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Risks of real estate investment and their management in the Finnish market area

Bachelor's thesis

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ABSTRACT

The purpose of this thesis is to find out what risks are associated with real estate investment and how they can be managed in the Finnish housing market. The theoretical part of the work was carried out as a literature review and the research itself was conducted with the help of semi-structured interviews. The interview was attended by professionals with many years of experience in the field. Based on the study, it can be stated that there are many different risks associated with investing in real estate. Understanding these and preparing for them is at a really good level in Finland. Based on research, there are several ways to prepare for each risk.

Keywords: Real estate, investing, risk management, Finnish market area

INTRODUCTION

As the world recovered from the 2008 financial crisis, linterest rates began to fall. Credit has been cheaper than ever in the past decade. In financial institutions, mortgage lenders are often the largest loans an individual takes. Real estate investing is considered a very simple form of investment due to the ease of use of leverage and low interest rates. This drives a megatrend in Finnish real estate investment, which attracts more and more people every year (Vuokranantajat, 2022b).

Real estate investing is considered an easy and fairly risk-free form of investment (Sarah Sharkey 2022). The rental market is considered relatively stable and demand is always there. For example, housing rents have only fallen in one year since 1970, and even then rents have fallen by only 0.5% (Orava & Turunen 2017). Real estate investing is a long-term and patient-friendly form of investment. As a rule, the investment object is purchased with the help of an investment loan, the installments of which are used to pay the rental income from the object. The purpose of the loan is to obtain a positive cash flow, i.e. to utilize the so-called debt leverage (Miller, M. H. 1977). However, history does not guarantee the future and it is dangerous to assume that the same trends in value appreciation and rental income will continue. population change, migration to metropolitan areas, new banking regulations and, more recently, challenges posed by the coronavirus are all factors that make it difficult for housing investors to do business in Finland (Vuokranantajat, 2022a). Investing in housing has always been considered a very safe form of investment and capital growth, but this is no longer considered safe.

The most typical and in many ways the most lucrative way to participate in household investment is through debt financing. Investing in real estate is an attractive option, especially in times of low interest rates, because it's easy to "take advantage" of leveraged returns. Leverage, in this sense, refers to the loan's share of the total investment amount, which reduces the equity requirement while increasing the return on capital. This means that the tenant of the apartment pays installments and interest on the loan. So it's easy to see why Finns see real estate investing as a solid form of investment, given that mortgage rates have been low for so long. But private housing investors must also prepare for the toughest of times. There are trends and factors that are sure to affect returns for home investors and raise current rates.

The purpose of this study is to examine the risks associated with a real estate investment in the Finnish market and how to mitigate these identified risks. In order to be able to illustrate the matter in more detail, the thesis first creates a theoretical overview of the term real estate investing and goes through the main principles.. The purpose is to identify risks, analyze them and find ways to deal with them. Therefore, it is important to identify the characteristics of each risk in order to find ways to control them. There are many factors that affect real estate investment, which also make the risk appear to be diversified. This is a very important note when considering real estate as an investment. Fundamentals of investing, regardless of investment objectives, risk and reward go hand in hand. The research begins with the theory of real estate investment and deals with the risks associated with it. The empirical part has been carried out as a qualitative study with the help of a semi-structured interviews. Qualitative research can uncover new variables and things that are difficult to identify through quantitative research alone. The study first sought to gain a comprehensive understanding of housing assets, housing investments and associated risks through real estate literature and scientific articles. Extensive material from Finnish professional literature, Statistics Finland and surveys of Finnish landlords was used. Then try to find ways to deal with them through this theoretical basis and through interviews with experts in the field.

1. REAL ESTATE INVESTING

In this section, we will look at real estate investing as a concept and its basic principles. The subject of the review is the Finnish market area and for this reason the section also deals with the Finnish market area. There is always an essential risk associated with investing, and this section reviews the risks that have arisen based on a review of the literature and the issues that affect them.

1.1 Principles and purpose of real estate investment

Real estate investment is based on investing capital in real estate in order to achieve economic benefits. Real estate investment can be counted as an investment instrument alongside others, like funds and stocks. The investment can be either direct or indirect. Direct housing investment refers to a situation where you invest your capital directly in a property or part of a property. In this case, the return is completely dependent on the return on one asset. (Kallunki, Martikainen & Niemelä 2008, 115). Banks in Finland, as elsewhere in the world, also offer a way to invest indirectly in real estate. For example, Osuuspankki, one of Finland's largest banks, offers its customers real estate funds through which investors can invest indirectly. It offers a great deal of diversification between different properties and apartments and thus also offers its investor an effortless solution. The investor does not have to worry about matters and costs related to the maintenance of the property, for example.

