Valeant Pharmaceuticals Intl Inc.: Why its Pricing Strategy Is Immoral and Unsustainable

Description

It's not uncommon for someone to complain about an overpriced product. Whether it's gasoline, bottled water, or designer handbags, consumers often feel like they are being gouged.

But Americans are particularly angry about the high cost of pharmaceuticals. According to the Kaiser Health Tracking Poll, large majorities of Americans believe that the government should take action to lower drug prices. Remarkably, "government action to lower prescription drug prices" was nearly as popular among Republican respondents as a full-scale Obamacare repeal.

Drug companies maintain that there is nothing illegal or immoral about raising drug prices. After all, it is very expensive to develop a drug, and without the ability to charge high prices, these costs simply could not be recovered. Besides, free-market economics should dictate what drugs cost, not government regulation.

But when it comes to pricing actions by **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX), it's not that simple. We take a closer look below, and by the end you'll see why the company's pricing strategy simply cannot last.

At first glance, it seems that nothing is wrong

A common argument made against Valeant is that it doesn't do much R&D. Instead, it acquires drugs from other companies then jacks up their prices. Thus, Valeant, as the argument goes, is simply engaged in pure profiteering.

Yet this is a flawed argument. Even though Valeant does not develop its own drugs, it still must pay to acquire them. And if Valeant didn't charge high prices, then the company couldn't fully compensate the drug's developer for its R&D efforts.

But there are other reasons why Valeant's pricing strategy is immoral and unsustainable.

What makes Valeant’s pricing strategy immoral

If Valeant’s drugs achieved remarkable results, then their high cost would be justified. But that’s not the case at all.

For example, Jublia, which is used to treat toenail fungus, costs roughly $10,000 per treatment cycle, but it is far less effective than alternatives. Atralin is nothing more than a US$600 tube of Vitamin A gel. Solodyn, which is used to treat acne, costs US$1,000 per month, while its generic equivalent costs just US$30.

So, how does Valeant get away with such prices? Well first of all, the company minimizes the cost to end-users through its patient-assistance programs, thus placing the burden on insurers. Secondly, Valeant spent over US$20 million last year on payments to physicians, which could have easily resulted in more prescriptions for Valeant products.

To put it bluntly, Valeant is able to charge far more for its products than they are reasonably worth. And the company has been using sneaky tactics to do so.

What makes Valeant’s pricing strategy unsustainable

Valeant’s pricing strategy may be running on empty. The company is under numerous investigations from regulators, any number of which could force the company to make big changes to its business model.

There are also actions the federal government could take, such as allowing Medicare to negotiate discounted drug prices. This would require action from Congress, which is never a given, but it is easy to imagine given the bipartisan fury over this issue. Insurers will fight back as well.

So, even though Valeant may look cheap, this company’s problems are only just beginning. Your best bet is to avoid the stock.

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