Can Valeant Pharmaceuticals Intl Inc. Recover From its Implosion?

Description

Exactly one year ago today, **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) was trading at a little over $300 a share. It was considered a hedge fund hotel because all of the major players held large stakes in the company. In their eyes, Valeant was only just getting started.

And then the implosion happened.

Regulators started to question why it was charging so much for drugs it had recently acquired. There were accusations of fraud through its partnership with Philidor Rx Services. It became the ultimate bad boy in the pharmaceutical space. Other companies followed, getting beaten down by the focus the media and government had on the space.

Michael Pearson, former CEO of the company, retired and was then replaced by Joseph C. Papa, a seasoned pharmaceutical chief with the incentive to succeed. In the event that Valeant reaches $270 a share (which would take a serious turnaround), he'll receive a $500 million payment. With the stock trading at just a little over 10% of what it used to, Papa has his work cut out for him.

The first thing on the docket is paying down its debt. Pearson took the company on a buffet of acquisitions, buying products and companies left and right in his quest to build one of the largest pharmaceutical companies ever. But now it sits on US$32 billion in debt. Valeant's debt is three times the size of its market cap, so it has work to do.

Fortunately, management recognizes this. It pledged to pay back US$1.7 billion in debt by the end of 2016. Thus far, it has already paid back US$1.3 billion. Despite what some analysts have suggested, Valeant actually generates significant cash flow, making it possible to pay back these loans. Despite paying off US$1.3 billion, its cash position grew to US$850 million from US$600 million.

Valeant has also announced that it would begin selling its non-core assets to further pay down debt. This doesn't include its prime assets, such as Bausch + Lomb, but management believes that it canget US$8 billion for the 20% of non-core assets it's selling. I'm skeptical only because Valeant likely overpaid for these assets, since it believed it could just hike prices, and, more importantly, it is in a position of desperation. Competitors are likely to take advantage of that.

Valeant also announced that it was shaking up its chief financial officer position by replacing Robert Rosiello with Paul Herendeen. The market loves this. David Risinger at **Morgan Stanley** gave three reasons why this change was good. First, Herendeen has experience working for public and private pharmaceutical companies and has a return-on-capital mindset. Second, he has operational experience. And finally, he is well respected, which will add credibility to the company.

If Papa is going to get the company back to $270 a share and get his $500 million payday, he's going to need a top-notch team around him.

Should you buy?

I'm beginning to warm up to Valeant.

It has taken a beating, its stock price was obliterated, and many have called it dead. But it's generating some serious cash flow, it has strong brands, it's paying down its debt (albeit slowly), it will sell non-core assets to speed up debt repayment, and finally, it has brought on an expert executive who will further legitimize Valeant.

While it still carries significant risk, investing in Valeant could turn out to be a very lucrative trade.

CATEGORY

1. Investing

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