The main principle in both direct and indirect real estate investment is the pursuit of a positive cash flow (Tuomi & Sarajärvi 2013). As a rule, real estate investment involves the use of leverage. An individual or company with good solvency can easily obtain a mortgage from a bank, which they can use to invest in real estate. Mortgages are the cheapest loans on the market. When compared to investment loans offered by banks, there may be a 2-3% difference in the banks margin. The leverage gives the investor cheap debt to accumulate its own assets. The apartment to be purchased acts as collateral for the loan itself and the equity must be in proportion to the purchase price of the apartment 15-25 percent. The purchased property is leased to the tenant and the income is based on the rental income from the property.

In direct and indirect real estate investment, the difference is the amount of capital that is invested. Property prices have developed steadily in Finnish history due to accelerating demand. In indirect real estate investment, units are bought from real estate funds, so even smaller capital is enough to start it, unlike in direct real estate investment where the investment needs more capital in the background. The definition of a property covers the dwelling and the land belonging to it. this entity cannot be moved but is firmly in place (Brueggeman, Fisher 2011, 4)

1.2 Real estate investment risks

In principle, housing investment binds a really large amount of capital to the investment object, which consists of both debt and equity. With a large amount of capital, there are essentially many different risks associated with an investment. Understanding these requires a broad understanding of the market and the factors involved. Understanding these is vital for investment (Orava, Turunen 2017, 296). In the next chapter, we look at the risks from three different perspectives that Orava and Turunen have highlighted. These include cash flow risks, risks related to the investment and the investor, and more recently other risks that cover environmental and political risks. Just like any other investment, investing in housing has risks. However, direct residential complexes are very different from other forms of investment and therefore have different risks (Leväinen, K. 2013). Risk management needs to consider what might go wrong and how to prepare. Leväinen also explained that since one of these risks is sometimes identified, it is necessary to find out how to minimize the damage it causes. An important aspect of risk management is knowing the risk you are taking, because by the time it becomes a reality, it is too late to think about risk management.

1.2.1 Market risks

Market risk is one of the most significant risks related to real estate investing. A private real estate investor alone will not be able to influence the market, which highlights this risk. The market is dependent on both the world economy and the fixed income market. Fluctuations in markets and interest rates can have a major impact on the real estate market. Market fluctuations directly affect the value of housing and, at worst, major crises and disruptions affect demand for real estate. The weakening of demand is reflected in the real estate market as a fall in property prices (Curcio, R., Anderson, R. & Guirguis, H. 2014). In addition to the homeownership market, the rental market is also becoming increasingly important. Perceptions of homeownership are changing.

Therefore, one can appreciate the more ease and effort that renting a home can bring. This contributes to the basic requirement of real estate investment that there is demand in the rental market. The return on a property includes not only rental income but also a possible increase in the value of the property (Kallunki, etc. 2008, p. 25). After all, one of the basic requirements of being a real estate investor is that the return on capital from investing in real estate corresponds to the risk level of the investment. However, it cannot be assumed that the rental market will remain the same in the future. The importance of inflation is also reflected in the housing market at the level of house prices. Accelerating inflation weakens the purchasing power of people who may have to compromise on housing solutions (Rakli 2022)

Investment homes are often bought with leverage and the loan can account for up to 75 percent of the purchase price of the home. Different banks in Finland determine the regulations related to housing investment and how much they are willing to finance for the purchase of an investment object. Interest rate risk is becoming one of the most significant risks in real estate investing. The idea of investing in real estate is to utilize debt and leverage, which means that the financial contribution is often as large as possible when buying a property. In this way, the investor is able to tie up as little equity as possible.

An investment home loan is often a floating rate loan that is either tied to the bank's own reference rate or the Euribor rate set by the European Central Bank. According to Orava and

Turunen (2017, 250-251), there are four different ways to prepare for interest rate risk; interest rate hedging, fixed interest rates, lower leverage or savings.

The interest rate hedging product and the fixed interest rate provide the investor with guarantees for future interest rate increases. For the future, the investor knows the level at which interest rates can rise to the maximum and be able to determine the required rental level for the return. With a smaller leverage, an investor is not as vulnerable to interest rates as with a larger leverage. With savings, the investor is not able to directly influence the level of interest rates, but is able to prepare for the increase in costs caused by rising interest rates in the reserve fund (Sijoitus 2011).

When investing in a home or property, there is always a risk that the value of the property will collapse or fall during ownership. In this case, we are talking about the price risk associated with the investment. Market values fluctuate considerably less for housing and the market is much more stable than, for example, the stock market. According to Guirguis (2014, 64), price risk only materializes when buying or selling an apartment. However, the situation does not affect the home exchange so much, because if the prices are low, you can also buy a new home at a cheaper market price. Investment housing is often a longer-term investment and rental income is steady. The owner usually has no interest in selling the investment when the market value is low. Despite its low market value, rental income is steady and, from an investor’s perspective, the time to sell an apartment is poor (Bordes, Currie & Söderström 2013, 42). When buying a property, attention should be paid to the cash flow from the investment property and not to the increase in the value of the home. The housing market experienced a sharp decline in Finland in the 1990s, but otherwise the rise in prices has been steady and there have been no collapses. The rise in market values is expected to continue in the future. Purchasing should be especially concentrated in growth centers instead of smaller sparsely populated areas (Wessman, R. 2019).

