

Opportunities and threats of mega merger: A case study of sun pharmaceuticals and Ranbaxy laboratories

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Abstract

Merger and acquisition in global pharmaceutical sector is not a new concept. The burst in M&A tendency in pharmaceutical sector is an inception to make the industry look like a pyramid. The present study is based on recent merger of Sun Pharmaceutical Industries and Ranbaxy; Sun Pharmaceutical Industries is a multinational pharmaceutical company having strong presence in the generic drug market in India. The company has a tremendous track record of 20 successful acquisitions. Sun Pharma after acquisition of Ranbaxy became India's 1st and world's 5th largest generic drug making company. Our study deals with impact of acquisition on financial health and profitability of the company. To come to a conclusion pre-acquisition and post-acquisition financial data have been analysed.

Keywords: Mergers, Acquisitions, Sun Pharma, Ranbaxy, Financial ratios

1. Introduction

To protect the business from the drastic downfall, many firms chose to take a step by making business combinations. Stepping towards M&A is a winning way to combine to successful alike business. With M&A synergy power of the two companies are combined to crater a business that is most suitable for the demand of the market and its stakeholders. Merger is a case where the acquired company deliberately delivers its assets and liabilities in the hands of the acquiring company. As a result, the company being acquired can survive another phases of competition in business cycle. However, the phenomena of merger and acquisitions of the two businesses would certainly leave an impact on its stakeholders; it may be negative or positive. Due to the financial stress of the company being acquired the stakeholders may feel the off-putting impact and hence it is quite obvious for the stakeholders to be nervous and uneasy at the kick-off of the initial phase of M&A.

2. Objectives of study

- To find out need of Sun Pharma and Ranbaxy merger.
- To find out whether Sun Pharma made the right step by acquiring the troubled Ranbaxy.
- To find out the impact of merger on stakeholders.
- To highlight post-merger challenges that Sun Pharmaceuticals will be facing.

3. Research methodology

Source of Data

Present study is based on secondary data. The data were composed from the official directory and data base of Centre for Monitoring Indian Economy (CMIE) PROWESS, published annual reports of Sun Pharmaceutical Industries and Ranbaxy Laboratories taken from their websites. Various journals, magazines and websites have also been used as sources of data.

Period of Study

The study covers a period of five years from 2011 – 2015.

Scope of the Study

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

4. Interpretation and analysis

About Ranbaxy

Ranbaxy Laboratories was established in 1961 and is a member of a leading global pharma innovator the Daiichi Sankyo group (Tokyo, Japan). Prior to merger with Sun Pharma, Daiichi Sankyo was also a majority shareholder of Ranbaxy which was having 63.4% outstanding shares in it. Ranbaxy has its business in 43 countries and 21 manufacturing facilities located in 8 countries across the world. Ranbaxy Laboratories has impressive portfolio of products which are sold over 150 countries. Despite satisfactory sales numbers the company was suffering loss since 2011. So Ranbaxy after struggling to improve its financial position went under merger with Sun Pharma at a crucial time.

Table 1: Ranbaxy Key Milestones

1961	Ranbaxy incorporated in India
1973	Ranbaxy goes public and listed subsequently
1978	First major step for becoming an MNC, Set up a JV plant in Nigeria
1997	Crossed Sales of \$200 m (Rs. 1,000 Cr) with exports over \$100 m (Rs. 500cr.)
1998	Enters in world's largest Pharma Market
2001	Launched its first para IV product <i>Cefuroxime Axetil</i>
2004	Crossed \$1b in global revenue
2008	Hybrid business model with Daiichi Sankyo
2014	Sun Pharmaceuticals and Ranbaxy Laboratories, announced their merger

*Source: Ranbaxy investor presentation, 2014

About Sun Pharmaceutical Industries

Sun Pharmaceutical Industries is a pharmaceutical company having global presence, it is largest company in Indian generic drug market. Sun Pharmaceutical Industries has credit of successful acquisitions of 16 companies at the time it acquired Ranbaxy in April 2014. This mega acquisition was an effort to make the company a

combined entity claiming the 5th largest generic drug making company in the world and the largest pharmaceutical company in India. The main reason behind it was Ranbaxy running into trouble with the FDA issues in the recent years. The present paper deals with the future growth prospects of Sun Pharmaceutical, possible threats and challenges that the company could face after acquisition.

