



Policy Snapshot: *Interest subsidies*

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POLICY SNAPSHOT INTEREST SUBSIDIES

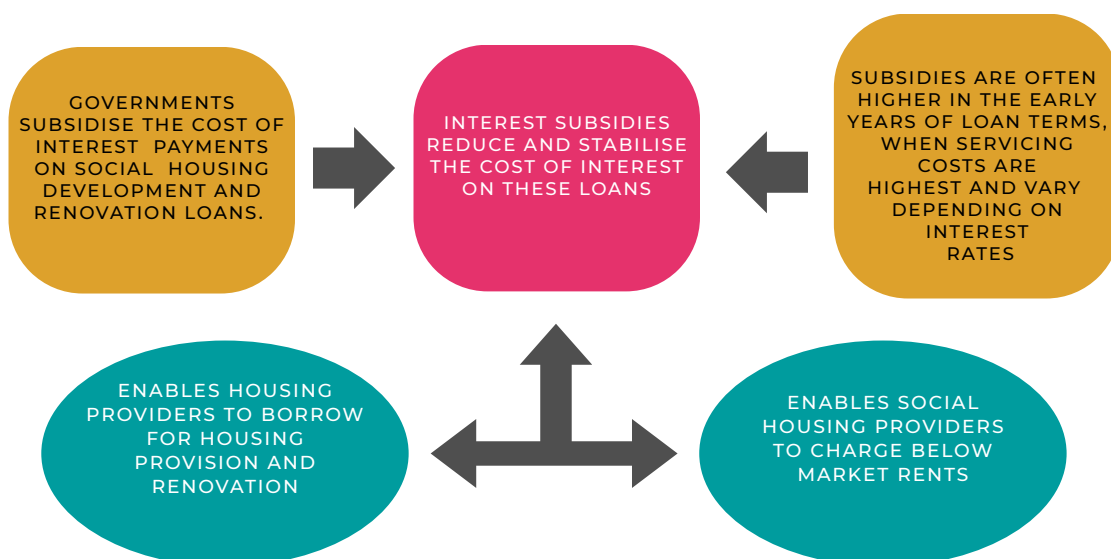
WHAT ARE INTEREST SUBSIDIES?

These are government subsidies that reduce and even out the costs of interest payments on social housing development or renovation loans. They are often provided during the early years of loan terms, when the burden of interest payments is greatest compared to revenue from rents. Interest subsidies were more commonly provided in the mid and late twentieth century when interest rates were generally higher and more volatile than has been the case in recent decades. However, they still play an important role in the social housing financing system of several European countries.

WHY ARE THEY USED?

They reduce interest rates on social housing development and renovation loans and also stabilise interest costs over the lifetime of these loans. This enables social housing providers to let these dwellings at below market rents.

HOW DO THEY WORK IN PRACTICE?



WHERE ARE THEY USED IN EUROPE?

Interest subsidies play an important role in financing social housing provision in Denmark. The primary programme for providing these is called the ydelsesstøtte til almene boliger (benefit support for social housing).

These subsidies provided by this programme **vary according to the interest rate social housing providers pay on borrowing from commercial lenders** (primarily from private mortgage banks, which are funded by bond issuances).

The interest subsidies are designed to ensure that the total annual loan repayments do not exceed 2.8% of the initial capital costs of housing development (adjusted for inflation). Because loans from mortgage banks provide most (86-90%) of the capital for social housing development in Denmark, the interest subsidies ensure that social housing providers' capital financing costs are largely stable and predictable.

The costs of these interest subsidies are covered primarily by central government. However, if they exceed an expenditure target the Danish National Building Fund also contributes to these costs. This fund is funded from the rents paid by social housing tenants.





WHERE ARE THEY USED IN EUROPE? (CONTINUED)

Interest rate subsidies are also provided for social housing development loans in Finland. They are provided by a state institution called Valtion asuntorahasto (State Housing Fund - VAR), which was established in the 1990s to ensure that social providers could borrow at affordable rates of interest.

This subsidy is provided if the interest rate on the state-guaranteed **loans**, which partly fund social housing provision in Finland, **exceeds 2.3%.** The subsidy provided is 90% of the interest costs above 2.3% in the first year of the loan, but this decreases **incrementally over time.** For instance, it falls to 81% of this excess in year five of the loan and to 2.25% by the fortieth year.

The majority of the loans subsidised using these arrangements have variable interest rates; therefore, as would be expected, spending on this subsidy varies. As would be expected, spending on these subsidies varies over time depending on interest rates. It was just €1.8 million in 2022, but rose to €87 million in 2023 as a result of rising interest rates.

WHAT ARE THE RELATIVE STRENGTHS AND WEAKNESSES?

Strengths	Weaknesses
<ul style="list-style-type: none">• Provides a cost subsidy which enables charging of submarket rents.• Can increase the availability of commercial finance for social housing.• Reduces and flattens the cost of loans, which enables higher and more consistent social housing output across interest rate cycles.• Reduces the cost of social housing provision, thereby enabling the charging of below market rents.• Depending on their design and prevailing interest rates, this can be a shallow subsidy that is more affordable for governments.• Addresses the 'front-end loaded' nature of interest repayments, which are higher in the loan's early years	<ul style="list-style-type: none">• Likely to be on the government balance sheet• May not be required in the context of low and predictable interest rates.• Depending on the design of interest subsidies and the prevailing interest rate this can be an expensive subsidy for government.

Where can I learn more?

- Interest subsidies in Denmark - <https://www.nationalbanken.dk/media/3kpbqn34/analysis-no-24-new-financing-of-social-housing-strengthens-the-market-for-danish-government-securities.pdf>
- Information on social housing finance in Finland and Denmark - <https://www.housingeurope.eu/cost-based-social-rental-housing-in-europe/>
- EqualHouse Report on Financing Social Housing https://equalhouse.eu/media/Publications/Making_Housing_Affordable/EH%20WP5%20Finance%20Report%20Final%20for%20Website.pdf



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