FINANCIAL PERFORMANCE OF JOHNSON & JOHNSON AND ROCHE IN US: A COMPARATIVE ANALYSIS

Dissertation Submitted to

The IIHMR University, Jaipur

for the partial fulfillment for the award of the degree of

Master of Business Administration (MBA)

In Hospital and Health Management

by

Sanchi Bhasin

Under the Supervision and Guidance of

Dr. S.D. Gupta

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DECLARATION BY STUDENT

I hereby declare that this dissertation titled is the bonafide record of my original research work. I declare that it has not been submitted to any other university or institution for the award of any degree or diploma. Information derived from the published or unpublished work of others has been duly acknowledged in the text.

(Signature)

Name of Student

Sanchi Bhasin

Date: 25th June 2021

CERTIFICATE

This is to certify that Sanchi Bhasin in partial fulfillment of the requirements for the award of the degree of MBA (Hospital and Health Management) from the IIHMR University, Jaipur has successfully completed her/his internship at ZS Associates during January 18, 2021 to March 15, 2021.

Mr. Sanjay Joshi

ZS Associates

Preceptor/Head of the Organization
Name of the organization

Place: New Delhi

Date: 26th june 2021

CERTIFICATE

This is to certify that dissertation titled Financial Performance of Johnson & Johnson and Roche in US: A comparative analysis is a record of the research

work undertaken by Sanchi Bhasin in partial fulfillment of the requirements for the award of the degree of MBA (Hospital and Health Management) from the IIHMR University, Jaipur under my guidance and supervision and his/her approach to the research study has been sincere, scientific, and analytical.

Faculty Guide- Dr. S.D. Gupta
IIHMR University, Jaipur

Date: 29 June, 2021

School Dean- Dr. Dhirendra Kumar
IIHMR University, Jaipur

Date: 29 June, 2021

Abstract

The pharmaceutical market is an extremely competitive and booming sector. To gauge competition and compare different companies, financial metrics such as ratios can be used to evaluate the performance of different entities within the sector. Such an analysis helps key stakeholders: investors, end users and the company itself. This study focuses on two of the major players in pharmaceutical industry: Johnson & Johnson and Roche in US. The objective is to evaluate them based on financial ratios to make better financial decisions and understand different strategies by the companies through their financials. The analysis is done using the company's financial reports, 10k filings and analyst reports. A ratio analysis was done to examine parameters such as liquidity, profitability, solvency, asset management and market value. From the study it was seen that Roche performed better than Johnson & Johnson on most parameters despite being a smaller firm in terms of market capitalization. On closer look at the strategy however, Roche maybe a better investment with a lower stock value delivering high returns but in far sight owing the higher benefits vs the risk and opportunities in store, Johnson & Johnson would be a better choice despite the stock being over-valued.

Key words used: Ratio analysis for pharmaceutical companies, Financial statement analysis, Roche, Johnson & Johnson

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Financial Performance Of Johnson & Johnson And Roche In US: A Comparative Analysis

1. Introduction

The quantitative interpretation of a company's financial performance is called ratio analysis. It gives useful information on the profitability, solvency, operational efficiency, and liquidity positions of the business, as reflected by the financial statements.

When comparing, a single ratio isn't enough. Several ratios must be examined together and compared to previous year's ratios, or even to other companies in the same industry.

1.1 Time series or Trend Analysis

It is a method of evaluating trends over time by determining percentage increases or declines in comparison to a base year

1.2 Cross sectional Analysis

This helps in comparing two firms at a single point in time like a cross sectional study

1.3 Industry Analysis

The purpose of industry analysis is to evaluate and assess a company's health and performance in contrast to its industry.

1.4 Financial Ratio Analysis

It entails going over existing data. It can be used to provide managers the information they need to make crucial and useful decisions. A company's goals and objectives rely on these. It entails analyzing financial statements in order to comprehend information that is important for management decisions.

Financial statement analysis is necessary for determining trends and correlations among financial statement items. Internal and external (analysts, creditors, and investors) evaluation of the financial statements is done

1.5 Building blocks of Financial Ratio analysis

1.5.1 Liquidity

The firm's ability to meet its immediate obligations

1. **Current Ratio**
   Indicator of a company's capacity to meet short-term obligations with short-term assets; how much of current assets are available to cover each dollar of current liabilities
2. **Acid-Test Ratio (Quick Ratio)**
   The quick ratio measures a company's capacity to pay down current creditors without relying on inventory sales.

1.5.2 Solvency

The firm's ability to meet its long-term obligations

1. **Debt ratio**
   Creditors contribute what percentage of a company's assets.
2. **Equity Ratio**
   This ratio determines how much of a company's assets are donated by its shareholders.
3. **Debt / Equity ratio**:
   The protection provided to secured creditors is measured by this ratio.
4. **Times Interest Earned (Interest Coverage Ratio**)
   This is the most frequent metric for determining a company's ability to protect its long-term creditors.

