

# GlaxoSmithKline

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ANNUAL REPORT 2018

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The global pharmaceutical industry was worth \$ 1 trillion in 2014 and \$1.2 trillion in 2018. [1] With the advent of technological innovation in healthcare it is expected that the industry could reach \$1.5 trillion by 2023. Breakthrough innovations in the field of bioscience have led to an upward trend for pharmaceutical companies. Biotechnology has introduced various vaccines and medication for the treatment of major infections like HIV and certain types of cancer.

One of the players in the global pharmaceutical industry that has revolutionized the biomedical industry is GlaxoSmithKline plc most widely known as GSK. GSK is a British multinational pharmaceutical company based in Brentford, London. GSK started as a merger of two companies Glaxo Wellcome and SmithKline Beecham.

In 1873 Joseph Nathan and Co. were established as a general trading company in New Zealand. They started to produce dried milk baby food from excess milk creating a product called Defiance, then as Glaxo. Later, Glaxo Laboratories was incorporated as a separate subsidiary in 1935 in London. Joseph Nathan the majority shareholder restructured the company by making Glaxo the parent company and made the company public on the London Stock Exchange. Followed by the acquisition of Allen & Hansbury in 1958 a reputed British pharmaceutical company, Glaxo bought Meyer Laboratories in 1978. Glaxo had established a strong foothold in the pharmaceutical industry following the acquisitions.

Burroughs Wellcome & Company was established by two American pharmacists Henry Wellcome and Silas Burroughs in London in 1935. In 1920, Burroughs Wellcome opened research and manufacturing in the United States. The scientists at Burroughs made breakthrough innovations in drugs that are still being used in today's world. In 1995, Glaxo and

Burroughs merged together to form Glaxo Wellcome plc. Glaxo Wellcome laid off 10000 jobs worldwide to restructure its Research and Development division. Following that year, Glaxo Wellcome acquired Affymax, who were experts in combinatorial chemistry.

By 1999, Glaxo Wellcome had become the third-largest pharmaceutical company revenue-wise. Its products included Imigran (treatment of migraines), salbutamol (Ventolin)(for treatment of Asthma), Zovirax(for treatment of cold sores), and Retrovir and Epivir (for treatment of AIDS). The company had become the largest manufacturer of drugs for HIV/AIDS and Asthma. The company had a workforce of 59,000 which comprised 13400 people in the UK, 76 operating companies and 50 manufacturing facilities worldwide. Their seven of its products were among the world's 50 top-selling pharmaceuticals. They had established their R&D centers in Hertfordshire, Kent, London and Verona in Italy, and manufacturing plants in Scotland and North England. They had expanded themselves across the globe in the US, Japan, Europe, and the Far East.

SmithKline Beecham was a company formed as a merger of SmithKline & French and Beckman Inc to form SmithKline Beckham Inc which in 1989 change to SmithKline Beecham Inc. SmithKline Beecham's story started when Thomas Beecham in 1848 launched Beecham's Pills laxative in England giving birth to the Beecham Group. In 1860, Beecham was widely involved in pharmaceutical and consumer products like such as Macleans toothpaste, Lucozade and synthetic penicillin research. John K. Smith had opened his first pharmacy store in Philadelphia in 1830. After 35 years, Mahlon Kline joined the business which after 10 years the company was named to Smith, Kline & Co. Again, after a merger with French, Richard and Company, in 1929 the company's name was changed to Smith Kline & French Laboratories as their primary focus

of the business was more on research. Later they made two acquisitions Norden laboratories and Recherche et Industrie Thérapeutiques in Belgium to change their focus of business operation to vaccines. As a part of expanding the company's portfolio, Smith Kline & French Laboratories purchased seven laboratories across the US and Canada in 1969. In 1982, they bought Allergan to establish their business in eye and skincare products. In 1995 SmithKline & French and Backman Inc merger took place to form a new organization, SmithKline Beecham.

