Institutional Rental Market in Poland
An emerging market in the residential sector
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Polish rental market: a chance for institutional investors

Investments in residential rental property are currently in vogue in many Western European countries, including the UK and Germany. The institutional investors' appetite for buy-to-let schemes is in fact larger than what's available on the market, which has led some investors to look at new property developments and seek opportunities abroad. Poland has already become one of the core countries in the EU for investments in commercial property. But should institutional investors also consider the Polish residential rental market?

The answer is yes. Demand for rental property is currently on the rise in Poland, supported by demographic and economic trends. At the same time, there is a shortage of existing rental stock offering adequate quality at market prices. Investment funds were the first to invest in new quality supply, but these investors often made mistakes in product choices and untimely investments. However, the present circumstances are very favourable for rental investments. Despite a stable demand for housing on the primary market and decreased price levels by 15-20% since the peak in 2008, there is significant oversupply of new units. Developers are struggling with slow sales and are now selling units at discounted prices. There is also rising interest among developers to sell entire buildings en bloc, as many of them have built up significant land banks. On top of these factors, the macroeconomic environment in Poland is sound with regard to growth, demographic and social trends, legal and tax issues, as well as facility management and rental services.
Key supporting trends

Poland's highlights include economic and political stability and a large domestic market. The banking sector has proven resilient and remains stable. EU membership guarantees safety and stability in legal terms. The country's demographic situation is among the most favourable within the EU, with the young forming a large share of the population. Many major international funds already operate in Poland, chiefly in the commercial property segment. The Polish market is no entry barrier for investors already active in the country. Tax and business structures are comparable with those applied across the EU, rules are clear and structures well tested.

Though the Polish housing market mostly focuses on owner occupancy, over the past few years renting has become an alternative for many households. Tightened requirements for mortgage financing, uncertainty on the labour market and limited economic growth perspectives lead to households being uneasy about getting into long-term debt. The typical strategy of young Polish couples and singles – first buying a small apartment and living there for a period of 5 years or so before moving into a larger apartment – has become too expensive.

Besides these current tendencies, housing needs and living patterns are changing fundamentally in favour of the rental sector. The young generation of Poles has a different attitude towards property. The symbolic need for ownership is gradually becoming less convincing, while mobility and liquidity rationales become more prominent. The migration mostly of young people to Warsaw and other large Polish cities is ongoing and fuels the need for rental properties, especially when it comes to students and young people in search of work. An increasing number of people is calling for support of the rental housing market, including government members, interest groups and the media.

It is no surprise to me that German institutional investors are increasingly taking interest in Polish multifamily housing projects. As investment opportunities in Germany get scarcer, expansion to Poland seems to be a natural step for German funds. It is the right point in time in the Polish property cycle, developers are interested in delivering the right investment product and the right expertise is available in Poland to support such investments.

Hans Maltz, Property Market Analyst
Rental market scale & quality

The vast majority of both existing and new residential property in Poland belongs to private individuals. According to official statistics (2011 National Census), around 10.7% of the dwelling stock is rented at reduced rents, mostly in communal or social housing (5.7%) and on the basis of cooperative tenancy (2.1%), followed by dwellings located in stock of state-owned companies (1.2%), the State Treasury (1.2%) and public building societies (TBS; 0.5%). The remaining housing stock is mainly owner-occupied, though includes a certain number of units rented by the owners for free market rents. Official data estimate this market segment to cover some 2.2% of all households, although this number seems to be underestimated and account for at least twice as much in reality. An institutional commercial rental market is virtually non-existent, though. Apparently, the rental sector for free market rents by private landlords is most developed in Poland’s largest cities and resort towns.

The most recent official data from the 2002 National Census show that 21% of households in Warsaw lived in rented apartments, although about half of this comprised rentals in social and communal housing. The private rental sector remains highly opaque and hard to estimate. A large amount of rental agreements are not officially registered to avoid taxation (even though the government has recently introduced eased lump-sum taxation).

In the free rental market, one can distinguish between three types of rental property using criteria such as technical quality, building age, management or legal/contract issues: (i) rental units in new housing stock, (ii) rental units in old housing stock of decent quality as well as (iii) rental units in old housing stock of low quality.

