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Are Robust Financials Driving The Recent Rally In Promotica S.p.A.'s (BIT:PMT) Stock?

Promotica (BIT:PMT) has had a great run on the share market with its stock up by a significant 16% over the last month. Given the company's impressive performance, we decided to study its financial indicators more closely as a company's financial health over the long-term usually dictates market outcomes. Specifically, we decided to study Promotica's ROE in this article.

Return on equity or ROE is a key measure used to assess how efficiently a company's management is utilizing the company's capital. In short, ROE shows the profit each dollar generates with respect to its shareholder investments.

See our latest analysis for Promotica

How Do You Calculate Return On Equity?

Return on equity can be calculated by using the formula:

Return on Equity = Net Profit (from continuing operations) ÷ Shareholders' Equity

So, based on the above formula, the ROE for Promotica is:

38% = €4.6m ÷ €12m (Based on the trailing twelve months to December 2020).

The 'return' is the yearly profit. Another way to think of that is that for every €1 worth of equity, the company was able to earn €0.38 in profit.

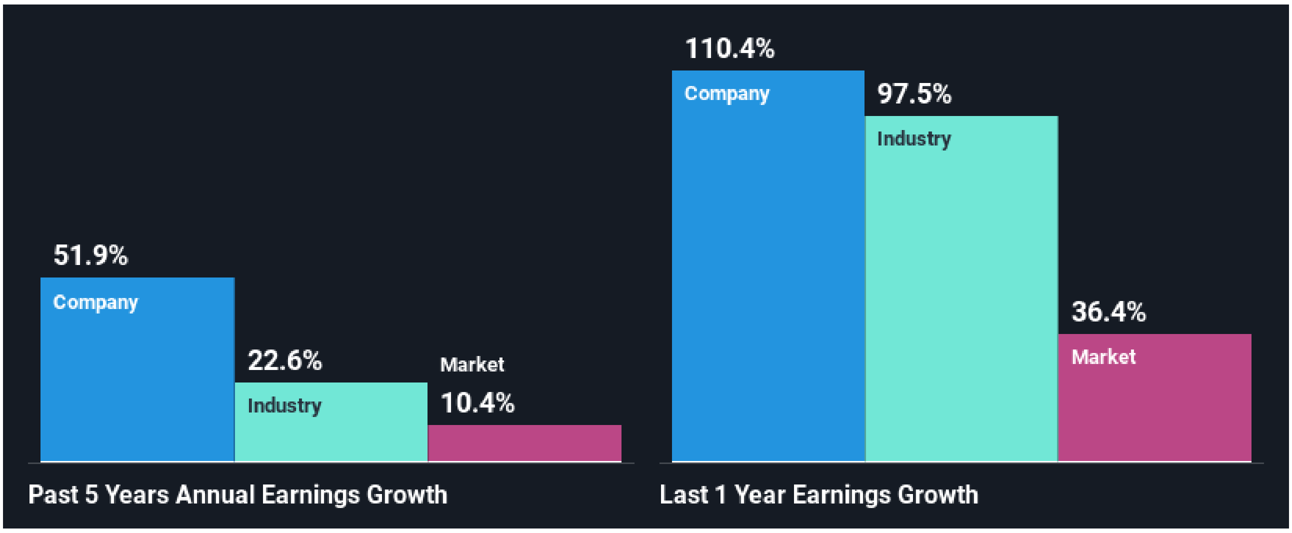
What Is The Relationship Between ROE And Earnings Growth?

So far, we've learned that ROE is a measure of a company's profitability. Depending on how much of these profits the company reinvests or "retains", and how effectively it does so, we are then able to assess a company's earnings growth potential. Generally speaking, other things being equal, firms with a high return on equity and profit retention, have a higher growth rate than firms that don't share these attributes.

Promotica's Earnings Growth And 38% ROE

Firstly, we acknowledge that Promotica has a significantly high ROE. Additionally, the company's ROE is higher compared to the industry average of 17% which is quite remarkable. Under the circumstances, Promotica's considerable five year net income growth of 52% was to be expected.

We then compared Promotica's net income growth with the industry and we're pleased to see that the company's growth figure is higher when compared with the industry which has a growth rate of 17% in the same period.



Earnings growth is an important metric to consider when valuing a stock. What investors need to determine next is if the expected earnings growth, or the lack of it, is already built into the share price. Doing so will help them establish if the stock's future looks promising or ominous. One good indicator of expected earnings growth is the P/E ratio which determines the price the market is willing to pay for a stock based on its earnings prospects. So, you may want to check if Promotica is trading on a high P/E or a low P/E, relative to its industry.

Is Promotica Making Efficient Use Of Its Profits?

Promotica's three-year median payout ratio to shareholders is 21%, which is quite low. This implies that the company is retaining 79% of its profits. So it seems like the management is reinvesting profits heavily to grow its business and this reflects in its earnings growth number.

Conclusion

Overall, we are quite pleased with Promotica's performance. Particularly, we like that the company is reinvesting heavily into its business, and at a high rate of return. Unsurprisingly, this has led to an impressive earnings growth. If the company continues to grow its earnings the way it has, that could have a positive impact on its share price given how earnings per share influence long-term share prices. Not to forget, share price outcomes are also dependent on the potential risks a company may face. So it is important for investors to be aware of the risks involved in the business. To know the 4 risks we have identified for Promotica visit our risks dashboard for free.