

# Strategic CSR through Healthcare: A Case study on Indian Pharmaceutical Companies

Susanta Datta<sup>1</sup> & Vinayak Karande<sup>2</sup>

## Abstract

*Indian Pharmaceutical sector contributed 2.4% in global pharmaceutical business in terms of value and 10% in terms of volume. It is anticipated to grow at a CAGR of 12.89% over 2015–20 to reach USD55 billion. Indian healthcare sector, one of the fastest growing sectors, is expected to advance at a CAGR of 17 % to reach USD250 billion over 2008–20. Under the newly enacted Companies Act 2013 in which under section 135 make Corporate Social Responsibility (CSR) as an obligation that companies need to spend 2% of average the last three years net profits on CSR activities which has been initiated since April 1, 2014 as per Companies (CSR) Rule 2014. Based on public disclosure of 11 pharmaceuticals companies out of top 100 company based on SEBI market capitalization, prescribed CSR spending and actual spending have been increasing during financial year 2014-15 to financial year 2015-16. Using Porter and Kramer (2006), we categorise strategic CSR and Responsive CSR activities based on their expenditure at the state level implementation and analyse both quantitative as well as qualitative data in order to arrive with significant findings. Our findings are quite consistent with the real life practices along with company's long term plan to create new business opportunities through strategic CSR. Over the period of time the issue of sustainability and inclusive nature of growth have been ensured and that strategic CSR would likely to increase access to healthcare facilities to the socially excluded people. CSR become one of the non-price competition instrument as well as reducing non-financial risk which also ensure through better public disclosure practices under corporate governance mechanism of pharmaceuticals companies.*

**Keywords:** Corporate Social Responsibility, Corporate Governance, Strategic CSR, Public Policy.

**JEL classification:** D21, M14, Q58.

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## I. Indian Pharmaceutical Industry:

The evolution of Indian pharmaceutical market has been taken place in four different phases. Firstly, phase I considered the scenario before 1970 when pharmaceuticals market was strictly dominated by the foreign companies with marginal presence of the domestic companies. Secondly, phase II considered the pre economic liberalization period during 1970 to 1990. In 1970, Indian parliament passed Indian Patent Act which boosted the process of initiation of pharmaceutical business in India and as a result of that several domestic firms set up their infrastructure for production and started operation in the early 1990. During the LPG regime after introduction of new economic policy 1991 with an open economy set up, export driven market strategy was promoted and as an outcome, several business initiative to carry out operation in foreign countries by Indian companies has been promoted from time to time. Phase III experienced with Patents (Amendment) Act 2005 which led to adoption of product patents in India has helped Indian companies to become a major destination for generic drug manufacture. Phase IV considered 2010 and beyond time span and also experienced with numbers of increasing patent filings by pharma players and leading pharma companies have increased their R&D spending on new cost-effective generic products to strengthen their presence across global markets. (IBEF, 2017)

Indian pharmaceuticals market can be classified into three sub segments: (a) generic drugs, (b) Patented drugs and (c) Over the Counter medicine. As per as overall market share is concerned, generic drug segment

<sup>1</sup> [Corresponding Author] Assistant professor, Dept. of Economics, R.K.Talreja College of Arts, Science and Commerce, Ulhasnagar, Thane, Maharashtra. Email: [susantadatta2005@gmail.com](mailto:susantadatta2005@gmail.com)

<sup>2</sup> Research scholar, Commerce - Business policy & administration, R.A.Podar College of Commerce & Economics, Matunga, Mumbai, Maharashtra. Email: [vinayakkarande9@gmail.com](mailto:vinayakkarande9@gmail.com)

represents the largest segment with 72% of total revenue in domestic market share along with 20% of the global export share in the Pharmaceuticals market. While the other two segments viz. patented drugs and over the counter medicine constitute 9% and 19% respectively. The recent trends suggests that the market is expanding at a faster rate with a cumulative average growth rate of 17.46 % during 2005-16 with the market increasing from US\$ 6 billion in 2005 to US\$ 36.7 billion in 2016 and is expected to expand at a CAGR of 15.92 per cent to US\$ 55 billion by 2020. By 2020, India is likely to be among the top three pharmaceutical markets by incremental growth and sixth largest market globally in absolute size. India's cost of production is significantly lower than that of the US and almost half of that of Europe. It gives a competitive edge to India over others. (ibid)