1.5.3 Profitability

1. **Net profit margins**

This metric measures a company's capacity to generate a profit from sales.

2. **Gross Margin (Gross Profit Ratio)**

   After accounting for cost of goods sold, this ratio determines how much money is left over from sales to pay operational expenditures and profit

3. **Return on Total Assets**

   This ratio is widely regarded as the most accurate overall indicator of a company's profitability.

4. **Return on Common Stockholders' Equity**

   This metric reveals how effectively the company used the owners' money to generate revenue.

1.5.4 Market Value

1. **Price-Earnings Ratio**

   Investors frequently use this metric as a broad guideline for determining stock values. In general, the higher the price-to-earnings ratio, the more growth potential a company has.

2. **Basic Earnings per Share**

   This metric shows how much money was made for each outstanding share of common stock.

1.5.5 Asset Management

1. **Accounts receivable Turnover**

   This figure indicates how many times a company's receivables are converted into cash per year.

2. **Total Asset Turnover**

   This metric assesses how effective assets are at generating revenue.

1.6 Understanding the financial performance of pharmaceutical companies

Pharmaceuticals have long been one of the market's best performers. They've grown even more crucial after the outbreak of COVID-19. Investors looking to invest in the top pharmaceutical firm are frequently faced with a plethora of options. Off late, two companies namely in particular, Johnson & Johnson and Roche, have been leading the race in this market. With a constant battle of pushing the first vaccine out and finding a solution to end the pandemic, understanding the financial performance of these companies gives a bird's eye view of the performance and the future promises of the company. This research benefits all three important stakeholders: the company, potential and existing investors, and the end user.

1.7 About the companies

Johnson & Johnson

Johnson & Johnson (J&J) is a multinational firm based in the United States that creates medical equipment, pharmaceuticals, and consumer packaged goods. It was founded in 1886. Johnson & Johnson is one of the most valuable firms in the world.

Roche

Roche is a healthcare research and development firm. Diagnostics and Pharmaceuticals are the two segments in which it operates. Oncology, immunology, ophthalmology, infectious disorders, and neurology are among the areas where pharmaceuticals are developed. The Diagnostic section relates to disease diagnosis using in vitro diagnostics. Fritz Hoffmann-La Roche started the corporation on October 1, 1896, and it is headquartered in Basel, Switzerland.

1.8 Rationale

Johnson & Johnson and Roche have been selected as they have consistently maintained their position among the top pharmaceutical companies globally. They have often been pitted against each other as competitors. The goal of this research is to examine the financial statements of these prominent pharmaceutical businesses during the last five years in order to acquire a better understanding of how to make better business decisions.

The ratios used in this research were chosen to focus on the company's and industry's financial developments.

2. Objectives

2.1. To compare the financial performance of Johnson and Johnson and Roche over five years (2016-2020) related to

i. Liquidity Ratios
ii. Profitability ratios
iii. Debt coverage ratios
iv. Asset management ratios
v. Market Value ratios

2.2.To understand the strategic options applied by the company from it's financials

3. Literature Review

An extensive review of literature has pointed out that financial performance evaluation is of essence in order to evaluate effienct resource allocation and utilization.

Gopinathan Thachappilly (2009), in his article discusses about the Financial Ratio Analysis for Performance evaluation. Its analysis is typically done to make sense of the massive amount of numbers presented in company financial statements. It helps evaluate the performance of a company, so that investors can decide whether to invest in that company. Here we are looking at the different ratio categories in separate articles on different aspects of performance such as profitability ratios, liquidity ratios, debt ratios, performance ratios, investment evaluation ratios. [1]

Chin--Feng (2005) [2] in his article mentions that financial ratios are the simplest tools for evaluating the financial performance of the firm.

