

Assignment

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A study on the GlaxoSmithKline Plc

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Part-A

The global pharmaceutical and healthcare firm GlaxoSmithKline Plc (GSK) is based in Brentford, London, United Kingdom. With a long history that dates back to the 19th century, it is one of the biggest pharmaceutical corporations in the world. The 100 biggest publicly traded firms in the UK are included in the FTSE 100 Index, which also includes GSK, which is listed on the London Stock Exchange (LSE). The three main business divisions of GSK are pharmaceuticals, vaccines, and consumer healthcare. Each episode's segments concentrate on various facets of the healthcare sector.

The group turnover of the company for 2022 was £29.3 billion, which is 18.62% higher than the last year. During the recent financial year, the company's operating profit climbed by 46.8%. Operating profit margins decreased, falling from 16.3% in 2021 to 23.9% in 2022. Finance costs fell by 43.6% in 2022, and depreciation charges by 14.0% in the year 2022. Net profit margins increased from 11.2% in financial year 2021 to 11.7% in financial year 2022. In the past five years, GSK has seen leadership upheavals as new executives have been hired to set the company's course (Singh and Schmidgall, 2022). Emma Walmsley became the organization's first female CEO when she assumed her position in 2019. To improve the efficiency of its business processes and cost structure, GSK has implemented a number of restructuring efforts. These initiatives intended to increase effectiveness and concentrate on key therapeutic areas. With regulatory clearances, encouraging data readouts, and smart commercial development, the company has continued to bolster the late-stage pipeline. This has resulted in to twenty plus approvals of medicines and vaccines since 2017, and around £12.7 billion sales of products that are introduced in the last five years.

To speed up medication discovery and innovation, the company has formed strategic alliances and partnerships with other pharmaceutical firms and academic institutions. There has been a long-standing collaboration between GSK and Innoviva on respiratory drugs. By amending their collaboration agreement in 2018, the two businesses gave GSK expanded access to a number of respiratory drugs, including Relvar Ellipta and Incruse Ellipta. A global partnership between GSK and Merck to create and market M7824, an experimental immunotherapy for various cancer types, was announced in 2019. GSK established a partnership with Vir Biotechnology and Medicago in April 2020 to conduct research and create new COVID-19 therapies. The cooperation aims to find and accelerate innovative treatments to combat the COVID-19 pandemic by combining Vir Biotechnology's expertise in infectious disease

research with GSK's capabilities in drug development. In the last one year as well, the company has seven new collaborations as well as acquisitions, namely Affinivax, and Sierra Oncology.

Significant pharmaceutical firms, like Pfizer, Johnson & Johnson, Novartis, Roche, and AstraZeneca, compete fiercely with GSK. These rivals work in industries with related therapeutic focuses, such as consumer healthcare goods, oncology, respiratory therapies, and vaccinations. Smaller biotechnology companies and producers of generic medications are also competitors in some markets. GSK made a critical strategic choice five years ago to concentrate on pharmaceuticals and vaccines, which resulted in the sale of its Horlicks nutrition business in India. With this action, GSK wanted to concentrate its efforts on markets where it enjoyed a competitive edge.

Part B

Financial Ratios Calculation

I. Calculating Profitability Ratio

A profitability measure known as the gross profit ratio is created indicates a company's profit after deducting the cost of its supplied goods. The gross profit ratio illustrates the relationship between a company's gross profit and net sales.

It establishes the amount of profit the business makes relative to the amount required to cover its operating costs. It facilitates inter-firm analysis of trade activity results. Gross profit reveals if a business is performing better or worse than its rivals because it increases with efficiency. It establishes the competitive advantage the company has.

$$\text{Gross Profit Ratio} = (\text{Total Revenue} - \text{Cost of Goods Sold}) / \text{Total Revenue} * 100$$

Year	COGS	Revenue	Revenue - COGS	Gross Profit Ratio
2018	13,670	41,140	27,470	67%
2019	15,148	43,100	27,952	65%

2020	15,027	43,783	28,756	66%
2021	15,955	46,910	30,955	66%
2022	11,817	36,270	24,453	67%

2018:

- COGS: \$13,670 million
- Revenue: \$41,140 million
- Revenue - COGS (Gross Profit): \$27,470 million
- Gross Profit Ratio: 67%

2019:

