



Valeant Pharmaceuticals Intl Inc.: This Hedge Fund Manager Says Buy

Description

Through repeated acquisitions and pharmaceutical drug-price increases, **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) took its shares from \$8 in 2011 to \$340 in 2015. In the last six months, however, the company's stock has fallen by over 80% to just \$44 a share. Renowned hedge fund manager Bill Ackman is taking advantage of the dip; he now owns roughly 5% of the company, constituting 14% of his entire portfolio.

Should you follow suit?

The issues

First, Valeant's drug-pricing practices are under investigation by multiple U.S. agencies. The issue stems from possible predatory pricing schemes. For instance, after acquiring two cardiovascular products last year, the company reset their prices by more 200-500% despite making no formulaic changes.

A report by Citron Research showed possible misconduct, alleging that Valeant manipulated specialty pharmacies to artificially boost demand for its drugs, leading to higher prices. Citron even went as far to call Valeant "the pharmaceutical Enron." Chief executive officer Michael Pearson is preparing to step down and has been subpoenaed to testify before a U.S. Senate committee.

The second issue is more immediately important. Valeant failed to file its annual report on time, potentially triggering a technical default on its debt. Fortunately, on April 7 the company reported that "creditors holding more than 50% of the company's loans in principal amount voted yes to a waiver and amendment to its credit facility."

This extended the deadline for filling its report to May 31, while the deadline for filing its first quarterly report has been extended to July 31 from June 14. Valeant now has some breathing room to manage its \$31 billion in debt, but the investigation issues continue to persist.

Why does Ackman say buy?

While Valeant clearly has some serious structural issues, most of its business is still generating billions in credible cash flow. According to Ackman, investors have lost confidence in the financials, the management team, and in the company's strategy. Once these issues are inevitably addressed, the stock price will jump to reflect the intrinsic value of the company instead of pure uncertainty.

"The stock effectively trades at below three times earnings," he said, calling it a "remarkably low valuation" for a business of this quality.

To ultimately restore investor confidence, Valeant will need to replace its CEO, reaffirm its corporate governance, and issue its complete annual report.

"[The] interesting thing is it's much easier to restore confidence by making those kinds of changes. And we expect fairly rapid recover in the stock price on the basis of restoring confidence in the business," said Ackman.

More difficult will be resolving ongoing investigations. Even with some operating changes, regulatory uncertainty could keep a lid on shares for some time. At worst, it could end in the collapse of the entire company (think Enron). Ackman is surely banking on the ample upside should his view be correct. If he's wrong, however, shares could end at \$0. It's a tough bet.

CATEGORY

1. Investing

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