The first type of rental unit is typically situated in new housing projects completed by developers over the past 5-10 years or in refurbished stock. Rental units are characterised as having reasonable to good quality. Also the estate itself as well as common areas in the building will be of decent quality. The owners consist of households that have moved to a larger dwelling and for some reason kept the former one. Other landlords are individual investors and a few institutional investors. The property is either individually managed or managed through small service providers. Tenancies are regulated by a standard rental contract, commonly limited to one year, which can potentially be extended.

The second type is made of rental units in old housing stock, either built in the socialist era or in the pre-war period. The unit itself typically has an acceptable quality, though the building and common areas are often in poor shape. These units are typically inherited and rented out without any long-term vision and with limited financial means for modernisation or renovation. Since rents in large cities are already high, landlords are reluctant to invest in any improvements. The tenancy is regulated by a standard contract, with the same limitations as in the first case.

The difference between the second and third types is that the quality of the third one is at best mediocre and that there is no tenure agreement at all. Tenants have no assurance that they will not be removed. However, rental levels are low.
Rent levels

Given the housing shortage and relatively high price of apartments, renting on the free market is for many households the only option to live in an individual dwelling in Poland’s large cities. It is particularly common among young people migrating to cities for work or education. Yet, it also affects many existing city residents desiring to live on their own, for example, adult children leaving the parental home for the first time or ex-spouses after divorce.

Rent levels are relatively high when compared to income. The highest rent levels can be found in Warsaw, which also offers the widest choice of rentals. A studio unit of 30 sq. m usable floor area costs a total of some PLN 1,500 per month on average. This is about one third of the average salary in Warsaw. Typical one-bedroom and two-bedroom units achieve averages of PLN 2,000 and PLN 2,900, respectively. The average rental level in the Polish capital exceeds PLN 46 per sq. m, i.e. more than EUR 11. Extremely high rents in the city centre evidently impact the high average level. However, in peripheral districts rents can be as much as 40% cheaper.

The second-tier markets of Krakow, Wroclaw, Poznan and the Tri-City reveal cheaper rents from PLN 30-35 per sq. m, i.e. approximately EUR 7-9. The monthly rent level for a typical studio unit is at about PLN 1,100 in Krakow, Wroclaw and the Tri-City. In Poznan the rent for a studio is somewhat lower, while on occasion one may find a rental offer of PLN 1,100 for a studio in the very city centre. Rents are lower in subcentral locations with good transport links, while the lowest rent levels can be found in case of apartments in peripheral areas. Though not as marked as in the case of Warsaw, apartments in peripheral areas of these cities display rental levels of up to 20% lower.

Offers for apartments at market rents can be found in privately owned stock in condominiums and cooperative housing. The quality of the rental units offered can vary greatly. The majority of free-market rental properties in the Polish capital are still located in buildings constructed during the socialist period. Others are situated in pre-war housing stock. Only a few of these rental units are refurbished. New quality housing constructed during the past 10-15 years has been sold primarily to owner-occupiers, although part of this stock has been subsequently let by the owners.

From my experience, the management of the letting process impacts greatly on the success rate. We are able to let a studio unit within an average of 21 days (or 5.8% average void period), while large luxury units take obviously longer. The rent level plays a key role for each type though: An owner who demands a 10-20% higher rent than the local average at best doubles the time to let, while lower rents can considerably speed up the letting process.

Sławek Muturi, Polish Residential Landlords’ Association
Case studies

Only a few institutional investors have rental property portfolios in Poland. This is mainly due to the fact that most of the Polish housing stock, which could potentially be rented at free market prices, is held by individual apartment owners. Privatisation of housing stock has led to dispersed ownership structures and it is hard to find whole buildings that belong to one landlord. Exceptions are a number of pre-war tenement buildings, which have often been subject to restitution proceedings and restored to their original owners. Thus, investment opportunities for institutional investors are scarce within the existing housing stock. For funds that want to invest in rental property there is a need to concentrate on new residential projects built by developers.

Examples of investments into rental property portfolios indicate that the rental market has potential, though many investment schemes were flawed in terms of product choices and untimely investments.

Holland Park
In 2006 ING Real Estate sold two apartment buildings comprising 64 units to Keen Property Partners (KPP), which continued letting the apartments for extended periods. After receiving a permit to change the designation to residential purposes in 2009, the investor continued letting the apartments but decided to gradually sell the portfolio to individual buyers. By now only a few units remain in the hands of KPP, all of them are offered for sale – even offered with a 2-year rent guarantee calculated at a 5% rate of return on investment within one year.