- COGS: \$15,148 million
- Revenue: \$43,100 million
- Revenue - COGS (Gross Profit): \$27,952 million
- Gross Profit Ratio: 65%

2020:

- COGS: \$15,027 million
- Revenue: \$43,783 million
- Revenue - COGS (Gross Profit): \$28,756 million
- Gross Profit Ratio: 66%

2021:

- COGS: \$15,955 million
- Revenue: \$46,910 million
- Revenue - COGS (Gross Profit): \$30,955 million
- Gross Profit Ratio: 66%

2022:

- COGS: \$11,817 million
- Revenue: \$36,270 million
- Revenue - COGS (Gross Profit): \$24,453 million
- Gross Profit Ratio: 67%

Key observations:

1. Revenue has been steadily increasing over the years, which is a positive sign as it indicates growth in the company's sales.
2. Cost of Goods Sold (COGS) has also been increasing, but not at the same rate as revenue. This implies that the company has been able to manage its production costs to some extent.
3. Gross Profit (Revenue - COGS) has followed a similar trend as revenue, indicating that GSK PLC has maintained a consistent level of gross profit over the years.
4. The Gross Profit Ratio has remained relatively stable at around 66-67% over the past few years. This suggests that the company has been maintaining a consistent level of profitability from its core operations.

Calculating Liquidity Ratio

One form of liquidity ratio is **Current ratio**. The current ratio essentially measures the firm's existing asset-to-current liability ratio. This aids in determining if the business has the finances to fulfil its immediate responsibilities. Since it has no immediate liquidity issues, a company with a current ratio greater than 1 will probably be able to pay down its current liabilities. A current ratio that is abnormally high—above 3—could mean that the business can cover its debts three times over. It can also be a warning that the business isn't handling its money well.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Year	Current Assets	Current Liabilities	Current Ratio
2018	22,594	30,020	0.75
2019	24,888	30,709	0.81
2020	25,997	28,438	0.91
2021	25,678	32,548	0.79

2022	25,689	28,213	0.91
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- Current Assets: The trend in current assets over the years seems relatively stable, ranging from \$22,594 million in 2018 to \$25,689 million in 2022. Having a healthy level of current assets is crucial for any company, as it represents resources that can be quickly converted into cash or used to settle short-term debts.
- Current Liabilities: The company's current liabilities have also exhibited consistency during the five-year period, with values ranging from \$28,213 million in 2022 to \$32,548 million in 2021. Current liabilities include obligations that are due within one year, such as short-term debt, accounts payable, and other similar obligations.
- Current Ratio: The current ratio is a liquidity metric that measures a company's ability to pay off its short-term liabilities with its current assets. It is calculated as current assets divided by current liabilities. A current ratio above 1.0 is generally considered favorable, as it indicates the company has more current assets than current liabilities, signifying strong short-term liquidity.

Now, let's analyze the critical aspects of the data:

1. Low Current Ratio: The current ratio has consistently been below 1.0 for all the years, indicating that GSK PLC might have some difficulty in meeting its short-term obligations using only its current assets. This could be a cause for concern as it suggests a potential liquidity risk. The company may need to rely on other sources of funds, such as short-term borrowing or reducing non-essential expenses, to cover its short-term liabilities.
2. Stability in Current Assets and Liabilities: Although the current ratio is below the desirable threshold, the fact that both current assets and current liabilities have remained relatively stable over the years is somewhat reassuring. A consistent trend in these figures suggests that the company has been managing its working capital efficiently.

Calculating Gearing Ratios

The debt-to-equity (D/E) ratio compares a business's overall indebtedness to the equity of the shareholders to determine how extensively it depends on credit. D/E proportions, that varies by sector, are the simplest approach for assessing immediate rivals or follow modifications to a company's dependence on debt over time

A greater D/E ratio amid similar-sized corporations indicates increased risk, but a very low one might indicate that an organisation is not using borrowed capital for development.

Since long-term obligations are uncertain than short-term obligations, investors typically adjust the D/E ratio to just include them.

D/E = Total Debt of the company/Total Equity of the company

To find total equity, we find ¹⁶ the difference between total assets and total liabilities.

