



Why Bill Ackman Makes Valeant Pharmaceuticals Intl Inc. Shareholders Nervous

Description

During a lengthy conference call back in November, Pershing Square hedge fund manager Bill Ackman laid out his bull case for **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX), infamously stating, “The biggest regret I have with Valeant is that we’re not in a position to buy more.” I’m sure by now he wishes he could take that quote back.

Making matters worse for Mr. Ackman, his losses could put further downward pressure on Valeant’s share price. We’ll take a closer look below.

Pershing’s losses

Mr. Ackman would have bought more Valeant when he made that call, if only he had the capital to spare. But he did find a cheaper way to bet on the company: options.

To be more specific, Mr. Ackman made two very large option trades in late November, buying calls and selling puts in each of them. One of those trades has since expired, but Mr. Ackman is still on the hook for over nine million put options that expire in early 2017 (according to Pershing’s most recent filings).

Those puts have a strike price of US\$60, meaning that as of this writing, those puts are now over US\$200 million in the hole. On top of that, Pershing lost about US\$700 million on its Valeant shares on Monday, and its call options will most likely expire worthless.

What this means for Valeant’s shares

The fall in Valeant’s shares will undoubtedly trigger a margin call on the Valeant put options, forcing Pershing to come up with the cash. This may force Pershing to sell stocks.

If investors decide to flee Pershing, then the fund could be forced to sell even more stocks, including Valeant’s. Of course, this would cause fund performance to deteriorate, causing more investors to flee, and so the cycle goes. It’s no coincidence that **Herbalife Ltd.** shares increased on Monday; investors are betting that Valeant will be under a lot of pressure.

Pershing is not alone

Valeant is commonly referred to as a “hedge fund hotel,” meaning that a lot of hedge funds own the shares. And these funds usually hold very concentrated positions. For example, Valeant represented 32% of the Sequoia Fund’s portfolio back in August.

Thus we could easily see some big forced sales in Valeant’s shares, which would drive the stock down further. If you own any shares, watch out.

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