Can Investors Expect Anything Good From Valeant Pharmaceuticals Intl Inc.?

Description

It seems every week there is another problem with **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX). Bond holders are hinting that Valeant will default on its debt and wind up losing everything. It can be difficult to see through all the noise to determine whether or not Valeant will be able to turn things around and potentially reward investors.

So let's stick to the facts.

A default was only going to take place if Valeant didn't file its 10Q by July 18. It filed its 10Q on June 7, more than a month sooner than when management actually promised to have it for investors. There's no denying that the company has $30 billion in debt, but it's not going to default unless it stops making payments. All this talk about a default appears to be fear and uncertainty.

Yet there is one important thing to remember about the default: in the event of bankruptcy, common shareholders are the last to get anything. Those who lent money to Valeant receive money first, and often there's nothing left for the average investor.

In that 10Q for the first quarter of 2016, things were a little chaotic. It had $2.4 billion in total revenue, which is actually up 9% from the restated first quarter of 2015. However, its GAAP EPS was actually a loss of $1.08. Yet its adjusted EPS (non-GAAP) was a positive $1.27. Further, its GAAP cash flow from operations was $558 million, up 14% year over year.

My primary concern is that its organic-based revenue–the money from products it already owns–was down $289 million. It's only earning more revenue from new acquisitions.

Then there's the updated full-year 2016 guidance. Management expects revenue to be in the range of $9.9-10.1 billion, which is down from an original expectation of $11-11.2 billion. Valeant expects that its adjusted EPS will be anywhere from $6.60 to $7.00, which is down from $8.50 to $9.50. So management expects the company to make less money.

What should investors do?

There are two things that matter most to me when it comes to Valeant.

The first is whether or not the company can be profitable when it can't egregiously overcharge for drugs. Its business model had been to acquire a company or portfolio of drugs, make sure they crossed the regulatory finish line, and then hike the price. In some instances, the price hike was hundreds of percentage points. If it can be profitable without doing that, I'll be confident.

The other thing it needs to show me is if it can actually get its debt under control. A debt load of $30 billion for a company like Valeant is far too much. Fortunately, it can sell some of its assets to pay down that debt. Sources tell the *Financial Post* that Valeant is considering selling its Amoun Pharmaceutical Co. division, which it acquired last year for US$800 million.

Valeant also has other non-core assets that it might sell, specifically some of its Latin American operations.

Finally, it's believed that dermatological acquisition Obagi Medical Products Inc., the Provenge treatment, and some of the Marathon Pharmaceuticals drugs may also be sold.

For an investor who wants to pick up shares, right now is a very risky time. While I have faith in its experienced new CEO, Valeant is a big company that will take time to turn around. If it shows in future earnings that it is growing its organic revenue and actually making a profit, this company will become a buy. Further, if it starts to pay down debt, it could become a very attractive company. For now, research and wait for the right moment.

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