

A Study on Financial Health of Select Indian Pharmaceutical Companies

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ABSTRACT

This paper focuses on “A Study on Financial Health of Select Indian Pharmaceutical Companies. The Pharmaceutical industry in India” is the world's third-largest in terms of volume. According to Department of Pharmaceuticals of the Indian Ministry of Chemicals and Fertilizers, the total turnover of India's pharmaceuticals industry between 2008 and September 2009 was US\$21.04 billion. While the domestic market was worth US\$12.26 billion. The industry holds a market share of \$14 billion in the United States. According to India Brand Equity Foundation, the Indian pharmaceutical market is likely to grow at a compound annual growth rate (CAGR) of 14-17 per cent in between 2012-16. India is now among the top five pharmaceutical emerging markets of the world.

Key words: Research and Development, Intellectual Property, Quality Assurance, Common wealth of Independent States

INTRODUCTION

Industries play an important role in the economic development of any nation. Industries make the country self reliant by fulfilling the various needs of the people. In india, industrial economy is dominated by various industries like, automobile, iron and steel, real estate, cement, tourism, energy, textile, airlines, pharmaceutical, biotechnology, electronics, hardware and power industry. Of them, pharmaceutical industry is one of the fasted growing and life saving sector. The pharmaceutical industry plays a key role in promoting and

sustaining development in the field of medicines. Indian pharmaceutical industry boasts of quality producers and approved regulatory units. This industry have a success story of providing employment opportunities for millions and ensuring that essential drugs at affordable prices are available to the vast population of this sub-continent. International companies associated with this sector have stimulated, assisted and spearheaded this dynamic development in the past 55 years and helped to put India on pharmaceutical map of the world.

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The Indian pharmaceutical sector is highly fragmented with more than 20,000 registered units. It is said to be the fourth largest in the world in terms of volume. It has expanded drastically in the last two decades. The leading 250 pharmaceutical companies control 70% of the market share. It is extremely fragmented market with severe price competition and government price control. The Indian **Pharmaceutical industry in India** is the world's third-largest in terms of volume. According to Department of Pharmaceuticals of the Indian Ministry of Chemicals and Fertilizers, the total turnover of India's pharmaceuticals industry between 2008 and September 2009 was US\$21.04 billion. While the domestic market was worth US\$12.26 billion. The industry holds a market share of \$14 billion in the United States. According to India Brand Equity Foundation, the Indian pharmaceutical market is likely to grow at a compound annual growth rate (CAGR) of 14-17 per cent in between 2012-16. India is now among the top five pharmaceutical emerging markets of the world.

With the expected growth rate of 14% per annum, Indian Pharmaceutical sector is expected to create more jobs in India in 2014 and add 45,000 fresh openings to its current strength. Not marred by recession or inflation, the pharma sector has a

pharmaceutical industry will see tremendous growth in the coming years as consumer spending on health care is increasing on the rise in India. Grasping the situation, many Multinational and Foreign Pharma companies steps their foot in India, thereby putting the domestic pharma companies under the pressure of survival.

competitive advantage of prospering steadily and thus attracts lots of young professionals looking at pharmaceutical as their prospective career option. This sector has also been responsible in creating a rich talent pool of researchers, scientists, doctors and project managers.

The need of skilled manpower in the pharmaceutical industry ranges widely from Research and Development (R&D), Quality Assurance (QA), Intellectual Property (IP), manufacturing to even sales and marketing. What the pharma industry needs is to have better policies to retain and nurture the existing talent and equip them with necessary skills.

The Challenges of Indian Pharmaceutical industries are

- Greater customer expectations
- Restricted discovery and developing process
- Effective product life-cycle management
- Increase in pricing policies

- Traditional management culture
- Infrastructure challenge
- Talent retention

Exports of pharmaceuticals products from India increased from US\$6.23 billion in 2006–07 to US\$8.7 billion in 2008–09 a combined annual growth rate of 21.25%. According to PricewaterhouseCoopers (PWC) in 2010, India joined among the league of top 10 global pharmaceuticals markets in terms of sales by 2020 with value reaching US\$50 billion.

OBJECTIVES OF THE STUDY

- ▶ To study liquidity position of 'select' Indian Pharmaceutical companies.
- ▶ To analyse the long-term solvency position of these pharmaceutical companies.

