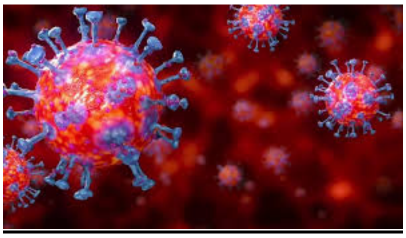

Why taxpayer-funded rescue packages warrant equity

Globally, governments are spending trillions of dollars in an effort to keep economies and businesses afloat during these unprecedented Covid-19 times.

While this should generally be applauded, we should not forget that that money must come from somewhere. Any money governments hand out is money we, as taxpayers, ultimately need to pay back. There is no such thing as a free lunch.

Governments are basically able to access money in one of three ways:

- Tax collection;
- Issuing government bonds (=borrowing money); and
- Asset Sales (i.e. rail, energy, social infrastructure, etc.)

Government assets are finite and eventually governments run out of assets to sell/privatise. That leaves only tax collection and borrowing funds (which even governments need to pay back) as sources of ongoing income for governments.

Accordingly, we, the taxpayers, ultimately pay for these extraordinary rescue packages. But is this a good deal for us as taxpayers?

In tangible terms, we get very little in return for providing these funds other than that we possibly help businesses bridge a very tumultuous time and potentially create a situation where some employees will have a job to go back to when normalcy returns. These are good outcomes but even if we assume the funding provided results in saving all targeted businesses and jobs, are we maximising value for money?

The political system (and media) is now completely focussed on both the immediate health and short-term economic outcomes. Long-term thinking about the consequences of these unprecedented rescue packages gets no airtime.

Dealing with the long-term financial implications of the enormous cash injections (i.e. balanced budgets, debt reduction, ability to fund future growth, etc.) does not get a mention and is clearly not a high priority as governments are fighting day-to-day fires. However, the long-term financial ramifications *should* be a key consideration because the financial fall out of these enormous rescue packages will have a great and lasting impact on all of us long after Covid19 is a distant memory.

As far as providing economic rescue packages are concerned, governments should approach this situation much more like a private enterprise investment. For the larger rescue packages (e.g. over $10M), the government should insist on a commensurate equity stake in the businesses that receive taxpayer-funded rescue packages. When some economic normalcy returns, the government can then liquidate these equity positions to reduce its debt levels. This is no different from companies raising private equity to obtain capital for growth or expansion and having to give up equity in return.

If politicians (and/or their advisors) do not seriously look at equity in exchange for taxpayer funding as an option now, we will saddle ourselves and many future generations with enormous unnecessary long-term debts/deficits that will put a serious strain on any future growth.

Governments taking equity in exchange for taxpayer-funded rescue packages are nothing new. Just one example where equity taken in exchange for rescue funds was implemented successfully was during the recent GFC. The "Big Three" U.S. car companies of General Motors, Chrysler and Ford all faced potential insolvency. Because of the $US80 billion dollar lifeline provided by the Troubled Asset Relief Program engineered by the Bush and Obama Administrations, the U.S. auto industry managed to recover. Jobs were saved and businesses on the brink were able to transition and avoid bankruptcies. Furthermore, the government was able to sell its equity position post GFC for $US70B. Net cost to the taxpayers was only $US10 billion (rather than $US80 billion) and all three automakers were saved at the time. This is a huge win-win situation.

Governments should invest vast sums of capital into the economy to limit the severe economic impact of the Covid-19 crisis. However, for any large contributions/investments the government should also be taking a commensurate equity stake as consideration for this taxpayer funded financial assistance. Doing so will benefit everyone and will protect future generations from the long-term financial consequences of these very large cash injections. Failure to do so is, in my view, an unacceptable and lazy option that short changes both the country and taxpayers.

Government should quickly set up a special unit with experienced finance people and commercial negotiators so it can quickly, efficiently and fairly agree valuations for larger businesses that are entitled to government support.

Equity in exchange for government rescue packages should be common practice.

Happy Investing

Nanne van 't Riet
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