In order to harnessing competitiveness along with greater transparency, Government of India introduced the National Pharmaceutical Pricing Policy, 2012 in order to ensure greater transparency in terms of pricing strategy of pharmaceuticals industry. Indian parliament passed Companies Act 2013 in order to ensure greater corporate governance, transparency, disclosure of financial risk and non-financial risk to its stakeholders of every company. Under this backdrop, our endeavour is to examine whether this new CSR law ultimately helps Indian Pharmaceuticals Company to reap out benefits of comparative advantage along with creating Shared Value for the society following Porter & Kramer (2006) as well as to promote non-price competition through CSR.

## II. Companies Act 2013 and CSR:

### Section 135 of Companies Act 2013:

India is the first country in the world which makes Corporate Social Responsibility (CSR) as an obligation to both Private Sector and public sector enterprises. The Ministry of Corporate Affairs has notified Section 135 and Schedule VII of the Companies Act 2013. Accordingly, to adhere the Companies Act 2013, the Companies (Corporate Social Responsibility Policy) Rules, 2014 has come into effect from April 1, 2014 and every company, private limited or public limited, which either has a net worth of Rs 500 crore or a turnover of Rs 1,000 crore or net profit of Rs 5 crore, needs to spend at least 2% of its average net profit for the immediately preceding three financial years on corporate social responsibility activities. (The Companies Act, 2013). As per the Company (Corporate Social Responsibility) Rules 2014, CSR activities should not be undertaken in the normal course of business and must be with respect to any of the activities mentioned in Schedule VII of the 2013 Act. The report of the Board of Directors attached to the financial statements of the Company would also need to include an annual report on the CSR activities of the company in the prescribed format as mentioned below:

1. A brief outline of the company's CSR policy, including overview of projects or programs proposed to be undertaken and a reference to the web-link to the CSR policy and projects or programs
2. The Composition of CSR Committee
3. Average net profit of the company for last three financial years
4. Prescribed CSR Expenditure (two percent of the amounts in item 3 above)
5. Details of CSR spent during the financial year
  - a. Total amount to be spent for the financial year:
  - b. Amount unspent, if any: N.A.
  - c. Manner in which the amount spent during the

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
SINo.	CSR project or activity identified	Sector in which the Project is covered	Projects or Programs: (1) Local area or other; (2) Specify the State and district where projects or programs were undertaken	Amount outlay (budget) project or program wise	Amount spent on the projects or programs Subheads: (1) Direct expenditure on projects or programs (2) Overheads	Cumulative expenditure up to the reporting period	Amount spent: Direct or through implementing agency	No. of Beneficiaries
1								
2								
3								

## III. Indian Pharmaceutical Company and Corporate Social responsibility (CSR)

There are 152 numbers of companies available in the BSE website which has submitted their Business Responsibility Report since 2010. However, after introduction of New Companies Act 2013, we consider only