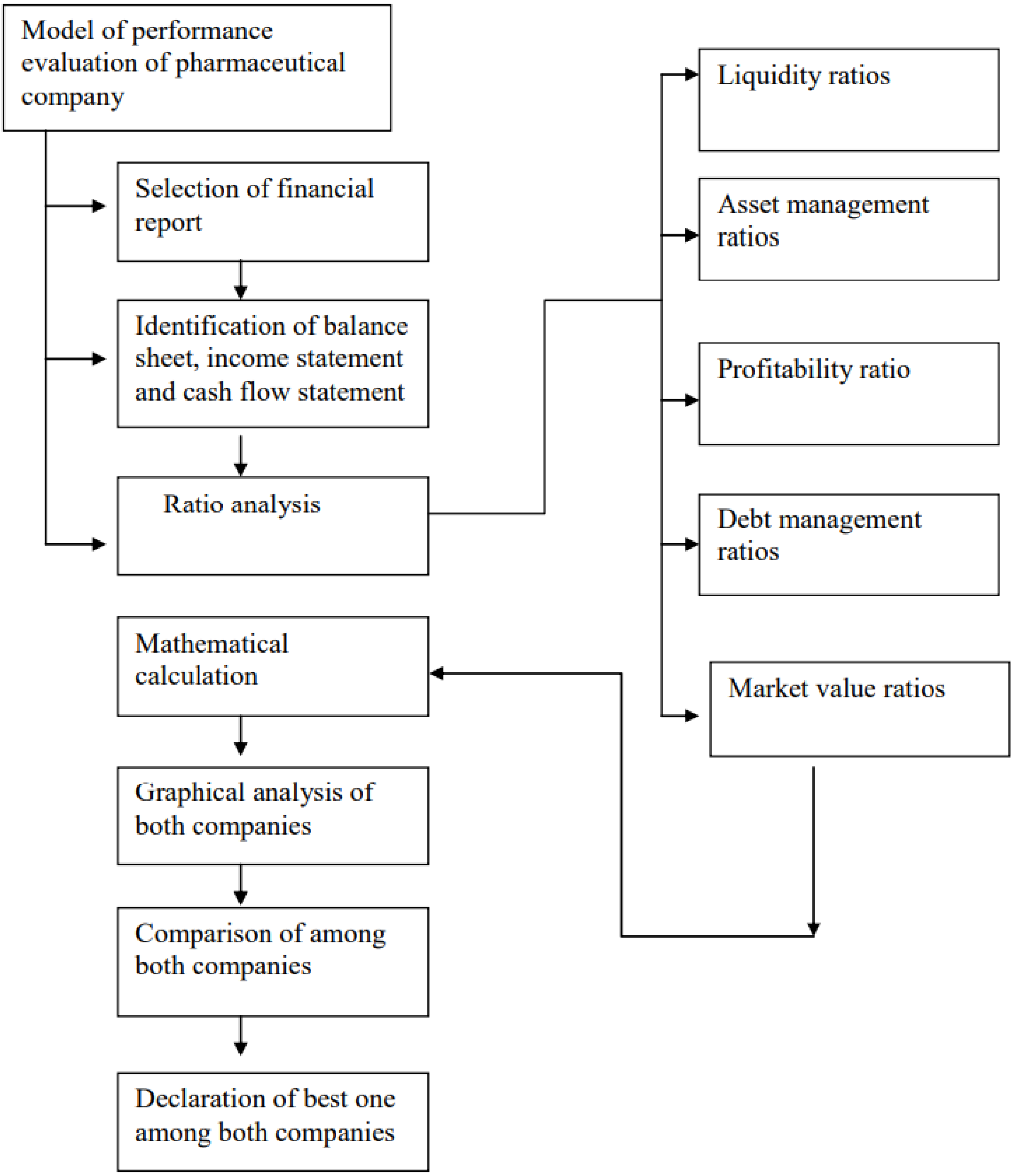
Ashok Kumar (2019) [3] in his paper stated that evaluation of a firm's performance and operations; it is the analysis of the financial statement of an enterprise. The analysis of financial statement can be best done by various yardsticks of which, the important is known as ratio or percentage analysis. Ratio is a numerical or an arithmetical relation between two figures. It is expressed when one figure is divided by another. Accounting ratios show inter-relationship which exist among various accounting data. Accounting ratio can be expressed in various ways such as, a pure ratio, a rate or a percentage. Ratio analysis is certainly a very admirable device because it is simple, and it has a predictive value. Management and other users thus, rely substantially on the financial ratios based on accounting data for making assessments and predictions of past performance, present position and probable future potentials. One important way for diagnosing the financial health is to measure the profitability, liquidity, activity and solvency and the level of the bankruptcy of enterprise.

A study published by Sejal Purabiya (2020) [4] highlights the importance of understanding the financial performance of pharmaceutical companies specially in time like that of COVID-19. It cites how this analysis assists in understanding the financial history of the industry in terms of strengths and weaknesses in order to cope with the unfavorable COVID 19 situation.

4. Methodology

- **Study design**
  To identify pharmaceutical firms and acquire secondary data on their financial performance in order to construct financial ratios, a cross sectional descriptive study methodology was adopted.
- **Data collection**
  Secondary data was gathered using a systematic approach. A search string involving "Ratio analysis for pharmaceutical companies, Financial statement analysis + Roche + Johnson & Johnson" was done.
  Articles, financial fact sheets, journals, analyst and business reports, and other sources were mostly used to do the research.
- **Sample design**
  The top two performing pharmaceutical businesses from the top five global pharmaceutical companies were chosen using a judgement sampling technique.
- **Duration of the study**
  April 2019 to June 2019 (Three months)
- **Sources of secondary data**
  i. Balance sheets
  ii. Income statement
  iii. Cash flow
  iv. Annual reports, 10K filing
  v. Company website
  vi. Analyst report