1.2.2 Cash flow risks

Cash flow risks are an essential factor when talking about real estate investing. The return is based entirely on maintaining cash flow and keeping cash flow positive. In the next chapter, we'll take a closer look at these.

Interest rates have remained low worldwide for an exceptionally long time since the 2008 financial turmoil eased. This has created an opportunity for financial companies to offer their customers cheap loans for almost the last 10 years. However, the state of the market and financial stability cannot be expected to remain at the same level in the future (Erkkilä 2019). Market failures have not been avoided in this case either, and the most recent example is the financial crisis of 2008 mentioned above. Companies lent money on too easy terms, which eventually led to the collapse of the global housing market and eventually to the global financial crisis (Ala-Nissilä 2011, 19). Since the crisis, financial institutions have come under tighter supervision and the financial sector has become more regulated. In Finland, all financial institutions are responsible for their activities and report to the Financial Supervisory Authority (Finanssivalvonta 2010). A more regulated operating environment in the operations of financial institutions will bring security and stability to the financial markets, but this does not, according to Ala-Nissilä, prevent market fluctuations and possible new global crises, which in turn will affect access to finance.

A housing company owned by a housing investor's share may also be exposed to financial risk. The company's financial condition should be considered when making a purchase decision. The finances of a poorly managed company may have been in a bad position, and as a result, the company's position in the eyes of finance companies is deteriorating (Erkkilä 2019). A company in financial difficulty will not be able to cope with its costs, and in the worst case this could lead to insolvency in a situation where the company should undergo, for example, an acute renovation (Orava & Turunen 2017, 210.). If the solvency of the owner, ie in this case the investor, is not sufficient to obtain a loan, the house will not be renovated, which will lead to a decrease in the value of the investment object.

The landlord and the tenant are parties to the lease of a residential apartment. They enter into a mutual agreement to rent an apartment that is binding on both parties. The landlord is obliged to hand over the apartment to the tenant for residential use, for a fee paid by the tenant. The lease agreement defines the exact conditions for the start and end of the lease period. Neither party will be able to terminate the agreement immediately, but the notice period will take effect upon notice of termination. However, this period of notice may be waived in the event of a breach of contract by either party. Most often, these violations come from the tenant (Puttonen & Kivisaari, 1997b 167).

The risks associated with renting can be divided into two. The first and more common risk that a real estate investor may face is the risks associated with empty months. Empty months refer to the time when the rental apartment is vacant and the landlord does not receive a tenant for that period. The landlord has running costs every month, regardless of whether the apartment has a tenant or not. These costs pose a significant risk to the return on investment. This risk can be reduced by choosing a suitable property as an investment target (Lindström 2014, 221). It is important for profitability that the property is located in an area where it is easily rented. For example, small studios in the vicinity of the university are a great option when choosing an investment destination. There are enough good tenants for such properties and due to their small size they are suitable for a single person, both for a student and for a working person. The aim is to reduce the risk related to renting and empty months by concluding lease agreements. Contracts are often made for a fixed period, in which case the tenant is obliged to rent the property for at least a year. After this, the lease will continue to be valid for the time being. The statutory notice period if the tenant terminates the contract is one month. This gives the landlord some time to find a new tenant, but often this can be too short a time to find a suitable tenant (Kaleva & Olkkonen 1996, 12).

Even if there is a tenant in the apartment, there is an essential risk to the tenant's ability to pay. Despite a binding lease, there are all too often situations in the market where the tenant is unable or unwilling to make the required payment. The easiest and most common way to ensure a tenant’s solvency is to go through his or her credit history. There are several companies in Finland from which an individual can check another person's credit information. This shows the tenant's previous payment behavior, and the bad payment behavior leaves an entry in the register, which in this case is easy for the landlord to pick up (Leväinen 2013, 210). With credit information, it is possible to prune out bad candidates, which means that rents are more likely to be paid in full and on time.

The landlord is obliged to cover the costs incurred for the wear and tear of normal living in the apartment. However, in the case of renting, there may be a risk of the apartment being destroyed or damaged by the tenant's own actions or negligence. Landlords try to prepare for these with a rent guarantee. The rent security is often either a one-month or two-month rent, which is returned to the tenant after the end of the lease if the condition of the home is what it was at the beginning of the tenancy. Damage caused by the tenant can be covered by rent guarantees if the apartment is damaged either after or during the lease (Huffman, F. 2002).

