Capital subsidies cover a portion of the costs of developing a rental or for-sale property, thereby improving its affordability and economic viability.

Because a capital subsidy does not need to be paid back, it reduces the amount that must be borrowed or obtained through an equity investment by a private party to develop a rental property. Lower debt service levels allow a project to charge lower rents and still be economically sustainable.

The Low Income Housing Tax Credit (LIHTC) is one type of capital subsidy (in essence, it provides dollars that do not need to be paid back by the project), but additional capital subsidies are often needed even for properties that receive LIHTC awards. While the equity raised by syndicating LIHTCs covers a substantial share of development costs, in many cases, the LIHTC equity plus the debt supportable by rents at the target level are insufficient to fully cover all development costs. In these cases, additional capital subsidies are needed to serve as “gap financing” to supplement the equity provided through the LIHTCs and enable a project to be economically viable.