



Valeant Pharmaceuticals Intl Inc.: Is It Going to Default?

Description

At the end of last week, **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) revealed that it had received a notice of default from its bondholders due to a delay in filing its first-quarter earnings report. Whenever a company receives a notice of default, investors need to pay attention.

To prevent any sort of default, it will need to file its 10Q by July 18; if it doesn't, the company has some problems. Fortunately, the company expects to file its 10Q by June 10, so any sort of default is not likely to be imminent.

However, this is an important issue to understand because Valeant is sitting on \$30 billion in debt. Should the company go into default, it'll likely enter bankruptcy. When a company goes bankrupt, there's a pecking order on who receives compensation first; common shareholders—the average person who holds stock—are the last to receive compensation.

Think about that ... you might hold shares of the stock, but with \$30 billion in debt, unless the company's assets are worth much more than that, the debt holders might be the only ones who walk away with any value.

Fortunately, Valeant is making some moves that should help prevent the danger of any default.

It has brought in an incredibly experienced CEO. Joseph Papa has decades of experience in the pharmaceutical space. He's been CEO at two different healthcare companies. Before that, he was a COO. And he's been responsible for the launch of Celebrex, Diovan, and Lotrel—commercially successful products.

Based on his contract, he's only going to get really rich if he can turn the company around. His base salary is US\$1.5 million, which could increase to US\$2.25 million. He also received a cash payment of US\$8 million for giving up equity at his former company. The real kicker is the US\$10 million in stock options plus the performance-based restricted shares amounting to 933,416. Ultimately, if the stock ever reaches US\$270 again, he'll be paid US\$500 million. So he's incentivized to make Valeant great again.

Part of how he might be able to do that is by paying down some of that debt. Valeant's strategy was to buy companies, fire employees, and hike the price of the drug. Now that it's under scrutiny from the government, it may need to start operating like a true pharmaceutical company.

Step one might be to divest some of its assets. Xifaxan, a gastrointestinal drug, is estimated to have future sales of \$1 billion a year. There's also Obagi and S0lta, which are aesthetics products, and CeraVe, a skincare product.

But the really lucrative asset is Bausch & Lomb, the optical division. Some analysts have suggested that, should this division be sold, the proceeds could be used to pay down 66% of Valeant's debt. But the company would be giving up a very profitable division.

All in all, there are a lot of moves the company can make. Because of this, I don't believe Valeant is going to default. Further, I believe that this is likely the low for Valeant; therefore, it might be time to start moving this stock from the research column to the buy column. I expect, under Papa, this company should start to see significant increases over the coming years. Buy low, sell high. I think this is the low.

CATEGORY

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