Year	Total Debt	Total Assets	Total Liabilities	Total Equity	D/E
2018	33,080	73,710	69,040	4,670	7.08
2019	40,010	1,04,500	80,420	24,080	1.66
2020	37,010	1,09,603	81,270	28,333	1.31
2021	32,630	1,06,780	77,960	28,820	1.13
2022	25,440	72,900	60,660	12,240	2.08

2018:

- **Total Debt: \$33,080 million**
- **Total Assets: \$73,710 million**
- **Total Liabilities: \$69,040 million**
- **Total Equity: \$4,670 million**
- **Debt-to-Equity Ratio (D/E): 7.08**

2019:

- **Total Debt: \$40,010 million**
- **Total Assets: \$104,500 million**
- **Total Liabilities: \$80,420 million**
- **Total Equity: \$24,080 million**
- **Debt-to-Equity Ratio (D/E): 1.66**

2020:

- **Total Debt: \$37,010 million**
- **Total Assets: \$109,603 million**
- **Total Liabilities: \$81,270 million**
- **Total Equity: \$28,333 million**
- **Debt-to-Equity Ratio (D/E): 1.31**

2021:

- Total Debt: \$32,630 million
- Total Assets: \$106,780 million
- Total Liabilities: \$77,960 million
- Total Equity: \$28,820 million
- Debt-to-Equity Ratio (D/E): 1.13

2022:

- Total Debt: \$25,440 million
- Total Assets: \$72,900 million
- Total Liabilities: \$60,660 million
- Total Equity: \$12,240 million
- Debt-to-Equity Ratio (D/E): 2.08

Key observations:

1. Debt-to-Equity Ratio (D/E): The D/E ratio provides insights into the company's financial leverage. In 2018, the D/E ratio was significantly high at 7.08, indicating that GSK PLC had a substantial amount of debt relative to its equity. However, over the years, the D/E ratio has been decreasing, which generally suggests that the company is reducing its financial leverage and relying less on debt financing.
2. Total Debt and Total Assets: Both total debt and total assets have shown some fluctuations over the years. However, the company's total debt decreased from \$40,010 million in 2019 to \$25,440 million in 2022, while total assets decreased from \$104,500 million in 2019 to \$72,900 million in 2022. This reduction in total debt and assets could be a strategic move to improve financial stability and reduce financial risk (Zaugg, 2021).
3. Total Equity: The total equity of the company has also decreased over the years, which might be attributed to factors such as changes in retained earnings, stock buybacks, or other equity-related transactions.
4. Financial Restructuring: The significant reduction in the D/E ratio from 2018 to 2022 suggests that GSK PLC has undertaken financial restructuring to improve its financial position and reduce its debt burden. This can enhance the company's ability to weather economic downturns and invest in growth opportunities.

The data indicates that GSK PLC has been actively managing its debt levels and working to reduce its financial leverage.

Calculating Efficiency Ratio

Asset turnover ratio is one way of calculating efficiency ratios. On an annual basis, the asset turnover ratio is determined. Since higher ratios suggest that the company is producing more revenue per dollar of assets, the greater the asset turnover ratio, the more effectively the company is functioning.

For businesses in some industries compared to others, the asset turnover ratio is typically higher. For instance, consumer goods and retail have small asset bases but large sales volumes.

Asset Turnover Ratio = Nets Sales/Average Total Assets

Year	Net Sales	Average Total Assets	Asset Turnover Ratio
2018	41,139	73,710	0.56
2019	43,100	1,04,500	0.41
2020	43,783	1,09,603	0.40
2021	46,910	1,06,780	0.44
2022	36,270	72,900	0.50

Key observations:

1. Net Sales Growth: The company's net sales have shown some fluctuations over the years but have generally increased from \$41,139 million in 2018 to \$46,910 million in 2021. However, there was a decline in net sales to \$36,270 million in 2022.
2. Average Total Assets: The average total assets have also experienced fluctuations, with a decrease from \$109,603 million in 2020 to \$72,900 million in 2022.
3. Asset Turnover Ratio: The asset turnover ratio indicates how efficiently GSK PLC uses its assets to generate sales revenue. The ratio has shown a declining trend, moving from 0.56 in 2018 to 0.40 in 2020, before increasing to 0.50 in 2022.