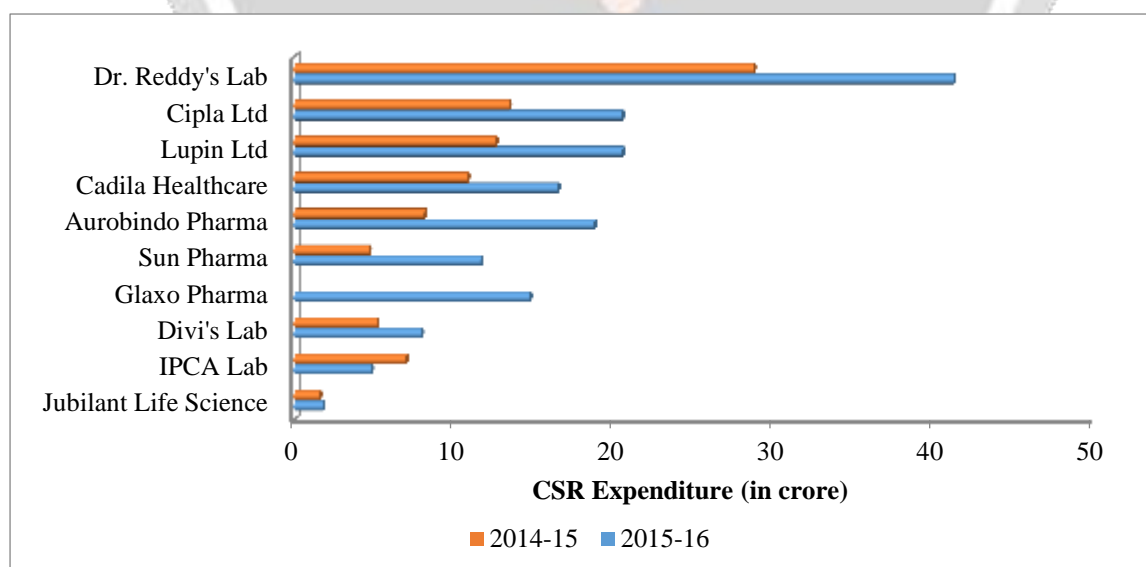
financial year 2014 – 15 and 2015 – 16 for this study. Following are 10 Pharmaceuticals Company<sup>3</sup> which have submitted their public disclosure through Business Responsibility Report as per SEBI's National Voluntary guideline initiated as a part of corporate governance mechanism. The consolidated CSR expenditure<sup>4</sup> (for both financial details of representative pharmaceuticals companies are tabulated in Table 1.

**Table 1: Company wise details CSR expenditure for FY 2014-15 and FY 2015-16**

Company Name	2014-15	2015-16	Grand Total (percentage)
Dr.Reddy's Laboratories Ltd.	28.71	41.20	69.92 (27.93%)
Cipla Ltd.	13.43	20.48	33.91 (13.55%)
Lupin Ltd.	12.58	20.51	33.09 (13.22%)
Cadila Healthcare Ltd.	10.82	16.46	27.27 (10.90%)
Aurobindo Pharma Ltd	8.13	18.76	26.89 (10.74%)
Sun Pharmaceutical Industries Ltd.	4.67	11.66	16.32 (6.52%)
Glaxosmithkline Pharmaceuticals Ltd.	Not Applicable	14.70	14.70 (5.87%)
Divi's Laboratories Ltd.	5.15	7.93	13.08 (5.23%)
IPCA Labs	6.97	4.80	11.77 (4.70%)
Jubilant Life Sciences Limited	1.56	1.78	3.35 (1.34%)
Grand Total	92.02	158.28	250.30 (100.00%)

Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

Among the pharmaceuticals companies, top 5 companies contributed 77% of total expenditure and the respective share are as follows: 28% for Dr. Reddy's laboratories Limited, 14% for Cipla Limited, 13% for Lupin Limited, 11% Cadila Healthcare Limited and 11% for Aurobindo Pharma Limited. (Figure 1)



**Figure 1: CSR Expenditure (in crore) by Company during FY 2014-15 & 2015-16**

Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

<sup>3</sup>Excluding Ranbaxy, Sun Pharma Advanced Research

<sup>4</sup>Refer to appendix 1 for financial yearwise company wise CSR expenditure

