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A Study on Impact on Financial Performance of Indian Pharmaceutical Companies

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Abstract:
The International market scenario has displayed big innovation in the past few years in terms of the Mergers and Acquisitions. Due to the entry of new companies with advanced technology, globalisation, changing customer behaviour, shareholder wealth demands etc. Mergers and Acquisition is a useful device for the development and expansion in every Industry. This research aim to the impact of acquisition on financial performance in the pharmaceutical sector and two companies have been taken for the research. These two companies are Dr. Reddy's Laboratories and Cipla which is listed in National stock exchange. This research used the before three years and after three years consolidated financial data of acquirer companies. This present research carried by 13 major financial ratio like Current Ratio, Operating Cash flow to Liabilities Ratio, Net Profit Ratio, Return on Capital Employee, Return on Equity, Debt to Equity Ratio, Debt to Assets Ratio, Debt Ratio, Capital Gearing Ratio, Inventory Turnover Ratio, Fixed Asset Turnover Ratio, Debtor Turnover Ratio, Creditor Turnover Ratio. Therefore, it is concluded that there is no significant difference in financial performance between pre and post-acquisition.

1. Introduction

Acquisition is also called Takeover. An acquisition is the purchase of one business by another entity. A merger is the combination of two companies into one by either closing the old Business into one new Business or by one Business absorbing the other.

In histories, M&A arise in the late 19th century United States. In 1708, for example, the East India Company merged with an erstwhile competitor to replace its monopoly over the Indian business. In 1784, the Italian Monte dei Paschi and Monte Pio banks were combined as the Monti Reuniti. In 1821, the Hudson's Bay Company merged with the rival North West Company.

The idea of merger and acquisition (M&A) was not popular until the year 1988 in India because of the regulatory and restrictions of MRTP Act, 1969. According to this Act, a company or a firm has to follow a forced and difficult method to get permission for merger and acquisition. The post-independence era witnessed a some negotiated mergers between large business groups. During the before liberalization licensing era till 1991, few entity indulged in irrelevant diversifications by the availability of licenses.

1.1 Trends in Mergers and Acquisitions in India, after 2011

India has become the most sought after destination for M&A deals. Even though our economy is still in the infant stage but still this economy is huge enough to provide opportunities for foreign investments. The pickup in the M&A activities have been seen from the time of election of the Narendra Modi led government, which has been responsible for some game-changing developments in the form of demonetization and progressive reforms in the form of GST which is going to drive the businesses towards an inorganic growth. The initiatives of the Government of 'Make in India', 'Digital India', 'Swatch Bharat' have also played a very important role in transforming India and pushing the economic progress. This favourable impact on India due to reforms in policy regimes can have "domino effect" which will lead to enhanced availability for the country's future missions. But the Indian economy needs the support and consultancy to ensure the progress in the coming years as well. But most importantly if India wants to keep progressing in the M&A space it needs to refine its legal framework so that it makes it easier for doing the businesses abroad and the legalities involved in them.

The future of the M&A activities in India seems bright as despite the lingering effects of demonetization, the trend of consolidation is expected to continue in 2017 as well as domestic activity is expected to remain robust even in 2017 with market expansion becoming a critical element of companies strategic agenda with consolidation deals likely to gain across sectors. Many big –ticket disinvestments by the debt laden companies can be expected in the power, cement, real estate and telecom sectors. Outbound investments are also expected to be led by oil and gas sector and pharmaceuticals and technology sectors are also expected to be active in strengthening their market position by consolidation. Inbound deals are also expected to grow with relaxed FDI norms and the Finance Minister in the Union Budget FY 17-18 cited an FDI increase of 36% over the past year which indicates the growing interest of the foreign investors in India.

2. Literature Review

Abbas et al. (2014)[1] examined financial performance of banks in Pakistan after Merger and Acquisition. They took 10 Pakistan banks for sample. They used financial ratio like profitability ratio, leverage ratio, efficiency ratio and liquidity ratio for analysis. The researcher found that no positive improvement in the financial performance after merger and acquisition.

Mboroto (2012)[2] analyzed to the effect of mergers and acquisitions on the financial performance. This research was carried on with only 4 sample companies that doing merger and acquisition in the period of 2002-2012 in petroleum firms in Kenya. For this study, return on equity, return on asset, liquidity management, macroeconomics factors and management efficiency as the dependent variable. The result presented that in the era of post-merger and acquisition, ROA of standard size overall financial performance has a major impact of mergers and acquisitions activity.