In 2000, Glaxo Wellcome and SmithKline Beecham announced a merger in January to form GlaxoSmithKline. The merger was completed in the following December. The global headquarters is based in Brentford, London. Since the year 2001 to 2010 GSK has made significant progress in the pharmaceutical industry with a series of acquisitions and establishing a strong foothold in the vaccines sector. Has completed a series of acquisitions like New-Jersey base Block Drug for \$1.24 billion in 2001. IN GSK acquired CNS Inc who manufactures products like Breathe Right nasal strips and FiberChoice dietary supplements. In 2009, GSK acquired Steifel Laboratories the world's largest dermatology company for \$3.6 billion US dollars. In 2009, the FDA approved GSK's vaccine for treating H1N1(Swine flu) influenza protection. GSK has also made collaboration with Pfizer for HIV research through ViiV Healthcare. Followed by that GSK also made the acquisition of an Argentine pharmaceutical company Laboratorios Phoenix and UK-based company Maxinutrition.

Since 2011, GSK has heavily in its own companies to expand horizons to the international markets. In the year 2012 GSK made significant investments in its manufacturing facilities in England. In 2014 GSK raise around \$1 billion in its Indian pharmaceutical unit, GlaxoSmithKline Pharmaceuticals to 75% to focus more on the merging markets. IN the same

year GSK and Novartis agreed on a deal worth more than \$20 billion dollars, where Novartis sold its vaccines division to GSK and in return buying GSK's cancer division. GSK in the coming years invested in many companies like GlycoVaxyn, Banaja KSA Holdings Company, and Tesaro. In 2018, GSK planned a buyout of a 36.5% stake in their joint venture with Novartis for \$13 billion. This acquisition was an initiative with breaking up that would spin-off the company's Consumer division. Last year December, GSK announced it was creating a joint venture with Pfizer to combine their consumer healthcare division with a 68:32 partnership, where 32% will be owned by Pfizer.

GSK has its business separated into three main divisions: Vaccines, Consumer Healthcare and Pharmaceuticals Products. GlaxoSmithKline's mission is "to help people so more, feel better, live longer". They have made it a mission to serve the people by making innovations in the healthcare field. Meet their mission statement GlaxoSmithKline invests heavily in its research and development division. GSK has a robust strategic business model that aims to increase growth, reduce risk and enhance its long-term financial performance. They prioritize growing a diversified global business, deliver more products of value and simplify their operating model. As a part of its priorities to diversify the business, GSK has acquired Novartis's vaccine business and combined its Consumer Healthcare business to create a new joint venture. 40% of the group's revenue is from outside the USA and Europe. GSK has also introduced new products in 2014 and established 40 new molecular entities in phase II and phase III. As a part of the third priority, they are striving to reduce complexity in their business and become more efficient. As a result, they have freed up most of their resources so that they can invest them elsewhere. They have made an annual savings of 3.5 billion pounds since 2008. GSK also strives

for conducting responsible business. They make sure their values are embedded in their culture and decision making which makes them closer to society's expectations.

GSK is not only a big player in the pharmaceutical industry. Companies like Johnson & Johnson, Pfizer, Novartis, Merck, Hoffman-La Roche, and Sanofi are the big names in the industries (Refer chart at the bottom for comparison of GSK in relation to its competitors). If we compare the market capitals of these mammoth pharmaceutical companies, Johnson & Johnson stands in the first place with a market capitalization of US\$369 billion followed by Hoffman-La Roche with an incredible number of US\$265 billion and Novartis at US\$233 billion. GSK currently stands fourth on the podium worth with an overall market capitalization of US\$277 billion.

