AREA STUDI MEDIOBANCA

GLOBAL INDUSTRIAL MULTINATIONALS
WITH A FOCUS ON DEFENCE INDUSTRY GROUPS

Total sales and capex up by 13.3% and 17.5% respectively in 2022, with all sectors growing

Defence industry multinationals: increase in aggregate revenues of 6% expected in 2023
Stock market performance bucking trend in 2022:
up 34.6%, compared to a 11% decrease for the global index
In a sector dominated by the United States:
Leonardo eighth largest player in the world by total sales, Fincantieri sixth for investments

Global defence spending has exceeded $2bn for the first time since 2021,
37.9% of which attributable to the United States and 13.9% to China

Milan, 4 April 2023

The Mediobanca Research Area has analysed the annual financial statements of more than 240 **global industrial multinationals**, broken down by segment. The companies posted aggregate revenues of €12,300bn in 2022, and at the year-end reflected an aggregate market capitalization of €22,300bn, equivalent to 23% of the overall value of the world's stock markets. The survey also contains a focus on the **world's thirty largest defence industry groups** with individual revenues of over €1.5bn, fifteen of which are based in the United States, ten in Europe, and five in Asia.
The presentation is available for download from **www.areastudimediobanca.com.**

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Multinationals: comparison between different sectors, financial statements and stock market performance in 2022

Total sales posted by the world's largest industrial multinationals were **up 13.3% on 2021,** with all sectors reporting increases. Leading the way in this respect were the oil and gas multinationals, whose turnover increased by 53.6%, followed at a distance by the automotive groups (revenues up 19.2%), iron and steel companies (up 17.3%) and fashion industry operators (up 14.9%). Below-average but still double-digit growth was posted by the digital payments, food, and beverages industries, which posted increases of 12.6%, 11.9%, and 11.4% respectively, while the increase in sales reported by multinationals in the following sectors was slower: aircraft manufacturers (up 9.6%), pharmaceuticals (up 8.9%), large-scale distribution (up 8.1%), WebSoft (up 7.8%), electronics (up 6.8%), media and entertainment (up 6.3%), telecommunications (up 4.5%), and defence (up 4.0%). All sectors have now exceeded their pre-Covid figures, with the single exception of aircraft manufacturers.

The **EBIT margin (EBIT as a percentage of total sales)** posted by the multinationals was down slightly, at **16.4% (down 0.2 p.p. on 2021).** The digital payments sector was again the most profitable, recording the highest Ebit margin (30.5%; up 1.0 p.p.), followed by the oil and gas companies (27.4%; up 3.8 p.p.), which have now overtaken the pharmaceutical manufacturers (26.7%; up 1.9 p.p.) in second place. The electronics firms also recorded above-average profitability levels (21.2%; down 1.3 p.p.), as did the beverage industry operators (18.7%; down 0.6 p.p.). The aircraft manufacturers brought up the rear with an aggregate EBIT margin of 1.6% (up 0.1 p.p.).

In 2022 **investments showed an increase of 17.5% versus 2021**, with all sectors reporting increases, and above-average increases reported by the fashion operators (up 44.8%), oil and gas companies (up 27.8%), aircraft manufacturers (up 26.8%), and large-scale distribution firms (up 25.5%). **Investments accounted for 6.1% of total revenues,** with above-average figures reported by the telecommunications (14.4%), electronics (12.6%), and WebSoft (9.6%).

The multinationals' **financial structure** shows an improvement on average, due to the increase in equity (up 0.2%) being slightly higher than the increase in borrowings (up 0.1%), for a net equity/debt ratio of 1.4x at end-June 2022. The oil and gas industry was the most solid (net equity 2.8x debt), followed by iron and steel and electronics with 2.3x and WebSoft with 2.0x. Cash and liquid assets were down 2.7% on 2021, and at end-June 2022 represented 30.2% of total borrowings. The electronics industry giants were the most liquid, followed by the oil and gas and WebSoft multinationals.

