



A STUDY OF SHAREHOLDER VALUE CREATION OF SELECTED INDIAN PHARMACEUTICAL COMPANIES

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ABSTRACT

Maximizing wealth to shareholders is becoming India's new corporate standard. Wealth of shareholders is calculated in terms of the returns on their investment they earn. Traditionally, the metrics used to assess a business organisation's productivity and profitability have been accounting-based indicators such as ROI, ROE, ROCE, EPS, RONW and financial ratios. Yet now the value-added metrics of a day have emerged as a replacement for the conventional accounting-based acts. The explanation behind this is that a business organisation's financial output is calculated from the interest point of view of the shareholders. Value added reflects the wealth produced over a given time by an enterprise. No company will thrive and expand if its current and future shareholders struggle to produce value. Consequently, value added is a simple metric used to measure an enterprise's financial efficiency. While keeping this in mind, this study is an attempt to use regression analysis to examine value development in the Indian Pharmaceutical Industry from 2005 to 2014.

KEYWORDS: Value Creation, Economic Value Added, Market Value Added, ROI.

INTRODUCTION:

In recent years the maximization of shareholder interest has become the dominant corporate norm. The Business, which gave shareholders interest the lowest preference, now bestows the highest preference on it. The wealth of shareholders is determined by the returns they earn on their investment. It can be either in dividend forms or in capital appreciation form, or both. Various stakeholders use financial information to determine the current performance of a company and also to predict the future. The maximization of the shareholder interest is considered one of the basic objectives of all corporations. There are numerous value-based management (VBM) systems, shareholder value analysis (SVA) research (1986), and the two well-known ones are Economic Value Analysis (EVA) developed by Stern Stewart (1990). Maximizing shareholders' interest is becoming India's new corporate standard.

INDIAN PHARMACEUTICAL INDUSTRY:

Throughout the 1960s and 1970s the Indian pharmaceutical industry was dominated by multinationals. 7 out of the top 10 were multinationals who dominated the industry on the basis of their blockbuster labels.

In the 1990s the situation was reversed, with Indian national companies making 7 out of the top 10. The transition was supported by encouraging policies and regulatory procedures that gave the Indian manufacturers impetus. This was combined with the technological skill of Indian scientists and technocrats, who took advantage of the process patent regime's ability to introduce imitations of patented goods to the Indian market at affordable prices. Both the entry and departure costs in the pharma industry was minimal compared to the global context.

The drug policy (revised every 8th year beginning in 1971) was intended to improve product availability and affordability but placed pressure on demand and productivity, forcing the industry to reinvent itself. The entire domestic market became immediately a generic (or branded generics) market in 2005, with the advent of drug patents.

According to Union Minister of State for Chemicals and Fertilizers, Mr. Srikant Kumar Jena, India is one of the world's largest and most advanced pharmaceutical industries in exporting generic medicines worth USD 11 billion.

By comparison, India is predicted to rank among the top 10 pharmaceutical markets worldwide by 2015. The rising Indian population segment of the higher income community will open up a potentially USD 8 billion market for expensive drug sales by 2015. By 2015, overall domestic sales are estimated at USD 20 billion, making India truly a lucrative market. Issues related to health services need to be addressed in order to allow India to leverage this opportunity to become the world's largest consumer market.

Pharmacy retail is rising at 20-25 per cent per annum. The unified size of the pharmaceutical retail industry has the potential to rise to USD 9bn by 2011.

REVIEW OF LITERATURE:

Madhu Malik (2004) studied the relationship between shareholder capital and certain financial variables such as EPS, RNOW and ROCE. Using correlation analysis it was found that the correlation between EVA and RONW, ROCE, was positive and strong.

Karam Pal Singh and Mahesh Garg (2004) looked into the Indian corporate disclosure of EVA. The study revealed only 32 companies out of 50 produced positive EVA and 18 companies damaged the wealth of their shareholders in 1998.

Singh (2005) explored an effective way of assessing the success of the bank and also pointed out which Indian banks have been able to build (or destroy) the wealth of shareholders since 1998-1999 through 2002-2003.