The financial statements are prepared in accordance with IFRS. Coming to their Income statement GSK has had significant growth in its Revenue from the years 2016 to 2018. GSK's revenue in 2016 was 27.8 billion GBP which increased to 30.1 billion GBP in 2017 and a slight increase to 30.8 billion GBP. Growth between 2017 and 2018 was 2%. Over the years the turnover had steady growth for GSK. Breaking down the revenue of 2018, the Pharmaceutical division had the majority contribution towards the turnover with revenue of 17.3 billion GBP. Compared to last year the Pharmaceutical sector had a flat growth rate. Sales were primarily driven by the growth in HIV sales and Respiratory products, Nucalla and Ellipta portfolio. This was compensated by a lower sale of Seretide/Advair and Established Pharmaceuticals. Vaccines resulted in a total of 5.9 billion GBP which is a 14% increase from the last years. Vaccines sales were driven by Shingrix (for Shingles) and influenza and the Hepatitis vaccine. Consumer healthcare sales, on the other hand, declined by 1%. Consumer Healthcare division had a

cumulative turnover of 7.7 billion GBP. Consumer healthcare division has a strong share in the international markets compared to the vaccines. Internationally the highest revenue of GSK comes from the US market. There was a 6% growth compared to 2017. A significant market share comes from the International and Europe market. From the Income Statement, we can also infer that in 2018 GSK has lowered the R&D expenses compared to 2017 which has positively affected the Operating Profit (34% increase). But if we have a look at the Profit after taxation (Net Income) it has increased by a whopping 84% since 2017. The main reason is the decrease in the tax rate from 38.5% to 15.7%. It has played a major role in increasing the Net Income for GSK. (Refer to the chart section below)

The key financial ratios play a critical role in decision making for the organization. The current ratio for GSK increased from 0.59 to 0.75 which is a positive sign as their current liabilities decreased in 2018. Even their Quick Ratio increased from 0.38 to 0.50. GSK needs to decrease it over the years. But considering their new partnership with Pfizer in 2019 [3], loans have influenced the low quick ratio. Also, Short-term and Long-term borrowing have increased from 2017 to 2018. My assumption here is GSK is planning to support in their new Joint Venture with Pfizer for the consumer healthcare business, Gross margin increased from 65.73% to 66.77% which is a good indicator of growth. Return of Assets has been increased from 3.84% to 6.96%. The return on equity also had an upward trend from 62.16% to 110.18%. The Return on Sales also increased from 7.18% to 13.12%. The Debt to Equity has been high for 2017 and 2018. The lower the ratio the less risky investment it is for the investor. But if we have a look at the return on equity ratio it has been increasing every year. Finally, we conclude that GSK has a steady growth over the years and a healthy fiscal year 2018.

The following is the SWOT analysis for GlaxoSmithKline:

**Strengths** – GSK's pharmaceutical division has the highest turnover compared to the other divisions. GSK should strive to maintain it as continuing its world-class research.

GSK has been doing really well when it comes to respiratory products. They have been the backbone of GSK for a long time.

**Weaknesses** – Their established pharmaceutical products have a decline over 2 years need to find the reason for that decline. Must research if there is an actual decline in the need for the product or is a threat from a substitute competitors' product. Also compared to the other three divisions, Europe's sales have been plummeting. GSK should focus on the European market or else competitors will take their place.

**Opportunities** – Consumer healthcare merger with Novartis didn't really give positive results in the past, but now their consumer healthcare division has a new opportunity with Pfizer which they must strongly get a hold of it.

**Threats** – Need to focus on the European and International markets. In Europe growth has been flat and 1% decline in the rest of the international market.

Apart from the stupendous progress of GSK in the pharmaceutical industry had its ups and downs over the years. In the past, GSK faced charges against their medicines Paxil and Avandia. GSK also faced charges for bribing doctors in China to use their drugs. They have successfully settled those lawsuits with appropriate charges. GSK is currently facing charges against its medicine Zofran (anti-nausea medicine) which has links to birth defects. As of now, the lawsuit is still going on. Recently Unilever is going to acquire the GSK's Indian Horlicks business.[4] This means GSK is no more going to sell Horlicks. GSK has also discontinued an



ointment called Altargo from 2<sup>nd</sup> July 2018. [5] GSK has extensive research in oncology and is a big player in their industry.

