



Is it Time to Say Goodbye to Valeant Pharmaceuticals Intl Inc.?

Description

Shares of **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) were on fire earlier this year, having risen an amazing 92% in the four months between April and July.

Yet since then, the stock has cooled off, giving back some of those gains and closing trading on the Toronto Stock Exchange on Friday at \$18.13.

Analysts have cooled off Valeant too — the average rating being given to the stock by Bay Street is a “Hold” with an average target price of \$19, suggesting that there may not be much life left in the current rally.

That's at least partially owing to the fact that company has been facing difficulty as it transitions from an aggressive acquisition strategy to a period of cost rationalization and asset sales.

The string of acquisitions, which saw the company spend in excess of \$26 billion between 2011 and 2015, has left Valeant with a seemingly insurmountable amount of debt on its balance sheet.

As of the company's second-quarter reporting, Valeant owed \$27.6 billion in debt compared to just \$3.9 billion of shareholders' equity for an incredible 7.1 times debt-to-equity ratio.

Making matters worse, the company is being forced to completely re-think its old business model, which had seen it forego spending on research and development (R&D) in favour of acquiring businesses that had established pipelines of drugs, which Valeant would then assume responsibility for, market, and sell.

The unfortunate result today is that amid a lack of R&D spending, the company is now seeing its EBITDA (earnings before interest, taxes, depreciation, and amortization) shrink and is being forced to sell assets to shore up its balance sheet.

If the current trend persists, it could be dire straits for Valeant and its shareholders.

That's because the company has a long way to go before the debt issue can be put to bed.

Valeant has \$811 million in debt coming due during the second half of 2017 and \$502 million coming due in 2018, but the real challenge will come in 2020, when the company faces \$5.7 billion of debt maturities.

The good news is that the payments due in 2017 and 2018 don't pose much of a threat to the company, as Valeant should have enough cash flow generated from its existing operations to meet those obligations.

Even the \$5.7 billion coming due in 2020 can be managed, provided the company is successful in getting fair value for some of the non-core assets it picked up during its buying spree.

Keep in mind that during the first half of 2017, the company was able to execute \$2.1 billion of divestitures; so, while there is still a long way to go, maybe it isn't time to panic just yet.

Don't say goodbye, for now

Foolish investors willing to hang on to their shares in Valeant through the turnaround period may find that their patience could be handsomely rewarded.

As Valeant retires its outstanding debt, that value, which used to belong to the company's bondholders will transfer to the company's shareholders, which currently hold less than 15% of the company's total enterprise value.

The law of small numbers dictates that if the current strategy of debt reduction proves successful, shareholders in Valeant stock could very well see the value of their investment multiply in short order.

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Date

2025/07/27

Date Created

2017/10/12

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jphillips

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