Panigrahi (2005) discussed how the Added Economic Value (EVA) is superior to the Added Market Value (MVA). This was investigated by ITC Ltd's financial results which adopted the EVA as its measurement of performance.

Ghanbari and Sarlak (2006) studied economic added value in the Indian automotive industry. The study's objectives are: to measure and evaluate the Economic Value Added (EVA) of companies in the automotive industry, and to define the industry's EVA trend over the study period.

RESEARCH OBJECTIVE:

1. To analyse the trend and growth of shareholders' value in Indian Pharmaceutical Industry in terms of Economic Value Added, Market Value Added and return on investment
2. To examine the relationship between EVA, MVA and ROI in comparison to shareholder value.

RESEARCH METHODOLOGY:

Sampling Design:

Convenient sampling technique is applied for study.

Period of the Study:

The present research paper will cover a period of ten years from 2009-10 to 2018-19. The financial data for these years will be compiled from the annual reports of respective pharmaceutical companies. Data required for analysis has been taken from Capital line and CMIE Prowess.

Tools for Analysis:

There are many techniques which may be used for analysing the shareholder value measurement. Regression model has been used to analyse the shareholder value measurement

Data Analysis:

Looking at the empirical results of the regression model I may conclude that the return on net worth affects the company's return on investment and is important at a level of 5 per cent. This means the relationship between return on investment and net worth return has been positive (2.270). It was also concluded that the return on investment affected by the 1 percent increase in return on net value by 2,270 per cent. It means higher net worth returns contribute to higher investment returns.

I also consider that the company's debt equity ratio is positively related to ROI and also important in the company's results at a point of 5 per cent. The relation between investment return and debt equity ratio has been positive (2,254). This means 1 percent shift in the debt equity ratio in Return on Investment has

affected 2.254 percent. It means high debt equity ratio contributes to a increase in the company's return on investment.

The company's creditor pace is important at 5 per cent and negatively associated with the return on investment in the company's financial results, the relationship between the return on investment and the pace of the creditor was negative (-2.346). It means 1 percent shift in the pace of creditor has been influenced by 2.346 percent in Return on investment. This means businesses should take care of the vendors and make prompt payments to maximize investment returns. The interest coverage ratio is linked positively (5.243) to the return on the firm's investment potential. At 1 per cent point, the interest coverage ratio is important. This means that investment return is determined by the 1 percent increase in interest coverage ratio by 5.243 per cent. It can be said that increase in interest coverage ratio will leads to increase in ROI.

Results of the regression analysis show that the value of R^2 is 0.775, which shows that 77.5 per cent of aggregate data is explained by the sample regression. The overall model with modified R^2 value of 0.746 is also important. So the model specific to Indian Pharmaceutical Industry can be inferred. Therefore the model is suitable for analysis.

The classical theory of finance said the value development of the firm's shareholders is based on the willingness of firms to gain and firms to return to their net worth. Based on the research on regression, I have shown that the return on investment by the company is highly dependent on net worth economic return, debt equity ratio, and the velocity and price earnings ratio of the maker.

CONCLUSION:

While EVA calculation is not mandatory for pharmaceutical companies, they are keenly interested in these calculations because they believe it ensures greater transparency for managerial actions, facilitates them in aligning their performance with the expectations of shareholders, allows them to prepare substantive performance reports, provides incentive incentives on a reasonable and equal basis.

Internationally recognized companies such as Dr. Reddy's, Nicholas Piramal and JB Chemicals adopted the EVA model and all reported positive EVAs. In its annual report for the financial year 2009-10 JB Chemicals announced an EVA of 1,143.41 crore. The Indian pharmaceutical industry must capitalize on the massive IT and biotechnology strides it is making. The industry's future will depend on its ability to diversify its risks, to what degree it can develop its distribution network, co-marketing and licensing arrangements, forward-looking and backward integration capabilities and mergers and acquisitions. Particular attention is required in respect of its R&D spending. The investment made in R&D may / may not yield returns in this industry; hence the risk is very high which makes the industry very conservative in this field. The industry should be able to take chances with positive attitude, and this in the future would yield rich dividends.

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