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# IMPACT OF MERGERS AND ACQUISITIONS (M&AS) ON PHARMACEUTICAL INDUSTRY IN INDIA: A CASE STUDY

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**ABSTRACT:**

*Mergers and Acquisitions is a global phenomenon to gain a competitive advantage for the entities. It is a tool of inorganic growth where two firms combined each other and uplift their financials, research & development and gain synergy i.e. operational and financial both. Apart from this, in 2018, India saw more than 1,200 mergers and acquisitions (M&As), the highest in the current decade. Therefore, the paper studies basic concepts of Mergers and Acquisitions and assess its motives in the pharmaceutical sector of India. The study is descriptive in nature. In line with that, the paper presents a case study with reference to the Sun Pharmaceutical and Ranbaxy laboratories acquisition and examines the long term impact of merger on financial performance of Sun Pharma.*


**KEYWORDS**: *Mergers & Acquisitions (M&As), Competitive position, Inorganic growth, Indian Corporations.*

## A. INTRODUCTION

Companies restructure itself by adopting either expansion techniques or disinvestment techniques. Mergers and Acquisitions are used as technique of effective corporate restructuring and expansion tool in the business scenario worldwide. They are effective tool in the hands of the management to attain greater efficiency through synergies and growth opportunities.

Merger can be defined as a method of unification of two or more players into a single entity where one survives and others lose their corporate existence. It may take two forms, either absorption (A+B=A) or consolidation (A+B=C), whereas Acquisition is defined as acquiring effective control over the assets or the management of a company by another company without any combination of businesses or companies. In this way, in the acquisition, companies may remain independent, separate legal entity, however, there may be a change in control of companies.

## DRIVERS FOR MERGERS & ACQUISITIONS

Mergers and acquisition (M&A) is a major part of the corporate world. Intermediaries / Investment bankers arrange M&A transactions, which unites separate companies together to form bigger ones. When they're not creating big companies from smaller ones, corporate deals do the reverse and separate the companies through spinoffs or carve-outs. Deals can be worth hundreds of millions, or even billions. Deals can change the fortunes of the companies & Key executives involved.

**Some of the key drivers for mergers & acquisitions are mentioned following-**

- **Gaining a competitive advantage or larger market share:** Mergers can offer the acquiring company a chance to grow market share without having to really earn it by taking every necessary step themselves - instead, they buy a competitor's business. This may happen when the buyer takes over a major competitor, reducing its competition and increase its market share. If it has a sufficiently predominant position because of acquisition, it could then exercise more power in setting prices as well.
- **Synergy:** Synergy is the most common word used in M&A activity, which is the idea that by combining business activities, performance will increase and costs will decrease. Reaping various economies be it purchasing economies due to larger order size and bulk-buying discounts, various specialization skills on account of a huge pool of resources.
- **Geographical, product, or other diversification:** A company may acquire another company in a seemingly unrelated industry so as to reduce the impact of a particular industry's performance on its gain. This, in turn, may improve the stock price of a company; giving conservative investors more confidence in investing in the company. Predictability and consistency of earnings are generally enhanced stock valuations. Two companies may be ready to combine their products or services to achieve a competitive edge over others within the marketplace.
- **Cross-selling of products and services:** This relates to the complementary products an acquiring company can sell to the customers of its acquired company. As an example, a bank buying an insurance company might sell its banking products to the insurance companies' customers. At the same time, the insurance company might cross-sell the bank's customers its insurance products
- **Economy of scale:** A combined company can cut its fixed costs by removing duplicate departments, groups and operations, so lowering the company's costs relative to the same revenue stream, which would result in increasing profit margins. Companies may decide to merge into order to gain a better distribution or marketing network. If a company buys out one of its suppliers, it is able to save on the margins that the supplier was previously adding to its costs; this can be referred to as a vertical merger.
- **Taking advantage of tax benefits:** A money-making company can buy a money- losing and use the target's loss as their advantage by reducing their tax liabilities if the tax laws allow. In any case, this should not be the only driver for acquisitions.

## B. NEED OF THE STUDY

Pharmaceuticals industry perhaps seen most merger and acquisition activities than any other industry. Merger and acquisition is very common for pharmaceutical companies for example even Sun Pharma acquires one or two companies every year. The industry work like a pyramid where at the bottom small and new entered firms do research and development, and on the top big corporate do marketing job. So the small firms are acquired by top companies. Apart from this, pharmaceuticals industry id one the fastest growing industry of India. According to the reports in next five years India will become one of the top 10 countries in medicine segment. So it is very important to measure the relevance of merged firm and efficiency of merger and acquisition.