Poland Geared Growth
City Life PCC Limited, a Guernsey-based open-ended investment company, created the Poland Geared Growth cell in May 2006. The investment strategy was to bulk buy apartments as buy-to-let investments. The target market was corporate tenants and professionals. The fund attempted to bulk buy at discounts of some 5% to 15% off the asking price. Although the purchases took place at the market’s peak, current net yields are reported at 3%. All properties in the Core Portfolio, with one exception where 24 out of 46 units are rented, are fully let out.

Besides these funds investing in buy-to-let schemes, several institutional investors have invested in residential development projects or housing development companies. An example is Arka BZ WBK Fundusz Rynku Nieruchomości 1 and 2, both investing partially in stakes in residential projects and investment sites designated for residential use. Another case is BPH Nieruchomości Europy Wschodzącej, which has invested in several developers active in Poland. The German insurance company Allianz also offers funds investing in developers active in Poland.
Renting and facility management

Renting process

Long-term funds typically do not take on high rental risk, but purchase larger property portfolios that have already been let. In this case, the funds deal with the ongoing management of leases and the properties. In contrast, a family office investor whose aim is to build up a larger rental portfolio, is likely to take the burden of the rental risk, once the property is bought from the developer. Alternatively, a deal with the developer could presume a certain occupancy level with tenants with predefined contracts. In any case, the lease-up of a newly built development is an essential element in the whole business model.

Several well-functioning and reliable rental agencies are available in Poland’s large cities. Rental services are currently offered by brokers and by small specialised companies that provide both facility management and rental services. The transparency of the rental market is increasing, though there is room for improvement. Very few apartments are leased by agents based on an exclusivity arrangement. Thus, apartments are typically presented in several listings on the internet. Due to this dispersed structure of the rental housing stock, the success rate for rentals is hard to measure. However, the experience of rental brokers indicates that vacancy rates for proper rental products can be held below 5%. On the other hand, it is tough to rent an ill-fitting product on the market. It is crucial to get the choice right for the rental project, including the structure of the apartments by unit type and floor space, adjusted to the specific location and target market.

The most common rental product comprises apartments sized up to 50 sq. m, though the demand for larger units has risen in the recent years. Tenants are interested in apartments located in central locations and in those products in the outskirts where prices are up to 30 percent lower. At present, most units available for rent are owned by private individuals. The majority of leases are signed for a period of 12 months.

Mariusz Kania, Metrohouse & Partnerzy S.A.
Principal matters that are part of our full management service include lease signing, rent collection and monthly distribution of received payments to housing association, utilities suppliers and of course to landlords. Other less frequent topics such as voting at community meetings, renewal of insurance policies, ventilation/AC inspections, property tax and perpetual usufruct payments and of course dealing with leaks and other surprises also fall within our remit.

Tom Leach, Leach & Lang Property Consultants

Facility Management

Appropriate facility management services are another key factor for rental properties owned by institutional investors. Despite the lack of an established institutional rental market in Poland, there is long-term experience in facility management of condominiums. Numerous companies offer facility management for residential property, typically for condominiums or housing cooperatives. This service type is well established and it is easy to find companies that have the relevant competence and structures suitable to offer facility management services for institutional rental housing stock. Facility managers in Poland are experienced in the management of condominiums including the collection of utility fees, which is similar to the collection of rents and deposits. Several facility managers for rental property have track records not only on the residential market, but also related to letting services for commercial property.

Typically real estate funds either have their own in-house portfolio managers and asset management or they outsource these services, while facility management and the rental process are commonly outsourced to local companies. There are only a few companies that offer holistic asset management services for rental units. However, this can be explained by the fact that institutional investors are yet to build up sizable rental portfolios.
Legal issues

The rental of residential apartments in Poland is regulated primarily by the Civil Code and the Act of 21 June 2001 on the protection of residential tenants and communal apartments (“Act on the protection of residential tenants”). The perception of the law is that it tends to act as a hindrance to rental investments rather than a help. However, we believe that the law should not negatively affect the development of the institutional rental market. This market should operate in a similar way to how it operates in Germany.

