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How to make profits shine

by PHILIPP IMMENKÖTTER

Summary

What do Volkswagen, Vonovia and Infineon have in common? Their financial figures sparkle more beautifully than the economic reality. The reason: subsidies.

Zusammenfassung

Was haben Volkswagen, Vonovia und Infineon gemein? Ihre Finanzkennzahlen funkeln schöner als die wirtschaftliche Realität. Der Grund: **Subventionen**.



What do Volkswagen, Vonovia and Infineon have in common? Their key financial figures sparkle more beautifully than the economic reality. The reason: subsidies.

State funds help companies to reduce production, investment or financing costs. Lower costs mean higher profits.

But what would the companies' profits look like if they had not received subsidies? What influence do the subsidies have on valuation and key financial figures?

In order to estimate the impact of subsidies on the companies' financial ratios, we assume that a company would not have received state support but would still have implemented the same projects. It should be noted, however, that a company without subsidies might not have made the same decisions.

As the allocation of subsidies is concentrated in Germany, we look at the eleven of the 40 DAX companies that, according to their annual reports, have each received more than one billion euros in subsidies over the past ten years. The eleven companies are BASF, BMW, Continental, Deutsche Bank, Deutsche Telekom, E.ON, Fresenius, Infineon Technologies, Mercedes-Benz Group, Volkswagen and Vonovia.

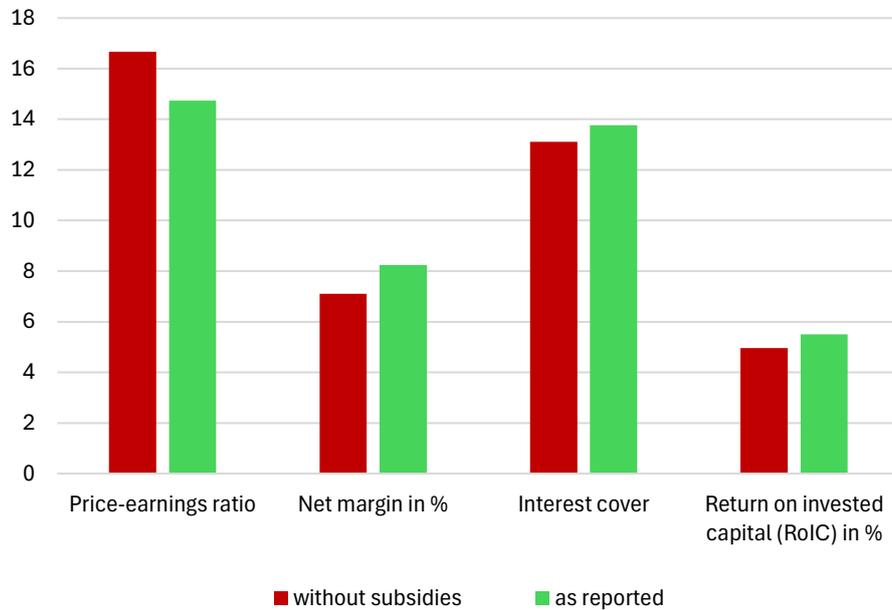
The impact of subsidies is the strongest on the valuation. To do this, we look at the price/earnings ratio and compare the share price at the end of 2023 with the average profit over the past ten years. Without subsidies, the valuation of the eleven companies would rise by 12 per cent on average. While the companies were valued at an average P/E ratio of 14.7 at the end of 2023, this would only be 16.7 without the state funds.

The influence of subsidies is also noticeable in other key financial figures. The net margin of the eleven companies is on average 1.2 percentage points higher as a result of the subsidies than without them. In terms of interest cover (EBIT compared to interest payments), the subsidies increase the ratio by 0.7. The impact on the return on investment is also measurable, but at half a percentage point it is small.



Subsidies and valuation

Averages for 11 heavily subsidised
DAX companies



Note: 11 DAX companies that report a cumulative total of more than one billion euros in government grants in their annual reports for the financial years 2014 to 2023. To calculate the alternative key figures, the subsidies reported in accordance with IAS 20 are added to the corresponding key earnings figures. Price/earnings ratio is the share price at the end of 2023 in relation to the average profit over the past 10 years. Any tax effects are not taken into account. Net margin is net profit divided by sales. Interest cover is EBIT divided by interest expense. Return on capital employed is net profit divided by average equity and debt capital for the financial year. Source: Refinitiv, annual reports. Status: 07/10/2024.

Subsidy policy in Germany and the EU contributes to the fact that the key financial figures of German companies look better than they actually are. Although subsidies give companies a competitive advantage in the short term, they can lead to inefficiencies in the long term, making companies sluggish and unprofitable.

When making investment decisions, investors should always bear in mind the subsidies that a company has received. Subsidies can give the financial figures a varnish that makes the companies look better than they actually are.



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