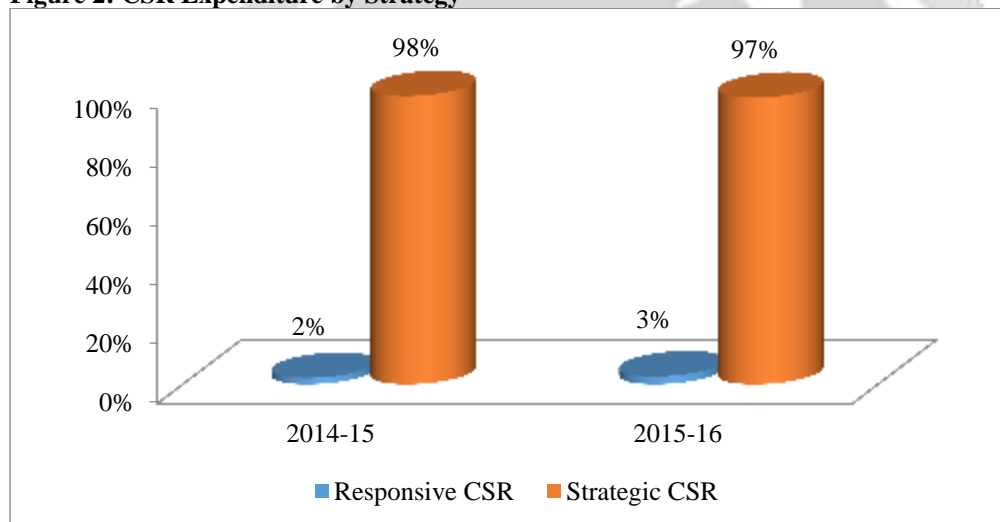
#### IV. Case Study Design:

Porter and Kramer (2006) mentioned that companies can reap their comparative advantage benefit from their strategic action and implementation part is concerned. There are two different strategies – Strategic CSR and Responsive CSR-. Strategic CSR is much more concerned about creating new market opportunities which is not directly related to their business, but it will concerns with other aspects of the business like broad vision of the company, maintaining a good industrial relationship with the local community which can helps them to create new market for themselves along with satisfying inclusive nature of growth. Responsive CSR is more concerned about direct benefit with existing business operation. Both type of CSR will ultimately non-financial risks of the companies along with creating shared value for the society. Now which strategy is better is depending upon (a) whether considering for short term benefit or long term benefit along with its gestation lag; (b) whether opt for short term implementation or long term implementation; (c) whether direct more of implementation or indirect way of implementation through specialized agency and so on. All these queries can be addressed with the help of “transaction cost economics” (Williamson 1975, 1976 and 1979).

#### V. Case Analysis:

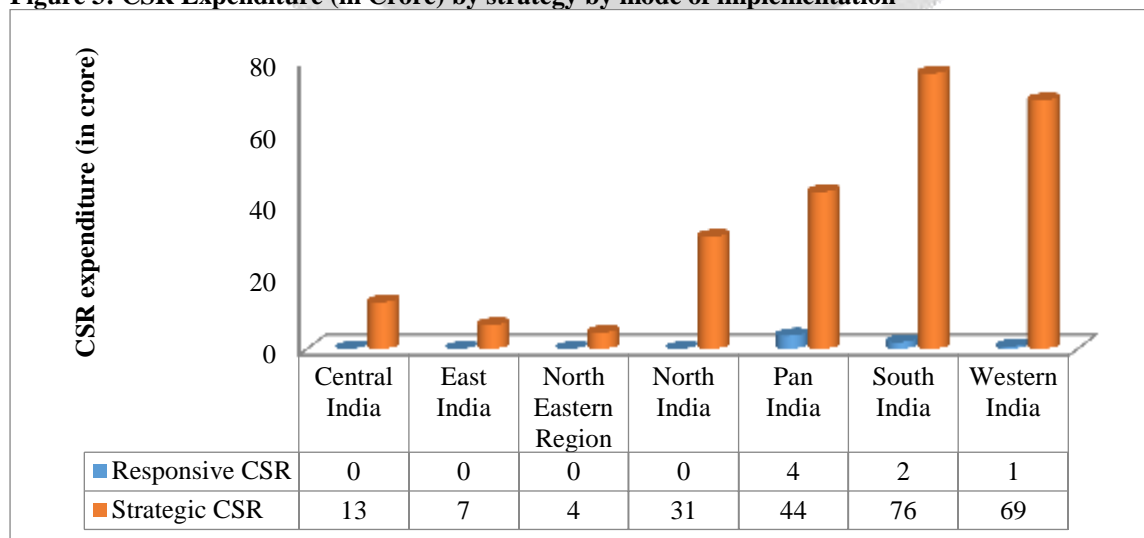
To formulate and monitor the CSR policy of a company, a CSR Committee of the Board needs to be constituted (The Companies Act, 2013). CSR committee will choose the ultimate strategy in alignment with their goals vis a vis allocation of CSR funds. It is quite evident that Indian pharmaceuticals companies preferred Strategic CSR much more as compared to Responsive CSR. While 98% of CSR expenditures are strategic in nature, while very marginal presence is there under responsive CSR during the financial year from 2014-15 to 2015-16. (Figure 2)

