Valeant Pharmaceuticals Intl Inc. Is Down 15%: Is it a Buy?

Description

When you're dealing with a beaten-down and debt-ridden company like **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX), things are going to get volatile. And that's exactly what's been going on with Valeant, with shares down over 15% in the last 10 days. But volatility goes both ways, and it's possible to find a great entry price when other investors are scared.

So, we have to ask ourselves if this is the perfect time to buy the dip and pick up shares of Valeant. First, we need to understand whether the possible gains outweigh the risks or if this company is simple a house of cards just waiting for a big gust of air to knock it over.

Step one: look at the debt

Before Valeant's drop from greatness, Valeant borrowed tens of billions of dollars in its quest to acquire assets. Valeant's strategy was simple. If it borrowed money to purchase a drug that was already being sold, it could increase the price and pay the debt down with the additional cash flow. But when that strategy surfaced, Valeant had to change course.

Unfortunately, Valeant now has a lot of debt without the ability to egregiously boost prices.

On August 15, Valeant paid back the remaining US$500 million owed on a 6.75% senior note that was coming due in 2018. Valeant has been tactically selling non-core assets, using the funds to pay back its bond holders. Valeant is now surpassing its originally goal of paying back US$5 billion by February 2018, so that's a good step.

This also means that Valeant has time. Its next major debt maturation is in 2020, when it will have to redeem US$5.8 billion. An additional US$10.5 billion is due by 2022, so a major part of Valeant's recovery depends on what happens over the next five years.

Step two: start growing revenue

By selling so many different assets, the company's revenue has dropped. Management originally projected US$8.9-9.1 billion in revenue for the year, but after selling off Dendreon Pharmaceuticals, they dropped that projection to US$8.7-8.9 billion. So, where’s the money going to come from?

Management is betting big on the recently launched Siliq, a psoriasis drug, which is supposed to be far better than its competitors. Valeant is currently charging US$3,500 per month, which is much cheaper than its competitors, because it is looking to take market share. Another reason for the cheap price is that Siliq carries a black-box warning. This is the strictest warning put on a drug when evidence shows serious hazards from taking the drug.

But if Valeant can convince physicians to prescribe it anyway — they hope doctors see the benefits outweighing the risks — then it could be a major line of business. Analysts are conflicted; one suggested it might be a US$250-million-a-year business, while another believes it could be a US$600-million-a-year business. Obviously, investors want the latter.

In total, Valeant continues to move forward with a variety of product launches and hopes that these new products will be able to increase revenue by US$100 million. And if those products gain traction, 2018 and 2019 should be even stronger.

Bottom line

A turnaround is a two-step process for Valeant. It bought time by paying back so much of its debt, but now Valeant needs to grow revenue. If it can achieve that, this could turn out to be an amazing investment. Having a small high-risk position might be worth it for those that can stomach the volatility. And this dip is the right time to buy.

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