Sharma (2013)[3] analysed the impact of merger on the financial performance of Metal merging companies. This study took 9 companies for sample during the year 2009-10. The research analysed by accounting ratio and t-test. The study found that the not significant improvement in case of liquidity and leverage but the profitability results showed significant.

Singh (2015)[4] examined on the financial performance of the ICICI bank after buy. This study analysed by various financial ratios like, Net Profit Margin, ROA, ROE, ROI, Return on Advances, Debt/Equity ratio, Current Ratio, Quick Ratio and EPS. Also he used t- test. Financial data are covered during 2004 to 2014. The results found that half of ratios have significantly changed after mergers. While other half of ratios have not significantly changed after merger. The research concluded that no significance different between pre and post period.

Syukur and Fitri (2016)[5] analysed impact on financial performance of the acquisition by acquirer companies'. The research took 21 Indonesian companies for sample. Also they used accounting ratio

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[4] Singh, S. (2015). Mergers in service sectors: Post merger financial analysis of ICICI bank. IJAR, 1(9), 485-488.

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and statistical tool t-test for analysis. The researcher found that the liquidity, leverage, efficiency, profitability, and market value decrease insignificantly a year after the acquisition. The study concluded that there is no significant difference in financial performance between pre and post-acquisition.

3. Research Methodology

3.1 Objective of Style

1) The main object of present research is to analyses the impact on financial performance of the acquisition
2) The objective of the study is examining financial performance is improved or not after acquisition.

3.2 Significance of the research

This analysis through Management of the company can take decision based on Acquisition. Also management can know about impact on profitability after acquisition process.

3.3 Hypothesis

H_0 – There are no significant difference in financial performance of selected companies between pre and post period.
H_1 - There are significant difference in financial performance of selected companies between pre and post period.

3.4 Sampling Design

Two Pharmaceutical companies have been taken for this study. Convenience Sampling method of Non probability has been taken for this research. Name of the selected companies as follows:
1) Dr. Reddy's Laboratories
2) Cipla

3.5 Period of the Study

Six years of data from 2013-14 to 2018-19 are included in this study. In which included three years of before acquisition and three years of after acquisition.

3.6 Sources of the data

The research is mainly based on the secondary data. Secondary data have been taken from annual reports of respected companies under the study.

3.7 Research Tool

Accounting ratio and t-test used for this research.

3.8 Limitations of the Study

- The whole research is based on the secondary data of selected Pharmaceutical from annual report.
- Two companies have been selected for the research. So these two companies are not representing particular sector.
- The duration of the study is very short.

4. Data Analysis

Table 1: Different Accounting Ratios of Dr. Reddy's Laboratories

No.	Name of Ratios	Pre- Acquisition				Post- Acquisition			
		2013-14	2014-15	2015-16	Average	2016-17	2017-18	2018-19	Average
1	**Current Ratio (Time)**	1.78	1.74	1.73	**1.75**	1.15	1.52	1.88	**1.52**
2	**Operating Cash flow**	0.34	0.37	0.59	**0.43**	0.25	0.26	0.49	**0.33**

	to Liabilities Ratio (Time)								
3	**Net Profit Ratio (%)**	15.00	15.89	13.99	**14.96**	9.32	6.86	13.11	**9.76**
4	**Return on Capital Employee (%)**	25.84	24.62	20.31	**23.59**	11.60	8.63	13.83	**11.35**
5	**Return on Equity (%)**	24.96	23.71	18.39	**22.35**	10.54	7.53	13.91	**10.66**
6	**Debt to Equity Ratio (Time)**	0.30	0.20	0.13	**0.21**	0.09	0.24	0.18	**0.17**
7	**Debt to Assets Ratio (Time)**	0.51	0.47	0.42	**0.46**	0.44	0.44	0.38	**0.42**
8	**Debt Ratio (Time)**	0.15	0.10	0.07	**0.11**	0.05	0.14	0.11	**0.10**
9	**Capital Gearing Ratio (Time)**	0.26	0.15	0.09	**0.17**	0.04	0.20	0.16	**0.13**
10	**Inventory Turnover Ratio (Time)**	1.52	1.57	1.47	**1.52**	1.36	1.40	1.43	**1.40**
11	**Fixed Asset Turnover Ratio (Time)**	0.75	0.73	0.58	**0.68**	0.53	0.58	0.63	**0.58**
12	**Debtor Turnover Ratio (Days)**	93	102	99	**98**	100	107	98	**102**
13	**Creditor Turnover Ratio (Days)**	441	336	289	**355**	281	336	265	**294**

