of adverse market changes and high inflation. Considering a real property in terms of stability of its value, a potential investor can also rest assured that the rate of increase in property prices in the market significantly exceeds the rate of loss of value due to technical wear and tear. In this respect, it should be noted that real estate investment has the potential to generate twofold income [11]:

- current income resulting from the regular rent payments,
- capital gains arising from the sale of real estate.

The above arguments show the advantages of real property investments. However, just like any other investment, real estate investments also have drawbacks. If the market for real estate is efficient, we would expect the price appreciation experienced by real estate investors to be similar to the appreciation of broad-based real estate indices. On the other hand, there are reasons to believe that real estate investors may outperform real estate indices [10]. The main one is the aforementioned capital intensity since the purchase of any real estate is connected with the expenditure of several hundred thousand zlotys. It is quite a large amount of money from the point of view of most private investors. Low liquidity, which is directly related to the high purchase price of the property on the market, is another disadvantage. Poor liquidity of real property is not only related to the problem of finding a buyer, but also to the number of procedures related to sales (drawing up a notarial deed, verifications, analysis of the legal status). Furthermore, properties require management and continuous investment to be kept in good condition [6].

Summarising the essence of investments into real estate, it can be stated that such an undertaking may bring very positive economic results if carried out by an experienced investor. It should be noted, however, that despite the assumed low investment risk, lack of knowledge of management principles, overestimated purchase, and incorrect investor's decisions may result in negative consequences and, as a result, lead to losses or a significant decrease in the effectiveness of the investment. The objective of this study is to identify the risks that affect the profitability of such investments based on a survey performed.

2. Risk of investments into real properties

Business failure is a characteristic feature of all economies. It has an impact on a business as well as on its surroundings. Therefore, it is necessary to mind the prediction of the risk of business failure [18]. In risk assessment, it is important to identify the risk factors of the project and then, by estimating them, to take them into account when making an investment decision, which should be supported by the research described in the work.

Large institutional real estate investors, such as life insurance companies and pension funds, may tend to diversify their real estate portfolios by property type. Diversification is shown to potentially enhance portfolio efficiency [31] and to increase returns [37]. The need to exploit the benefits of diversification by exploring a wider range of alternative investment options makes the investment safer [26].

Risk in investment activity is a measure of a broader economic risk. Normally, the notion of risk is not only limited to possible losses but encompasses the possibility to generate profit [27, 35].

Thus, the risk is tantamount to the likelihood of not obtaining the return expected by the investor and is a decisive issue at the stage of making investment decisions. Every decision is a choice with consequences, and any action taken based on that decision involves a risk [11]. Real estate including the housing market, in contrast to the financial market, has its characteristics of risks which includes fixed physical attributions, specific locations, long-lived and illiquid assets, as well as large indivisible investments [20, 15]. The profitability of investing in real estate, which by its very nature requires significant capital expenditure, is to identify a situation where the market level of rentals will justify the capital expenditure incurred, expressed through the purchase price. The main six variables that have the greatest impact on investment success are: purchase price, increase in the market value of the property, operating costs, effective gross income, loan interest rate, and loan duration. The application of the discount cash flows (DCF) method makes it possible to determine how the cash flows behave in a way that is impossible with other methods. The net present value (NPV) is the best-known method to date which can be used independently to assess the effectiveness of an investment. In practice, the risk of different projects is very rarely at the same level, as confirmed by the diversification technique. Several smaller investment projects carry less risk than one large project. The NPV favours larger projects, while smaller ones have a lower risk [28].

From the point of view of cash flows, the real estate investments entail the following significant risks:

- capital risk related to the possibility of a loss of the initial capital,
- income risk related to the probability of not achieving the profit assumed in investment analyses.

In terms of the risks concerning the coordination and support from other groups, the contractors do not have sufficiently effective measures to proactively mitigate the risks arising from homeowners' cooperation. Proactive risk management needs to enhance the risk perception of risk-source-related stakeholder groups in consideration of their more effective proactive measures compared to the affected groups. Stakeholders related to risk sources should share the risk, and their increased responsibilities can motivate them to enhance their awareness of proactive risk management [22].