## C. REVIEW OF LITERATURE

### There are following papers on the similar topic were studied:

**Sun and Tang (2000)** they identified the source of gains in merger and acquisition transactions within the railroad industry; market power or efficiency power and also the results have shown that stockholders of acquiring firms do not gain from mergers, whereas stockholders of acquired firms and industry counterparts gain positive market-adjusted returns.

**Choi and Harmatuck (2006)** investigated the enhancement within the operating performance over the long run as well as examining management motives behind mergers and acquisitions and the results have shown that operating performance reported slight improvement however at an insignificant level. Managers tend to increase their own wealth instead of the wealth of shareholders.

**Malhotra and Zhu (2006)** dole out a study of post-acquisitionshort-term impact and long-term impact on the acquiring firms' shareholders' wealth as well as the impact of the acquisition on the acquiring firms' financial performance and the results shown that the domestic market has a significant positive response to the short-term announcement. With respect to long-term announcement impact, Indian international acquisitions underperform their bench market. Net sales to growth and foreign export sales increased after the acquisition whereas other financial ratios decreased post acquisitions.

**Majumdar et al. (2007)** examined the effects of mergers of local exchange firms in the U.S. on the financial performance and efficiency level and the results show that the cash flow decreased after mergers. For sales growth, the pattern was ambiguous and driven by increased market presence. The impact of mergers on the measures of efficiency and synergy was negative.

**Nalwaya and Vyas (2008)** studied the impact of mergers and acquisition on financial performance vis-a-vis value creation of Indian company and the result of the study is that the earnings growth after the merger was found at the much higher rate resulted in value addition to shareholders. A substantial dividend growth was discovered after the merger of the sample company.

**Sinha and Kaushik (2010)** examined the financial performance of the companies before and after the merger and the result of the study 1) there is a significant correlation between financial performance and mergers and acquisition deals. 2) Difference between pre and post-merger current ratio position is not statistically significant. 3) Pre and post solvency parameter and Overall efficiency parameters are statistically significant. Thus, the results have reported that more than half of merging firms showed improved financial performance in the post-merger time period. Target firms shareholders generally enjoy positive short-term returns investor in bidding firms frequently experience share price underperformance in the month of following

**Dutta and Dawn (2012)** measured and analyzed pre and post-merger financial performance of select banks and the results show that 1) all merged banks showed significant growth of total assets after the merger. 2) The average profit earned by merged banks during the post-merger period was higher than the profit earned during the pre-merger period. 3) All sample merged banks have shown the tremendous growth in revenue income after merger compared to revenue income before the merger. 4) Most of the sample merged banks have shown a significant change in the average growth of deposits and number of employees after the merger.

**Ghosh and Dutta (2014)** explored the overall strategic impact of mergers and acquisitions in the telecom sector of India and the result of the study is the ratio between the compensation of employees and PAT has been the only parameter where the performance has improved after the merger. Since three out of four parameters have shown no significant enhancement during the post-merger phase.

**Goyal and Joshi (2014)** probed that the market leadership, growth and diversification, synergy, risk, economies of scale and strategic integration are motives and rationality for mergers.

**Dr. Rajeshwari (2014**) studied about merger and acquisition, as a popular strategic option for growth and the result of the study is merger and acquisition can be the best tool for growth in this competitive and dynamic business environment.

**Turka and Sasan (2015)** studied the significance of mergers and acquisitions and to know how "Make in India campaign" will open the avenues for mergers and acquisitions and the results show that the merger and acquisition create synergies, economies of scale, expanding the operation and cutting costs.

## D. OBJECTIVE OF THE STUDY

1. To weather acquisition has any impact on the research and development of company.
2. To find out the pre and post financial performance of sun Pharma.
3. To find out the impact of sun Pharma merger on shareholders wealth.
4. To find out long term financial impact of merger on Sun Pharma.

## E. RESEARCH METHODOLOGY

### Source of Data-

Present study is based on secondary data. The data were composed from the published annual reports of Sun Pharmaceutical Industries and Ranbaxy Laboratories websites. Various journals, press release and announcement have been used.

### Period of Study-

The study covers a period from 2014 – 2015.

### Scope of the Study-

Present paper covers two pharmaceutical companies 'Sun Pharmaceutical Industries' and 'Ranbaxy Laboratories' only.

