Valeant Pharmaceuticals Intl Inc. in Talks to Sell $10 Billion Division: What Now?

Description

Just before the markets closed on Tuesday, reports came out that **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) was in talks to sell the recently acquired Salix Pharmaceuticals for US$10 billion to **Takeda Pharmaceutical Co.** The news sent shares skyrocketing. Whenever rumours come out about possible deals, it can be both very exciting as well as incredibly nerve wracking.

So to answer the question in the headline of what to do now, I say do absolutely nothing. We are not in the business of trading or making emotional decisions. While it is true that shares went up, we need to think about what the company will be like in the next couple of years rather than the next couple of hours or days.

With all that said, let's talk through this deal.

If this deal were to go through, it would have significant implications for Valeant, primarily because it is sitting on US$32 billion in debt. If you've been reading my coverage of Valeant, I've expressed concern about this. By getting the debt under control, I believe Valeant will be in a better position to grow more organically.

There's only one problem: it only bought Salix a year and a half ago for US$14.5 billion including net debt. In other words, the company effectively rented the business for 1.5 years and is stuck with a $4.5 billion price tag for that rental. But Valeant has new management, and it has to work with what it has–irrespective of what decisions former management made.

According to *The Wall Street Journal*, the terms of the deal are that Takeda will pay US$8.5 billion for the company plus additional royalties. And in the event this deal falls through, there is another bidder waiting to participate.

So for investors who have been holding this stock, my recommendation is to wait and see where the stock goes. But what about those that have been sitting on the sidelines? Should they get in?

That depends entirely on your risk tolerance. Valeant used to be considered a hedge fund hotel because every hedge fund owned a piece. The stock rose wonderfully over the years, and investors thought the sky was the limit. Then it started to experience problem after problem, and shares proceeded to tank.

All that said, if this deal does go through, I believe Valeant is definitely worth considering, and there are a few reasons for that.

Valeant has a top-notch CEO leading the company. Joseph Papa has a $500 million incentive to get shares back to $270. And Papa has done a solid job leading other pharmaceutical companies.

Valeant kicks off incredible amounts of cash flow, despite it paying back its debt. So far this year, it has paid back US$1.7 billion of its US$32 billion in debt. And yet its cash position grew from US$600 million to US$850 million. That means that it is still generating good money from its products, is paying down debt, and is putting itself in a position to get more aggressive with debt repayment.

Anytime there is acquisition news, investors get excited. However, we need to think about this in the long term. This sort of a deal (if it goes through) would play a big part in Valeant becoming a leaner and more efficient operation. And getting the debt under control is a great way for Valeant to reward investors. For those who own it, I would wait to see how things shake out. And for those who want to own it, I would wait for more concrete news.

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