1.2.3 Other risks

In the housing company, the company is responsible for the maintenance of the property and the related costs and expenses. Based on these, the shareholder pays the company a cost-based consideration. The consideration is affected by many factors, including the costs related to heating, the costs of renting the land and the costs related to waste management. The monthly or annual costs of the above are not fixed but may fluctuate according to the market. For example, rental rates are indexed annually. The rise in the market for heating and electricity, for example, will lead to higher prices, which will have a direct impact on the return on investment housing from the investor's point of view. In order to minimize these, it is worthwhile for the investor to focus on companies that receive rental income, for example (Orava & Turunen 2017, 207–208.).

There are also strong risks associated with the consequences of political decisions in housing investment. (Orava & Turunen 2017, 197–198). Decisions can affect interest rates, which, as in the past, equally affect income from housing. According to Orava and Turunen, political decisions also affect the support systems in Finland. The decisions could cut the budget for support schemes, which will ultimately be borne by investors. For example, the Social Insurance Institution of Finland, which supports the housing of several Finns, supports housing through support schemes, either through housing or living allowances. Cutting these subsidies will lead to a deterioration in tenants budgets, forcing them to invent or find cheaper housing solutions when needed. According to Orava and Turunen, it is almost impossible to prepare for political risks, because the actions of an individual do not affect these decisions. Of course, where possible, apartments or real estate could be leased to companies, so that decisions for individuals and companies would not be mutually exclusive, but this would in turn require a much larger capital commitment.

In Finland, the climate is slightly more favorable for housing than, for example, in the United States. In Finland, natural disasters are very rare that could cause housing damage and pose environmental risks. Of course, the risks and damage caused by natural phenomena also occur in Finland, but these are really rare according to Orava and Turunen. These can take the form of changes in the soil of the dwellings, such as subsidence. Due to the rainy and humid climate, the houses are constantly exposed to moisture, but Finland is used to this and construction methods can prevent these. Orava and Turunen consider the environmental risks in Finland to be negligible and, according to them, it is not possible to prepare for these either, except by looking at the construction history of dwellings and looking at the repair history and repair needs.

2. RESEARCH METHODOLOGY AND DATA

This chapter discusses the implementation of the study. It introduces the method used in the research and the collection of data used in it. It also analyzes the research method and evaluates and considers its reliability. The chapter is divided into two different sections, the first examining the research method and data collection method and the second analyzing the method and its reliability.

2.1 Implementation of the research and collection of data

The empirical part of the study has been carried out as a qualitative study, and interviews have been used as the research method. Understanding the research topic requires professionalism and therefore the interview became the method. Qualitative research tends to focus on a smaller number of cases and to examine them as closely as possible (Tuomi & Sarajärvi 2013, 67). The questions were the same for everyone, but the interviews allowed for a free discussion on the topic, which allowed for a more focused focus on the research problem. Interviews can be categorized into three, there are structured, semi-structured non-structured interviews. (DiCicco-Bloom, B. and Crabtree, B.F. 2006) Interviews are a key interaction between two or more people in which the interviewer and the interviewee interact and thus aim to get the most comprehensive picture possible of the subject of the study. Four real estate investors with different backgrounds and a total of several decades of experience in the industry were interviewed in this study. The individuals will not be mentioned in the study by name, but will be compared to them with the letters A, B, C and D. Person A has more than 20 years of experience in housing investment and has worked in the real estate industry throughout his career. He has 21 investment apartments in his portfolio. Person B operates in the same real estate industry and has 12 investment homes in his portfolio and more than 10 years of experience behind him. Person C and D participated in the interview as a couple. They are self-employed and have a portfolio of 72 apartments with 9 years of experience. The interviews focused on quality in particular, and in order to be able to look at the matter from the investor's point of view, the aim was to select the interviewees on the basis of experience and reliability. In this way, it was possible to ensure that the research result could be considered reliable.

According to DiCicco-Bloom, B. and Crabtree, B.F., a semi-structured interview is often the only source of information in a qualitative research project, these interviews often last more than 30 minutes. In this study, the semi-structured interviews have been the only source of information in addition to the literature review and 3 interviews have been conducted, each lasting approximately 45 minutes. In a semi-structured interview, the questions are the same for everyone, but the interviewees are able to answer open-ended questions and bring out their own views.

The theoretical part of the research was compiled by the author of the research himself, and the empirical part of the research was also carried out by the researcher through an interview. In assessing the reliability of a qualitative study, the researcher himself is the main subject of review. The data collected should be examined as objectively as possible and the challenge of this assessment lies in the assessment of impartiality. The interview questions were determined by the risks that emerged in the theoretical part. This made it possible to compare the implementation of theoretical knowledge in practice. This gives depth to the research and a good approach to the research problem. All questions were essentially related to the risks of real estate investing and the interviewees were given the opportunity to present their own point of view. Through open discussion, the risks were addressed even more deeply. The experts are very interested and this allowed for a very comprehensive discussion.