All sources of risk influence the level of overall risk which is one of the investor's decision-making criteria [3]. Despite the perception of the risk of real estate investment as low, it is impossible to eliminate it. It should be also noted that this risk is often disregarded by small investors. It is possible to effectively mitigate the risk in question to ensure the expected rate of return on a given investment through efficient management, which includes identification, measurement and control of risk sources. There are many studies on the risk of investing in real estate in the literature, however, they refer to very broad investment in real estate, and as such, they may be applied for investments of natural persons in residential units to a very limited degree only [16, 42, 44, 45]. The classification of risks of investing in real estate, which can be considered appropriate to investments into residential units, is as follows [24, 30]:

- risk related to the purchase of the real estate,
- risk associated with the sale of the real estate,
- risk related to the lease of the real estate,
- other external risks.

The risks associated with the purchase of real estate include:

- valuation risk, which is related to the possibility of unreliable assessment of the property market value,
- transaction risk, which is closely related to the contract conclusion process, as any errors in the contract may prevent a smooth takeover of the property by the buyer or lead to the transaction being cancelled.

The risks associated with the sale of real estate include [21]:

- valuation risk and transaction risk, which are the same as
- in the case of property purchase,
- liquidity risk, since due to its high value, the real estate asset is characterised by low liquidity.

In the case of risks related to the lease of real estate, we can distinguish [6]:

- Risk of lack of tenants is the most important type of risk, as it directly determines whether the investment yield will be obtained. It should be noted that the risk of shortage of tenants is mainly related to the demand in the real estate market. This type of risk can be effectively mitigated by appropriate actions, such as the purchase of the real estate in an appropriate location, concluding contracts in such a way that they end in the high season and not in the low season, as well as extensive marketing activities.

• Risk of tenants' failure to perform under the agreement: in this case, the risk of a failure to pay the rent is the most significant. However, this risk can be mitigated through appropriate clauses included in the agreement and thorough checks of the prospective tenants.

The remaining risks can be classified as other external risks and include:

• Market risk related to the possibility that an investor may incur a loss due to changes in property prices, rental rates, or taxes. Specifically, housing risk factors are defined as housing return differentials between the given period's highest and lowest-ranked housing markets, defined concerning certain market characteristics [19]: risk of state interference in the property market, including the possibility of state influence on profitability or ownership of investments. All the risks mentioned above apply to investors whose investments are based solely on the purchase of a ready-made property.

Researchers have long been asking the question of whether the sample rates of return imply that the decision to own households instead of rent was economical. The question of what these sample rates of return may imply about those earned over the same period by including a charge from each year equal to the product of the member's invested equity capital. The answer is simple: that implies investors view housing as significantly riskier in the ex-ante sense than common stocks [1].

In the area of research into the risk of investing in real estate, one can cite the results of a study by Allen [2], who examines the risks of different forms of investment and assigns them ratings from 1 to 10 (the higher the rating, the higher the risk is). Concerning developed properties, the highest rating was assigned to liquidity risk (7 points) followed by management risk (6). Slightly lower was the perception of risk concerning the loss of yield or market risk as a result of the associated risk, with a score of 4 points. Other risk factors were assigned lower ratings.

The thesis that the risk of the real estate market is estimated as moderate was put forward in 1990 by Komar who estimated the weights of different types of risk for different financial instruments. The risk of various forms of investment according to Komar is presented on a scale from 1 to 10. The market risk of 6–7 points, bankruptcy risk of 5 points, and inflation risk of 1 point prove that the risk associated with real estate is moderate. The author assigned the highest weight, 10 points, to liquidity risk.

Although these studies were conducted years ago, they show a continuing perception of real estate investment risk as low and point out the main risk factors.

3. Identification of risks connected with investments into residential premises

Chandra-Putra and Andrews say: *The econometric tradition offers the hedonic pricing model, an established method in real property studies that sticks close to the empirical data and is useful for estimating the typical tradeoffs that economic actors make* *among quality attributes of goods and environmental qualities at a given point in time, including the loss of value due to flood risk* [14, 38] *the extent to which flood risk is capitalized into property value shows the evolution over time* [4] *and the presence of neighbourhood effects* [12]. *However, the hedonic model does not adequately detect the non-marginal changes present within the dynamics of the real property market* [8]. A questionnaire-based survey was conducted to identify risks that affect the profitability of investors that invest in residential units. A survey with multiple-choice questions was prepared. The questions concerned the risks that the respondents encountered in connection with their investments in flats, indicating which of them caused the greatest difficulties and which contributed to a decrease in the expected rate of return. The questionnaires were then sent to investors. The survey was conducted based on resources and relations with a company specialized in lease management carrying out its operations in the area of the 5 largest Polish cities and operating the Mieszkaniami.pl website, which attempted to contact 100 investors with whom the survey was conducted. The research sample was selected purposively, therefore the results presented below should be treated with caution, as hypotheses constituting a contribution to further research, especially in the context of the recent pandemic. The described results are only a fragment of this research.

