Evaluating the financial performance of Companies from the Pharmaceutical Industry

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Abstract: *The pharmaceutical industry has become a highly competitive environment, which is why performance represents the key element to stay on a market. Evaluating the performance of the economic entities from this sector is of high importance for the management, shareholders, trading partners and creditors. This study focuses on investigating and analyzing the financial statements for 12 drug producing companies in Romania. The analysis is based on data corresponding to the period 2008-2015.*

Key-words: *financial statements, performance, pharmaceutical industry*

1. Introduction

The pharmaceutical market refers to the industry of manufacturing and marketing drugs. In the past years the consumption of drugs has increased per inhabitant, the period 2008-2015 being quite favorable for the pharmaceutical market from Romania. In times of crisis and economic uncertainty, the companies from the pharmaceutical sector have registered economic growth, but given the fact that competition is quite fierce, performance remains an important criterion for maintaining your company on the market. Also, it can not be neglected the structure of the analyzed sector, because on one hand it can determine the sectors' competitive intensity and on the other hand its average profitability (Drumea, 2004).

Dincă and Dincă (2014) have analyzed financial performances for five Bucharest stock exchange listed companies using an econometric model with data for 2014-2011. The authors found that 64% of return on investment's (ROI) evolution was explained by the influence exerted by the determinants of the cash conversion cycle, by return on assets and by the relative modification of the sales turnover. Deari and Dincă (2015) have analyzed financial performances of 40 selected Romanian companies for the 2009-2013 period. They found that the companies with higher current to total assets ratio have higher assets turnover and ROA. The performance of an economic entity can be analyzed by using its financial

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statements, namely with the help of the profit and loss account. An economic entity is performing if it has the ability to make profit (it's cost effective) and if it has the ability to pay its debts on short and long term. For profit and must be performance company win customers' trust (Neacşu, 2015).

2. Methodology

Financial performance is a vast topic developed at all academic levels and in the professional practices. The interest shown in this topic was present in the concerns of Romanian and foreign authors, experts in finance, accounting, financial management, evaluation, general management, value management. The main objective of this study is represented by the analysis of the financial performance of companies from the pharmaceutical sector in terms of their ability to obtain profit, in the dificult economic context of the period after 2008. The population on which the study was conducted targets 12 economic entities which produce pharmaceutical products. There were chosen the first 12 economic entities which recorded the highest sales in 2015. The paper focuses on analyzing the performance of economic entities from this sector. The financial performance indicators are calculated by the author based on the information provided by the individual financial statements of these categories of companies, elaborated for the period 2008-2015. The analysis involved the investigation of financial statements from several consecutive financial years, over a period of 8 years (2008-2015). Examining the financial statements over several consecutive financial years is supposed to enhance the value of the analysis. The financial situation in the case of an economic entity is highlighted through the financial - accounting information published in financial reports, namely by reflecting the financial position in the balance sheet and the financial performance in the profit and loss account. Every economic decision taken by an entity involves a strict and precise analysis of all economic and financial events and transactions as well as of the data provided by the financial statements. This paper presents an analysis of the evolution and dynamics of the financial performance reflected in the financial statements of the economic entities from the pharmaceutical sector. The study addresses the financial performance in terms of the profit and loss account, by analyzing the following indicators: turnover, the net result and the return on equity (ROE). Performance is not just about an entity's ability to make profit, but also its ability to pay its short and long-term debts. Thus it was also calculated the degree of indebtedness for the 12 economic entities from the pharmaceutical sector. An economic entity's financial performance represents its ability to obtain profit from its business as a result of carrying out its economic activity. Thus, for an economic entity to be efficient from a financial point of view it is imposed the condition to conduct a profitable activity, which enables first of all the remuneration of all the

factors of production involved, as well as achieving a surplus, represented by the overall result of the economic activity.

An indicator that measures the performance of companies, used as a criterion for ranking them in terms of their economic importance is the ***turnover***. The turnover represents the value of sales made over a period of time by an economic entity. This indicator allows assessing the place of the company in its sector, its market position, its skills to launch and develop different activities which would bring profit. However, the change of the turnover is reflected on the main financial indicators as well as on the efficiency of the activity of economic entities. In the manufacturing sector, the net turnover expresses the total volume of businesses and includes all the revenue from the sale of the products obtained. The dynamics of the turnover for the 12 economic entities producing drugs is shown in Table 1.