Table 2: Sun Pharma at a Glance: Post merger

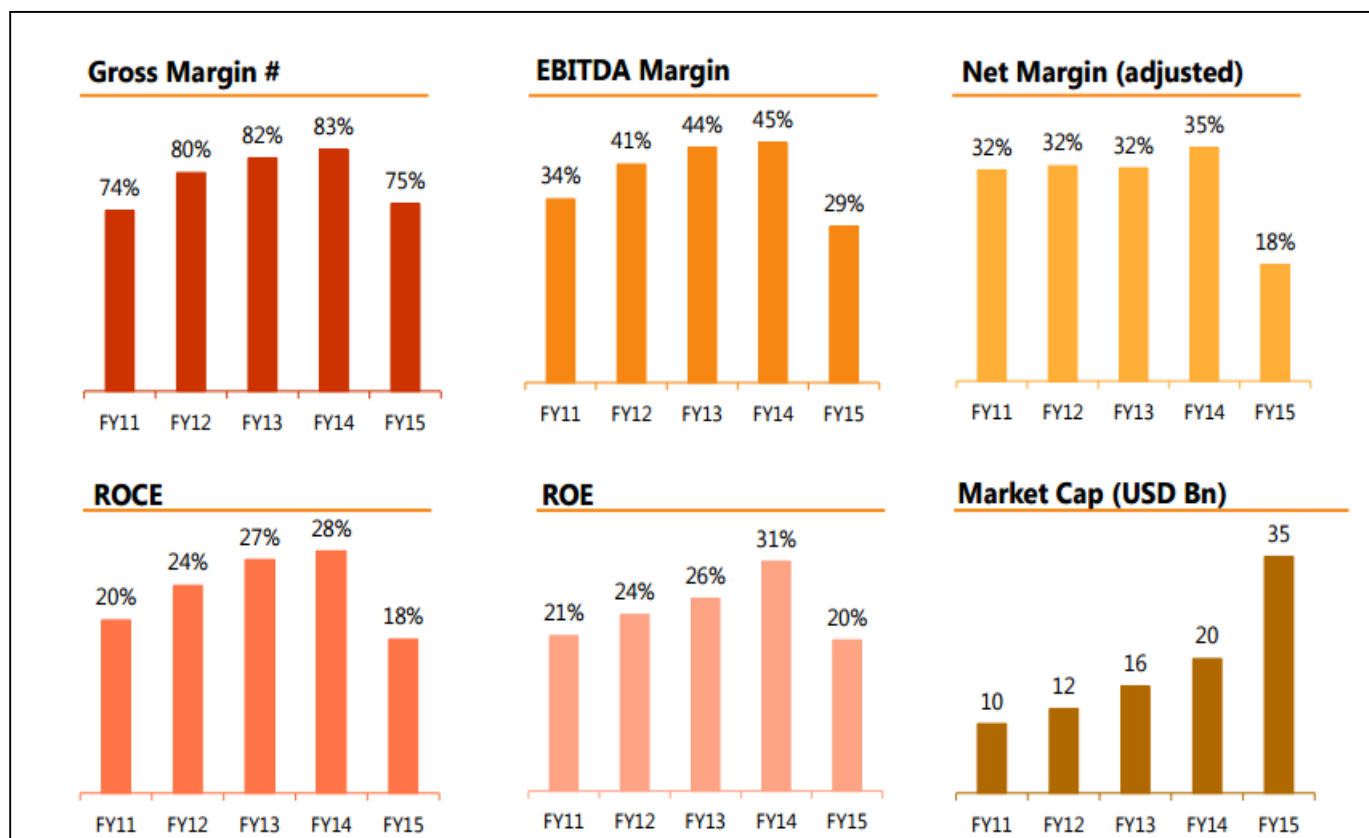
5th Largest Global Specialty Generic Company	
US	Ranked 5th in US* / Largest Indian Pharma Company in US
India	No. 1 Pharma Company in India
Emerging Markets	Largest Indian Pharma Company in Emerging Markets
Europe	Expanding presence in Europe
Manufacturing Footprint	50 manufacturing sites across the world
Market Presence	Presence in more than 150 countries across branded and generic markets
Product Portfolio	Portfolio of more than 2,000 products across the world
Employees	30,000+ global employee base
Quality Compliance	Multiple facilities approved by various regulatory authorities across the world including USFDA
R&D and Manufacturing	Capabilities across dosage forms like injectables, sprays, ointments, creams, liquids, tablets and capsules
Addressable Segments	Specialty products, branded generics, complex generics, pure generics & APIs

