Public Funding of Investment Projects: Objectives

Germany offers a number of project financing incentives to all investors – regardless of country of provenance. Funds are provided by the German government, the individual federal states, and the European Union (EU). Incentives in Germany have a sustainable effect as they support companies in different project stages: from setting up new production or service facilities to R&D activities.

Supporting New Investments

Many incentives target new investments with a specific focus on promoting economic growth. Funding to the tune of approximately EUR 21 billion has been freed up by the EU (co-financed using means obtained from German federal and federal state budgets) for the period 2021 to 2027. In addition, Germany and its individual states also make their own incentives funds available.

When it comes to investor production or service facility set-up costs, investors can count on a number of different public incentives programs. Cash incentives provided in the form of non-repayable grants form an important instrument used.

Promoting Innovation

A major focus of financial support available in Germany is put on assisting research and development (R&D) activities as they are considered to be among the most important areas for the development of the German economy. Industry and the public sector have made a commitment to spend around 3.5 percent of national GDP per year on R&D activities until 2025. This amounted to EUR 106 billion R&D spending in 2020. The campaign “High-Tech Strategy 2025” - as successor initiative of the “High-Tech Startegy” - has been launched by the German government to foster the advancement of new technologies.

Incentives Instruments

Incentives in Germany are available through different public funding instruments, different institutions and for different funding purposes. The individual funding requirements may, for example, result from investment projects, research and development activities, personnel recruitment, working capital needs or other specific purposes. The different incentives instruments including grants, loans and guarantees are generally available for all funding purposes and can normally be combined; thereby matching different business activity needs at different development stages of the company.

At a Glance

- Amount of EU-funding (EU Cohesion and Structural Policy) available 2021-2027: EUR 21 billion
- Annual R&D spending (industry and public sector): EUR 105 billion in 2020
- Efficient incentives support according to company’s project needs

Incentives in Germany

Funding purposes				
Investments	Working Capital	Research & Development	Specific Purposes	Personnel

Financing supported by the following public funding instruments (combinations of instruments usually possible)

Public funding instruments				
Grants	Loans	Guarantees	Equity Capital	Mezzanine Capital

Meeting the Capital Needs of Investment Projects

Germany has organized its economic promotion policy according to the needs of enterprises. Incentives support is guided by the financial needs of a company’s individual project, thereby making the business activity assistance very efficient. During the investment phase (when capital needs are high), cash incentives programs reimburse direct investment costs by providing non-repayable cash grants. Public loan programs and guarantees round off investment project financing. Once operations have started, labor-related incentives programs support companies during all stages of putting together a workforce. Particular emphasis is placed on R&D projects which receive financial assistance from a number of different programs.

Public Funding of Investment Projects: Instruments

Public funding in Germany is multifaceted and is essentially structured into four pillars: direct grants, public loans, public guarantees, and equity capital. The various instruments are used in a wide range of incentive programs.

Grants for Investments, R&D, and Hiring Personnel
Direct grants are of central significance within the Gemeinschaftsaufgabe *"Verbesserung der regionalen Wirtschaftsstruktur"* (GRW - Joint Task for the Improvement of Regional Economic Structures) incentive program, which is used in designated support areas. GRW grants are mainly designed to reduce the investment costs for building new business premises. Other grant programs are used to stimulate activities related to research and development or the deployment of new technologies and are offered by a wide range of specialist institutions. Grant programs for employment are also noteworthy.

Project Financing by Public Loans
Public promotional loans are another attractive and important funding instrument. Such loans are available for investments, working capital, R&D projects, recruitment or other specific purposes relating to the investment project in Germany. These funds are awarded by the publicly owned KfW Group at the national level, and by the business development banks at federal state level. Complementary public guarantees are used to simplify investor access to financing by strengthening their collateral (leverage).

Project Financing by Private Equity
Innovative start-ups in particular have to rely largely on financing through equity such as venture capital (VC). In Germany, appropriate VC partners can be found through the *Bundesverband Deutscher Kapitalbeteiligungsgesellschaften e.V.* (BVK - German Private Equity and Venture Capital Association). Special conferences and events like the *Deutsches Eigenkapitalforum* (German Equity Forum) provide another opportunity for young enterprises to come into direct contact with potential VC partners. Public institutions such as the VC-entities of the different business business development banks and public VC companies may also offer partnership programs at this development stage.