Model for financial performance evaluation



5. Ratios Used for Analysis

- Current Ratio = Current assets /Current liabilities
- Quick Ratio= (Current Assets-Inventories)/Current Liabilities
- Accounts receivable turnover = Sales / Accounts receivable
- Accounts Payable turnover = Sales / Accounts Payable
- Net Profit margin = Net profit after tax/sales
- Gross Profit margin=Gross profit/sales
- Return on Total Assets =Net profits after taxes / total assets
- Return on common stock equity = Net income /stockholders' equity
- Debt Ratio =Total liabilities / Total assets
- Book value per share = Common stockholder's equity / Outstanding shares

6. Data analysis and results

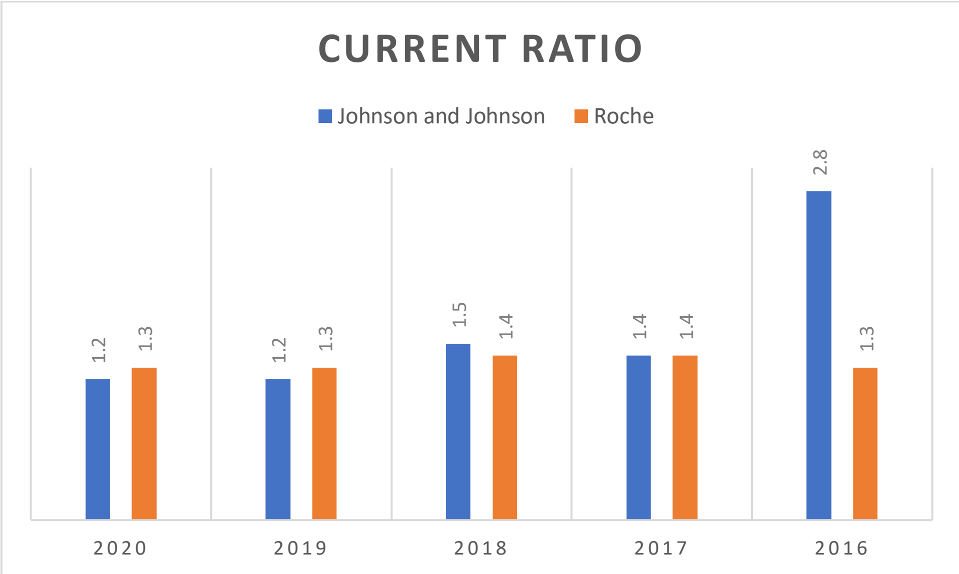
Competitor analysis- criteria for selecting this companies

Organization	(Market capitalization in millions)
Johnson & Johnson	**$435.77 Billion**
Roche	**$287.85 Billion**
Pfizer	**$220.56 Billion**
Abbott	**$213.19 Billion**
AbbVie	**$202.25 Billion**