## ABOUT SUN PHARMACEUTICALS

Sun pharmaceuticals laboratories limited is pharmaceutical company. The company is known for manufacturing and marketing pharmaceuticals product in India. It has four plants located in Sikkim and Jammu. Sun Pharma has significant presence in generic, branded and OTC segment. The company has strong foothold in the segment of neurology, central system, cardiology, medicine, diabetes, gynecology etc. Sun Pharma mostly rely on acquisition of profitable companies with good knowledge base. The company believes in acquiring patents which gives them readymade formulas, drug and processes, they are more inclines towards commercializing new product developed from improving their already developed firms.

Sun Pharma is ranked No. 1 in the pharmaceutical industry with a total market share of 8.5%. The Growth rate is 6% which is equal to the average growth rate of the pharmaceuticals industry. Sun Pharma ranked No. 1 by prescriptions with 13 different classes of doctors. It holds robust position in the chronic and acute segment. Out of country's top 300 pharmaceuticals brands, Sun Pharma owns 30 brands. Out of these 30 brands top 10 brands contribute approx. 18% of Indian revenues. The company has low product concentration and focus more on growth driven by a basket of brands. The product portfolio includes differentiated offerings for hospitals, inject able and generics for retail market. Sun Pharma is also one of the well-known brands in the world for its research and development activity. It has an extensive sales force with more than 9,200 strong field force covering over 60, 00,000 doctors.

## RANBAXY ACQUISITION- ONE PLUS ONE GREATER THAN TWO

Sun Pharma acquired Ranbaxy Laboratories limited-an integrated, research based, international pharmaceutical company from Daichii Sankyo in all stock transaction for USD 3.2 billion. The deal completed in March 2015. After the acquisition Sun Pharma became world's fifth generic Pharma Company and India's largest drug maker. Daiichi Sankyo became the second largest shareholder in Sun Pharma. In the year 2013 the consolidated turnover of Ranbaxy was more than consolidated turnover of Sun Pharma but the Ranbaxy issue with USA FDA affected its market value. The deal expanded the presence of company and enhanced the positioning in the specialty generic landscape. According to annual report of Sun Pharma "The combines entity's manufacturing footprint covers six continents with products sold in over 150 nations with a stronger presence in the US, India, Asia, Europe, South Africa, CIS and Russia and Latin America".

## ANALYSIS AND INTERPRETATION

FINANCIAL RESULTS

(₹ in million except dividend per share and book value)

| Particulars | Standalone: Year ended 31st March, 2015* | Standalone: Year ended 31st March, 2014* | Consolidated: Year ended 31st March, 2015* | Consolidated: Year ended 31st March, 2014* |
|---|---|---|---|---|
| Total Revenue | 82,287.7 | 30,065.5 | 279,811.0 | 166,325.9 |
| (Loss) / Profit after tax | (14,741.3) | (28,285.2) | 45,393.8 | 31,414.7 |
| Dividend on Equity Shares | 7,219.5 | 3,106.7 | 7,219.5 | 3106.7 |
| Corporate Dividend tax | 1,469.7 | 528.0 | 1,469.7 | 528.0 |
| Transfer to Various Reserves | 0 | 0 | 1.9 | 0 |
| Amount of dividend per equity share of ₹ 1/- each | 3.0 | 1.5 | 3.0 | 1.5 |
| Book value per equity share ₹ 1/- each** | 95 | 36 | 107 | 89 |

***SOURCE:*** *Annual report of Sun Pharma 2014-2015*

Consolidated Book value of equity share of Sun Pharma in year 2014 was 89 rupees as given in above table. The acquisition increased the book value per share also. It increased to 107 rupees in the year 2015 in consolidated balance sheet and to 95 in standalone balance sheet.