Table 1 present different ratio. In this table average net profit ratio of post-acquisition period are less than pre-acquisition period. So net profit are less receive in post-acquisition period. Also return on capital employed and return on equity of Post- acquisition period are less than compare to Pre – acquisition period. Solvency ratios of pre-Acquisition periods are more compare to post acquisition. So good financial position in pre-acquisition period of Dr. Reddy's Laboratories. Inventory turnover ratio and fixed turnover ratio of Pre acquisition period are higher than Post acquisition period. Higher Inventory Turnover Ratio and Fixed Asset Turnover Ratio are indicating good management. So not good financial management in post-acquisition period. Other ratios are representing not good performance after acquisition.

Table 2: Different Accounting Ratios of Cipla

No.	**Name of Ratios**	**2013-14**	**2014-15**	**2015-16**	**Average**	**2016-17**	**2017-18**	**2018-19**	**Average**
1	**Current Ratio (Time)**	2.20	1.95	1.12	**1.76**	2.64	2.82	3.29	**2.92**
2	**Operating Cash flow to Liabilities Ratio (Time)**	0.61	0.30	0.23	**0.38**	0.72	0.38	0.45	**0.52**
3	**Net Profit Ratio (%)**	13.75	10.41	11.01	**11.72**	7.25	9.60	9.34	**8.73**
4	**Return on Capital Employee (%)**	17.34	13.99	15.46	**15.60**	6.93	8.77	10.30	**8.67**
5	**Return on Equity (%)**	13.81	10.94	12.70	**12.49**	7.99	9.71	9.73	**9.14**
6	**Debt to Equity Ratio (Time)**	0.07	0.08	0.07	**0.07**	0.36	0.30	0.32	**0.33**
7	**Debt to Assets Ratio (Time)**	0.25	0.30	0.42	**0.32**	0.38	0.36	0.36	**0.37**
8	**Debt Ratio (Time)**	0.06	0.05	0.04	**0.05**	0.22	0.19	0.20	**0.21**

9	**Capital Gearing Ratio (Time)**	0.03	0.03	0.02	**0.03**	0.28	0.25	0.24	**0.26**
10	**Inventory Turnover Ratio (Time)**	1.47	1.26	1.35	**1.36**	1.46	1.44	1.44	**1.45**
11	**Fixed Asset Turnover Ratio (Time)**	0.97	0.98	1.08	**1.01**	0.56	0.55	0.61	**0.57**
12	**Debtor Turnover Ratio (Days)**	59	64	63	**62**	64	77	95	**78**
13	**Creditor Turnover Ratio (Days)**	635	725	587	**649**	614	659	490	**588**

Table 2 present different ratios. In this table net profit ratio of post-acquisition period are less than pre-acquisition period. So net profit are less receive in post-acquisition period. Also return on capital employed and return on equity of Post- acquisition period are less than compare to Pre –acquisition period. Solvency ratios of pre-Acquisition periods are more compare to post acquisition. So good financial position in pre-acquisition period of CIPLA. Fixed turnover ratio of Pre acquisition period is higher than Post acquisition period. Higher Fixed Asset Turnover Ratio is indicating good management. Therefore, not good financial management in post-acquisition period. Other ratios are representing not good performance after acquisition.

5. Finding and Conclusion

5.1 Finding

- Average net profit margin of Dr. Reddy's laboratories and CIPLA was decrease in post-merger, which indicates there is no significant difference in the pre-acquisition and post- acquisition net profit margin.
- Return on capital employed and return on equity of both companies was decrease in post- merger, which indicate no significant difference in the pre- acquisition and post- acquisition.
- Solvency ratio of Dr. Reddy's laboratories and CIPLA was increase in Post-acquisition. So which indicates there is significant difference in the pre- acquisition and post- acquisition in Solvency Ratio.
- In Inventory turnover ratio, fixed assets turnover ratio, Debtor turnover ratio and creditor turnover ratio no significant difference in the pre- acquisition and post- acquisition.

6. Conclusion

The study analyzed on financial performance of selected pharmaceutical Indian companies in pre-acquisition and post-acquisition period. It is concluded that there is no significance difference between pre-acquisition and post-acquisition. Overall financial performance of companies is decrease after acquisition. This poor performance is not caused by only acquisition process, but also other factors are considered.

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