Top two performers from this list were chosen: Johnson & Johnson and Roche

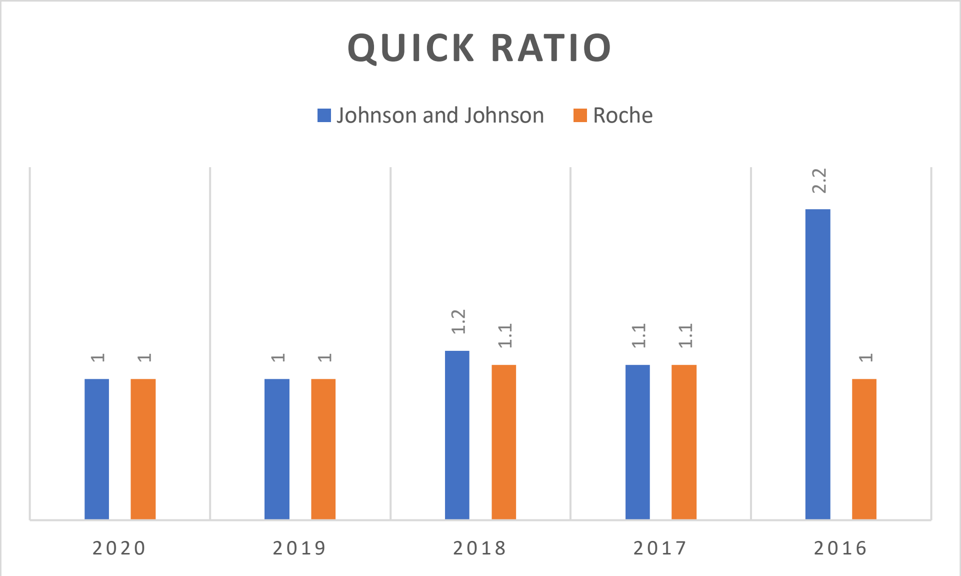
7. Results of the analysis

Current ratio



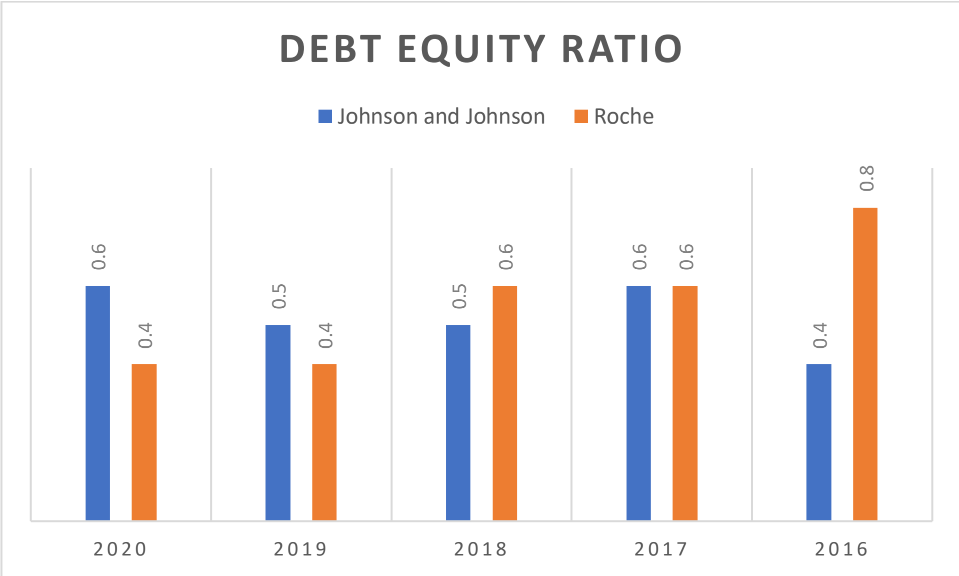
- The current ratio is a prediction of a company's ability to pay down short-term debts.
- On an average, Roche has shown consistency in terms of working capital to meet current liabilities. However, Johnson & Johnson has demonstrated a downward tendency in recent years.
- The downward trend with Johnson and Johnson maybe attributed to a dip in sales in the medical devices vertical. The drop from 2016 is attributed to it’s acquisition of Actelion Ltd. for $30 billion in cash, which isn’t entirely negative as this has proven to be good investment for Johnson & Johnson.
- Both companies in this aspect are almost at par with each other and the industry average

Quick ratio



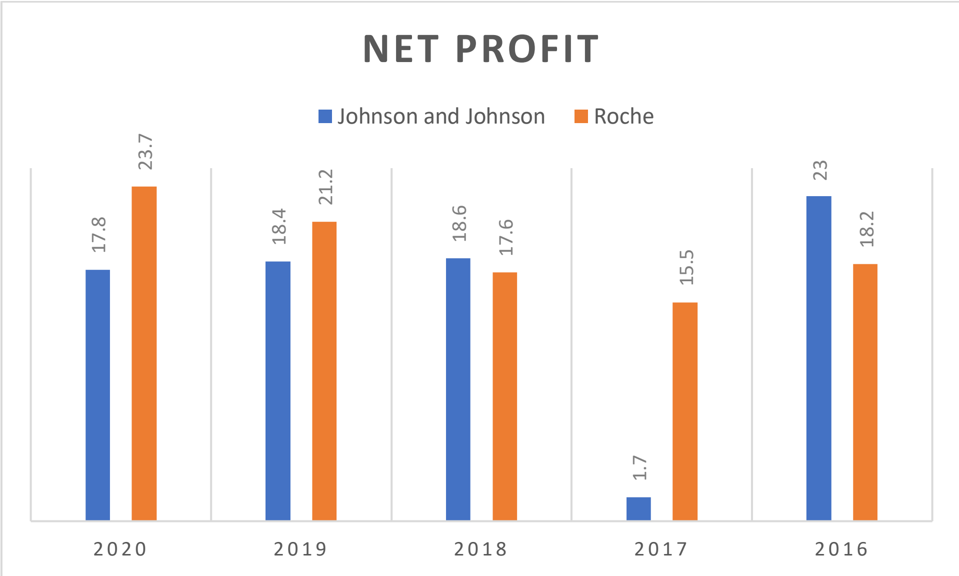
- The quick ratio measures a company's means to pay down current obligations without relying on inventory sales.
- Johnson & Johnson has demonstrated a downward trend over the years, whereas Roche has remained consistent across ups and downs, making Roche a better overall investment decision.