## Balance Sheet

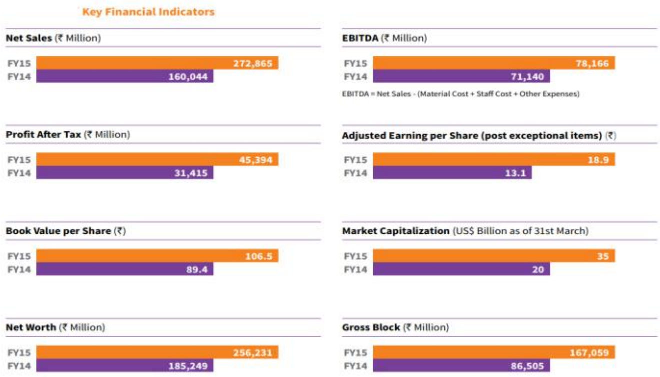
₹ in Million

| | Note No. | As at 31st March, 2015 | | As at 31st March, 2014 | |
|---|---|---|---|---|---|
| **EQUITY AND LIABILITIES** | | | | | |
| **Shareholders' Funds** | | | | | |
| Share Capital | 1 | 2,071.2 | | 2,071.2 | |
| Share Suspense Account | 48 | 334.8 | | - | |
| Reserves and Surplus | 2 | 225,307.7 | 227,713.7 | 72,007.6 | 74,078.8 |
| Share application money pending allotment | | | 149.0 | | - |
| **Non-current Liabilities** | | | | | |
| Long-term Borrowings | 3 | 11,703.2 | | 46.4 | |
| Deferred Tax Liabilities (Net) | 4 | - | | 1,928.4 | |
| Other Long-term Liabilities | 5 | 143.7 | | 13.8 | |
| Long-term Provisions | 6 | 24,225.1 | 36,072.0 | 25,241.9 | 27,230.5 |
| **Current Liabilities** | | | | | |
| Short-term Borrowings | 7 | 42,528.1 | | 24,043.7 | |
| Trade Payables | 8 | 14,850.3 | | 3,800.6 | |
| Other Current Liabilities | 9 | 32,475.5 | | 7,610.1 | |
| Short-term Provisions | 10 | 20,666.9 | 110,520.8 | 6,880.3 | 42,334.7 |
| **Total** | | | 374,455.5 | | 143,644.0 |
| **ASSETS** | | | | | |
| **Non-current Assets** | | | | | |
| Fixed Assets | | | | | |
| Tangible Assets | 11A | 31,152.9 | | 12,575.6 | |
| Intangible Assets | 11B | 699.8 | | 96.1 | |
| Capital Work-in-Progress | | 10,863.2 | | 4,804.6 | |
| Intangible Assets under Development | | 42.7 | | - | |
| | | 42,758.6 | | 17,476.3 | |
| Non-current Investments | 12 | 257,822.3 | | 61,557.3 | |
| Long-term Loans and Advances | 13 | 18,952.3 | | 7,614.9 | |
| Other Non-current Assets | 14 | 419.5 | 319,952.7 | 1.1 | 86,649.6 |
| **Current Assets** | | | | | |
| Current Investments | 15 | 939.3 | | 8,600.0 | |
| Inventories | 16 | 21,892.5 | | 9,183.8 | |
| Trade Receivables | 17 | 18,028.2 | | 9,801.5 | |
| Cash and Cash Equivalents | 18 | 4,164.6 | | 1,414.8 | |
| Short-term Loans and Advances | 19 | 6,966.9 | | 3,093.2 | |
| Other Current Assets | 20 | 2,511.3 | 54,502.8 | 24,901.1 | 56,994.4 |
| **Total** | | | 374,455.5 | | 143,644.0 |

***SOURCE:*** *Annual report of Sun Pharma 2014-2015*

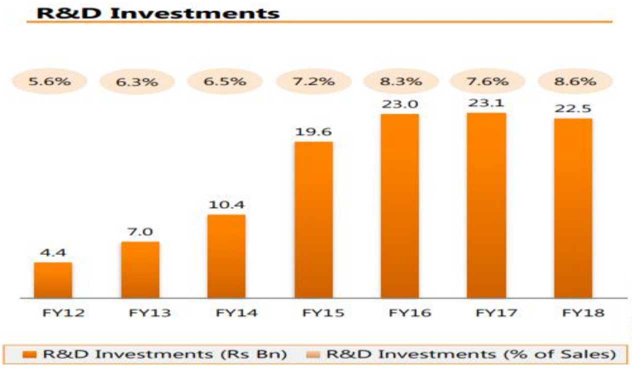
The percentage change in value of intangible assets in the year 2015 was 508%. Intangible assets of pharmaceuticals are patents and approvals of drugs. The acquisition with Ranbaxy increased intangible assets more than 500 times.The acquisition has also affected the sales of Sun Pharma. The changes in net sales were consistent till the year 2014. There was a sudden increase in the net sales in the year 2015, and from 2016 the change in sales become consistent again.

## KEY FINANCIAL INDICATORS




***SOURCE:*** *Annual report of sun Pharma 2014-2015.*

## RESEARCH AND DELOPMENT (R&D) EXPENDITURE




***SOURCE:*** *Annual report of sun Pharma 2014-2015.*

R&D is the backbone of Pharmaceutical industry and a key determinant of future growth and profitability. The expenditure on research and development has drastically increased in the year 2015 and has been rising consistently. The R&D expenditure in the year 2014 were 10.4 billion rupees which rose to 19.6 Billion rupees. This means acquisition deal has given a push R&D activity in Sun Pharma also.

