



## Should You Buy Valeant Pharmaceuticals Intl Inc. Before its Earnings Report?

### Description

**Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) is reporting its third-quarter earnings results on Monday. Should investors consider buying its shares today or wait until after the earnings report?

### The business

Valeant is a global specialty pharmaceutical company that develops and markets prescription and non-prescription pharmaceutical products. The business focuses on dermatology, eye health, and other niche therapeutic areas that target growth markets.

### Sales growth, earnings growth, and valuation

From 2010 to 2014, Valeant's sales increased at a high rate of over 40% per year. In the same period, its earnings per share (EPS) also grew at a rate of over 40% per year. The question is whether or not that high growth can be sustained.

#### Year Sales Growth EPS Growth

2010		
2011	108.6%	46%
2012	44%	51%
2013	62.7%	47.3%
2014	43.2%	45.7%

In the past month, the shares have come down 30% from a high of \$319 due to questioning of its high-priced drugs. However, Valeant is not the only drug company that was affected by this issue.

At about \$218 per share, the company is priced at a price-to-earnings ratio (P/E) of 16.5, which is a discounted multiple to pay for a business that is expected to grow earnings between 20-25%.

## Debt, financial health, and free cash flow

However, the company's debt levels can be hard to stomach for some investors. For example, its debt-to-cap is around 80%. S&P gives Valeant a credit rating of BB-, so the shares are not considered investment grade. An investment grade requires a minimum credit rating of BBB-.

In 2009 its debt-to-equity ratio was 0.28. From then on it only continued to increase. From 2010 to 2014 it grew from 0.73 to 2.87 at 40.8% per year.

From 2010 to 2014 its free cash flow increased from U\$246 million to U\$1.8 billion, or 65% per year. At least while the company was taking on debt, it was also increasing its cash flow generation. So, this indicates that Valeant is making good use of borrowed money.

But Valeant can only borrow so much to spur growth, because eventually it will have to pay off the debt. Still, at least the company has a current ratio of 1.5, indicating that its current assets are 1.5 times its current liabilities, so that it's able to pay off its short-term obligations.

## In conclusion

Even though Valeant shares are discounted based on its P/E, due to its large debt levels, I only consider it to be fairly valued. After all, investors would be taking on more risk by buying its debt-heavy shares. If I were to add it to my portfolio, it will only make up, at most, 1% of it.

I'm not encouraging the timing of the market, but around earnings report time, the market can get especially emotional about a company. Valeant Pharmaceuticals Intl Inc. could go up or down 10% in one day.

Because Valeant Pharmaceuticals shares are fairly valued, Foolish investors can act cautiously by buying half a position now and finishing off the position after the earnings report. That is, if you plan to buy \$5,000 worth of shares, you can buy \$2,500 worth today, and buy more after the earnings report.

If the price goes up, it means the company is doing better than expected. If not, then you might be able to spend that \$2,500 on more shares at a lower price.

## CATEGORY

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1. Editor's Choice

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