STATEMENT OF THE PROBLEM

The Indian pharmaceutical industry is facing hard times of these days with many financial problems. The Indian pharmaceutical industry today is in the front rank of India's science – based industries with wide ranging capabilities in the complex field of drug manufacture and technology. It ranks very high in the third world countries in terms of technology, quality and the vast range of medicines manufactured. From simple headache pills to sophisticated Antibiotics and complex

cardiac compounds, almost every type of medicine is now made in India.

Indian Pharmaceutical companies like Aurbindo Pharma, Cipla, Cadila Health Care, Dr.Reddy's Labs, Piramal Health Care, Ranbaxy Labs, Torrent Pharma tops the 10 list. The domestic pharma companies face many challenges from reputed multi-national pharma companies. They also state that there would be challenges such as hike in the input cost which might put some pressures on the profit margins that may in turn affects their efficient performance in the long run. Hence this researcher feels it important to study the financial strength especially short term and long term solvency strength of domestic pharma companies – which decides the ability of firm for staying in business.

METHODOLOGY OF THE STUDY

Sample units:

The present study was purely based on secondary data. Required data were collected from the prowest Database. The researcher states that among 31 Indian Pharmacy companies under the head "Indian bulk drugs and formulations" listed in BSE, top-listed 5 companies has been selected as sample size whose annual turnover are of equal strength. The five Indian pharmacy companies selected as

sample units are: Aurobindo pharma, Cadila Health Care, Cipla, Dr.Reddy's Labs & Ranbaxy Labs.

PERIOD OF STUDY

The study analyse the liquidity and long term solvency of 'select' Indian Pharma companies for a period of 8 years from 2004-05 to 2011-12.

TOOLS OF ANALYSIS

Financial tools namely ratio analysis, Z-score and Statistical tools namely Mean, Standard deviation, coefficient of variation and CAGR have been used for analysis.

REVIEW OF LITERATURE

The editor of Corporate India (2012) states that Mumbai – based market operators shared that Cipla might surprise one and all. This Indian pharma company has performed well and has earned net of Rs.1123.96 Crore on a total turnover of Rs.6977.50 Crore for the year ended march 2012 against a net profit of Rs.960.39 crore on a turnover of Rs.6331.09 crore for the previous year. The company still awaits the court verdict in the appeal against Rs.1654.92 crore tax notices, which is pending. The equity capital of Rs.160.58 crore is supported by free reserves of Rs.7565 crore plus, making it a bonus candidate as well. In the event of the court decision coming in its

favour, a liberal bonus is not ruled out. It is worth accumulating for medium to long term rewards on every decline.

Pankaj patel(2012) observed that Cadila health care has been growing from strength to strength on the financial front. During the last five years, its sales turnover has spurred around two and a half times – from Rs.265 crore in the fiscal 2007 – 08 to Rs. 686 crore in the fiscal 2012. The company's financial position is very strong. At the end of March 31, 2012 its reserved stood at Rs.2582 crore as against its equity capital of Rs.102 crore, and that too after a 1:2 bonus issue made in 2010. The March 2012 quarter performance of the company is quite indicative of the healthy days ahead.

Nagarajan and Burthwal(1983) in their research work have examined the relationship between profitability and capital structure, using a sample of thirty eight Pharmaceutical firms in India for the period 1970 – 1982. Two measures of profitability i.e. ratio of net profit to the total sales revenue and the ratio of net profits to total assets were used to find out the determinants of profitability. The analysis demonstrated that under the condition of price control, the most significant determinant of the profitability of the firms was vertical integration. They also found that size and advertising intensity were not the major determinants

in deciding the capital structure. The coefficient of growth rate of sales was positive and significant, suggesting that factors on the demand side of a firm had a greater impact on profitability than on supply side.

RESEARCH GAP

Even though few studies have been carried over to analyse the financial performance This ratio indicates the safety of different interested parties of Pharma companies like creditors, banks, investors, auditors etc.

ANALYSIS OF FINANCIAL HEALTH OF INDIAN PHARMA COMPANIES

of Indian Pharmaceutical companies, no study attempts to make a depth analysis of their liquidity and solvency position in particular. Solvency – Short-term, usually called as ‘Liquidity’ and long-term solvency - states the ability of the firm to meet its current and future obligations respectively.

Overall solvency position of the firm are classified into two as: Short-term solvency ratios and long-term solvency ratios. The liquidity and long term solvency position of Indian Pharama companies has been analysed through key ratios.

