



Valeant Pharmaceuticals Intl Inc.: If You Believe Management, it's a Screaming Buy

Description

By now, you're likely very familiar with the **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) story.

If not, let me quickly sum it up. Short-selling firm Citron Research came out with evidence that it thinks points to accounting irregularities. The smoking gun is a company called Philidor, which owns several specialty pharmacies.

Although drugs sold through Philidor accounted for nearly 6% of Valeant's revenue, the company never disclosed that it had a relationship with Philidor. In reality, Valeant had paid Philidor \$100 million for an option to acquire the company at some point in the future.

Valeant subsequently announced that it was severing all ties to Philidor.

The real issue comes down to disclosure. Valeant's management didn't figure the relationship was important enough to disclose to investors. Citron—and many others—disagree, and rather strongly, too. If investors can't trust Valeant on this, the bears argue, what else is the company lying about? That's a very slippery slope that many investors don't even want to think about.

The obvious choice for investors is to stay very far away from a situation like that. Successful investing involves a margin of safety. If we can't trust what management is saying, there's no margin of safety. It's that simple.

But perhaps investors are looking at this the wrong way. What if recent events have actually made it easier to trust Valeant's management? Because if you believe the numbers, the company looks to be very cheap at today's levels.

The bull case

Billionaire investor Bill Ackman recently outlined the bull case for Valeant.

It goes something like this: according to Ackman, Valeant's big mistake wasn't Philidor, since many of its competitors are using a similar strategy to boost sales. Rather, the big blunder was underinvesting in its public relations. Valeant is a hard stock to fully understand because it has so many moving parts.

Most of Valeant's investor base is what Ackman calls "quite sophisticated," but the company was still vulnerable to short-seller attacks simply because many investors don't fully realize everything it has going on.

Additionally, Ackman brought up the point that even if Valeant had done something wrong, it likely wouldn't be punished that severely. He brought up the case of **Novartis**, which was targeted by the Department of Justice for using kickbacks to boost sales. The original lawsuit levied against the company was for \$3.35 billion. It eventually settled for just a fraction of that at just \$390 million. Sure, \$390 million is still a lot of money, but it's something a company like Valeant can easily handle.

Finally, there's the valuation perspective. Ackman thinks Valeant is primed to grow earnings exponentially over the next few years; the company still has the ability to earn US\$22 per share in 2020. According to a recent management presentation, the company is poised to earn US\$7.5 billion in EBITDA in 2016, which works out to more than US\$21 per share. The earning power sure looks to be there, anyway.

Unfortunately, that large EBITDA number will likely take years to manifest itself into real earnings per share. With more than \$30 billion in long-term debt and a credit rating that isn't great, Valeant is paying billions per year in just interest alone. Still, assuming you believe management's projections, it's obvious that Valeant has some pretty serious earnings potential.

The Valeant investment thesis is relatively simple. If you believe management's bullish forecasts, the stock looks to be a buy at today's levels. Valeant bulls can at least be assured they've got some very smart people who are bullish on the stock with them, and, unlike with Enron back in the early 2000s, it's pretty obvious Valeant's products are real.

There are many reasons why investors would avoid Valeant. But if what management says is true, it's also very easy to understand the bull thesis. Ultimately, it's up to each investor to make up their own mind.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:BHC (Bausch Health Companies Inc.)
2. TSX:BHC (Bausch Health Companies Inc.)

Category

1. Investing

Date

2025/07/08

Date Created

2015/11/12
Author
nelsonpsmith

default watermark

default watermark