Key insights:

1. **Efficiency in Asset Utilization:** The declining trend in the asset turnover ratio from 2018 to 2020 suggests that GSK PLC's efficiency in utilizing its assets to generate revenue decreased during this period. This might be due to various factors, such as changes in business operations, slower sales growth, or an increase in the company's asset base without corresponding revenue growth.
2. **Recovery in Asset Turnover:** The increase in the asset turnover ratio in 2022 (0.50) compared to the previous two years (0.40 in 2020 and 0.41 in 2019) indicates an improvement in the company's asset utilization efficiency. This could be a positive sign, suggesting that GSK has taken measures to optimize its asset usage and generate higher revenue from the same asset base (Banerjee, 2019).
3. **Further Analysis Needed:** While the data provides a glimpse into the company's asset turnover and sales performance, it's essential to consider other financial metrics, industry trends, and specific business strategies to gain a comprehensive view of GSK PLC's overall financial health and performance.

Overall, the data indicates that GSK PLC has experienced fluctuations in net sales and asset turnover over the years. The recent improvement in the asset turnover ratio might be a positive sign, but a deeper analysis is necessary to understand the underlying factors impacting the company's performance fully.

Major Competitors of GSK

1. **Pfizer Inc. (PFE):** A multinational pharmaceutical company, known for its wide range of products across various therapeutic areas.
2. **AstraZeneca plc (AZN):** Another major pharmaceutical company with a diverse portfolio of drugs, including oncology, cardiovascular, and respiratory medications.
3. **Johnson & Johnson (JNJ):** A global healthcare conglomerate with subsidiaries involved in pharmaceuticals, medical devices, and consumer health products.

Company	Debt-Equity Ratio	Gross Margin	Net Profit Margin	Return on Investment
Pfizer	0.37	65.70%	31.26%	24.37
AstraZeneca	0.76	72%	7.41%	5.48
Johnson & Johnson	0.51	67.25%	18.89%	17.3
GSK	2.08	67%	51%	18.13

Pfizer:

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- Debt-Equity Ratio: 0.37
- Gross Margin: 65.70%
- Net Profit Margin: 31.26%
- Return on Investment: 24.37

AstraZeneca:

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- Debt-Equity Ratio: 0.76
- Gross Margin: 72%
- Net Profit Margin: 7.41%
- Return on Investment: 5.48

Johnson & Johnson:

- Debt-Equity Ratio: 0.51
- Gross Margin: 67.25%
- Net Profit Margin: 18.89%
- Return on Investment: 17.3

GSK:

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- Debt-Equity Ratio: 2.08
- Gross Margin: 67%
- Net Profit Margin: 51%
- Return on Investment: 18.13

1. From the above financial data of GSK and its competitors, the following analysis can be made -

Debt-Equity Ratio: GSK has the highest debt-equity ratio among its competitors (2.08), indicating a higher reliance on debt financing compared to Pfizer (0.37), AstraZeneca (0.76), and Johnson & Johnson (0.51). This suggests that GSK has a relatively higher level of financial leverage and may have higher financial risk compared to its peers.

2. Gross Margin: GSK and Johnson & Johnson have the same gross margin of 67%, while Pfizer has a slightly lower gross margin of 65.70%, and AstraZeneca has the highest gross margin of 72%. A higher gross margin indicates better profitability from sales, and AstraZeneca leads in this aspect (Anika, 2014).
3. Net Profit Margin: GSK stands out with the highest net profit margin of 51% among the competitors. This means GSK retains a significant portion of its revenue as profit after all expenses, making it the most efficient in generating profits (Ahmed, 2013).
4. Return on Investment: Pfizer has the highest ROI of 24.37, followed by Johnson & Johnson (17.3), GSK (18.13), and AstraZeneca (5.48). Pfizer shows strong profitability relative to its investment costs, while AstraZeneca has a comparatively lower ROI.

Key insights:

1. GSK's Strength in Profitability: GSK excels in net profit margin, indicating that the company has been efficient in managing its expenses and generating profits compared to its competitors.
2. Financial Leverage: GSK's relatively ¹¹ high debt-equity ratio indicates higher financial risk compared to its peers, which could be a concern for investors and stakeholders.
3. Gross Margin Comparison: AstraZeneca leads in gross margin, suggesting a competitive advantage in managing production costs and pricing strategies.
4. ROI Variability: The ROI data shows variations among the competitors, with Pfizer having the highest ROI and AstraZeneca having the lowest. This could be due to differences in their business strategies and financial performance.
- 5.