General rules of the rental law

Polish rental law does not impose any statutory or administrative limits on the amount of lease rent in respect of institutional leases. The parties may therefore freely negotiate the initial rent for residential premises. There is also freedom to agree on whether to conclude a lease for a fixed or unspecified period of time. Therefore, in most cases, at the initial stage of the lease the investor will set the rent at a high market level, ensuring a return from the invested capital and a reasonable profit. Legal regulations admittedly provide for a number of rational limitations for rent increases, however, they do not have any substantial influence on the profitability in the first years of the investment project. The situation changes, when, with the passage of time, the quality of the premises substantially deteriorates, or if the subject of the investment projects are inhabited tenement houses in very poor condition.

In principle, a landlord is entitled to increase the rent if the level of the landlord’s rent proceeds is insufficient to cover expenses related to maintenance of the premises and ensure a return on capital and plus a margin. In such a case, the annual rent increase cannot exceed 1.5% of the development or acquisition costs of the premises (or 10% of the costs of permanent improvements that increase the value of the premises) plus reasonable profit. Reasonable profit is defined in precedents as comparable with the State Treasury’s bond yields (the notion of “reasonable profit” does not affect the initial rent agreed in new leases).

No limitations are applicable if a rent increase results from inflation, increases of charges which are beyond the landlord’s control (electricity, water, gas, etc.), or if the annual rent following the rent increase does not exceed 3% of the reinstatement value of the premises. The relevant reinstatement value indicators for the respective cities and regions in Poland, based on statistical data, are officially published by the public authorities every 6 months.

Under the Act on protection of residential tenants, rental increases may occur every 6 months subject to a minimum 3-month notice period. If the tenant does not accept the new financial terms, he or she is entitled to refer the matter to court, which will decide whether the rent increase is justified. In such court proceedings, the landlord must prove the legitimacy of the increase.
Maintenance and termination rules

Statutory rules for sharing apartments’ maintenance costs are favourable for the landlord, as the majority of such costs are borne by the tenant. For instance, a tenant is responsible for the maintenance of floors, windows, doors, bathroom fittings and stoves, whereas the landlord’s duties are in principle limited to media installations and structural repairs. However, the rules concerning the maintenance of the subject of lease may be contractually modified by the parties.

Rental contracts for both fixed and unspecified periods of time may be terminated by the landlord only for causes expressly listed in the Act on the protection of residential tenants (e.g., 3 months’ rent arrears plus an ineffective 1-month grace period, a tenant’s gross infringement of the lease contract or if a tenant subleases the premises without the landlord’s prior written consent).

Conversely, a tenant is entitled to terminate a rental contract for an unspecified period without stating any reason with 3 months’ notice, unless the contract provides for a different notice period. A lease contract concluded for a fixed period may be terminated by the tenant only in the circumstances set out in the contract.

Enforcement of arrears and eviction rules

Enforcement of rental arrears is possible through a fast-track procedure with reduced court fees, which is provided for in the Code of Civil Procedure. The court process may be lengthy when it comes to eviction claims. This may pose a risk for the landlord; however the situation is improving each year.

Eviction rules based on final court verdicts have recently been relaxed. At the same time local municipalities have been obliged to provide social housing or temporary accommodation for evicted tenants. If a tenant does not vacate the premises following a court verdict (or on the lease termination date), the landlord is entitled to compensation in the amount of the market value of the rent for each month of non-contractual use. If the local municipality fails to provide social housing or temporary accommodation for an evicted tenant, then the landlord is entitled to compensation claims against the municipality. According to precedent, in such circumstances the local municipality is responsible jointly with the tenant for payment of compensation.

Summary

The rental system in Poland has many similarities with the German landlord-tenant laws. From the legal perspective, investing in rental properties in Poland is sound, and currently binding laws do not hinder the proper performance of residential leases.
Tax and company issues

In principle, from the corporate and tax perspective, investing in rental properties in Poland does not differ much from investing in other businesses. Such investments may be undertaken through special purpose vehicles established in Poland, which operate in the rental business, or, to some extent, investments may be carried out without any corporate establishment in Poland. Similarly, the rental sector is subject to the same tax rules as other typical businesses.

General rules of conducting business

Entities from the European Economic Area (“EEA”) and some other countries may undertake commercial activity on the same conditions as Polish citizens and companies. The freedom to establish and conduct business granted to entities registered outside of the EEA is slightly different, but there are no significant barriers to successfully running a business in Poland.