Source: Annual report and IR presentation of Sun Pharmaceutical Industries, 2015.

Sun Pharma after acquisition of Ranbaxy has become world’s 5th Largest Global Specialty Generic Company and largest Indian pharma company. It has a portfolio of more than 2,000

products with 50 manufacturing sites across the world and emerged as a faster expanding presence in Europe.

Profitability and Returns of Sun Pharma over last Five Years



#FY15 numbers include the impact of Ranbaxy merger

Source: Annual report and IR presentation of Sun Pharmaceutical Industries, 2015

Table 3: Comparative Study of P&L and Balance Sheet Summary of Sun Pharma Pre and Post Ranbaxy merger. (All Figures in Rs. Mn)

P&L Summary	FY14 (Pre-Acquisition)	FY15 (Post Acquisition)
Net Sales	1,60,044	2,72,865
Gross Profit	1,32,250	2,05,473
EBITDA	71,141	78,166
NET Profit	31,415	45,394
Net Profit (Adjustment)	56,589 [#]	47,771 [#]
R&D Spend	10,418	19,550
Balance Sheet Summary		
Shareholders' Funds	1,85,250	2,55,897
Loan Funds	24,890	75,963
Net Fixed Assets	58,242	1,10,201
Investments	27,860	27,163
Cash and Bank Balances	75,902	1,09,980
Inventory	31,320	56,680
Sundry Debtors	22,004	53,123
Sundry Creditors	13,283	31,538

[#] adjusted for provision related to generic Protonix settlement.

Source: Annual report and IR presentation of Sun Pharmaceutical Industries, 2015

Sun Pharma pre ranbaxy merger reported a Net Sales of 1,60,044 (in Rs. Mn) in FY 2014, while post Ranbaxy merger Net Sales has gone upto 2,72,865 (in Rs. Mn) in FY 2015 which show synergy benefit after successful merger. Gross Profit also increased from 1,32,250 to 2,05,473 similarly Net profit spurted from 31,415 to 45,394, EBITDA in FY 2014 was

71,141 while post-merger it increased to 78,166 in FY 2015, while we see pressure on its adjusted net profit which declined from 56,589 to 47,771. No doubt the balance sheet of the company shows strengthened position after mega merger almost at every parameter.

Table 4: Financial Ratios

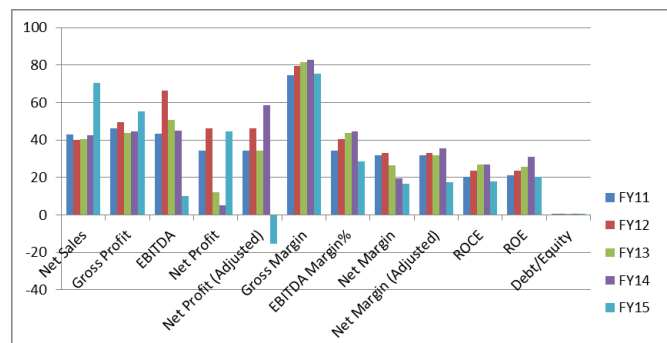
	FY11	FY12	FY13	FY14	FY15*
Net Sales	42.8	39.9	40.4	42.4	70.5
Gross Profit	46.3	49.5	43.9	44.4	55.4
EBITDA	43.2	66.5	50.9	45.0	9.9
Net Profit	34.4	46.3	12.3	5.3	44.5
Net Profit (Adjusted)	34.4	46.3	34.3 [#]	58.7 [#]	-15.6 [#]
Gross margin	74.4	79.5	81.5	82.6	75.3
EBITDA Margin%	34.1	40.6	43.7	44.5	28.6
Net Margin	31.7	33.2	26.5	19.6	16.6
Net Margin (Adjusted)	31.7	33.2	31.7 [#]	35.4 [#]	17.5 [#]
ROCE	20.3	23.8	26.7	26.9	17.8
ROE	21.0	23.8	25.7	30.9	20.4
Debt/Equity	0.04	0.02	0.01	0.13	0.30