Debt Equity Ratio



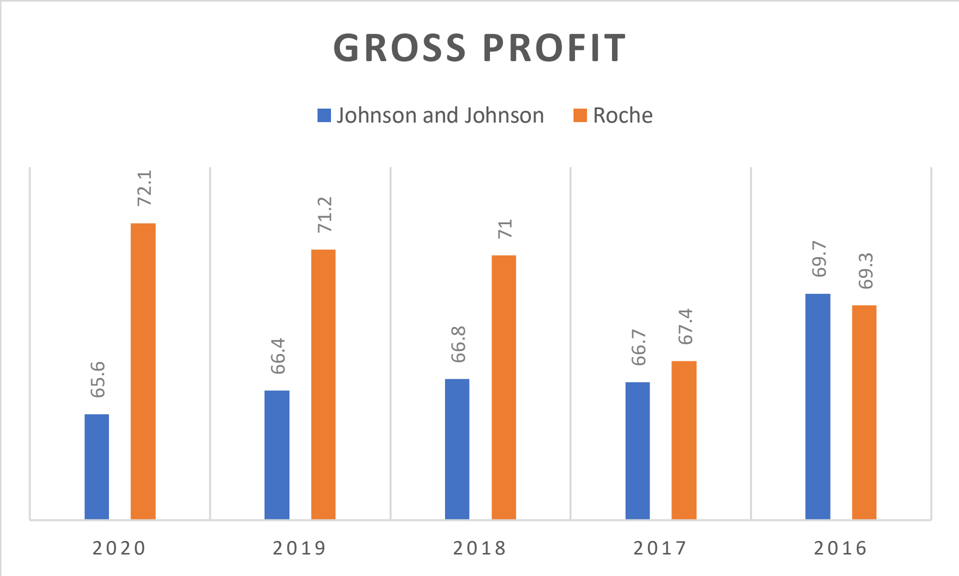
- From 2017 to 2019, Johnson & Johnson's debt-to-equity ratio improved, but from 2019 to 2020, it deteriorated dramatically.
- Roche has shown improvement in its Debt equity ratio over the years
- Although both are below the industry average. A high debt-equity ratio may be good if it is well below the industry average, which is the case here. This also prompts that the company is aggressively financing it's growth. In this case Johnson & Johnson, although it has a high debt ratio, it has enough capital to meet all it's obligations.
- In this case although Roche would seem a more appropriate choice, Johnson & Johnson strategically is better.

Net profit



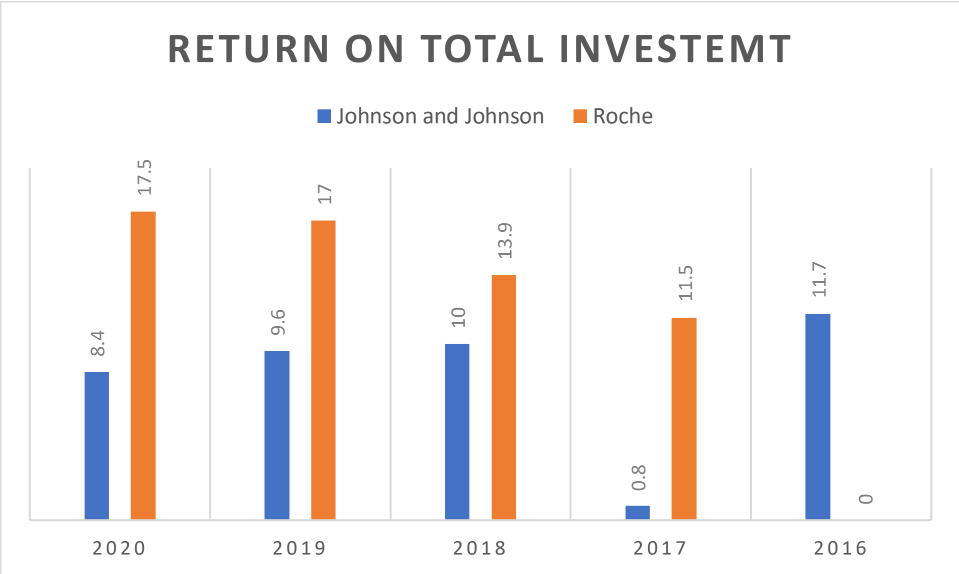
- Johnson and Johnson’s net profit has deteriorated from 2018 to 2020 despite it announcing the manufacture of COVID-19 vaccines. It an be attributed to declining sales it’s consumer segment and increase in Research and development costs.
- Roche on the other hand has shown consistent increase in the net profits making it a better investment option
- Roche in comparison to the industry average has been performing much better than Johnson and Johnson.

Gross profit



- Roche has seen an increase in gross profit over the years whereas Johnson and Johnson has shown a consistent decline in profits over the years.
- Roche has been performing well above the industry average whereas Johnson and Johnson has been at par with the industry trends