2.2 Method analysis and reliability evaluation

In qualitative research, reliability criteria can be divided into three parts, namely reliability, certainty, and robustness. Credibility refers to whether a researcher's conceptualizations and interpretations are consistent with the researcher's own perceptions. Taking into account the requirements of the researchers, the safety of the research can be improved. Confirmation means that the explanation made in the study is supported by similar phenomena in the past Descriptive research. (Eskola & Suoranta 2008, 212) All respondents in this study received similar responses, and these responses were reflected in the theory. so Therefore, the study can be considered reliable according to the above-mentioned transferability criteriaQualitative research emphasizes neutrality. The interviewer often has his or her own opinion and view of things and this clearly creates a difficulty in interpreting and filtering out the interviewees ’responses. The message can always be interpreted differently, and in the interview the interviewer must be able to filter out the interpretive answers according to his or her own views and keep them neutral. Impartiality and credibility must be able to keep the interviewer separate.

Examination of reliability and credibility is the key role of the researcher or interviewer when looking at the data collected. The study can be considered more plausible if uncertainties can be ruled out. In this case, the interviewees and the researcher have personal knowledge and information on the basis of which the research result can be considered more reliable. The interviewer works in the financial sector to finance investors and based on a review of the literature, the risks and the views of investors can be considered reliable.

3. RESULTS AND DISCUSSION

This chapter discusses the risks of real estate investment and their management based on the interviews conducted and the material obtained from them. The analysis of the research results aims to tell about the main research problem and the most important things as clearly as possible. The research results and the implementation of the theory in practice were analyzed by comparing the theoretical part with the result of the interviews.

3.1 Risks related to real estate investment in Finland

As discussed above, real estate investing is perceived as a smooth and fairly risk-free form of investment. However, it is important for an investor that the investor is aware of the prevailing risks for the present and the future and that they are able to anticipate and prepare for them. The ease and ease of housing investment that attracts more and more people in housing investment is attractive. Utilizing debt, that is, investing with the help of a debt lever, allows more people to become a home investor, because the share of equity does not necessarily have to be significant when starting out.

As a real estate provider, guardian of the nation's wealth, a major employer and one of the engines of the Finnish economy, the importance of the real estate industry to society cannot be underestimated. The sector accounts for more than 70% of the nation's wealth, and construction investment accounts for two-thirds of annual investment in the Finnish national economy (Rakli, 2022).

Finland has a population of about 5.53 million people and compared to them, there are really many apartments in Finland. At the end of 2020, there were approximately 3.12 million dwellings in Finland. The population of Finland is increasingly moving from smaller municipalities to larger cities and suburbs. Completely new residential areas are constantly being built in the vicinity of the largest growth centers. This explains why 80 percent of dwellings built in Finland since 1995 have been concentrated in growth centers (Knüpfer, S. & Puttonen, 2009). This highlights the most important starting point for real estate investing, location is everything.

The majority of the population moves to growth centers and thus takes demand there with them. In small agglomeration areas, demand may be minimal and this creates a high risk from an investor’s perspective.

The trend in housing investment is also reflected in housing construction in Finland. One third of the apartments in Finland are rental apartments, so the market is large for housing investors. The share is still growing, 51 percent of the homes completed in 2020 were rental apartments. The prevailing interest rate level has kept construction and investment costs low, which explains the prevailing rent-driven market. The market is currently in high demand for the purchase of real estate, there is currently more willingness to buy than properties for sale. This is well reflected in the recent results of Nordea, one of Finland's largest banks. Over the past two years, the number of mortgages granted has grown by almost 20 percent annually.

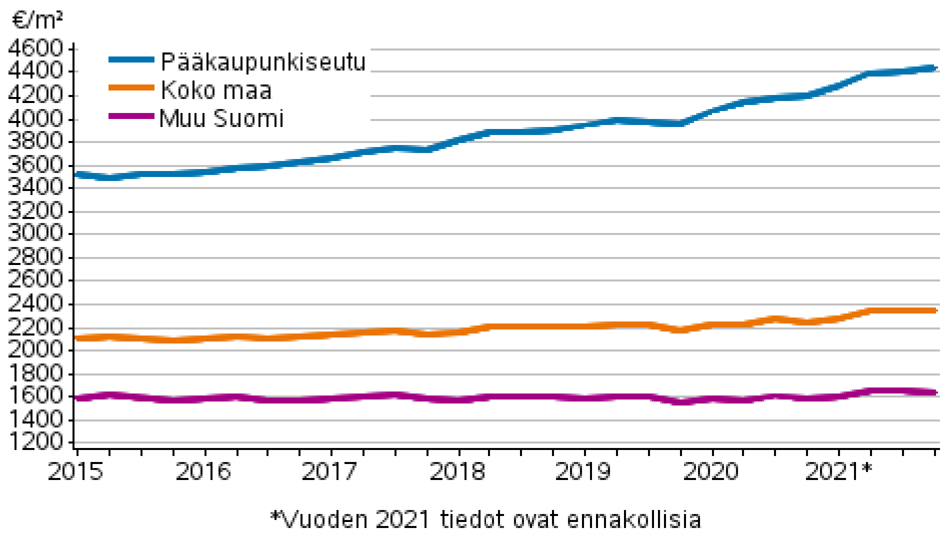

Figure 2. Housing price development in Finland since 2015
Source: Kettunen, P. (2021.). Tilastokeskus