The results allowed the identification of risks, comparison of such risks with classifications given in the literature, as well as the determination of their impact on the profitability of investments in residential units. Before the preparation of the questionnaire, pilot surveys were conducted in the form of interviews with small investors and a dozen or so cases of investments into residential units were analysed to make the questions more specific.

Appropriate identification of risks related to investments in residential premises should increase investor awareness, and therefore should also contribute to the improvement of profitability of future and existing investments. Currently, one can encounter investors who do not know much about property investments, but they know that the vast majority of their colleagues invest their capital in this way. That is why investment return is comparable to that of a bank deposit, and some may even suffer losses. Given the scale of the investment, the number of small investors, as well as the forecasts related to the increase in the number of such investments, research in this area is very much expected by investors and can be very helpful for them in the decision-making processes.

The research indicates that a relatively large number of investors are aware of the risk associated with investments into a residential property (Fig. 1). The largest number of respondents, 67% of those polled, perceive the risk related to tenancy. 19% are concerned by the risk of purchase. 12% of respondents see the risk related to the sale of real estate. Therefore, it can be stated that in the opinion of investors, the risk of tenancy and related factors are the most significant, while the exit from such investments, i.e., the risk related to the sale of real estate, is the lowest.

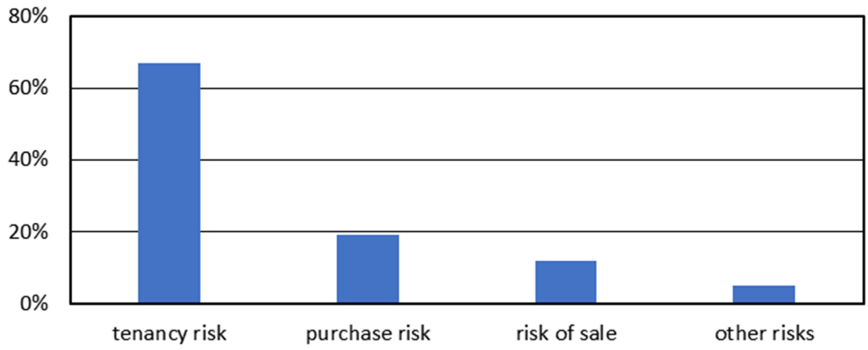

Fig. 1. Investors' awareness of risk connected with investments in property

The main risk factors associated with the purchase of real estate that have been identified include the location of the property, price, rate of return, preferences, tax strategy, building and the nearest neighbourhood, and others (Fig. 2). Research conducted on a selected sample shows that investors consider the price of the property to be the most significant risk factor. This is what 91% of the respondents said. The price is directly related to the rate of return, therefore investors should also indicate the rate of return which is strongly dependent on the purchase price of the property. Yet, only 23% of respondents are aware of the risk associated with the rate of return. The results show low economic knowledge of the respondents, probably caused by many articles in the press, on television or stories of their colleagues on how profitable and easy it is to invest in residential units.