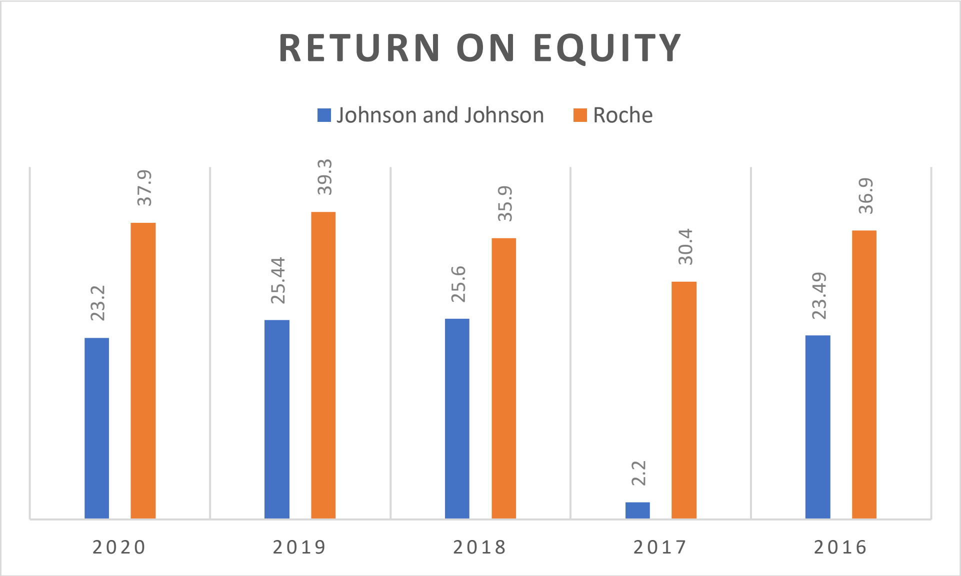
Return on Total Investment



- Roche has seen an increase in return on investments over the years whereas Johnson and Johnson has shown a consistent decline over the years.

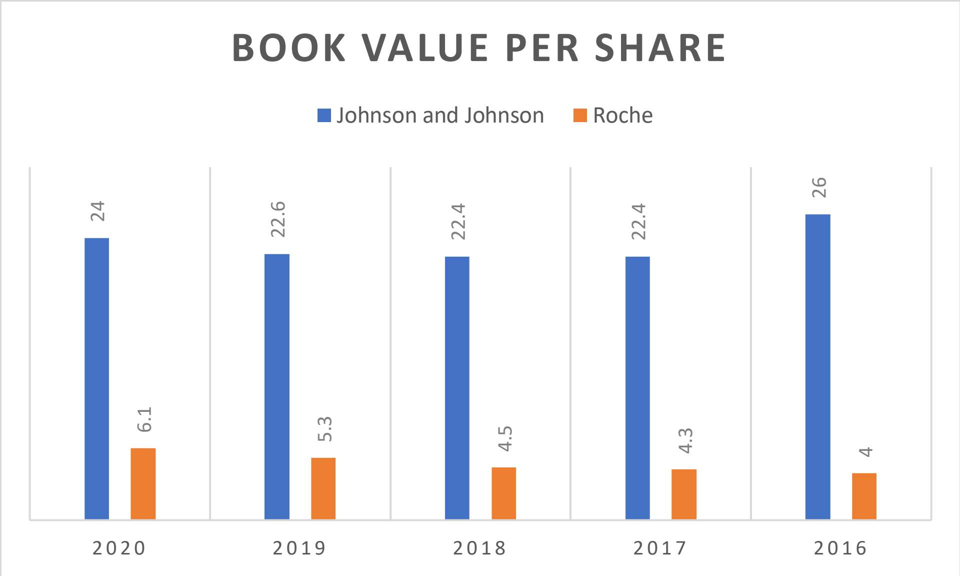
- Roche has been performing well above the industry average whereas Johnson and Johnson has been at par with the industry trends
- Roche is thus a better bet to invest than Johnson and Johnson

Return on Equity



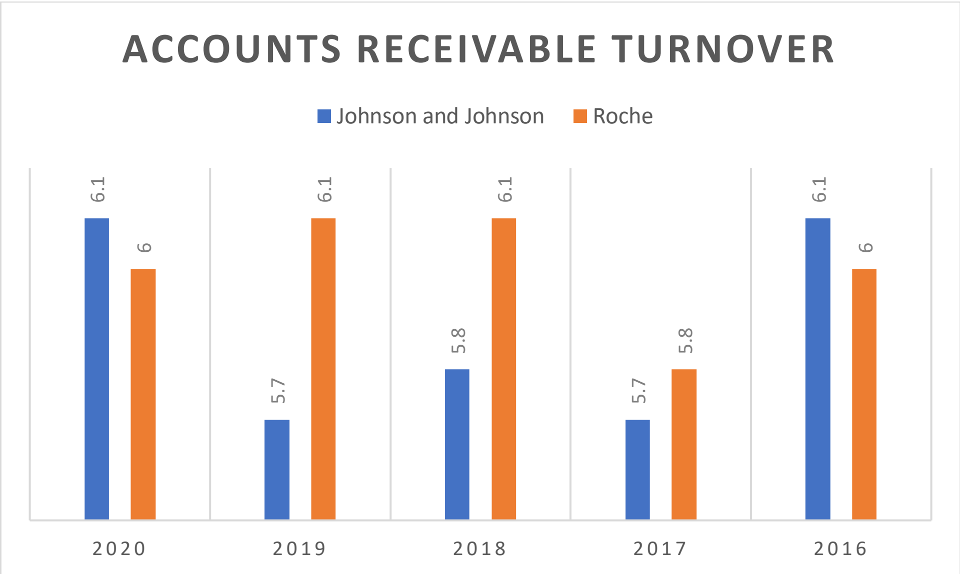
- Roche has seen an increase in ROE over the years whereas Johnson and Johnson has shown a consistent decline over the years.
- Roche has been performing well above the industry average whereas Johnson and Johnson has been at par or below the industry trends
- Roche is thus a better bet to invest than Johnson and Johnson

