

## A note on the private housing rental market in Poland

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### Abstract

Housing rental market share in Poland is low. I explore the reasons behind this underdevelopment with a survey conducted among SGH Warsaw School of Economics students. It turns out that tenure preferences of respondents are tilted towards owning, which can be attributed predominantly to psychological factors. Using a life-cycle model I evaluate the effect of the reforms aimed at improving the functioning of the rental market by increasing the quality of rental services, reducing the risk of investment in rental housing and removing fiscal incentives for owning. The results indicate that the reforms, if introduced simultaneously, would significantly increase the rental market share.

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### 1 Introduction

A safe place to live is among basic needs of households. The most popular form of satisfying housing needs is ownership. In this case the house serves a dual purpose: it provides utility and is an investment vehicle that allows for storing value. The alternative housing tenure is renting. It allows to separate the dual role of housing: the tenant derives utility from housing services and the landlord obtains profits from housing investment. The literature indicates that the tenure structure of the rental market has an important impact on the macroeconomic outcome. Some authors show that the availability of rental housing diminish the variability of the housing sector and reduce the risk of a house price bubble (Arce and Lopez-Salido, 2011; Cuerpo et al., 2014; Rubaszek and Rubio, 2017), whereas other authors argue that a well-functioning rental market enhances residential mobility and limits long-run unemployment (Blanchflower and Oswald, 2013; Lisi, 2016). On the contrary, there is a strand of literature that claims that home owners are more likely to invest in local community and social capital (DiPasquale and Glaeser, 1999).

Given the above discussion in the literature, in this study I argue that housing rental market underdevelopment in Poland should be regarded as a structural weakness. The scale of this underdevelopment is well illustrated by Eurostat data on the housing tenure structure. The detailed data for Poland in 2015 are as follows: “market price” tenants (4.5%), “reduced

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price” tenant (11.8%), owners without mortgage (72.8%) and owners with mortgage (10.9%). These figures compare to the share of “market price” tenants amounting to 15.4% in Italy, 19.8% in France, 39.9% in Germany and 49.2% in Switzerland. In the further part of the article I explain why renting is unpopular in Poland using the results of a survey on housing tenure preferences conducted among 195 students of the SGH Warsaw School of Economics. Then I will briefly discuss what kind of policies would help in developing the private rental market, using the results of model simulations described in detail in Rubaszek (2017).

## **2 The reasons behind rental market underdevelopment in Poland**

The high proportion of owners and a marginal share of tenants observed in Poland has several key reasons. As indicated by Lux and Sunega (2014) a very important factor behind a declining trend in the rental market share was the transfer of public rental housing into private hands, which took the form of a massive sale to sitting tenants. This is well illustrated by the Eurostat data, according to which the share of public rental in Poland decreased from 34.9% in 2007 to just 11.8% in 2015. The second factor is related to the development of the mortgage market. A steady decrease of nominal interest rates, better access to FX denominated loans and two programs enhancing house purchases on credit (“Rodzina na Swoim” and “Mieszkanie dla Młodych”) have led to an increase in the proportion of owners with a mortgage from 2.9% in 2007 to 10.9% in 2015. The next reason is related to ineffective regulations, excessive protection of “bad tenants” within the regular rent contract for instance, and the lack of consistent housing policy to support the rental market. This is aptly summarized by Priemus and Mandic (2000), who claim (as indicated by the title of their article) that in the countries of the region both private and public rental market at the beginning of the twenty-first century was “no man’s land.” The last factor behind high ownership rate is that Poles strongly prefer ownership to renting due to psychological factors. As indicated by Rubaszek and Czerniak (2017) owning is perceived as the only option to “feel at home”.

The survey presented in this paper builds upon my recent work with Adam Czerniak (Rubaszek and Czerniak, 2017), in which we describe the results of the survey conducted by IPSOS in June 2016 among a representative group of 1005 Poles. In this article I extend these results by conducting the same survey among 195 students from SGH Warsaw School of Economics (112 respondents from Jan. 2017 and 83 respondents from Jan. 2018).