Businesses registered within the EEA may conduct rental activity through a branch office or a subsidiary (usually a limited liability company: spółka z ograniczoną odpowiedzialnością - sp. z o.o.). Those from outside the EEA may operate through branches only if the legislation of the country in which they are registered allows Polish investors to establish branch offices (reciprocity). However, if some conditions are met (e.g., lack of own employees or infrastructure, apart from real estate, in Poland), such business may be carried out without any establishment (direct holding from abroad), although this is not a very common set-up.

In the past it was common to use special entities like spółka komandytowa (limited partnership, Kommanditgesellschaft) or spółka komandytowo-akcyjna (limited joint stock partnership, Kommanditgesellschaft auf Aktien) for tax optimisation. However, it is not advisable to choose these structures today due to planned amendments to the law, which will change their beneficial tax status.

Income tax and repatriation of profits

The basic corporate income tax (CIT) rate is 19%. A company with its seat or management board on the territory of Poland is subject to CIT on its entire income. Foreign companies are subject to CIT only on their income earned on the territory of Poland.

This CIT rate applies to income resulting from a rental business and to any future sale of an apartment or building rented. In contrast to companies, individuals who rent out premises are generally subject to an 8.5% flat-rate income tax only.

The most traditional ways or repatriating profits from Polish SPVs are: (i) dividends – 19% CIT, but a ‘parent-subsidiary’ exemption is available, (ii) interest and royalties – 20% CIT, but exemptions for EU investors are available, as well as (iii) know-how and management fees – 20% CIT, unless the relevant tax treaty on the avoidance of double taxation states otherwise.
VAT

The standard VAT rate is 23%. This rate applies to the majority of supplies of goods or services rendered for consideration. However, supply of residential premises (i.e. premises not designed for business activity) is subject to a reduced VAT rate of 8%. Further tax relief, in the form of tax exemption, is provided for leasing this type of premises, however for residential purposes only. A downside of this VAT exemption is a potential lack of the right to recover the VAT included in the purchase price of premises rented for residential purposes.

Purchasing real property

The relevant purchase agreement must be executed in the form of a notarial deed to be valid and effective. It will be subject to a notarial fee, which depends on the value of the purchased property. Subsequently, the transfer of ownership of the real property must be submitted to the land and mortgage register at the local district court, which is usually done by the notary public.

Tax depreciation

In principle, depreciation write-offs applied in accordance with the Polish CIT Act in relation to real properties are tax deductible. Tax depreciation is usually carried out according to the straight-line method and, in relation to real properties, takes 40 years (i.e. 2.5% per year). The depreciation base is, generally, the purchase cost. However, the foregoing rule does not apply to land and properties held in perpetual usufruct, which are not subject to tax depreciation. Any expenses incurred while purchasing these assets constitute tax-deductible costs upon their sale only.

Exit from investment

As a rule, exit from an investment may be made either through (i) a share deal – applicable to investment schemes including a Polish subsidiary or (ii) an asset deal – applicable to all investment schemes.

A share deal is one of the simplest methods of exit from an investment and mainly involves selling shares in the Polish SPV which operates the rental business. As a rule, such a transaction is not subject to CIT in Poland; however, according to the Polish-German tax treaty on the avoidance of double taxation, Polish CIT at 19% may apply. Moreover, a share deal will be subject to 1% stamp duty, levied on the market value of the sold shares and payable by their purchaser.

An asset deal usually constitutes a more complex form of exit, as it potentially requires further distribution of profits made on the exit and liquidation of the Polish SPV. Generally, income from such a transaction is subject to 19% CIT in Poland.
Investment schemes

The current residential market situation, along with the changing perception and attitude towards renting in Polish society, has opened a promising time window for investing in housing for rental purposes. We expect three main types of institutional investors to seek opportunities in residential rental property in Poland:

(i) **Opportunistic funds looking for distressed properties**

These investors count on opportunities on the current market due to the difficult sales situation that many developers are facing: there is a vast number of projects that are about to reach completion with very low presales levels, not to speak of the already large cohort of completed projects in drastic sales difficulties. These funds may invest in apartments dispersed over different buildings. The less successfully marketed projects, but well located and offering the right mix of dwellings, lend themselves to bulk investment by the weaker developers. At the same time banks are now more proactive in solving their client’s problems and thus more supportive of alternative solutions to avoid unnecessary reserves and write-offs.

