

# Differences Between Equity and Debt

Equity and equity-like investments differ from debt in the following ways:

- Depending on the structure of an equity investment, a borrower may or may not have to repay the investment. In contrast, a borrower must repay debt.
- The total dollar amount eventually recouped as a result of an equity investment is a function of company performance and is not known at the time of investment. The amount to be repaid to a lender is a function of the amount borrowed and the interest rate, and is known at the outset of the loan.
- A business owner does not guarantee an equity investment in his or her business. A small-business borrower usually does.
- An equity investment is almost always unsecured. Most small-business loans, particularly those financing fixed assets purchases, are secured.
- An equity investment typically requires no or modest payouts to the investor during the early years of that investment. A loan requires debt service payments from the outset or shortly thereafter.
- An equity investment may represent or eventually lead to an ownership interest in the business, depending on the structure of the investment. A lender has no ownership interest.

Only the imagination and experience of the investor limit the form of an equity investment. Common forms included common stock, preferred stock, profit-sharing agreements, warrants, and convertible subordinated debt.

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