**Table 1.** Characteristics of the respondents.

<b>Question</b>	<b>Fraction of respondents</b>
<b>Place of residence during childhood</b>	
Warsaw	31.8%
Other city	68.2%
<b>Housing tenure status</b>	
Owner	36.4%
Tenant	39.0%
SGH campus	4.6%
living with parents	20.0%
<b>Duration of stay in the current dwelling</b>	
below 1 year	18.5%
from 1 to 5 years	49.7%
above 5 years	31.8%
<b>Plans to change the dwelling</b>	
yes, before 5 years	81.0%
yes, after 5 years	8.2%
No	6.7%
<b>The most likely choice in case of moving</b>	
Buying	28.7%
Renting	65.2%
<b>A sentence closer to your opinion</b>	
Buying makes more sense as it is a good investment	72.3%
Renting is better as it enables financial liquidity	27.7%

I believe that analyzing the answers of WSE students provide value added in comparison to the results based on the representative sample for at least three reasons. First, understanding the perception of young adults towards housing tenures is important as the availability of stable rental housing has a tremendous impact on their strategies how to start a life of their own. This relates not only to the satisfaction from utilized housing, but also to professional career development or family formation. Second, WSE students are more mobile and more often leave in rented apartments in comparison to the rest of population, hence their opinion on the functioning of the rental market is more informative than the opinion of respondents who have always been homeowners. Third, WSE students are relatively fluent in economics,

hence should be better prepared to evaluate the relative merits of owning and renting. However, given that the sample is limited to young adults with economic educational attainment, the results of the survey should be treated with some reservation.

Let us focus on the results of the survey. Table 1 describes selected characteristics of the participating students. It turns out that about one third of them is from Warsaw and two thirds from another city or country. About half of them live in a rented apartment or in the university campus, whereas the other half cohabit with parents or is a homeowner. The majority of the respondents plan to change the place of residence in the short term horizon, where the most likely choice will be renting. This choice is however at odds with the general belief about the pros and cons of both tenure alternatives. About three quarters of students believes that *buying a house is a good investment decision over the life cycle*, whereas only one quarter of them selected that *renting makes more sense because it enables flexibility and financial liquidity and is a better deal than owning*.

**Table 2.** Preferred housing tenure.

	<b>buy</b>	<b>no opinion</b>	<b>rent</b>
<b>economic factors</b>			
mortgage vs. rent costs	40.5%	16.4%	43.1%
house price vs. rent fluctuations	54.4%	25.1%	20.5%
<b>psychological factors</b>			
social status	70.3%	23.5%	6.2%
freedom and independence	44.6%	12.9%	42.5%
comfort	80.5%	10.8%	8.7%
family	78.0%	13.3%	8.7%

The next set of questions was related to a detailed reasons behind housing tenure choices. Following the literature, I have focused on both financial and psychological factors (Coolen et al., 2002; Ben-Shahar, 2007; Bourassa and Hoesli, 2010). The upper panel of Table 2 shows that the level of mortgage installments is considered to be higher than the level of rents for 40.5% of the respondents, whereas 43.1% of them is of the opposite opinion. The distribution of answers is more tilted towards owning if the risk of rent increases is compared to the risk of house price decline. In this case 54.4% of respondents prefers to buy and only 20.5% to rent. This might be influenced by the common belief that buying a house is a good

investment over the life cycle. The bottom panel of Table 2 shows that due to psychological factors renting might lose as a viable alternative to ownership as a long-term solution to satisfy housing needs. The big majority of the respondents think that owning raises social status, improves comfort and satisfaction from housing services as well as provides a good and secure place for a family. On the contrary, for a large group of students renting allows for mobility, which has a positive impact on freedom and independence.

In the final set of questions I checked which factors, in the opinion of SGH students, are decreasing the attractiveness of being a tenant. The results in Table 3 show that constraints in arranging apartment and inspections by landlords diminish the comfort of living in a rented apartment. This might explain why psychological factors are tilted so much towards owning. In turn, the risk of rent increase as well as high level of rents are important in explaining why so many students believe that buying a house is a better financial decision than renting it. Finally, the popularity of renting is diminished by inefficient regulations related to tenant protection. In particular, the restrictive eviction regulations within regular rental contracts cause that most of the newly-signed contracts are temporary, with usual duration of one year. Consequently, renting is treated as a short-term method of satisfying housing needs rather than as a long-term solution.

**Table 3.** Factors decreasing the attractiveness of renting.

	<b>yes</b>	<b>no</b>	<b>no</b>
		<b>opinion</b>	
constrains in arranging apartment	68.2%	21.5%	10.3%
no protection against rent increases	63.6%	22.1%	13.4%
often inspections by landlords	50.8%	30.8%	18.4%
high rents	48.2%	39.5%	12.3%
no protection against eviction	44.6%	37.4%	18.0%
inadequate offer of houses to let	45.1%	38.0%	16.9%

### 3 Model simulations

So far I have shown that the share of private market tenants in Poland is low and presented a series of arguments explaining the reasons behind this outcome. In this section I will present a more formal discussion on the impact of economic and psychological factors on rental market share. For this purpose I discuss the results of counterfactual simulations conducted with a life-cycle, heterogenous agent model that I describe in details in Rubaszek (2017). In short,

the model economy is inhabited by many households, which differ by age, income, financial and housing assets. They derive utility from consumption of non-housing goods and housing services, which might be satisfied by owning or renting. The model includes several features important for the functioning of the housing market such as: (i.) taxes and subsidies, (ii.) mortgage interest rate spread and minimum down-payment constraint, (iii.) disutility of renting and (iv.) higher depreciation rate of rented dwellings than the owned ones. I show that these features have important impact on tenure decisions by calculating how housing market reform changes the share of the private rental market share.