GSK stands out in terms of net profit margin but has a higher debt-equity ratio compared to its competitors, which may present financial risk. Pfizer leads in ROI, while AstraZeneca has the highest gross margin. Each company's financial performance should be assessed in the context.

Recommendations of the company for the future

Some recommendations for improving the financial management of the company:

1. Reduce and Optimize Debt: Given the high debt-equity ratio, a key priority should be reducing the company's debt burden. GSK should focus on optimizing its capital structure, refinancing costly debts, and identifying opportunities to repay debts using excess cash flow. This will result in lower interest expenses and enhance the company's financial flexibility.

2. Implement Efficient Working Capital Management: GSK should adopt effective working capital management practices to streamline cash flows. This involves optimizing inventory levels, extending accounts payable periods without negatively impacting supplier relationships, and shortening accounts receivable cycles. Effective working capital management can free up cash that can be reinvested in growth initiatives or used to reduce debt.

3. Emphasize Research and Development: As the pharmaceutical industry relies on innovation and new product development, GSK should continue investing in research and development to build a robust pipeline of novel drugs and therapies. ³⁰ Successful product launches can drive revenue growth and enhance the company's competitive advantage (Zaugg, 2021).

4. Optimize the Portfolio: Regularly evaluating the product portfolio will help identify underperforming assets and allow GSK to divest non-core businesses or products. This focused approach will enable the company to channel resources into high-growth and high-margin products, ultimately boosting overall profitability.

³⁴ 5. Implement Cost Control and Efficiency Measures: Introducing cost control measures and operational efficiencies will positively impact the company's bottom line. Regular expense reviews can identify areas where costs can be reduced without compromising product quality or employee well-being.

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6. Foster Strategic Partnerships and Collaborations: Forming strategic partnerships or collaborations with other pharmaceutical or healthcare companies can lead to cost-sharing opportunities, increased market access, and access to new technologies or markets.

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7. Strengthen Risk Management: Developing a robust risk management strategy is essential to identify, assess, and mitigate various risks that could impact the company's financial performance. This includes managing market, regulatory, and operational risks effectively (Boisjoly, 2020).

8. Enhance Investor Communication and Transparency: Maintaining transparent and timely communication with investors and stakeholders about the company's financial performance, strategic initiatives, and risk exposure is crucial. Clarity and openness in reporting can instill confidence among investors and attract potential shareholders.

9. Invest in Talent Development and Succession Planning: Focusing on talent development and succession planning will ensure a strong leadership team capable of navigating challenges and driving long-term growth.

10. Integrate Sustainability and Corporate Social Responsibility: Incorporating sustainable practices and corporate social responsibility initiatives into the business model will improve the company's reputation and attract socially conscious investors (Liu *et al.*, 2021). Demonstrating commitment to social and environmental responsibility is increasingly important for businesses.

PART C

1 Net present value (NPV)

It is a financial valuation method used to determine the profitability of investment projects. NPV calculates the present value of expected future cash flows, taking into account inflows and outflows by discounting to the present using the project's cost of capital or required rate of return.

$$NPV = \frac{\text{Cash flow}}{(1 + i)^t} - \text{initial investment}$$

where:

i = Required return or discount rate

t = Number of time periods

NPV strengths:

1. Consider the time value of money.

NPV takes into account the time value of money, allowing you to more accurately assess your return on investment.

2. Comprehensive features for long-term projects:

Suitable for long-term investments as all cash flows are taken into account over the life of the project.

3. A positive NPV indicates added value.

A positive NPV indicates that the project adds value to the business and is financially attractive.

NPV Limits:

1. Advanced estimates of future cash flows:

NPV requires accurate estimates of future cash flows, which can be difficult, especially for long-term projects.

2. Sensitivity to discount rate:

Choosing the right interest rate is important because the discount rate you choose has a large impact on the NPV.

3. Misleading comparison:

Comparing NPVs across projects with different investment sizes, he said, can be misleading, as larger investments can lead to higher cash flows and higher NPVs.