At **year-end 2022** the **market capitalization** of the panel of industrial multinationals covered by the survey totalled €22,300bn, down 9.8% on 2021. However, the companies operating in the following sectors bucked this trend: defence (market cap up 27.1%), oil and gas (up 20.8%), pharmaceuticals (up 8.2%), beverages (up 2.6%), and aircraft manufacturers (up 0.8%). On average the multinationals have a market capitalization that is 3.4x higher than their net equity, with the digital payments multinationals and the pharmaceutical companies reflecting the highest ratios (6.0x and 5.5x respectively), whereas the telecommunications and iron and steel operators were the ones with the lowest stock market valuations. At **end-March 2023** the companies' aggregate market capitalization was €24,400bn.

Global defence spending[1]

Global defence spending in 2021 exceeded $2,000bn for the first time in 2021 (up 0.7% on 2020 and up 12% on 2012, in real terms), recording an **all-time high of $2,113bn (equivalent to 2.2% of global GDP),** or $5.8bn per day. Of this total, **37.9% was attributable to the United States** ($801bn), followed by China with 13.9% ($293bn), India (3.6%), the United Kingdom (3.2%), and Russia (3.1%); Italy ranked eleventh with 1.5% of the world's total ($32bn, equal to $88m per day).

The rankings change if we look at **defence spending as a percentage of PIL**: in this case it is the Middle Eastern and North African companies that rank first, with Russia in eleventh position (4.1%), the United States in fifteenth (3.5%), Ukraine in nineteenth (3.2%), China in 63rd (1.7%), and Italy in 76th (1.5%, having been 1.4% in 2012 and 2.1% in 1988). As required by NATO in 2014, **Italy** has gradually been increasing its defence spending with the objective of reaching 2% of its GDP by 2028.

The citizens which spend the most on defending their own country are those of Qatar, Israel, the United States and Kuwait, with more than $2,000 spent per capita in 2021; the $530 per capita spent by Italian citizens (equal to $1.5 per day) is roughly double the global average ($268) and 17% more than in Russia. The share of public spending earmarked for defence is highest in Belarus, Qatar, Oman and Saudi Arabia, with more than 20%, whereas Italy is towards the bottom of the rankings in this respect, with 2.6%, below the global average of 6.2%, which is exceeded by Russia (10.8%), the United States (8.3%), and Ukraine (7.8%).

Security as priority and focus on defence industry multinationals: financial statements and stock market performances

With the invasion of Ukraine and the war taking place on the borders of Europe, the global scenario has changed, with an increasing need to ensure **security**. The effects of this change in perception are reflected in the financial statements of the defence companies included for consideration in this survey and in their stock market performances: in 2022 capital spending on defence increased at more than three times the rate that revenues did, and these companies' stocks delivered the best performances.

In **2022** the aggregate **turnover** of the thirty global groups specializing primarily in defence totalled **€432bn**, €316bn of which is estimated to have been generated from this sector alone (up **4.0% on 2021** and **up 10.5% on 2019**). The panorama is **dominated by US players with 74%** of the total, followed by the European groups with 22%, and the Asian-based multinationals with 4%. A further **year-on-year increase of 6% in revenues is expected in 2023 versus 2022,** due to the increase in national budgets for defence spending in response to the increasing geopolitical tensions. The **United States, with their fifteen giants, also rank first in numerical terms,** ahead of France, some way behind with three companies; with two groups for each of Germany, the United Kingdom, Indian and **Italy**, which, with **Fincantieri and Leonardo, generated 21% of the European defence sector revenues and 4.7% of the global turnover**.[2]
The top five places by **revenues estimated to be generated from the defence sector** are all occupied by US groups: **Lockheed Martin** (€57.5bn), **Raytheon Technologies** (€37.1bn), **Boeing** (€35.6bn), **Northrop**

1 Stockholm International Peace Research Institute (SIPRI) data processed by Mediobanca Research Area.
2 Defence sector revenues accounted for 83% and 32% respectively of Leonardo's and Fincantieri's turnover in 2022.