The main reasons why in under the benchmark parametrization of the model households prefer to own rather to rent are as follows. First, the utility derived from living in rented house is lower than in the same house that is owned. The utility loss is assumed to be 15% and can be attributed to psychological factors described in the previous section. Second, the depreciation rate of rented apartments is higher than that for the owned ones (by 1 pp. per year). I interpret this difference as a reward for the risk of letting an apartment to a “bad tenant”, who cannot be evicted, combined with potential higher utilization rate of housing stock by tenants in comparison to owners (Sinai and Souleles, 2005). Third, there are taxes on income from renting (8.5%) and no taxes on imputed rents. Additionally I assume that the government subsidises interest payments on mortgages (a proxy for programs “Rodzina na Swoim” and “Mieszkanie dla Młodych”). The last two factors raise the relative cost of renting in comparison to owning: each year tenants have to pay about 2% of the house value more than owners for living in the same dwelling.<sup>2</sup> There are also reasons why households rent: transaction costs, the spread on the mortgage rate and maximum loan-to-value restriction. If a house is bought with a mortgage then the economic advantage to own diminishes from 2% to 0.4%, whereas the transaction costs cause that the size of the owned house might be inadequate to households needs.

I apply the proposed model to evaluate the results of selected changes in the functioning of the rental market. In particular, I focus on the following reforms:

1. Increasing the quality of renting services. In the model economy the disutility of renting is lowered from 15% to merely 5%, i.e. levels observed in European countries with well-functioning rental markets (Diaz-Serrano, 2009).

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<sup>2</sup>According to the data collected by Global Property Guide gross rental yields in Poland are relatively high and amount to 5.5% per year, see <http://www.globalpropertyguide.com/Europe/rent-yields>.

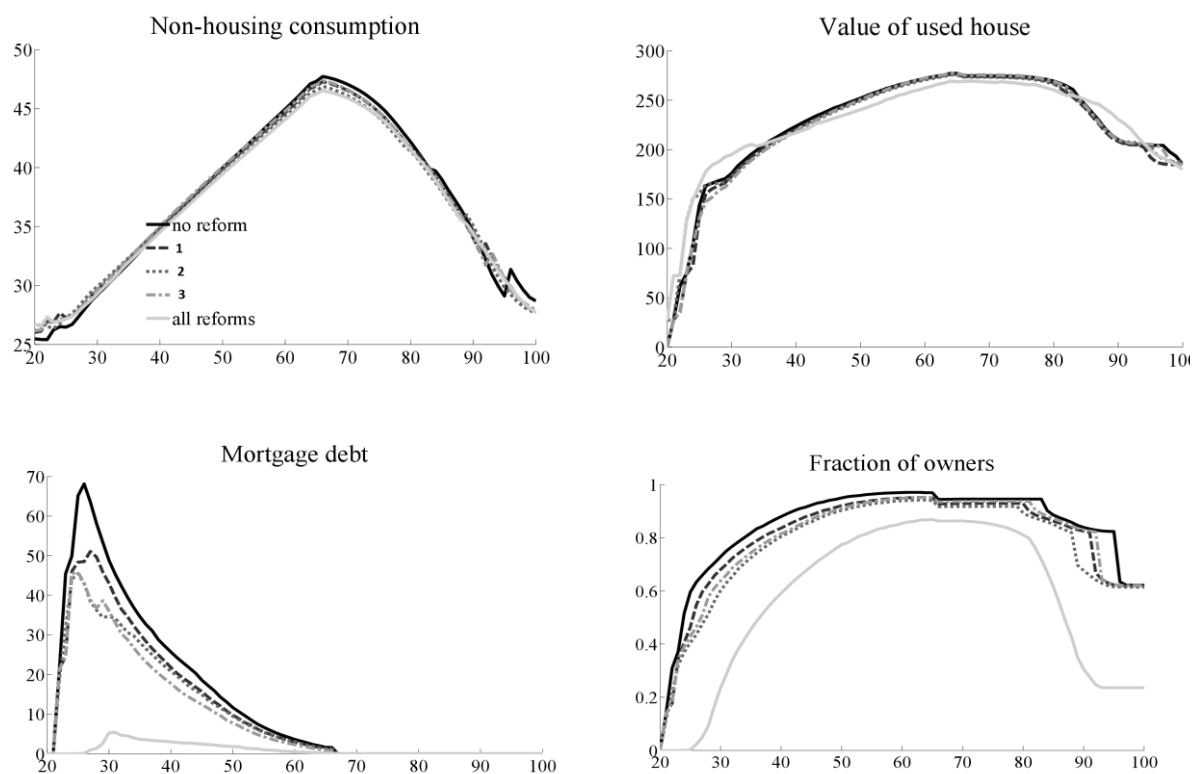
2. Increasing the protection of landlords against bad tenants or introducing policies subsidizing build-to-let investment. In the model economy the depreciation rate of rented houses declines by 1pp, i.e. to the level for the owned houses.