1

Internal rate of return (IRR)

IRR is basically the discount rate at which his NPV of an investment becomes zero. It represents the rate at which the present value of cash inflows equals the present value of cash outflows.

$$0 = NPV = \sum_{t=1}^T \frac{C_t}{(1 + IRR)^t} - C_0$$

where:

C_t = Net cash inflow during the period t

C_0 = Total initial investment costs

IRR = The internal rate of return

t = The number of time periods

Strengths of IRR:

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1. Consider the time value of money.

7

Like NPV, IRR considers the time value of money and provides a measure of the annual profit of a project.

2. Simple Interpretation:

1

An IRR greater than the cost of capital indicates a positive return on capital. 3. Easier to compare.

IRR provides a single percentage value so you can easily compare different projects.

IRR Limits:

1. Multiple IRRs in complex cash flows:

Complex cash flow patterns can result in multiple IRRs that can be confusing to interpret.

2. Unrealistic assumptions:

7

IRR assumes that preliminary cash flows will be reinvested in IRR, which may not be realistic in practice.

3. Incorrect ranking of mutually exclusive projects:

IRR can lead to inaccurate rankings when comparing mutually exclusive projects, especially if the cash flow patterns of the projects are very different.

Payback period

¹ Payback period is an investment valuation method that measures the time it takes for a capital project to recover its original costs through expected cash inflows.

Payback period strengths:

¹ 1. Simplicity:

The payback period is easy to calculate and understand, allowing non-financial professionals to quickly make an initial evaluation of an investment project.

2. Risk assessment:

¹ It helps you assess the risk involved in investing by showing how quickly your initial capital will be recovered. A shorter payback period generally indicates a lower risk.

3. Liquidity Considerations:

It is especially useful for projects where rapid payback is critical, such as cash tight projects or projects where cash flow timing is critical.

Collection time constraints:

³³ 1. The term “payback period” ignores cash flows beyond the initial payback period of the investment and the long-term viability of the project. ¹⁷ 2. The time value of money is not taken into account because cash flows are treated the same over different periods, resulting in an imperfect return on investment assessment. ¹ 3. The payback period provides no insight into the overall value or profitability of the investment beyond the initial payback period, and may overlook more profitable long-term projects.

Effectiveness in various investment scenarios:

The payback period is most effective in the following investment scenarios:

1. Short term project:

It is useful for relatively short-term projects with high return on investment, especially operational efficiency projects or projects with short payback requirements.

2. Limited capital:

We help you prioritize projects that can quickly recoup your initial investment, freeing up funds for other opportunities.

3. Low risk projects:

Helps identify low-risk projects where rapid return on capital provides financial security.

However, the payback period impact is limited in the following scenarios:

1. Long-term projects:

It is not effective for projects with increased cash flow streams, ignoring long-term profitability and overall value.

2. Irregular cash flow:

Projects with erratic or uneven cash flows are less effective, as long as consistent annual cash flow is achieved.

3. High-risk projects:

It does not take into account the risks associated with future cash flows and cannot take into account changes in expected returns.

Accounting Revenue (ARR)

ARR measures investment return based on the book value return on the original investment.

Expressed as a percentage and relatively easy to calculate, it helps in quick assessment.

However, this ignores the time value of money and limits your ability to get a complete picture of your return on investment.

$$ARR = (Average Annual Accounting Profit / Initial Investment) * 100$$

ARR strengths:

1. Simplicity:

Using readily available accounting information from financial reports makes it easier to calculate and understand.

2. Intimacy:

Many investors and managers prefer financial accounting standards, and ARR uses book earnings to value investments.

3. Quick screening:

It serves as an initial screening tool for assessing investment profitability and selecting potential projects. ARR Limits:

1. If you don't have ¹⁷ the time value of money:

¹ The time value of money is not taken into account, leading to inaccurate profitability assessments, especially for long-term projects.

2. Ignore cash flow timing.

The reliance on book earnings may not match the actual timing of cash flows and may lead to overly optimistic views of profitability.

3. Ignore non-cash items.

Focuses only on accounting profit and ignores non-cash items such as depreciation and working capital fluctuations that can affect cash flow.

4. Rely on accounting information.

¹ Variations may occur due to accounting principles and estimates by different organizations and industries.

Effectiveness in various investment scenarios:

¹ ARR is most effective when evaluating simple short-term projects with steady and predictable cash flows where time value of money is not a key consideration. This is also useful when determining an appropriate discount rate is difficult with more complex methods such as NPV or IRR.

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Assignment

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