*FY15 numbers include the impact of Ranbaxy merger

Source: Annual report and IR presentation of Sun Pharmaceutical Industries, 2015

The financial ratios of last five years show that Sun Pharma has been benefited to have acquired market share of Ranbaxy in many ways, particularly both Sales and profit have increased significantly after acquisition of Ranbaxy. At the same time the company is facing margin pressure after mega merger, the same can be observed in gross profit margin, EBITDA Margin%, Net Margin. Return to contributories has also declined significantly after merger which can be noticed through ROCE, ROE. The company has a record of having debt-free balance sheet but after acquisition the Debt/Equity has also increased which might be hard pill for Sun Pharma to swallow.

Graphical representation of key financial ratios post-merger



5. Finding and recommendations

Though mergers and acquisition gives rise to synergy power to both the companies yet it appears to have many negative impacts on the acquiring company. The company should look every issue in a special way and take an interesting care towards the challenges ahead specially in terms of future prospect of business, competition, investors value and most important its employees. Sun Pharma has to build trust which can introduce the opportunity growth to augment a great and suitable environment for its business and investors. As the Sun Pharma business is greatly depend on R&D, the company should invest more on it and Sun Pharma appears to be at right direction; in FY 15 (Post Acquisition) its R&D spend stood at Rs. 19,550 Mn from 10,418 in FY 14 (Pre-Acquisition). Another issue is to maintain the quality of its balance sheet; after acquisition Debt-Equity ratio of the company depict very pathetic story; Sun Pharma has been almost debt free record in pre-acquisition period with 0.04, 0.02, 0.01, 0.13 in FY 11, FY 12, FY 13 and FY 14 respectively but post acquisition in FY 15 its Debt-Equity ratio gone up to 0.30 which is not a good signal for maintaining shareholders' value. The acquisition is also poised to dilute return on equity from 27.9% to 27.5% in FY 2016. At the same time Sun Pharma's track record of handling acquired assets in the past years will enable it to succeed with its acquisition of Ranbaxy. Now the top priorities for both the companies is to secure 100% compliance with required manufacturing standard by the regulators, to amplify its spotlight on R&D and to accomplish muscular business intensification throughout the world.

6. Conclusion

Sun Pharma has splendid track record of acquisition in past as it made nearly 20 acquisitions with first in the year 1983. Sun Pharma acquired Ranbaxy from \$3.2 billion along with its debt assuming \$800 million. The most recent acquisition was in 2010 when it acquired majority stake in Taro Pharmaceutical Industries which proved to be a winning bet for the company which doubled its revenue in US market from \$484 million to \$1.1 billion. Despite the fact Sun Pharma has a splendid track record of successful acquisitions as seen previously in case of acquisition of Taro, DUSA and URL in the couple of years, we do feel Sun Pharma and Ranbaxy mega merger is the biggest one so far and therefore the most challenging too. Big issue to be faced by Sun Pharma is poor financial performance record of Ranbaxy. Yet our research shows that the company will be benefitting to generate synergy in years to come. The mega merger appears to be the demand of the time. By seeing Sun Pharma's capability to handle the balance sheet and providing value to its stakeholders in past acquisition, it can be concluded that the company has moved in right direction.

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