Book value per share



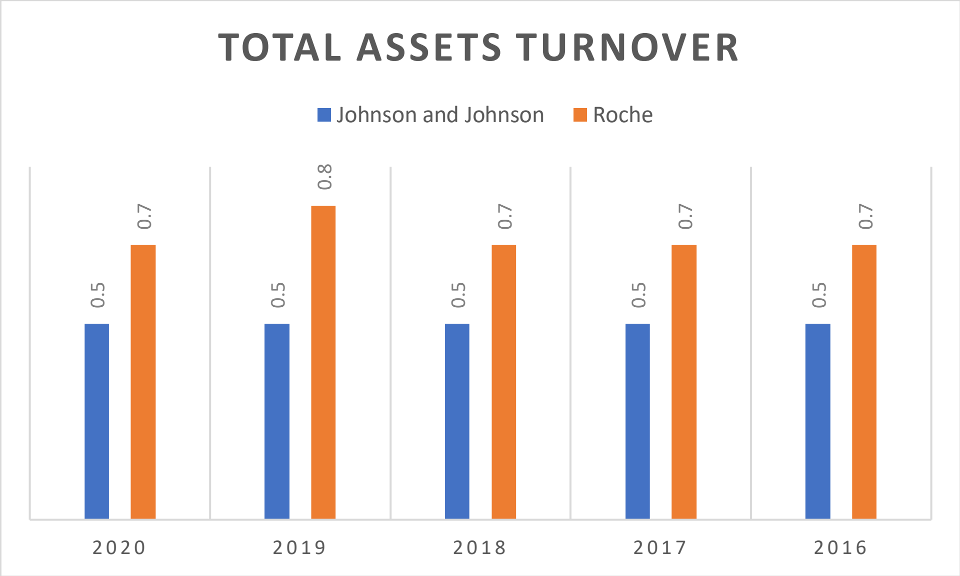
- Very high book value per share despite declining profits depicts a share that maybe overvalued.
- A high book value per share is desirable which is the case with Roche, but a Johnson and Johnson book value is inflated when compared to the overall performance of the company.

Accounts Receivable Turnover



- Johnson and Johnson despite showing a decline from 2018 showed an improvement in 2020. Roche on the other hand due to the pandemic did work in tandem with the industry trends making Johnson and Johnson a better choice here.

Total Assets Turnover



- Roche was experiencing an upward trend in the total assets' turnover up till the pandemic.
- Johnson and Johnson on the other hand has shown consistency in efficiently generating sales from its assets.
- Johnson and Johnson here is a better investment than Roche

8. Discussion

Roche has seen an increase in profits over the years which was largely led by it's immunology and neuroscience products. Drugs like Xolair and Actmera drove sales for Roche in 2016 but Ocrevus launch in 2017 became the best drug launch gathering >$3.5 billion in sales in 2019. This is seen as the increase in profits in 2018. The revenue source in 2020 was the temporary increase in molecular testing for Covid-19. In the long run however, Roche's current portfolio sees a looming threat from biosimilars and patent expiry for some of it's products. The company's acquisition plans are mostly around budding stage innovative bio-tech organizations. The play out would depend on choosing the right portfolio drugs.

Both the companies have been increasing their spending on research & development for new products, Johnson & Johnson's pipeline has shown greater promise with more number of approved products than Roche.

The Johnson & Johnson stock maybe over-valued at present but it's newly launched drugs- Imbruvica, Darzalex, and Stelara are swiftly gaining market share showing future promise. On closer observation it was seen that the company did manage to cut down on its operating expenses but the slip in revenue was faster than the increase. This also suggests the company's investment growth to derive sales. Despite this, the company's launch of Covid-19 vaccine, a promising portfolio and an efficient supply chain network depicts a future promise of being a good investment.

9. Conclusion

Johnson & Johnson has seen a decline in overall sales in the last few years but is still a valued company in the eyes of the investor due to the vast market offerings and previous performance. Pharmaceuticals was the only vertical that was in profits for J&J in 2020. Despite slipping profits the company did continue investing in research and development specially for its COVID-19 vaccine. From a future standpoint the company's pipeline is expected to gain momentum and drive sales for J&J.

Roche on the other hand due to its aggressive and upcoming oncology and diagnostic line has shown consistency in terms of growth and increasing revenue. It continued to sustain and ward off the damage from the pandemic by capturing the COVID-19 diagnostic market. Yet from a strategy standpoint this revenue growth maybe short-lived unless Roche considers diversifying it's present offerings.

Over all, in near term, Roche maybe a better investment with a lower stock value delivering high returns but in far sight owing the high benefits over risk and key opportunities, Johnson & Johnson would be a better choice despite the stock being overvalued.

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