In my opinion, I would love to be a part of this company if I get an opportunity in the future. Investing in GSK can be a good investment considering their steady growth over the years. GlaxoSmithKline has a history of mergers and acquisitions. GSK invests heavily in research and development. GSK recently has also made a joint venture. This can help the shares boosts considering it a non-risky investment. I would definitely invest in GSK.

#### References:

[1] An Easier Way to Understand the Pharma Industry. (2019, December 9). Retrieved December 11, 2019, from <https://marketrealist.com/2019/12/easier-way-understand-pharma-industry/>.

[2] GlaxoSmithKline. (2019, November 25). Retrieved December 10, 2019, from <https://en.wikipedia.org/wiki/GlaxoSmithKline>.

[3] GSK completes transaction with Pfizer to form new world-leading Consumer Healthcare Joint Venture. (2019, August 1). Retrieved November 29, 2019, from <https://www.gsk.com/en-gb/media/press-releases/gsk-completes-transaction-with-pfizer-to-form-new-world-leading-consumer-healthcare-joint-venture/>.

[4] Hirschler, B. (2018, December 3). Unilever swallows GSK's Indian Horlicks business for \$3.8 billion. Retrieved December 5, 2019, from <https://uk.reuters.com/article/uk-gsk-m-a-unilever/unilever-swallows-gsks-indian-horlicks-business-for-3-8-billion-idUKKBN1O20P3>.

[5] Discontinuation of Altargo 10mg/g ointment. (n.d.). Retrieved December 5, 2019, from [https://gskpro.com/en-mt/updates/2018/july/discontinuation\\_of\\_altargo/](https://gskpro.com/en-mt/updates/2018/july/discontinuation_of_altargo/).

## FINANCIAL STATEMENTS FOR FISCAL 2018

CONSOLIDATED INCOME STATEMENT FOR THE YEAR 2018 (Retrieved from the fy-2018-announcement report)

### **Total results**

	2018 £m	2017 £m	Growth £%
<b>Turnover</b>	<b>30,821</b>	30,186	2
Cost of sales	(10,241)	(10,342)	(1)
Gross profit	20,580	19,844	4
Selling, general and administration	(9,915)	(9,672)	3
Research and development	(3,893)	(4,476)	(13)
Royalty income	299	356	(16)
Other operating income/(expense)	(1,588)	(1,965)	
Operating profit	5,483	4,087	34
Finance income	81	65	
Finance expense	(798)	(734)	
Profit on disposal of associates	3	94	
Share of after tax profits of associates and joint ventures	31	13	
<b>Profit before taxation</b>	<b>4,800</b>	3,525	36
Taxation	(754)	(1,356)	
<i>Tax rate %</i>	<i>15.7%</i>	<i>38.5%</i>	
<b>Profit after taxation</b>	<b>4,046</b>	2,169	87
Profit attributable to non-controlling interests	423	637	
Profit attributable to shareholders	3,623	1,532	
	4,046	2,169	87
<b>Earnings per share</b>	<b>73.7p</b>	31.4p	>100

