Serialously – Another Acquisition for Valeant

Description

Valeant Pharmaceuticals (TSX:VRX,NYSE:VRX) is back in the acquisition ring after announcing the $343.8 million purchase of **Obagi Medical Products** (NASDAQ:OMPI) yesterday. Obagi is the 21st company Valeant has purchased since the beginning of 2011. The $344 million brings total cash spent on acquisitions to $6.3 billion over this period. Pretty amazing for a company that had a market cap of about $7 billion when the shopping spree began.

All clear

Obagi is a maker of skin care products that booked revenues of $120 million last year. Valeant is not only acquiring these revenue generating products, but the company also believes that it can realize $40 million of cost saving synergies. In addition, Obagi's distribution channel is an attractive asset that Valeant can leverage with its growing portfolio of dermatology related products.

On the surface, this deal looks pretty clean if you're a Valeant shareholder. Neither the $120 million in revenue nor the $344 million purchase price are overly material to a company that had revenue of $3.5 billion in 2012 and more than $900 million in cash on hand at last report. And, if Valeant can pad its bottom line by successfully integrating Obagi's business and realizing the proposed synergies, downside appears minimal.

For now

Regardless of its materiality, the Obagi deal makes it very clear that Valeant is going to keep on buying things. Valeant is a serial acquirer and has demonstrated phenomenal growth by implementing this strategy. It has taken a couple of big swings, like the 2011 $2.6 billion acquisition of Medicis, but for the most part, the company has knocked out singles and doubles with its purchases – like Obagi.

However, these singles and doubles with the odd home run have placed a huge burden on Valeant's balance sheet. The company is loaded with financial risk.

But beware the big one

Beyond financial risk, another huge risk is lurking for Valeant shareholders. Singles and doubles are fine for a while, but can only hold the serial acquirer's interest for so long. You can bet, somewhere out there lies a "company transforming" acquisition for Valeant.

Ask Hewlett-Packard shareholders how much fun these types of transactions are. HP purchased Autonomy several years ago for $11 billion and promptly had to write-off $8.8 billion when Autonomy fell short of expectations. HP shareholders were lucky that the company's balance sheet was in sound enough shape to absorb such a massive hit. Valeant simply does not have this luxury. Overpaying for a transformational purchase could mean the end.

The Foolish Bottom Line

Just like a leveraged investor, highly levered companies can blow up when faced with even the slightest bit of adversity. The combination of a highly leveraged balance sheet and possibility of overpaying for a massive acquisition at some point makes this Fool highly wary of Valeant's long-term viability.

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Fool contributor Iain Butler does not own shares in any of the companies mentioned in this report at this time. The Motley Fool has no positions in the stocks mentioned above.

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