Now, let's talk for just a minute in specifically natural terms. Here's the point: how well Christian leaders identify, access, and use the capital entrusted to us is a significant part of our effectiveness as Christian leaders in the modern world. And that's true whether you are looking at that personally or professionally!

So, let's take a look at just what the word "capital" means from a finance viewpoint. Here's a pretty classic definition for a modern organization: financial capital is the economic resources used by leaders and their organizations to provide products or services to those they serve. So, in a modern context, the use of financial capital is very relevant to both businesses and nonprofits, for sure!

Now then, just where do you start as a leader with regard to understanding the proper use of capital? Well, you look at two foundational options: debt capital and equity capital. And knowing the key differences between the two is an absolute must!

First and foremost, you should know that recent teachings by many in personal finance have pretty much demonized debt as bad. And, for sure, going into debt for the wrong reasons is indeed bad. But making a generalization like "debt is bad" is too simplistic. To start to get a handle on that, you will want to listen to my podcast that's named "is debt good or bad?"

Now, we are going to talk in terms of the key features of both types of capital. Stick with me here—it's going to get very targeted after we cover the basics. So, to begin, here's a summary of debt capital.

The first key feature of debt is that you have to pay interest to lenders for the use of their capital. Just like you pay rent to a landlord to use that landlord's real estate, you pay interest to use a lender's money. The actual interest rate, which is usually expressed as an annual percentage, varies widely based upon market factors and individual transaction risk. So, here's an example of a sentence we might hear: "Our company had to pay a high annual interest rate on a loan because we are a start-up organization that is riskier to lend to than a well-established, proven organization."

Now, the second key feature of debt is that you are likely to have to execute what's called a "security interest" in one or more key assets owned by the organization. That means the loan you obtained is "secured" legally by an asset or two—that is, the lender can enforce the sale of those assets you have pledged as part of the loan or mortgage if you or your enterprise as the borrower fail to properly make scheduled payments or otherwise default on key requirements of the debt agreement.

Next, the third key feature of debt is that you have to pay back what you borrowed. Well, duh, you say! Yes, everybody knows that you have to pay back the amount you borrowed! And yes, that's true, but the reason that's a key feature here is that it contrasts directly with equity capital, where the receiver of funds never has to pay back the funds that are advanced.

The fourth key feature of debt is that the receiver of funds typically does not transfer ownership interest in the organization. That simply means this: once the funds-receiver has fulfilled the requirements of the debt—paying back the amount borrowed and the interest, as agreed—then the lender simply goes away!

Now, let's contrast traditional equity capital with that debt capital we just talked about—illumination will come with the contrasts between the two. Here we go with the typical, most standard scenarios.

First, with equity capital, there is no interest to pay a lender—there is no type of rent at all that's due on the money received. Second, with equity capital, the lender is not given a security interest in assets. So, no pledge hampering your assets is required! Third, with equity capital, the receiver of funds does not have to pay back those funds. Clear as a bell, those are the three key differences between debt and equity!

© 2020 Kevin Miller All Rights Reserved

But here's the important catch, and indeed it's a catch that can get costly, difficult, complex, and perhaps even very problematic. You see, with equity capital, you give up a portion of the company, that is, you share ownership. That means you have a sort of partner. No, that means you very much have a *real* partner. But just how much of a partner? Well, that depends.

For example, in order to obtain the equity capital that you considered necessary, did you have to give up ownership of more than half of the company? Well then, you have effectively lost control and power over the company. Well then, how do you keep from doing that? That requires negotiation. But the investor may not be willing to give you control over the capital, perhaps due to your executive inexperience, or maybe because your company has an insufficient financial track record, or maybe the amount of capital requested as compared to the expected value of the ultimate payback to investors is deemed insufficient.

Does that sound unfair? Well, it all depends on whether you're the party asking for the funds or the party investing the funds! But here's a bit of a bird's-eye view. From the original owner's perspective, using equity capital can be very costly compared to using debt capital in those cases where the total amount paid for using the debt capital is dwarfed by the ultimate value of the portion of the company given up to the new equity investor. But, on the other hand—also from the original owner's perspective—getting funds from an equity owner and not having to pay back debt and interest may be exactly the right financial priority…in fact, it may be the *only* option if no new equity investor is willing to step forward. At any rate, if your enterprise is unable to be in business without an injection of capital—whether that's debt capital or equity capital—well, then, either option can be a life-saver for your enterprise, even if it's very costly!

We've just covered a sketch of what we might label more "vanilla" versions of debt capital and equity capital. The modern reality is that sophisticated capital markets have evolved to where there are many variations as to how capital is successfully raised using astute structures—that is, blending both debt features and equity features in the same financial instrument—from, say, debt that is convertible to equity …to debt that is issued with warrants to buy ownership later…to many other creative capital structures.

Here's the ultimate key to thinking about capital when you need it to survive…or to thrive. Are you competently prepared and are you structuring a deal that comfortably, realistically allows you and your team's skill set to be both a good, long-term steward for your organization and simultaneously a good steward for either the new lender of debt capital or the new equity investor?

The Apostle John tells us that the Holy Spirit gives us remembrance of Jesus' teaching, and we remember that Jesus gave us the parable of the talents: when the owner of capital funded three different people, the one who hoarded was the problem. Indeed, for the Christian, the access, the deployment, and the success with regard to capital that we are entrusted with is one of the primary ways we reflect Christ.

Does all this make your head hurt? It shouldn't. Every person hearing my voice is appointed to a particular position to help his or her workplace be a strong steward for the owner of the enterprise. That's especially obvious for the Christian, yes, working on behalf of God and His Kingdom alongside earthly stewardships.

Understanding and astutely applying opportunities involving debt capital and equity capital is a part of every Christian's basic stewardship literacy, practically applied! Some of the most important transactions you will ever be a part of in your life—buying a house, obtaining a mortgage, starting a business, giving for Kingdom purposes—well, all of those require a strong understanding of stewardship in the context of different options for obtaining or investing capital.

And what a privilege that is! So, whether you are seeking to obtain capital or seeking to invest capital, will that next transaction be debt capital or equity capital or some blend of the two? Go for it—your good stewardship is about to be unfolded before God…and all those people who you are transacting with!

© 2020 Kevin Miller All Rights Reserved

A&A: Application & Action

1. Are you and your team—whether that's your workplace, your church, or your family—equipped with the stewardship literacy to handle debt capital and equity capital issues wisely? Give easily identifiable examples for each.

2. Are you biased towards equity capital? Towards debt capital? Why? Be specific.

3. What current and planned, ongoing future steps are in place to work to ensure your organization's stewardship literacy is cutting-edge, including your understanding of debt capital vs. equity capital?

© 2020 Kevin Miller All Rights Reserved