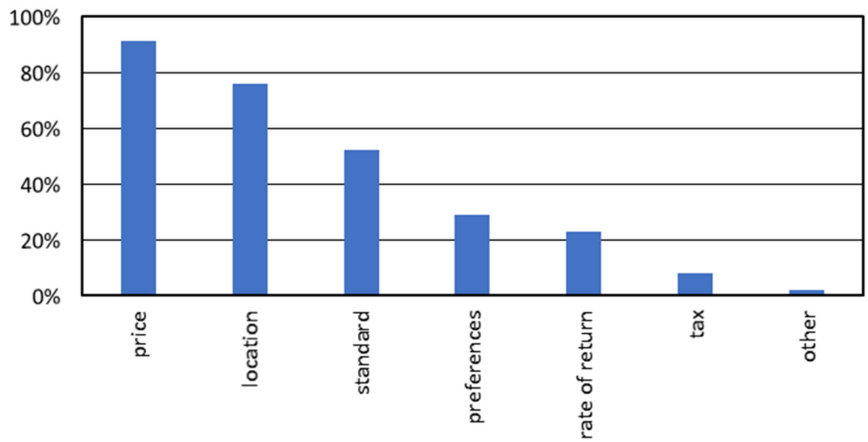

Fig. 2. Risks taken into account when purchasing property

The location is another risk factor that is the investors consider to be quite significant. 76% of the respondents indicated that the location of a property is important for them, and they take it into account when buying a property. This trend should certainly be assessed positively, as the choice of location directly influences the length of vacancy, i.e., the rate of return on investment. When buying real estate in the city centre, the risk associated with renting out, and more specifically the risk of lack of tenants, is certainly limited (in consequence, the length of possible vacancy is minimised). Moreover, buying a property in the city centre is more likely to increase the value of the investment and in the event of any turmoil in the real estate market, the risk associated with the decline in value is the lowest. The location factor may be also important for those investors who indicated that they were guided by their preferences when choosing their investment. In total, 29% of the respondents indicated their preferences, which is quite a lot. Investors' preferences may be risky in this respect since some people are looking for properties where they would like to live themselves. This leads to choosing, for example, flats on the outskirts of the city, where there is a lot of greenery, quiet, and beautiful views. Such a choice usually involves a long journey to the city centre, lack of tram connections, and therefore a high risk of lack of tenants (long vacancy periods), and in the case of problems in the real estate market, these are certainly the investments that are more likely to lose value. Another common example is finding a beautiful one--room flat in a new apartment building with a magnificent view and a very high price. Usually, the price of such an apartment is similar to the price of two-room apartments in the immediate vicinity. As a result, the rate of return on such investment will be low. It is more profitable and safer to purchase a more versatile property available for a wide range of tenants. Sometimes, investors buy expensive properties with large space areas and with luxury equipment. These are associated with a high risk of the vacancy rate, theft, and destruction. It is very difficult to rent a property with a TV set worth PLN 60 thousand in the living room, especially for a long time (c.f., Mieszkaniami.pl), and in the case of short-term rental properties of such kind are usually rented for special events. The premium real estate rental market in Poland is quite complicated and usually attracts foreigners, raised in a different culture or dishonest tenants whose intentions concerning rental are not fair from the very beginning.

The factor described as the building and the nearest neighbourhood was chosen by quite a large number of respondents of 52%. This is a fairly positive result, especially on the secondary market, where old houses may be in various conditions and the nearest neighbourhood may discourage future tenants.

The fact that the tax strategy was selected by only 8% of the respondents should be assessed negatively. This has a significant impact on a reduction in the rate of return on investment. When investing in a property on the secondary market, one can buy a property that has already been in use for more than 5 calendar years, and if it is fully owned, i.e., one can depreciate the property as a fixed asset, then the depreciation charges can amount to up to 10% of the value of the property. The possibility to set a high depreciation rate will ensure that there will be no need to pay income tax for a period of about 20 years (if settled according to general rules), which will significantly improve the investment profitability. In the case of residential properties with cooperative ownership rights, the depreciation write-offs can amount to up to 2.5% of the value of the property, as it is the intangible asset and not the fixed asset that is subject to depreciation. In the case of the purchase of property on the primary market or on the secondary market which is to be let within five calendar years, the maximum depreciation rate may be as low as 1.5% of the value of the property per annum. It is therefore clear that the tax strategy should be taken into account at the investment planning stage. Other factors, mostly the sentiment, were marked by 2% of the sample.