Table 1 CURRENT RATIO

Years	Cipla Ltd	Dr.Reddy's Lab Ltd	Cadila Health Care	Ranbaxy Lab Ltd	Aurobindo Pharma
2004 - 2005	1.44	2.93	1.03	1.19	1.2
2005 - 2006	1.42	0.81	1.15	0.97	1.39
2006 - 2007	2.12	2.83	1.08	0.96	1.8
2007 - 2008	1.5	1.33	1.42	0.78	1.71
2008 - 2009	1.16	1.47	1.13	0.84	1.3
2009 - 2010	1.46	0.98	1.21	0.85	1.34
2010 - 2011	1.81	1.16	1.17	0.9	1.68
2011 - 2012	2.19	1.25	0.93	0.61	1.45
Mean	1.64	1.59	1.14	0.89	1.48
S.D	0.34	0.76	0.13	0.16	0.20
C.V	20.82	48.02	11.78	17.69	13.78
CAGR	5.38	-10.10	-1.27	-8.01	2.39

Table 1 reveals that among the selected Indian pharmaceutical companies Dr.Reddy's lab current ratio for the years 2004-2005 and 2006-2007, Cipla ltd's current ratio for 2006-2007 and 2011-2012 seems to be good, since they are maintained above the standard norm of

2:1. Cipla ltd has highest mean of current ratio followed by Dr.Reddy's lab and Aurobinbo pharma. Except Aurobindo pharma and Cipla ltd all other Indian pharma companies shows negative CAGR. However, Cipla ltd's Mean current ratio is high among all the companies.

Table 2 QUICK RATIO

Years	Cipla Ltd	Dr.Reddy's Lab Ltd	Cadila health Care	Ranbaxy Lab Ltd	Aurobindo Pharma
2004 - 2005	0.65	2.44	0.43	0.62	0.7
2005 - 2006	0.71	0.52	0.56	0.55	0.91
2006 - 2007	1.19	2.37	0.48	0.55	1.22
2007 - 2008	0.88	0.91	0.7	0.44	1.07
2008 - 2009	0.68	1.05	0.61	0.62	0.82
2009 - 2010	0.79	0.6	0.65	0.59	0.76
2010 - 2011	0.87	0.76	0.66	0.69	0.96
2011 - 2012	1.05	0.86	0.56	0.49	0.81
Mean	0.85	1.07	0.58	0.57	0.91
S.D	0.18	0.81	0.09	0.07	0.16
C.V	20.63	1133.80	14.97	13.01	17.88
CAGR	6.18	-12.22	3.36	-2.90	1.84

Table 2 indicates that among the Indian pharma companies quick ratio, Aurobindo pharma's for the years 2006-2007 and 2007-2008, Cipla ltd's for 2006-2007 and 2011-2012 and Dr.Reddy's Lab's ratio

2008-2009 appears to be so good. Dr.Reddy's Labs has the highest mean of quick ratio followed by Aurobindo Pharma and Cipla ltd. Dr.Reddy's Labs and Ranbaxy Lab shows negative CAGR.

Table 3 DEBT – EQUITY RATIO

Years	Cipla Ltd	Dr.Reddy's Lab Ltd	Cadila Health Care	Ranbaxy Lab Ltd	Aurobindo Pharma
2004 - 2005	0.12	0.14	0.61	0.05	1.01
2005 - 2006	0.24	0.41	0.59	0.43	1.33
2006 - 2007	0.04	0.08	0.51	1.35	2.13
2007 - 2008	0.14	0.1	0.70	0.38	1.44
2008 - 2009	0.22	0.12	0.66	1	1.6
2009 - 2010	0.01	0.1	0.37	0.81	1.02
2010 - 2011	0.07	0.24	0.27	0.84	0.9
2011 - 2012	0.01	0.23	0.5	2.27	1.12
Mean	0.11	0.18	0.53	1.02	1.32
S.D	0.08	0.10	0.14	0.63	0.38
C.V	76.02	58.76	26.03	61.90	28.77
CAGR	-26.70	6.40	-2.45	61.11	1.30

Table 3 depicts the debt-equity position of Indian Pharma Companies. Except Aurobindo Pharma, no other Indian Pharma company maintains the ideal ratio of 1 whereas Ranbaxy Lab Ltd maintains

only for 3 years among the study period. Among the 5 companies, two sample units shows negative CAGR. Cadila, Cipla, Dr.Reddy debt-equity ratio is very poor during the entire study period of 10 years.