(ii) **Funds that want to build up a rental portfolio**

These investors attempt to employ developers in a critical situation but with promising land plots and use them as fee developers to build up a rental property portfolio within a mid-term perspective. After some 5-10 years of operation, an exit should be possible with a single en bloc sales operation to long-term investors. Alternatively, single units could be sold to individual buyers.

(iii) **Long-term funds**

These funds include long-term and risk-averse players like insurers or pension funds. They are open to buying under certain conditions, e.g.:

- a minimum investment volume of EUR 25-30 mln (i.e. 300-500 residential units);
- fully operating rented sizable properties (each 100+ units);
- fully rented units (or with limited vacancy);
- a clear ownership situation (no Swiss cheese, but whole buildings / blocks / wings).

As opposed to opportunistic funds, pension funds look for a blended risk rather than individual speculative lease terms. Stable long-term tenants are more valued than those paying higher short-term rents.
Lessons from outside

Having observed the development of the private rental housing market in other countries, funds that build up a rental portfolio and long-term funds seem to be the most relevant for Polish legal and housing market conditions. The idea of delivering new private buildings for rent on the Polish market seems to be promising and, in view of investors’ appetite for transactions portfolios, the demand for rental accommodation should be satisfied by various quality housing estates. Quality, along with demand and location, impacts the level of rental revenues. Diversity of tenants and facility management standards may provide an opportunity to create an interesting bundle and secure the preferred revenue level.

In Europe the German and UK models provide good examples for Poland. The institutional private rented sector in the UK has been small, although around 7% of households rent in the private market. These homes are typically owned by private individuals. In the UK the government has typically provided capital subsidies for affordable and social housing and has provided tax incentives to encourage home ownership (low property transaction taxes and no capital gains on a main home). Despite the economic downturn, the demographic pressures on housing supply continue in the major UK cities, particularly London. These pressures, in the absence of previous levels of mortgage credit and lower levels of spending on social housing, are starting to create a real interest in private or market rented tenures.

The UK Government launched a review of the constraints on rented supply and has set up a taskforce to oversee market developments. It has also launched a £1bln rental guarantee scheme to help attract long-term investors. Investors typically want to acquire /invest in completed units rather than expose themselves to planning and construction risk. In order to address this hurdle in the short term, the UK Government has put a loan scheme in place to help fund the construction of homes for rent.

Institutional investors are most active in countries with a significantly higher proportion of households in the private rented sector[1]; in Germany (49%), Switzerland (57%) and the US (33%). In these economies long-term tenancies are predominant and benefit from some form of rent control.

The prospect of an acceptable income-related return which is secure and long-term has been essential for institutional investors on the German market. Investors search for profit maximisation, portfolio improvement, maintaining market share, and look for expansion. As the German private rented market is pretty well saturated (in recent years the former public stock was gradually bulk sold to institutional investors), institutional investors that are experienced in this market have already invested in portfolios abroad.

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1 The definition of the private rented sector that is used in compiling official statistics varies from country to country and affects the percentage amounts in various statistics.
This pushes them to set up similar structures elsewhere, and Poland appears to be the best candidate. Solid economic fundamentals, a young open-minded population, growing mobility, a sizable major residential market allowing for risk diversification, lack of competitive schemes… all speaks for itself.

End investors (long-term funds) look for economies of scale and focus on creating meaningful asset portfolios. In order to meet their requirements transactions need to be consolidated to become more attractive. A recent transaction between Bouygues and Grainger demonstrates to the UK residential market the willingness to establish the private rented sector as a new asset class that will address the huge housing demand in the country. The decision on buying 500 new homes to let made by Prudential Property Investment Management in the first half of 2013 strengthens the belief that the private rented sector will continue to mature and develop and offer attractive returns.

Conclusions for Poland

Observing the development of the rental sector abroad, conclusions can be drawn for a long-term growth model of the institutional rental market in Poland. However, the housing market of Poland has its specifics and the lack of experience and track-record of large rental portfolios has to be taken into account. Thus, it is likely that the development of Poland’s institutional rental sector will depend on initial investors who build up first rental portfolios. These investors need to accept a higher risk level, as they must build and then rent the newly created portfolios of rental apartments. In return they count on higher yields through selling functioning portfolios of let apartments which are adjusted to the needs of long-term investment funds. Polish institutional rental market development model is presented on the scheme at the top of this page.