**Figure 2: CSR Expenditure by Strategy**



Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

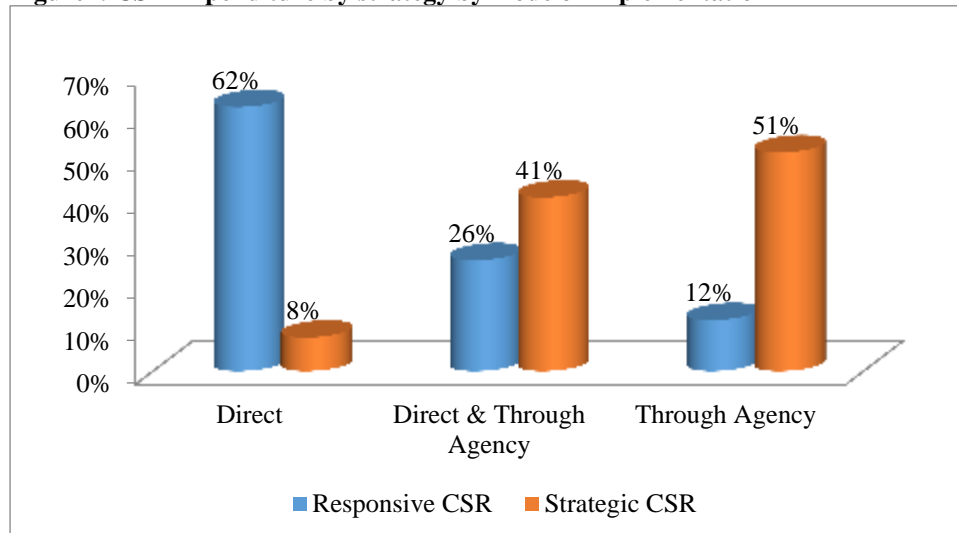
**Figure 3: CSR Expenditure (in Crore) by strategy by mode of implementation**



Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

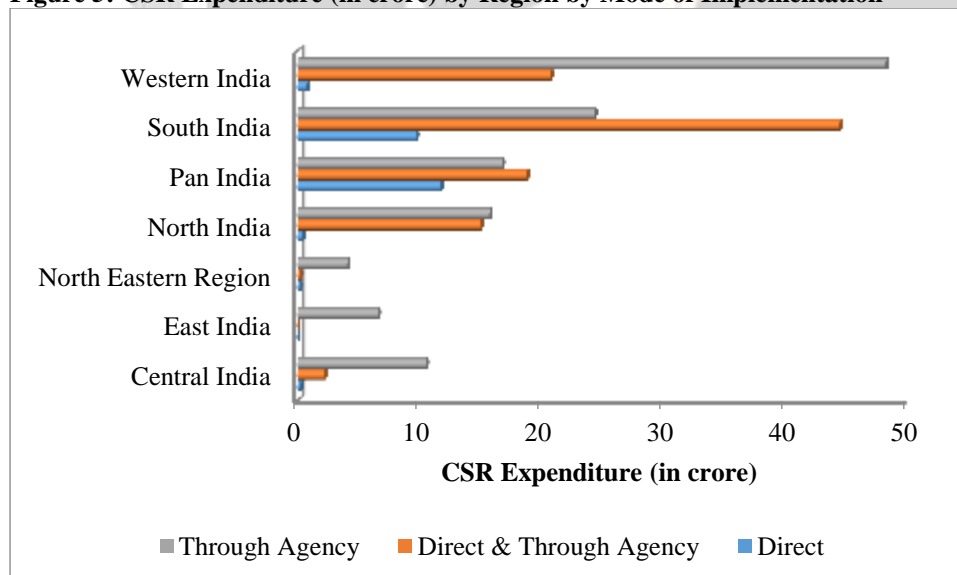
In determining CSR activities to be undertaken, preference would need to be given to local areas and the areas around where the company operates (The Companies Act, 2013). This has raised the question of concentration of CSR expenditure near plant vicinity. Due to lack of concordance between plant location and project location, it is difficult for us to predict whether plant location leads to concentration of CSR expenditure or not. Figure 3 represents distribution of CSR expenditure by strategy by mode of implementation across different geographical region. It is found that the concentration of strategic CSR expenditure is much higher in South India region followed by western region and North India region. Apart from geographical region companies also spends their CSR under the Pan India programme.