Nearly a third of all homes in Finland are rented, with around 880,000 currently in use, of which about half are non-subsidized rental apartments and about half of the rental apartments are rental apartments financed by state subsidized loans. Non-subsidized housing refers to housing that does not involve ownership, construction or management state or municipal support and their price or population selection is not regulated. In the 2010s, the number of rental homes increased by more than 100,000 units, while the share of condos declined (Fasoûlas, E., Manninen, P. & Niiranen, V. 2013). The players in the Finnish rental housing market are made up of many components, the largest landlords in Finland are municipal rental companies, companies providing unsubsidised rental housing and private investors. Compared to other European countries, Finland's public real estate market is smaller than average. As a result, the public real estate market in Finland is still quite limited (Falkenbach, Niskanen & Kiehelä 2013). Therefore, the importance of rental housing offered by private investors remains high. For private investors, the risks may be exacerbated because, usually they have less wealth than larger companies They necessarily have a slightly smaller diversification because there is not as much capital to invest. As a result, the risks increase even more from the perspective of a private investor.

3.2 Risk awareness among real estate investors

We also managed to address the risks mentioned above as well as in the theoretical part with the interviewees. At the beginning of the interview, the strategy they used to invest in real estate was reviewed with each participant. All interviewees A, B, C and D said they would focus their investment only on growth centers and larger cities and avoid sparsely populated areas. According to the interviewees, the selection of the property is strongly associated with rentability, which plays a big role in making the selection. Interviewees A and B focus only on one- or two-room apartments in areas where there is demand for those apartments. Indeed, Interviewee A described his choice as follows:

"I focus on buying apartments in growth centers with a lot of students. There is always a demand for small one- and two-room apartments among them."

Interviewees C and D said they also focus on their proximity to universities in their own strategy. In their own words, thanks to their larger portfolio, they have made it possible for them to purchase an entire apartment building that includes 22 apartments. However, they emphasize geographical decentralization in their strategy and do not intend to buy more housing in the area. Geographical decentralization in their strategy creates security for the decentralization of regional markets.

In the interview, the interviewees were asked to name the three most significant of the risks presented in the written review, and all A, B C and D interviewees named the risks related to the tenant, interest rates and the value of the dwellings as the greatest risks. All interviewees are aware of these risks, but for no one have the risks materialized to a greater extent. This is due to investors being aware of the risks and eliminating them as much as possible. All of them have concentrated their investment housing in growth centers and consider it unlikely that the value of housing in the area will decline. In the case of tenants in particular, the interviewees said that they surveyed the background well.

Interviewee B commented on the question:

"I cannot influence the market situation and the rise in interest rates with my own actions. In order to eliminate the risks, I try to identify potential tenants. Credit information must not indicate bad payment behavior, and talking to a potential tenant will quickly give you an idea of what kind of person you are. "

Only persons C and D who were interviewed have realized the risk of a bad tenant and negatively affected their cash flow. Partial damage to unpaid rents and the apartment resulted in a loss of cash flow for them due to the termination of the tenant and the renovation of the apartment. The case is pending in court, but they did not want to take a further position on it.

With accelerating inflation, future forecasts for rising interest rates are unfavorable to investors. Interest rates are expected to rise in the future and investors are aware of this and therefore all interviewees raised this to some of the biggest risks. (Lindström, J. 2014) Despite the predictions, everyone plans to continue investing and grow their portfolio in the future.

Interviewee A stated on interest rates:

"The accelerating interest rate economy will certainly have an impact on the future of real estate investing and this will certainly require some reorganization in the future. However, I am not giving up real estate investing and will continue to grow my portfolio.”

It can be clearly seen from the results of the survey that the experts interviewed identify the risks of housing investment excellently. In the theoretical part, the most significant ones were defined on the basis of literature and scientific articles
risks: price risk, interest rate risk, empty months risk, tenant risk, rent level risk, counterparty risk, political risks and natural phenomena risk. None of these became a new thing for the

interviewees, and all of these already had some sort of vision already in place. In addition to the identified risks, no significant new risks emerged. The views of the interviewees actually coincided completely with the characteristics of the risks defined in theory. The biggest risks were price risk and interest rate risk.