The described scheme creates the following challenges for both the initial investor and the long-term investor, namely an insurance or pension fund:

1. Economic feasibility of the entire process to secure long term profitability

While other economies enjoy some sort of public support for housing development, Poland offers very limited incentives to create affordable housing. Given this, the major challenge is to create efficiencies at each step of setting up a fully operational portfolio. Thus the key success factor from the investor’s perspective is to focus on the scale effect, quality of housing stock and competitive letting conditions.
The scarcity of sufficiently large portfolios on the market is a great opportunity for build-to-let market development. Obviously too many units cannot be expected in one location, thus a portfolio has to be gradually created based on projects including some 100-200 units.

Built to suit projects, with design and construction parameters set up to meet the local demand, are crucial to ensure quick letting to solid tenants. The cost of construction and the land significantly impact the long-term profitability, so it is very important to achieve an acceptable yield by limiting entry costs. Although, in some cases, it is possible to profit from efficiency during the construction period, the private rented sector should be service-driven in order to match future tenants’ needs and match accommodation standards of build-to-let facilities with the tenants’ demand and payment ability.

2. Ongoing labour-intensive management of the units

As residential stock requires ongoing management and a quick response to facility management issues, new developments are obviously a best fit for this scheme. Close cooperation between the developer, initial investor and the final long-term fund leads to the development of multi-family buildings including the right mix of flats – single vs. family, young vs. old etc. (depending on the location and access).

Given the transactional costs of reletting residential units, it is crucial to understand tenant dynamics and focus on “long-term” tenants. One should notice that, as the Polish rental market is growing, there is also a growing number of tenants looking for mid- to long-term solutions.

3. Quality of tenants

As a result of self-selection, people who look to rent from institutional landlords are more serious about their residential needs and more responsible. They look for more stable lease conditions, clear expectations between tenant and landlord, quick and high quality day-to-day services, standardised responses to issues etc. These are tenants who are willing to pay a premium for a superior service and peace of mind. They have clearer expectations and are easier to manage. As they are typically in a better economic position, the risk related to the provision of replacement dwellings in cases of overdue rent is limited. At the opposite end, one has to bear in mind that people live longer and the challenges of dealing with the housing needs of those in later life will become even greater. The most significant shift in housing demand expected in the next century is likely to address the needs and demands of an aging society, which will contribute to a diversification of the rental accommodation portfolios available for future investors.
Conclusion

The institutional rental market is an emerging business segment on Poland's residential market. It is a relatively new business, with only a small portion of the housing stock owned by institutional investors. However, the first funds have already invested in buy-to-let schemes and paved the way for new investors. These first rental portfolios show low vacancy rates, although yields are quite modest as purchases were made during the boom years when prices peaked. Even so, these investments have been tested and proved that there is demand for an institutional rental market in Poland. Now new investors can learn from the mistakes made by earlier investors and, in view of the market circumstances, it seems the right time to get into the market.

Prices of new apartments show a continued decreasing trend and sizable discounts are achievable for investors. Developers are seeking alternative forms of revenue in order to sustain company operations within changed market conditions. They are interested in cooperating with funds and to work on a fee basis to deliver the right investment product for a long-term rental scheme. It is not only supply that creates its own demand, though. Demographic trends and changed attitudes towards renting, mobility and liquidity support the demand side for buy-to-let schemes. The institutional rental market product is superior to the current market supply in aspects such as quality, management and security for long-term tenants.

Also the market environment is sound. There is the political will to establish an institutional rental market. The legal framework for the rental sector is sound. We do not see a problem with the provision of reliable facility management and renting services. There is sufficient experience with investment funds in Poland, on both the national and international level. Bank financing is available both for developers and institutional investors, from both Polish and foreign banks. We have all the necessary expertise to advise our potential investors in these fields.
About REAS
REAS is an advisory company specializing in issues relating to the residential market in CEE. Since 1997, we have been cooperating with developers, banks, investors and other entities operating in the housing sector. In 2007, REAS became a partner of Jones Lang LaSalle, the global leader in advisory services in the commercial real estate market.
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