**Figure4: CSR Expenditure by strategy by mode of implementation**



Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

**Figure 5: CSR Expenditure (in crore) by Region by Mode of Implementation**

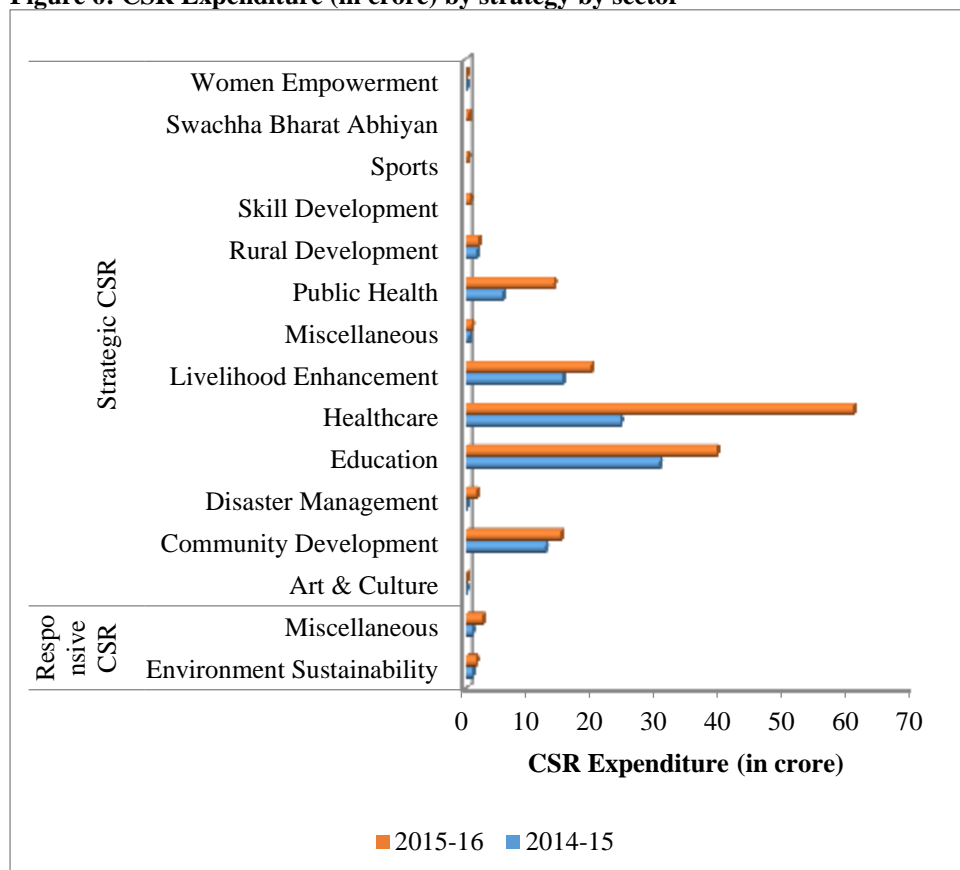


Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

A company can undertake its CSR activities through a registered trust or society, a company established by its holding, subsidiary or associate company or otherwise, provided that the company has specified the activities to be undertaken, the modalities for utilization of funds as well as the reporting and monitoring mechanism (The Companies Act, 2013). This ultimately leads to the issue of governance of hybrid contractual relationship under the framework of transaction cost economics according to Williamson (1975, 1979). It is important to note that companies preferred more to engage specialized agency to implement their CSR projects as compared to handled directly on daily basis. Due to lower allocation of fund, it is better for the companies to implement directly in the plant vicinity and as a result we found that direct method of implementation is much preferred for Responsive CSR while companies are hardly depending upon direct mode of implementation if and only if the

