Developers aiming to build housing affordable to low-income renters generally need public money to help cover the costs. To understand why, let’s look at how multifamily rental properties are financed.

**How is multifamily rental housing financed?**

Let’s start by thinking about how a home buyer purchases a home. Typically, a home buyer makes a downpayment and borrows the rest from a bank through a mortgage loan.

Multifamily rental housing is financed in a similar way. The downpayment is called equity and is paid by investors, who put some of their own money into the project. The rest of the costs are covered by a loan – also called “debt” – usually from a bank. These loans look a lot like a regular home mortgage. They can be fixed rate or adjustable rate, with terms lasting as long as 35 years.

For a market-rate rental property, equity and debt cover the total development costs of the property. These include the costs to construct a new development or renovate an existing development including the cost of acquiring the land.

Like a home, rental housing has a second major type of costs, called operating costs. For a homeowner, these are things like insurance, utilities, property taxes, and maintenance. Multifamily rental housing operators have all of these costs plus others,
like property management, security, administrative expenses, and marketing to advertise the building to potential renters.

How are monthly payments on loans and operating costs paid for? Homeowners repay their mortgage and other expenses out of their own resources – usually a salary from employment. By contrast, the owners of multifamily rental properties pay for financing and operating costs using the income from rents paid by tenants.

**So what happens to the financing prospects for properties that charge low rents in order to create affordable homes?**

Here’s where the need for public subsidy comes in. A property that charges lower rents generates less rental income. A property charging lower rents therefore can’t have as much debt and operating costs as a property that charges higher rents. That creates a problem, because the total of equity and debt can’t cover the costs of the development like it does in a market-rate property. Land costs are set by the market, and the property must meet basic construction standards regardless of who it serves.

At affordable properties, the lower rents usually lead to a gap between the funding an owner needs to develop and operate a property and the revenue available to do so.

To create an affordable multifamily rental property, this funding gap needs to be filled. To learn how to fill the gap, visit LocalHousingSolutions.org.