## CONSOLIDATED BALANCE SHEET FOR 2018 (Retrieved from GSK annual report 2018)

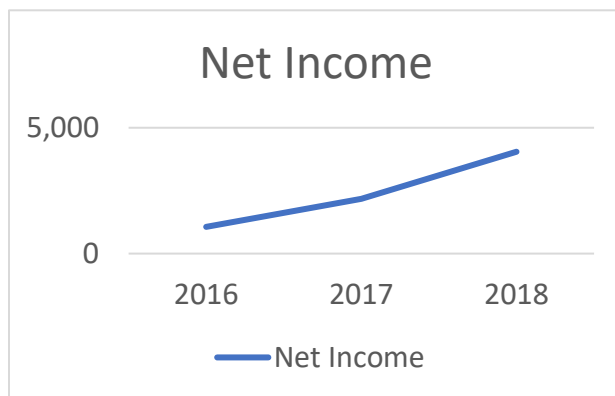
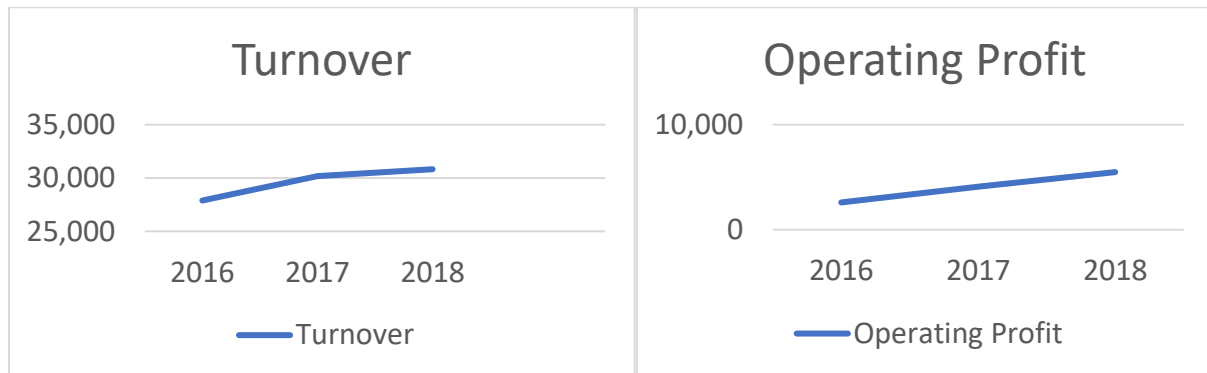
	Notes	2018 £m	2017 £m
<b>Non-current assets</b>			
Property, plant and equipment	17	11,058	10,860
Goodwill	18	5,789	5,734
Other intangible assets	19	17,202	17,562
Investments in associates and joint ventures	20	236	183
Other investments	21	1,322	918
Deferred tax assets	14	3,887	3,796
Derivative financial instruments	42	69	8
Other non-current assets	22	1,576	1,413
<b>Total non-current assets</b>		<b>41,139</b>	<b>40,474</b>
<b>Current assets</b>			
Inventories	23	5,476	5,557
Current tax recoverable	14	229	258
Trade and other receivables	24	6,423	6,000
Derivative financial instruments	42	188	68
Liquid investments	31	84	78
Cash and cash equivalents	25	3,874	3,833
Assets held for sale	26	653	113
<b>Total current assets</b>		<b>16,927</b>	<b>15,907</b>
<b>Total assets</b>		<b>58,066</b>	<b>56,381</b>
<b>Current liabilities</b>			
Short-term borrowings	31	(5,793)	(2,825)
Contingent consideration liabilities	39	(837)	(1,076)
Trade and other payables	27	(14,037)	(20,970)
Derivative financial instruments	42	(127)	(74)
Current tax payable	14	(965)	(995)
Short-term provisions	29	(732)	(629)
<b>Total current liabilities</b>		<b>(22,491)</b>	<b>(26,569)</b>
<b>Non-current liabilities</b>			
Long-term borrowings	31	(20,271)	(14,264)
Corporation tax payable	14	(272)	(411)
Deferred tax liabilities	14	(1,156)	(1,396)
Pensions and other post-employment benefits	28	(3,125)	(3,539)
Other provisions	29	(691)	(636)
Derivative financial instruments	42	(1)	–
Contingent consideration liabilities	39	(5,449)	(5,096)
Other non-current liabilities	30	(938)	(981)
<b>Total non-current liabilities</b>		<b>(31,903)</b>	<b>(26,323)</b>
<b>Total liabilities</b>		<b>(54,394)</b>	<b>(52,892)</b>
<b>Net assets</b>		<b>3,672</b>	<b>3,489</b>
<b>Equity</b>			
Share capital	33	1,345	1,343
Share premium account	33	3,091	3,019
Retained earnings	34	(2,137)	(6,477)
Other reserves	34	2,061	2,047
<b>Shareholders' equity</b>		<b>4,360</b>	<b>(68)</b>
<b>Non-controlling interests</b>		<b>(688)</b>	<b>3,557</b>
<b>Total equity</b>		<b>3,672</b>	<b>3,489</b>