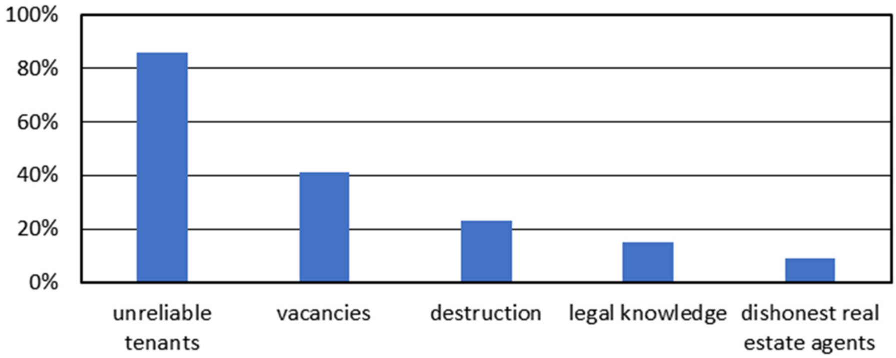

Fig. 3. The most significant risks associated with property rental

The risk associated with renting a property is the most noticeable among domestic investors (Fig. 3). The risk factor that causes the most concern is tenants' failure to perform their obligations under the agreement (no payment, no possibility to remove tenants from the premises, etc.), which was noted by 86% of those polled. The risk of the tenants' failure to comply is directly related to the lack of legal knowledge to which only 15% of respondents admit. The law relating to the rental of residential property in Poland is quite complicated and certain issues are sometimes ambiguous. An appropriate agreement can certainly reduce the risk associated with fraudulent tenants. The risk of failure to pay may also be mitigated thanks to entering into a contract with a management company, which will sign a properly secured lease agreement and other required documents with tenants, and will check the prospective tenants in the available Debtors Registers before executing any documents. Such actions will significantly reduce the likelihood of problems related to unreliable tenants. While discussing this factor, it is worth mentioning that some investors quite often overstate the rental fees. The cases in which the price significantly differs from the market average in a given period often lead to a situation in which the interested tenant that intends to sign the contract is a person who has not managed to rent other flats because of a failure to pass the checks. The same happens in the case of premises to be rented which are in very poor condition. It is quite common that difficult housing conditions attract difficult tenants.

The risk factor lack of tenants was indicated by 41% of respondents. It is quite an important factor as it results in a lower return on investment. Some companies on the market believe that one and a half to two months a year is a normal vacancy period that cannot be considered as a risk of a lack of tenants. According to information obtained from the specialists from Mieszkaniami.pl, some housing investments could have had 3–9 months of vacancy between successive lease agreements. The average annual vacancy period of properties managed by Mieszkaniami.pl was 16 days from the last period. The average of 16 days is a good result, but the company explains that new flats for rent are coming in all year round and those that come in the most difficult periods of the end or at the beginning of the year inflate the average. If we were to examine the average vacancy length of one specific property that is already managed for a longer time, this figure would be several times lower than 16 days. One can see that the difference is very significant. The length of vacancy should also be associated with the real estate location, marketing activities, and skilful planning of the lease agreement termination date.

23% of respondents are afraid of destruction and theft. This risk factor is mitigated thanks to the appropriate evaluation of a prospective tenant before signing the contract and a properly drafted contract, which means that the owner needs to possess sufficient legal knowledge.

9% of respondents are afraid of cooperating with dishonest real estate specialists. This is certainly due to previous experience of investors, stories told by family, colleagues, and media coverage. It is possible to mitigate this risk by a thorough reading of the agreement before signing and consulting with a lawyer if required.

4. Conclusions

Despite a significant increase in apartment prices, the investments in premises for rents are still attractive, as rental rates also increased considerably. The average profitability of net rent depends to a large extent on the investors and their knowledge of the market and associated risks. Small investors are looking for an alternative method of investing their funds which do not bring sufficient benefits while on bank deposits. One can earn much more on renting flats than on deposits. The investors, tempted by high-profit potential, accept the risk associated with this business.

Market data as of December 2020 (regularly reported by the National Bank of Poland) clearly shows that many of the deposits offered do not even cover inflation. The average interest rate on a deposit with a maturity of 6 to 12 months is just 0.2% which, after capitalisation and the deposit tax burden, works out to a comparable to a negative interest rate. It is not surprising, therefore, that people search for other solutions that will make it possible to protect money from inflation and multiply it at least a little.

However, when investing in residential properties, one should remember that renting a flat is not the same as buying treasury bonds or making a deposit in a bank. When depositing money in a bank one knows in advance when and how much will be recovered and in the case of a failure, money is secured by the Bank Guarantee Fund. Yet, when one purchases a flat for rent, there are not any guarantees. The survey results speak well for investors in the housing market, as they identify rental risk as the most significant risk perceived when investing in real estate. Several factors influence investment uncertainty, and a few key ones can be highlighted. In terms of renting itself, respondents paid particular attention to unreliable tenants. There is always a risk of dealing with dishonest people and although it can be mitigated, it happens that the tenant does not intend to pay rent after signing the contract, the Polish law protects the tenant more than the owner of the property. Another key factor according to the investors surveyed is property vacancy periods. It is also unknown when a tenant will be found, and each month of waiting for one is tantamount to a zero income and obligation to cover maintenance costs, including rent and other fixed expenses. Unexpected renovations or even devastation of the premises is also a problem recognised by the respondents. From the point of view of the investment in a residential unit, the surveyed investors paid special attention to price, location, and standard. The price of premises directly translates into the level of profitability of a given investment, and the location and standard have an impact on the previously estimated rental risks – a better location means shorter vacancy periods, and a similar impact may be exerted by the standard, which additionally influences higher rent, which translates into the rate of return.

All these should be taken into account when analysing the profitability of investing in a flat for rent and the associated risk. Thus, the awareness of risks of investments into residential premises is so crucial for the management of such investments, which translates directly into the level of return on the investment.

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