Company	Turnover (mil lei)							
	2008	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**
1	83	405	380	407	463	497	426	612
2	289	260	376	421	471	500	521	538
3	218	175	259	235	242	290	394	396
4	253	250	290	272	261	268	307	338
5	215	219	243	281	304	318	320	331
6	77	82	93	112	128	112	140	209
7	65	67	82	93	104	119	128	149
8	25	104	129	116	88	141	136	129
9	95	110	111	119	123	119	114	118
10	31	61	97	121	120	110	115	110
11	17	23	29	40	68	88	99	103
12	43	36	60	68	80	78	89	57

Table 1. *The turnover of the drug producing companies*

The companies listed in Table 1 are the top 12 companies producing pharmaceutical products in Romania which have recorded the highest sales in 2015. The turnover has registered an upward trend in the analyzed period (especially between 2011-2015), this trend is mostly due to an increase in the products sold as well as to an increase in the number of employees.

Another indicator showing the financial performance recorded by each sector is the ***net result***. This indicator expresses the efficiency of the entire activity developed by economic entities. Two of the analyzed entities have registered economic losses throughout the 8 years analyzed. The period of 2009-2012 was marked by decreases of the net result, due to an increase in the total expenses. Increasing the number of employees by the two companies which recorded losses, apparently had a positive effect on the turnover, but not on the

net result which had negative values in the period under review. The evolution of the stock market climate starting with 2008 resulted in a negative impact on the financial result due to the revaluation of the stock portfolio. It is one of the factors that competed at the volatility of the net result of the companies from the pharmaceutical sector in the period 2009-2010. The other 10 companies have registered positive and increasing values of the net income (Figure 1).
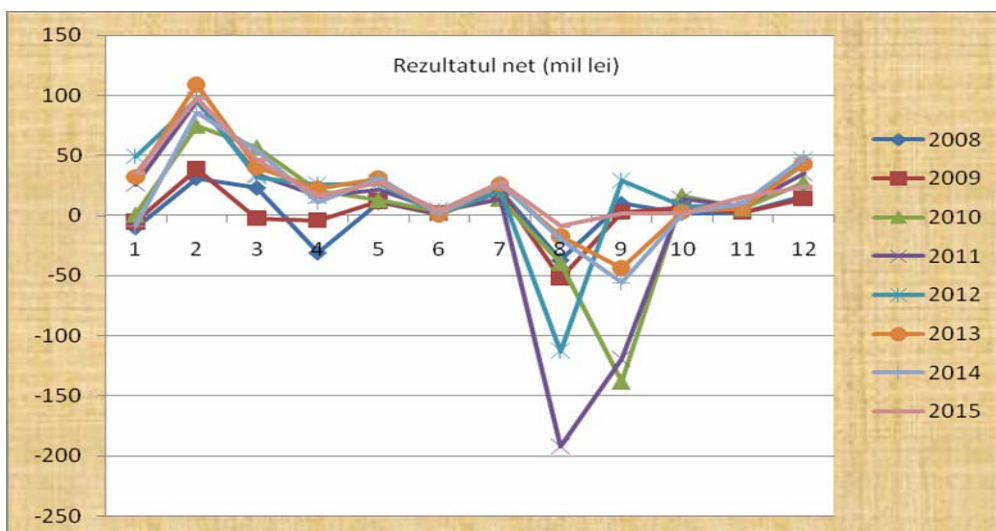