Table 4 ALTMAN'S Z - SCORE MODEL

Years	Cipla Ltd	Dr.Reddy's Lab Ltd	Cadila Health Care	Ranbaxy Lab Ltd	Aurobindo Pharma
2004 - 2005	2.875	2.361	2.246	2.582	1.781
2005 - 2006	2.944	2.205	2.375	1.886	1.812
2006 - 2007	2.988	3.233	2.225	1.540	1.909
2007 - 2008	2.606	2.298	2.258	1.386	2.079
2008 - 2009	2.460	2.262	2.259	0.956	2.109
2009 - 2010	2.614	1.706	2.429	1.38	2.344
2010 - 2011	2.669	1.648	3.44	1.726	2.368
2011 - 2012	2.787	2.267	2.14	1.161	1.872

Table 4 depicts the long term solvency position of Indian Pharma companies using Altman's Z score. Z score of below 1.86 the company is considered to be in the bankruptcy zone, its failure is certain and extremely likely and would occur probably within a two years. If a company has a Z score between 1.86 and 2.675 its financial viability is considered to be healthy. Above Z score of 2.675 the company is in a too healthy zone. Its financial health is very viable.

The analysis of Aurobindo Pharma's Solvency position states that except the first year of study period, the company is in healthy zone. Cadila Healthcare is also in healthy zone for 9 years while in 2010-

11, the company is in too healthy zone. Cipla Ltd's analysis reveals the company is always in too healthy zone thereby maintaining Z-score of above 2.675. Only during two years 2009-11, Dr.Reddy's Lab Ltd's is in dangerous zone. Ranbaxy's financial viability is really in dangerous state during the entire study period except the initial year of study.

FINDING OF THE STUDY

The major findings of the study are summarized below. The analysis shows that no company maintains the ideal current ratio of 2:1 throughout the study period.

1. Cipla Ltd's current ratio seems to be better compared with other companies where as Ranbaxy's ability to meet its current obligations seems to be very unsatisfactory.
2. Ranbaxy again too weak in maintaining its ideal quick ratio. And so, Cadila Healthcare. Aurobindo and Cipla maintains satisfactory ratio only for two years among the entire study period. However, the mean of Dr.Reddy's Lab Ltd seems to be good.
3. The mean debt-equity ratio of Aurobindo Pharma and Ranbaxy Ltd is found to be good during the study periods. Among the 6 study units, Aurobindo Pharma alone maintains the ideal debt-equity ratio of 1 during the 9 years of study period whereas Ranbaxy Ltd maintains for 3 years. The other companies' debt-equity ratios are really unsatisfactory.
4. Z-score analysis of Indian pharma companies shows that Cipla Ltd's health is too good and healthy during the entire study period. If Ranbaxy fails to recoup, it's about to reach the bankruptcy state. The financial viability of other Pharma companies seems to be healthy but not too healthy.

SUGGESTIONS AND CONCLUSION

On the basis of above analysis, The

following are the suggestions made to the sample units

1. All the pharma companies are suggested to maintain atleast close to ideal current and quick ratios. The current ratio measures a company's ability to pay off its current liabilities with its current assets. The quick ratio measures the firm's ability to meet its short-term obligations with its most liquid assets. If the company fails continuously, the reputation and goodwill may get affected.
2. Likewise the long term solvency position of Aurobindo Pharma alone seems to be ideal. A rising debt-equity ratio implies the higher interest expenses and beyond a certain point it may affect a company's credit rating, making it more expensive to raise more debts. A less ideal ratio imposes a question of survival of company.
3. The main purpose of calculating Z score is to warn the company concerned of its financial problems that may need serious attention and to provide a guide for action to avert the trouble head. Leaving the rest of company that are atleast in healthy zone, The policy-makers of Ranbaxy Lab Ltd should not let the company move to bankruptcy zone. This report provides an insight into the financial structure currently prevalent in the industry. he report builds a profiling of the

major contributions in the industry and analyses their relative short-term and long-term solvency position. Liquidity and solvency are the terms that refer to a company's state of financial health. A solvent company is one that owns more than it owes; it has a positive net worth and manageable debt load. Similarly, a company with adequate liquidity has

enough cash available to pay its debts. Solvency and liquidity are equally important and healthy companies must be both solvent and possess adequate liquidity. This report provides an insight for policy-makers of Pharma companies as how to make their company move in future.

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