3.3 Management of risks related to real estate investment in Finland

A core issue of real estate investment is risk awareness and handling. These guidelines are independent of the form of investment and apply equally to the stock market. The aim was to combine the theory presented in the research with the interviews as much as possible. The risks presented in the theoretical part were presented to the interviewed investors during the interviews. The theoretical part is well supported by the interviews, with respondents identifying all of the investment-related risks discussed here. All respondents identified key high risks related to interest rate, rent and geographic risk, which were also highlighted by Orava and Turunen (2017).

The risk related to interest rates was most highlighted by each of the interviewees and emphasized in their investment strategy. The European Central Bank has tightened its interest rate policy with ever-accelerating inflation, and this will grow in importance in both the mortgage borrowers' economy and the portfolio of mortgage investors. Each of the interviewees A, B, C and D has prepared for an increase in interest rates, but there were significant differences at this point depending on the investment strategy. Respondents A and B found the interest rate hedges offered by financial institutions expensive and emphasized the importance of the buffer fund. They are currently preparing for a 2% rise in interest rates and are currently putting the resulting cost increase into a buffer fund on a monthly basis. This, of course, slows down the possibility of growing the portfolio, but it works as an excellent way to prepare for the rise in interest rates, which is important and also highlighted by Kaarto (2015, 79). The strategy of interviewees C and D differed slightly from the others and they have tied more than half of their investment loans to a fixed interest rate offered by the bank. They have larger volumes, which means that the risk levels also increase with the higher leverage (Orava, Turunen 2017, 303).

However, despite the unified different strategies, everyone had protection against rising interest rates, but there are different ways to do it.

Figure 1. Development of 12-month Euribor since the 1990s
Source: Euro Area (Changing Composition) - Money Market - Euribor 1-Year - Historical Close, Average of Observations through Period - Euro, Provided by Reuters - Quick View - ECB Statistical Data Warehouse

It is not possible to liquidate real estate assets on a particularly fast schedule, which will increase the importance of buffer funds, especially according to interviewees A and B. Although the interviews were about real estate investing, the interviewees emphasized the diversification into different instruments. Quoting Interviewee B:

"Although I am a real estate investor, I do not put all my eggs in the same basket. I am also trying to find a bigger diversification between different investment instruments. In terms of real estate, I spread the properties geographically to growth centers. "

With sensible geographical diversification and a focus on growth centers, interviewees did not see a drop in price as a very relevant risk. Here, however, the location of the object is emphasized. This should be chosen from areas where there is constant demand for housing, ideally the demand regionally is greater than the supply. The view of the interviewees is supported by statistics on the price development of housing in Finland, which has been reflected in rising prices from year to year excluding the year 1970. Decentralization can reduce regional risk. It is not advisable to invest in cities or settlements that are too small if you want to reduce regional risk. Investors can control price risk by carefully familiarizing themselves with who to buy. In addition to target data, the location and size of the apartment also have an impact on price risk (Kaarto, M. 2015)In order to avoid free months, according to the dissertation, it is worth favoring the acquisition of investment targets from growing localities or downtown areas. It also makes sense to keep the rental level of the property slightly lower than the market price, which increases the interest of the property in the eyes of potential tenants.

All interviewees A, B, C and D think it is important to choose the resident and the tenant carefully. For example, a poor tenant can wreak havoc on an apartment, fail to pay rent, or otherwise neglect a lease. From an investor's perspective, all of these have a negative impact on cash flow. If the monthly costs remain the same and the cash flow is lost, even a profitable real estate investment will turn unprofitable for its investor. The risks to renting an apartment were felt to be partly self-inflicted. The credit check was raised by every single interviewee. Based on the interviews, there was no room for compromise in this matter. This will be able to exclude bad candidates, but unfortunately it will not be possible to achieve a definite result in this way either.

Interviewees C and D stated:

"If there is an indication in the credit information alone, we will not leave the apartment to rent to him. We do not make any exceptions in this regard. However, this does not exclude the risks of bad tenants. Whatever happens, you should react quickly to minimize the loss. "

Real estate investors can manage the risks associated with renting by taking the time to select a tenant. External help, such as rental agency should be used to ensure that tenant is okay. Home investors often feel that they are not legally the same as tenants in terms of rights and obligations. If the tenant still doesn't pay rent after signing the contract, the mortgage investor thinks the termination is too slow. By law, termination proceedings can only be initiated if rent has not been received for at least two months. After that, the unloading or customs clearance process itself takes at least two months. To ensure that tenant obligations are met, it is worth negotiating a reasonable security deposit. According to all interviewees, there is always a risk for the tenant to be prepared for financially as well as mentally. Rent risk refers to the uncertainty that a selected tenant will not be able to pay the agreed rent to the landlord. Risks can also materialize if the tenant fails to meet other obligations under the contract or causes other damage that affects the value of the apartment. This risk can only be combined with housing and real estate investments (Kaleva, H. & Olkkonen, O. 1996). Respondents C and D stated that the low-risk part of residential investment can be explained by the fact that it is a fundamental human need issue and that there are always new users.