Fig. 1. *Evolution of the net result*

Another indicator that expresses the ability of an economic entity to generate profit, is the rate of **return on equity (ROE)**. Return on equity is a significant indicator for assessing the economic and financial performance of a company for its internal diagnosis, as well as for the analyses required by the external partners (Căruntu, 2009). Return on equity expresses the ability of the equity to generate profit and the efficiency of using the own equity. Depending on the value of this indicator, shareholders can appreciate if their investment is justified and whether they should continue investing. *It is calculated by dividing the obtained net result by the value of the equity.* A high rate of return on equity thus enables the shareholders to obtain consistent revenues. The higher the return on equity is the more financial resources the company has at its disposal (Vasilache, 2009). The return on equity recorded fluctuating values between -36.36 and + 180. The rate was negatively influenced by the losses incurred in the period 2009-2012. The period of 2009-2012 encounters the companies on a negative curve due to the losses recorded, but it takes a positive turn in the next years. In order to increase the rate of return on equity and to stabilize the situation of the economic entities it is necessary for the net profit to grow at a higher rate than the growth of the equity.
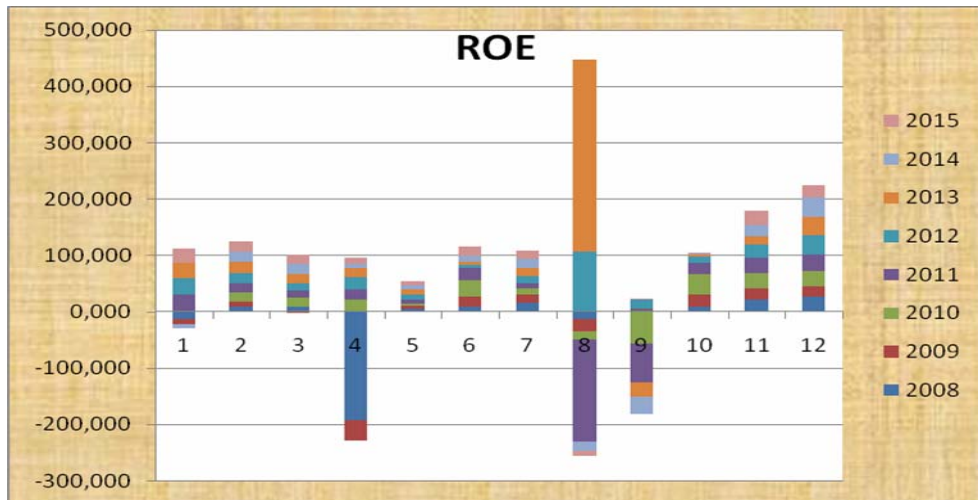
Fig. 2. *Return on equity*

An indicator that can quantify the amount of external financing in relation to the possibility of self-financing of an economic entity is the ***degree of indebtedness***. This may also be a barometer of the entity's independence face to its creditors (Anton, 2009). The degree of indebtedness is calculated as the ratio between total debt and equity. The higher this indicator is the more dependent the economic entity is on commercial loans or debts. A reasonable situation demands that this indicator does not exceed the threshold of 0.5. The degree of indebtedness of analyzed entities is between 0.06 and 25.45. The economic entities have registered a high degree of indebtedness face to its creditors, especially in the period 2009-2012. Among the analyzed companies, only two of them do not exceed the threshold of 0.5. Given the high level of the degree of indebtedness registered by the analyzed economic entities, we can say that their funding depends on a lower proportion of own resources and on a greater proportion of borrowed sources (usually bank loans). The mentioned entities may face the danger of insolvency, the given situation reflects an increased dependence on external sources.

3. Conclusions

The economic entities from the pharmaceutical sector have managed to overcome the difficult times specific for a period of economic crisis, registering an upward trend in turnover. The indicator return on equity recorded fluctuating values with a decreasing tendency in 2009-2012, but with a strong recovery in the coming years. The carried out diagnostic analysis has shown that the entities from the pharmaceutical sector have gone through difficult periods, especially between the

years 2009-2012. Another finding of this study refers to the rather sensitive position concerning the degree of indebtedness. In the case of four out of the twelve analyzed companies, the degree of indebtedness has recorded quite high values mostly in 2009-2011, which indicates a relatively low potential for self-financing, meaning that the economic entities finance themselves from external sources. One possibility for reducing debts would be compensating claims with debts, and thus eliminating the possible delay penalties. In conclusion, we note that the economic entities from the pharmaceutical sector show an overall positive financial performance that might generate significant added value, as evidenced by the calculated indicators. The present research has some limitations, inevitable in any scientific endeavor of this kind, that only open up new horizons for future research. A first restriction in appreciating the performances refers to the number of analyzed companies, and the temporary horizon.

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