## PRE AND POST IMPACT OF R&D IN SUN PHARMA


***SOURCE:*** *Annual report of sun Pharma 2014-2015.*

The rate of cumulative ANDAs (Abbreviated New Drug Application) approved is less than the rate of cumulative ANDAs filed. The total patents filed in the year 2014 was 478which rose to 597 in the year 2015. The cumulative products approves by ANDAs was 344 in the year 2014 which increased to 438 just after the acquisition. The patents are acquired through acquisitions deals. It means firms acquires patents to increase the market share. On the date of acquisitionSun Pharma had 139 ANDAs and 3 NDAs pending USFDA approval as of 31 March 2018.

**Leadership in key therapeutic areas**[11]

| Doctor Category | Prescription Rank (pre Ranbaxy acquisition as of October, 2014) | | Doctor Category | Prescription Rank (post Ranbaxy acquisition as of June, 2015) |
|---|---|---|---|---|
| Psychiatrists | 1 | | Psychiatrists | 1 |
| Neurologists | 1 | | Neurologists | 1 |
| Cardiologists | 1 | | Cardiologists | 1 |
| Orthopaedic | 1 | | Orthopaedic | 1 |
| Ophthalmologists | 1 | | Ophthalmologists | 1 |
| Gastroenterologists | 1 | | Gastroenterologists | 1 |
| Nephrologists | 1 | | Nephrologists | 1 |
| Diabetologists | 2 | Improved rankings due to Ranbaxy acquisition | Diabetologists | 1 |
| Consulting Physicians | 5 | | Consulting Physicians | 1 |
| Dermatologists | 6 | | Dermatologists | 1 |
| Urologists | 6 | | Urologists | 1 |
| Chest Physicians | 5 | | Chest Physicians | 1 |
| Oncologists | 8 | | Oncologists | 1 |

***SOURCE:*** *Annual report of sun Pharma 2014-2015.*

Sun Pharma focus more on basket of brands.Before acquisition deal Sun Pharma was a leading generic company in Psychiatrists, Neurologists, Cardiologists, Orthopedic, Ophthalmologists, Gastroenterologists and Nephrologists segments. But soon after the Ranbaxy acquisition, it became leading company in other major segments of the industry. This also improved the ranking of Sun Pharma in the market.

## EFFECT ON STOCK PRICES OF BEFORE AND AFTER ACQUISITION: SUN PHARMA



***SOURCE:*** *Annual report of sun Pharma 2014-2015.*

On the date of the announcement on April 7, Sun Pharma was trading at 587.25 rupees, with a price-to-earnings ratio of 617.69. On the other hand, Ranbaxy was trading on 449.09 rupees. The above figure shows, a sudden change in the stock prices. There was considerable effect of the merger deal on the stock prices of both the companies.

## FINDINGS

The analysis revealed that sun Pharma has been benefited by acquiring Ranbaxy. It took almost 30 years to sun Pharma to come at this point. Change in sales, profit book value, share prices etc., and show that merger has resulted in synergy benefit for both the companies. The most important thing to note in the case is the change in research and development expenditure. Acquisition has increased the expenditure of research and development by almost 1.5 times. Sun Pharma has deep history of merging and acquiring small companies. It usually target those companies that have strong research and development base. But the acquisition of Ranbaxy is very unique. Sun Pharma has acquired a bigger sized company without paying anything for it.

## LIMITATIONS OF THE STUDY

The present study covers only the analysis of financial decision taken by Sun Pharma. The study is confines to the pharmaceutical sector, but it can be extended to other sectors like service or manufacturing sector. There is scope to expand the study in more sectors like IT, Manufacturing, Banking which are too seeing more M&A. The study is one sided, i.e., the results are based on the analysis of financial records of Sun Pharma and impact of M&A on the Sun Pharma. More study can be done by analysing the financial records of Ranbaxy also to see to impact of M&A on the shareholders and wealth of Ranbaxy.

## CONCLUSION

Despite the fact that Sun Pharma has splendid track record of over twenty acquisitions in the past, Ranbaxy merger was biggest one so far and therefore was most challenging. After the acquisition Sun Pharma turned into India's largest and world's fifth largest pharmaceutical company. Our interpretation shows that there are tremendous increase in profits and sales of company soon after the merger. It can be concluded that company will be benefitting to generate synergy in years to come. The decision of merging Ranbaxy was productive and it has moved the company in right direction. According to annual report of Sun Pharma, the company is targeting synergy benefit from Ranbaxy by 2018. The company will be focusing on overall profitability improvement.

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