3. Removing the tax on income from renting and mortgage rate subsidies.

**Table 4.** The effects of the rental market reform.

	<b>no</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>full</b>
	<b>reform</b>				
fraction of tenants (%)	9.6	12.7	17.4	14.2	35.4
average age of first house purchase	28.0	29.1	30.6	30.1	37.9
fraction of households with debt (%)	20.0	17.8	16.4	16.0	4.6
mortgage debt to GDP (%)	40.2	37.2	36.2	34.4	12.5

Table 4 presents the aggregate effects of the reforms. The first row of the table shows that in the benchmark economy everyone tries to buy a house as quick as possible and only credit constrained households cause that some of the youngest households decide to rent (9.6% of all households). A single reform helps in increasing the rental market share, but the gains are not large: 3.1 pp., 7.8 pp and 4.6 pp for reforms 1, 2 and 3, respectively. However, given that there are interaction effects in the model, if the three reforms are introduced together, the share of tenants in the economy rises by enormous 25.8 pp to 35.4%. This shows that to make renting an attractive alternative to owning policymakers need to remove or alleviate all barriers that make renting unattractive. The next rows of the table indicate that the full reform also switches the average moment of the first house purchase by almost 10 years. Moreover, in the reformed economy most of house purchases is financed from savings rather than by mortgages. As a result the mortgage debt to GDP ratio decreases from 40.2% to merely 12.5%. This makes the financial sector more stable and the economy less susceptible to financial shocks. It should be noted, however, that in the model it is assumed that landlords finance rental housing purchases from their savings. This describes well the situation in Germany, where the majority of the rental housing is owned by investment and pension funds. However, it is also possible that landlords finance rental housing purchase with “buy-to-let” mortgages, which are very popular in the UK for instance. In this case the effect of the rental market reform on the stability of the financial sector is much lower.



**Fig. 1.** The effects of rental market reform by age cohorts.

The effects of the rental market reform on the decisions taken during the lifecycle are presented in Fig. 1. The upper panels of the figure show that the average paths of spending on consumption and housing services are little affected by the reform. In contrast, the bottom panels demonstrate that the impact of the full reform on the life-time path of mortgage debt and tenure structure is sizeable. The reform is strongly limiting the demand of households to take a mortgage in the early stage of life as they now satisfy their demand for housing services by renting.

## Conclusions

The share of the rental housing market in Poland is low. Using the survey conducted among SGH Warsaw School of Economics students I have showed that housing tenure preferences are tilted towards owning, predominantly due to psychological reasons. The respondents perceive ownership not only as a cheaper form of satisfying housing needs, but also as the only way to provide a safe place for the family and to really “feel at home”. The survey also identifies the most important barriers to demand for and supply of rental housing. Among the former, inefficient institutions and the lack of professional renting services turned out to be of



crucial importance. Given the above diagnosis, I have used a life-cycle model to quantify the effects of several rental market reforms. Simulation results indicate that a complete reform would shift the rental share from below 10% in the benchmark economy to about 35% in the reformed one. The additional result of the reform is a more stable financial sector, as the household debt to GDP ratio decreases substantially.

Based on the results of this study one might formulate a set of recommendations for housing policy. First of all, lowering the relative cost of renting in comparison to owning is very important to develop private rental market. This can be achieved by implementing regulations limiting the risk associated with investing in rental housing, eliminating fiscal measures promoting ownership or even introducing rent subsidies. Second, to develop the rental market housing policy should also take into account non-financial factors, which might decrease the satisfaction from being a tenant. In the longer horizons, stimulating the professionalization of rental services and smart regulations should contribute to changing psychological attitudes towards renting.

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