Why Bill Ackman Should Give Up on Valeant Pharmaceuticals Intl Inc.

Description

Bill Ackman has stood by his investment in **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX), despite losing over 90% of his original investment. He admitted that he regretted his initial investment in Valeant, but why does he still own shares in the stock? It's never a good idea to keep holding a loser, especially if there are suspicions of fraud. So it's a mystery as to why the billionaire activist investor still owns shares in this company.

Horrid quarter could be the start of a further pullback

Valeant recently reported a very disappointing quarter and lowered its outlook. It was expected that the quarter would be bad, but it was worse than everyone thought, and the stock responded by tanking even further. If you were a contrarian investor recklessly trying to catch a bottom in the stock, you would have been hurt bad.

It's a common misconception that because a stock has fallen so much, little downside remains, and that there's a margin of safety just because the stock is down. While this may be true in some cases, in most scenarios this is not the case, and you could post much bigger losses before you see any gains.

Valeant is making the effort to pay back its massive debt. The acquisition party is over, and it's time to clean up the mess that ex-CEO Michael Pearson left. Valeant has paid $1.6 billion back in debt so far this year, and it's doing its best to pay back the debt without liquidating core assets such as Bausch and Lomb.

While that $1.6 billion sounds like a lot, there are more debt repayments and divestments that must be made next year if the company is to survive. Valeant is going to have troubles financing any sort of R&D, which is required for a pharmaceutical company to be competitive in today's tough market.

Huge debt could limit upside in the long run

B + L International is the only business under Valeant that was reporting higher sales, and it'sexpected that R&D costs could go up in order to keep sales growth strong going forward. Valeant is ina very tough spot right now; it needs to pay back the mountain of debt as soon as it can.

Valeant told the media this month that it was negotiating with third parties for the sale of Salix. Such a sale will free up cash that will allow Valeant to be a bit more flexible than it is right now. If Valeant can get a deal that is close to the price it originally paid for it, then you can expect Valeant to soar. But if there's a larger than expected loss from this divestiture, then Valeant will continue to drop further into the abyss.

There's no bottom in this stock, and it's unwise to try to catch a falling knife. Don't be like Bill Ackman. If you can honestly say that you're holding the stock because you believe in the business–and aren't in it just because you don't want to realize a loss–then feel free to buy more. Be warned though, because volatility is pretty much guaranteed in 2017 as the company tries to turnaround.

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joefrenette