



Why Valeant Pharmaceuticals Intl Inc. Shares Are Down 19% in 2 Days

Description

In a research note published Friday, **Wells Fargo** analyst David Maris initiated coverage on **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) with an underperform rating, along with a \$65-68 target price.

Mr. Maris actually has a long history with Valeant. Back in 2003 he put out a negative report on Valeant's predecessor company, Biovail. He focused on the company's explanation that its numbers missed because a truck carrying a large amount of medicine crashed. For this report, he was fired from his job, embroiled in a lawsuit, and shunned by Wall Street. What makes this story especially awful is that he was right about the facts.

So Mr. Maris is certainly worth paying attention to, even though Valeant backers will undoubtedly argue that his experience makes him biased. Below are his main arguments against Valeant.

Accounting issues

Mr. Maris's main arguments concern Valeant's "considerable subjectivity" in its financial reports. To illustrate, he points out that receivables have grown far faster than sales over the past several years. He also doubts the validity of Valeant's cash EPS metric. And he is skeptical about the company's setting up of deferred-tax asset accounts.

Too much debt

Thanks to its acquisitive history, Valeant has about US\$30 billion of debt, and Mr. Maris thinks that this will become a serious burden. In fact, he thinks the company will need to use its entire free cash flow to pay this debt down.

The Walgreens deal

In mid-December, Valeant announced a new distribution deal with **Walgreens**, one that ideally would plug the revenue gap from the termination of Philidor. Investors initially reacted well to the news, sending Valeant's shares up by 17%.

But Mr. Maris is not impressed. He claims that Valeant has failed to explain what fees Walgreens will charge to distribute its drugs. He also says Valeant hasn't shed light on if the volume from Walgreens will make up for Philidor's absence.

Mr. Maris is probably on to something here. The mere fact that Valeant signed this deal right after the Philidor debacle indicates that Walgreens had the upper hand in negotiations. So those who are expecting the Walgreens deal to plug the gap is probably kidding themselves.

Some positives

In his report, Mr. Davis did acknowledge some positive aspects of Valeant's business. He cites a number of brands that are performing very well, including Xifaxan, the company's number one drug. He also notes that the company is well diversified by product line.

That being the case, this is still an incredibly risky stock, one that Mr. Davis thinks is overvalued. So even though the stock has come off a lot since his report was published, this is a name I would stay away from.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:BHC (Bausch Health Companies Inc.)
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Date

2025/07/20

Date Created

2016/02/23

Author

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