Grumman (€29.5bn) and **General Dynamics** (€25.9bn). **Leonardo** ranked in eighth position (with €12.2bn) and **Fincantieri** came twenty-third (with €2.4bn).
The **highest increase in revenues** was reported by Turkish-based company **Aselsan** (up 75.0% on 2021), followed by the two German companies **Hensoldt** (up 15.8%) and **Rheinmetall** (up 13.3%) and the two US groups **HII-Huntington Ingalls Industries** (up 12.1%) and **Booz Allen Hamilton** (up 11.8%), all of which reported double-digit growth. Both the **Italian companies reported above-average performances**: **Fincantieri** posted an **8.1%** increase in revenues and **Leonardo 4.1%**.
Profitability appears to be declining: the average Ebit margin decreased from 8.0% in 2019 to 7.3% in 2022. The best margins were reported by three state-owned companies: Turkish group **Aselsan** (25.2%), and the two Indian companies **Hindustan Aeronautics** (24.7%) and **Bharat Electronics** (20.6%).

There was double-digit growth in **investments**, which overall totalled near to €12bn (up 13.2% on 2021) and increased to 2.7% of total revenues (from 2.5% in 2021). Top place for intensity of investment was taken by US company **BWX Technologies** (8.9%), ahead of Turkish group **Aselsan** (6.7%) and the two German companies **Hensoldt** (5.6%) and **Rheinmetall** (5.4%). The **Italian groups are well positioned in this respect, confirming their industrial strength**: **Fincantieri** was in sixth place (4.0%) and **Leonardo** in twelfth place (3.3%).

Distribution of **dividends** was 5.2% higher than in 2021, with 81% of the total accounted for by the US groups' shareholders. The thirty defence industry multinationals also employed over **1.3 million people in 2022** (up 0.4% on 2019), 69% of whom were employed by the US groups.

On the **asset side**, the defence industry companies reported a net equity amount that was equivalent to borrowings as at end-2022, with the two Indian companies (**Bharat Electronics** and **Hindustan Aeronautics**), both of which are state-owned, being the most capitalized, ahead of French group **Dassault Aviation** (whose net equity was 25.7x its debt). Compared to 2019, net equity increased by more than minority interests (up 40.6% and 21.5% respectively). Liquid assets also rose by 34.3% (to pre-Covid levels), and were equal to 28.7% of borrowings as at year-end 2022.

The defence industry multinationals' **market capitalization** totalled €736bn at year-end 2022, representing 0.8% of the global stock markets' overall value (0.5% at year-end 2021). On average market capitalization was 4x higher than net equity, with the Italian firms being among those undervalued by the stock market: **Fincantieri**'s market capitalization is around 1.5x the company's net equity, and **Leonardo**'s 0.6x. At **end-March 2023** the aggregate market capitalization totalled €721bn, 80% of which was attributable to the US groups, and three US companies in the top three places: **Raytheon Technologies** (€131.9bn), **Boeing** (€117.2bn) and **Lockheed Martin** (€110.7bn). All the other companies reported market capitalizations of below €65bn.
In 2022 the **return on defence industry players' shares** (including dividends) was equal to **34.6%**, comfortably outperforming the global stock market index which reported a negative performance of 11.0%. In **1Q 2023** the aggregate value put on **0.2%**, with the best performances being recorded by Swedish group **Saab** (up 51.7%) and the two German companies **Hensoldt** (up 50.2%) and **Rheinmetall** (up 46.3%); **Leonardo** delivered the fourth best performance (up 34.2%), while **Fincantieri** came in eighth (up 11.6%).

Both the stock market and investors therefore seem to appreciate the **renewed value being placed on security**. This appears to be true despite the fact that the specialization of the defence companies impacts negatively on them in ESG terms. However, despite the changed geopolitical scenario, the acknowledgement of the importance of deterrence as an instrument for keeping the peace, and the need to protect democratic values, have all opened the debate on reconsidering the compatibility of sustainability with investment in the share capital of defence sector operators.

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