At a Glance

- International companies profit from incentives support with same conditions as German companies
- Combination of different incentives instruments normally possible
- SMEs often profit from preferential program terms

Criteria Determining Company Size

Company category	Staff head count	Annual turnover	Annual balance sheet total
Small enterprise	< 50	≤ EUR 10 million	≤ EUR 10 million
Medium-sized enterprise	< 250	≤ EUR 50 million	≤ EUR 43 million
Large enterprise	≥ 250	> EUR 50 million	> EUR 43 million

The criterion concerning the head count is compulsory. In addition, either of the annual turnover or the balance sheet criteria must also apply.
Source: European Commission

How to Determine Investment Project Incentives Levels
Each incentives program defines industries as well as forms of investments (e.g. greenfield or expansion projects) eligible for funding. International investors enjoy exactly the same conditions available to German investors. Each program has a set of criteria (such as company size, planned investment project and investment location) which determine individual investment project incentives levels. Company size is determined according to a European Union-wide classification system in which enterprises are categorized as being small, medium-sized or large according to their employee numbers, and annual turnover or annual balance sheet total. Most incentives programs offer the highest incentives rates to small and medium-sized enterprises (SMEs). Some programs may even specifically target SMEs. Other criteria determining project eligibility may be defined subject to individual incentives programs and federal state regulations.

Incentives Calculation Example

Germany Trade & Invest provides a range of inward investment services to international investors including project-specific financing and incentives consultation. We focus on a comprehensive incentives assessment based on the investor's project plan; followed by a calculation of available incentives support that simplifies incentives negotiations with local authorities.

Here we provide an example of how investment project financing can be complemented with financial support from Germany's different incentives instruments. The possibility to combine different instruments makes it easier for investors to structure project funding. Our example shows the opportunities that a combination of key public funding instruments offers.

Investment Case Scenario

An enterprise has decided to set up a production facility near the Polish border. Besides management, five new jobs will be created in order to run the facility. The company has more than 50 but less than 250 employees. With an annual turnover of EUR 30 million and a balance sheet total of EUR 35 million, the company meets the EU Commission's criteria for classification as a medium-sized enterprise. An investment of EUR 2 million in machinery and equipment is necessary for a successful realization of the project. The company has EUR 500,000 equity for the investment in place. The financial shortfall amounts to EUR 1.5 million.

Incentives Instrument I: Investment Grants

The calculation basis for determining the possible amount of investment grants receivable through the GRW program might be the actual investment costs (e.g. for buildings or machinery) or (assumed) wage costs for two subsequent years. The costs for the new facility's equipment and machinery are eligible for investment grants (the specific eligible costs for equipment are defined in the GRW regulations at the national and regional level). In this scenario, the calculation of the maximum possible grants amount is based on the number of new jobs to be created. The maximum eligible investment costs per new job are EUR 750,000 (as defined by GRW regulations), meaning that up to EUR 3.75 million investment costs would be eligible when creating five new jobs. The company's planned EUR 2 million investment lies within the scope of the maximum amount of eligible investment costs. Based on the incentive level in the Polish border region (35 percent for a medium-sized enterprise), the company can calculate with GRW investment grant funding of EUR 700,000.

Incentives Instrument II: Public Loans

The outstanding funding amount of EUR 800,000 (Investment: EUR 2 million – Equity: EUR 500,000 – Grants: EUR 700,000) for the planned investment could be covered by a public promotional loan. The "ERP – Promotional Loan SME" is one of the prominent loan programs provided by the KfW, the national business development bank of Germany. It offers long-term fixed attractive interest rates and loan maturities as well as no principal payments during the start-up years. A very interesting feature of the "ERP – Promotional Loan SME" is the available liability waiver of 50 percent of the pending loan amount. The liability waiver reduces the default risk for the intermediary commercial bank and creates an incentive to finance the project. Another option in such cases is to secure the loan using a public guarantee. The investor can apply for a public guarantee to reduce the risk from the project financing up to 80 percent of the remaining credit balance.

Final Investment Project Financing Structure

ME settling in C region bordering Poland

Investment Case Scenario	
Investment costs	EUR 2,000,000
Jobs to be created	5 (permanent)
Equity capital	EUR 500,000
Financing gap	**-EUR 1,500,000**
Incentives Instrument I: Investment Grants	
Max. eligible investment costs	EUR 750,000 per workplace
Max. eligible investment costs for actual project	EUR 2,000,000 (total investment sum)
Basic incentive level	35% of eligible investment costs
Amount of cash incentives	EUR 700,000
Remaining financing gap	**-EUR 800,000**
Incentives Instrument II: Public Loans	
Public promotional loan ("ERP - Promotional Loan SME")	**EUR 800,000**