volume of expenditure become larger. Under strategic CSR, only 10% expenditure has been incurred through direct mode of implementation while 90% of expenditure has been incurred through implementation agency (Figure 4). As per regional distribution of CSR expenditure is concerned, share is direct implementation mode is lower as compared to through agency mode. This phenomenon is quite consistent with the governance of hybrid contractual relationship as propounded by Williamson (1975, 1979)(Figure 5).

**Figure 6: CSR Expenditure (in crore) by strategy by sector**



Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

The activities that can be undertaken by a company to fulfil its CSR obligations include eradicating hunger, poverty and malnutrition, promoting preventive healthcare, promoting education and promoting gender equality, setting up homes for women, orphans and the senior citizens, measures for reducing inequalities faced by socially and economically backward groups, ensuring environmental sustainability and ecological balance, animal welfare, protection of national heritage and art and culture, measures for the benefit of armed forces veterans, war widows and their dependents, training to promote rural, nationally recognized, Paralympic or Olympic sports, contribution to the prime minister's national relief fund or any other fund set up by the Central Government for socio economic development and relief and welfare of SC, ST, OBCs, minorities and women, contributions or funds provided to technology incubators located within academic institutions approved by the Central Government and rural development projects. Figure 6 shows the distribution of CSR expenditure by strategy by sector. Under Strategic CSR, Education, Healthcare, Livelihood Enhancement, Community Development and Public Health are the leading Sectors and constituted 94% of total strategic CSR expenditure –34% for Healthcare, 28% for Education, 14% for Livelihood Enhancement, 11% for Community Development and 8% for Public Health-.

## VI. Conclusion:

Over the period of time the proportion of unspent amount volume has reduced and actual spending has increased over time. Pharmaceuticals Companies are now collaborating with specialized agencies in order to smooth operation of their CSR projects which is supported by transaction cost economics in order to promote inclusive nature of growth through their strategic CSR. Pharmaceutical sectors are also tries to harness their competitiveness through price based competition under National Pharmaceuticals Pricing Policy (NPPP) 2012 as well as Non price based competition through CSR under newly enacted Companies Act 2013. Porter discussed 5 forces analysis for price based completion viz. competitive rivalry, threat of new entrants, substitute products, bargaining power of suppliers and bargaining power of customers in order to exploit comparative

advantage through price based competition, while through non-price based competition under the newly enacted Companies Act 2013, using Porter and Kramer (2006) we find that around 98% CSR spending is following Strategic CSR policy. The economic rationale behind strategic CSR is (a) to create new market for future business and (b) to ensure inclusive nature of growth.

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#### Appendix

##### Appendix 1: CSR Expenditure by Strategy by mode of implementation during financial year 2014-15 to 2015-16

Strategy	Mode of Implementation	Financial Year		
		2014-15	2015-16	Grand Total
Responsive CSR	Direct	1.14 (59%)	2.67 (63%)	3.82 (62%)
	Direct & Through Agency	0.22 (11%)	1.39 (33%)	1.60 (26%)
	Through Agency	0.59 (30%)	0.15 (4%)	0.74 (12%)
Responsive CSR Total		<b>1.95 (2%)</b>	<b>4.21 (3%)</b>	<b>6.15 (2%)</b>
Strategic CSR	Direct	7.55 (9%)	11.70 (8%)	19.25 (8%)
	Direct & Through Agency	34.53 (38%)	65.02 (42%)	99.56 (41%)
	Through Agency	47.99 (53%)	77.34 (50%)	125.33 (51%)
Strategic CSR Total		<b>90.07 (98%)</b>	<b>154.07 (97%)</b>	<b>244.14 (98%)</b>
Grand Total		<b>92.02 (100%)</b>	<b>158.28 (100%)</b>	<b>250.30 (100%)</b>

Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

##### Appendix 2: CSR Expenditure by strategy by Sector during financial year 2014-15 and 2015-16

	2014-15	2015-16	Grand Total
Responsive CSR	1.9 (2%)	4.2 (3%)	6.2 (2%)
Environment Sustainability	1.0 (51%)	1.6 (37%)	2.6 (41%)

Miscellaneous	0.9 (49%)	2.7 (63%)	3.6 (59%)
Strategic CSR	90.1 (98%)	154.1 (97%)	244.1 (98%)
Art & Culture	0.0 (0%)	0.2 (0%)	0.2 (0%)
Community Development	12.5 (14%)	14.9 (10%)	27.3 (11%)
Disaster Management	0.0 (0%)	1.7 (1%)	1.8 (1%)
Education	30.3 (34%)	39.1 (25%)	69.4 (28%)
Healthcare	24.1 (27%)	60.5 (39%)	84.6 (35%)
Livelihood Enhancement	15.1 (17%)	19.6 (13%)	34.7 (14%)
Miscellaneous	0.6 (1%)	0.9 (1%)	1.5 (1%)
Public Health	5.8 (6%)	13.7 (9%)	19.5 (8%)
Rural Development	1.7 (2%)	2.0 (1%)	3.7 (2%)
Skill Development	0.0 (0%)	0.6 (0%)	0.6 (0%)
Sports	0.0 (0%)	0.3 (0%)	0.3 (0%)
Swachha Bharat Abhiyan	0.0 (0%)	0.5 (0%)	0.5 (0%)
Women Empowerment	0.1 (0%)	0.0 (0%)	0.1 (0%)
Grand Total	92.0 (100%)	158.3 (100%)	250.3 (100%)

Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

**Appendix 3: CSR Expenditure by strategy by sector and by mode of implementation during financial year 2014-15 and 2015-16**

	Direct	Direct & Through Agency	Through Agency	Grand Total
Responsive CSR	3.8 (17%)	1.6 (2%)	0.7 (1%)	6.2 (2%)
Environment Sustainability	1.9 (51%)	0.0 (0%)	0.6 (82%)	2.6 (41%)
Miscellaneous	1.9 (49%)	1.6 (100%)	0.1 (18%)	3.6 (59%)
Strategic CSR	19.3 (83%)	99.6 (98%)	125.3 (99%)	244.1 (98%)
Art & Culture	0.2 (1%)	0.0 (0%)	0.0 (0%)	0.2 (0%)
Community Development	1.5 (8%)	0.0 (0%)	25.8 (21%)	27.3 (11%)
Disaster Management	0.1 (0%)	0.0 (0%)	1.7 (1%)	1.8 (1%)
Education	3.9 (20%)	46.4 (47%)	19.0 (15%)	69.4 (28%)
Healthcare	0.2 (1%)	32.3 (32%)	52.1 (42%)	84.6 (35%)

Livelihood Enhancement	0.9 (5%)	18.5 (19%)	15.4 (12%)	34.7 (14%)
Miscellaneous	0.3 (2%)	0.3 (0%)	0.8 (1%)	1.5 (1%)
Public Health	9.7 (50%)	0.0 (0%)	9.8 (8%)	19.5 (8%)
Rural Development	1.6 (8%)	2.1 (2%)	0.0 (0%)	3.7 (2%)
Skill Development	0.0 (0%)	0.0 (0%)	0.6 (0%)	0.6 (0%)
Sports	0.3 (1%)	0.0 (0%)	0.0 (0%)	0.3 (0%)
Swachha Bharat Abhiyan	0.5 (3%)	0.0 (0%)	0.0 (0%)	0.5 (0%)
Women Empowerment	0.1 (0%)	0.0 (0%)	0.1 (0%)	0.1 (0%)
Grand Total	23.1 (100%)	101.2 (100%)	126.1 (100%)	250.3 (100%)

Source: Authors calculation based on BSE data for financial year 2014-15 and 2015-16

