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Equity or debt? Last time we needed trust, now we need future perspective!

The financial crisis of 2008 was a crisis of debt – triggered by debt handed out by banks as loans, fuelled by repackaged debt, wreaking havoc on interbank debt markets and culminating in the sovereign debt crisis. 2008 and the following years we also experienced a crisis of trust: banks, supervisors, even governments did not trust each other. So, one might say debt is very much about trust – the trust that someone honours his promise to pay back. The evidence seems to suggest that we have fixed our trust-issues over the last decade: the banking sector is stable, reinforced by better EU level regulation and strengthened pan-European supervision. Governments agreed to have the European Commission issue debt for the first time in history to fund a recovery program macroeconomic significance.

Unlike debt, equity is about future perspective: when you buy a share, contrary to debt, there is no promise that you get your money back, there is only a (hopefully well-grounded) perspective that the company succeeds. Looking at the current stock-market, future perspectives do not seem to be the issue. Here of course the low interest environment helps. But the stock-market is not the economy, and while companies associated with the digital economy may have profited, many brick-and-mortar business have suffered and piled on debt. Should we help them to convert their debt into equity?

As you will read in any economist's article at some point: It depends.

First, what is clear is that the future will be green and digital. Therefore, subsidising carbon-heavy businesses of the past will not help. Investors know that and are seeking green investment opportunities. Therefore, one important measure is to help investors identify green investments, as the European Commission recently did by developing the EU taxonomy for sustainable activities. Another measure is to actively support reforms in Member States to carry out reforms to develop green finance ecosystems or green bond markets. The Commission does that through the Technical Support Instrument.

Second, equity is most important for start-ups and innovative companies and difficult to access especially for SMEs. Therefore, the European Commission has launched several initiatives to foster access to equity: the Capital Markets Union to unlock more investments, also for SMEs. The Single EU Equity Financial Instrument to support European businesses' growth, research and innovation. Venture EU, the Pan-European Venture Capital (VC) Fund-of-Funds programme to further address Europe's equity gap by investing in VC Funds-of-Funds. The European Innovation Council Fund which just provided a first equity investment of EUR 178 million in breakthrough innovation.

Third, if the economic outlook brightens, equity becomes more attractive, debt more sustainable. This is the real solution for which we have to work, and the European Commission does: The Recovery and Resilience Facility, making €672.5 billion in loans and grants available, gives perspectives that the EU will emerge stronger and more resilient from the current crisis.