The level of risk awareness associated with real estate investing is really good among investors. The aim is to prepare as well as possible for all identified risks in the Finnish market by those invested in the region. There are many ways to do this based on your investment profile. Each investment profile has slightly different practices for hedging against each prevailing risk, but research shows that these should be prepared for.

Based on the results of the interviews, from the respondents' perspective, natural disaster risk and legal change risk are largely insignificant or uncontrollable or uncontrollable. Respondents did not consider and justify the risks of natural phenomena in any way, since in the Finnish real estate market various natural phenomena are so rare that their impact on housing is almost non-existent. However, people who own country homes are more likely to be affected by the risks of natural phenomena than home buyers in urban areas (Korkman, S. 2014).

CONCLUSION

This study deals with housing investment, housing investment risks and their management. The purpose of the study was to identify those associated with housing investment risk and find ways to protect yourself from risk. Its purpose is to understand the basics of housing wealth, characterize homeownership as an investment, identify the risks involved in housing investing and find ways to manage those risks. A literature study provides an overview of real estate investing and its principles. Based on previous research and literature, it attempts to highlight the risks of real estate investment. The empirical part of the study was conducted as a qualitative study. The survey was conducted through telephone interviews with four different real estate investors operating in Finland. All were asked the same questions and they could express their opinions. Real estate investment is perceived as a low-risk investment with a steady return and cash flow. An investor can easily leverage debt, especially at the prevailing low interest rates. However, this cannot be expected to continue, and interest rates are projected to rise. Real estate investment is a growing megatrend in Finland, which, due to its ease, attracts more and more Finns to join the investment format. However, real estate investing involves its own risks, as do all other forms of investment.

Based on the results of the study, it can be stated that real estate investors have an excellent knowledge of the form of investment and the risks associated with it. Interviewees identified all the risks involved in the interviews, but emphasized the relevance of a few of them. Real estate investing and the risks associated with it are diverse and it cannot be said that there is one and the right way to manage these risks. Each investor is aware of the risks involved, but there are slightly different approaches to managing them. The interviewees felt that awareness of the risks of real estate investment in Finland is at a good level and has risen especially during the last decade. This has been influenced by the trend of the matter, as a result of which there is a lot of literature on it and it has gained visibility in the media.

By far the biggest risks for the interviewees were the risks related to location, tenant and interest rate. The choice of tenant was emphasized by the interviewees and some background research should be done on this. A common practice among investors when choosing a tenant is to check credit records and charge a rent guarantee for one or two months. The credit information gives an idea of the tenant's payment behavior and the rental guarantee can cover any costs incurred. There is also an inherent risk involved in finding a tenant and empty months, but this can be minimized by the location of the apartment. The relevance of the location is emphasized in terms of price level and rentability. An apartment in a good location in a growth center is always in demand among tenants, thus avoiding empty months and cash flow losses. Investors also emphasized the location from the point of view of the price level, the price level of housing in growth centers has been historically rising and the respondents felt that the direction will be the same in the future, and there is no risk of a fall in prices.

Investors will not be able to influence the rise in interest rates with their own actions, but they will be able to hedge against it. Depending on the investment strategy, there were several ways, but based on the research results, it can be stated that an increase in interest rates must be prepared for. The most common means were either the purchase of an interest rate hedging product attached to the loan or the maintenance of a buffer fund. The relevance of the buffer fund was also evident in the case of empty months risks.

The literature review of the study and the result of the interviews are mutually supportive and the study can thus be considered reliable. The research can be used to provide information to those interested in real estate investors. For further research, data from several different countries could be used to determine how risk levels are realized for housing market returns in different countries. This would allow for an even broader view. This study can also be used as part of a broader and more comprehensive study of country-specific differences in real estate investment.

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APPENDICES

Appendix 1. Interview frame

1. How long have you invested in real estate?

2. What is your strategy as a real estate investor?

3. Do you invest in real estate through a company or as an individual and why?

4. Do you use third parties to help you sell and rent?

5. Why do you invest in housing and what is the buying decision process like?

6. By what means have you tried to control the risks listed below?

(a) The risk of an increase in interest rates

b) The risk of falling house prices

c) The risk associated with the tenant

d) The risk of empty months

e) The risk of a change in the level of rent

f) Legislative changes and political risks

g) Risk of natural phenomena

9. Were any housing risks not mentioned?

10. In your opinion, what are the 2-3 most significant risks of the above

11. Do you feel that the home investor is aware of all the risks associated with the investment?

12. What risks do you think there will be in the future?

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