# CONSOLIDATED CASH FLOW STATEMENT FOR 2018 (Retrieved from GSK annual report 2018)

	Notes	2018 £m	2017 £m	2016 £m
<b>Cash flow from operating activities</b>				
Profit after taxation for the year		4,046	2,169	1,062
Adjustments reconciling profit after tax to operating cash flows	36	5,701	6,089	7,044
Cash generated from operations		9,747	8,258	8,106
Taxation paid		(1,326)	(1,340)	(1,609)
<b>Net cash inflow from operating activities</b>		<b>8,421</b>	<b>6,918</b>	<b>6,497</b>
<b>Cash flow from investing activities</b>				
Purchase of property, plant and equipment		(1,344)	(1,545)	(1,543)
Proceeds from sale of property, plant and equipment		168	281	98
Purchase of intangible assets		(452)	(657)	(809)
Proceeds from sale of intangible assets		256	48	283
Purchase of equity investments		(309)	(80)	(96)
Proceeds from sale of equity investments		151	64	683
Contingent consideration paid		(153)	(91)	(73)
Purchase of businesses, net of cash acquired	38	–	–	17
Disposal of businesses	38	26	282	72
Investments in associates and joint ventures	20	(10)	(15)	(11)
Proceeds from disposal of interests in associates	38	3	196	–
Decrease in liquid investments		–	4	–
Interest received		72	64	68
Dividends from associates, joint ventures and equity investments		39	6	42
<b>Net cash outflow from investing activities</b>		<b>(1,553)</b>	<b>(1,443)</b>	<b>(1,269)</b>
<b>Cash flow from financing activities</b>				
Shares acquired by ESOP Trusts		–	(65)	(74)
Issue of share capital	33	74	56	89
Purchase of non-controlling interests		(9,320)	(29)	–
Increase in long-term loans		10,138	2,233	–
Repayment of short-term Notes		(2,067)	(2,636)	(865)
Increase in/(repayment of) other short-term loans		81	(564)	1,013
Net repayment of obligations under finance leases		(28)	(23)	(18)
Interest paid		(766)	(781)	(732)
Dividends paid to shareholders		(3,927)	(3,906)	(4,850)
Distributions to non-controlling interests		(570)	(779)	(534)
Contributions from non-controlling interests		21	21	–
Other financing cash flows		(25)	93	(421)
<b>Net cash outflow from financing activities</b>		<b>(6,389)</b>	<b>(6,380)</b>	<b>(6,392)</b>
<b>Increase/(decrease) in cash and bank overdrafts</b>	37	<b>479</b>	<b>(905)</b>	<b>(1,164)</b>
Cash and bank overdrafts at beginning of year		3,600	4,605	5,486
Exchange adjustments		8	(100)	283
Increase/(decrease) in cash and bank overdrafts		479	(905)	(1,164)
<b>Cash and bank overdrafts at end of year</b>		<b>4,087</b>	<b>3,600</b>	<b>4,605</b>
Cash and bank overdrafts at end of year comprise:				
Cash and cash equivalents		3,874	3,833	4,897
Cash and cash equivalents reported in assets held for sale		485	–	–
		4,359	3,833	4,897
Overdrafts		(272)	(233)	(292)
		4,087	3,600	4,605

## CHARTS REPRESENTING FINANCIAL DATA

Note: Charts are created using MS PowerPoint. The values are rounded for plotting purposes.



Turnover, Operating Profit and Net Income from 2016 to 2018.

