

NYSE **VRX**

VALEANT PHARMACEUTICALS INTL

PHARMACEUTICALS INDUSTRY

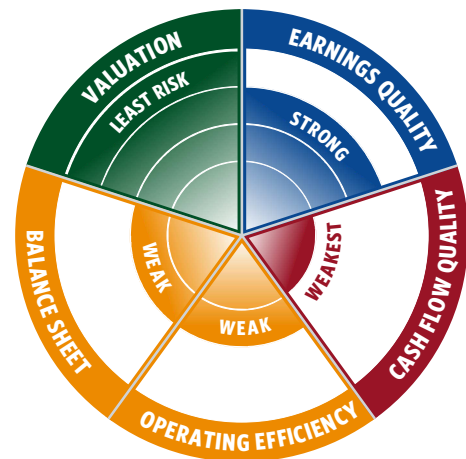
OVERALL RATING FOR 3RD QUARTER 2015 **SELL**

OUR EVALUATION OF VRX

VALEANT PHARMACEUTICALS INTL is showing strong Earnings Quality, and Valuation suggests a lower amount of price risk, but Operating Efficiency, Balance Sheet Quality and Cash Flow Quality are weak. When combined, VRX deserves a SELL rating.

The Valuation rating improved the most during the most recent quarter. Though this dimension and all of the others were either stronger or unchanged at worst, it was not sufficient to raise the overall rating.

FINANCIAL SONAR™ FOR VRX 3RD QUARTER 2015

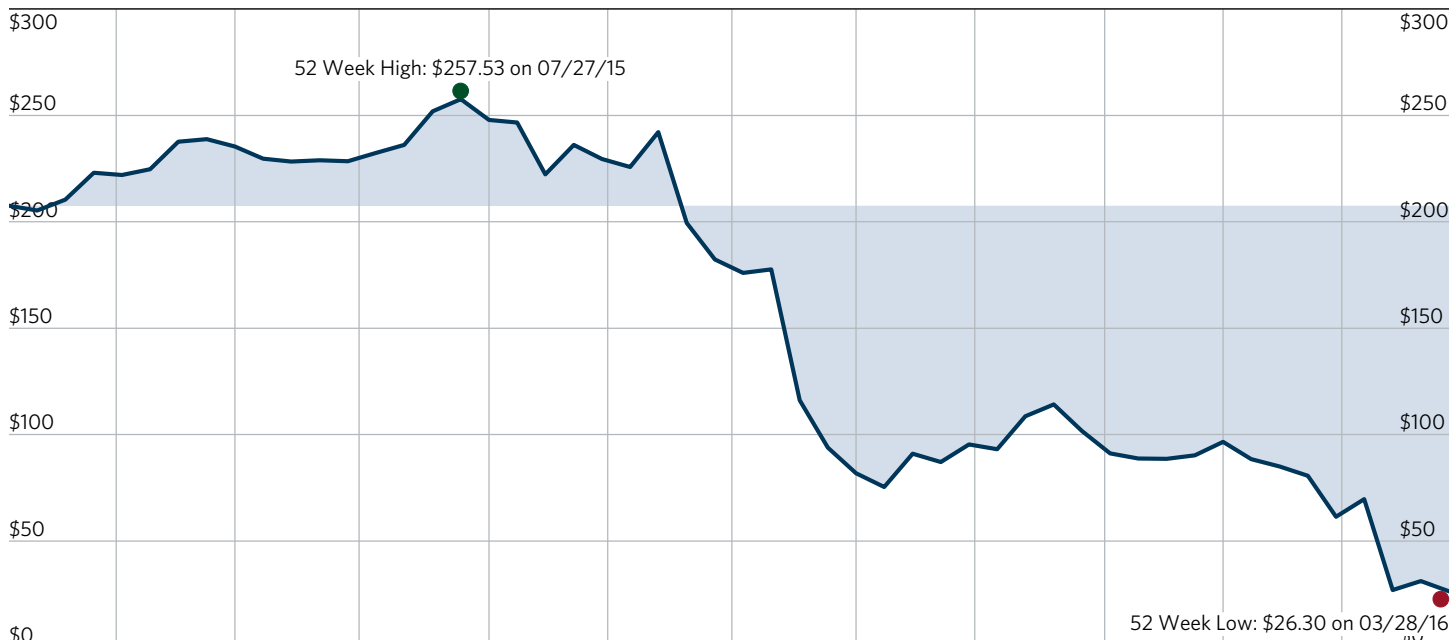


HISTORICAL RATINGS

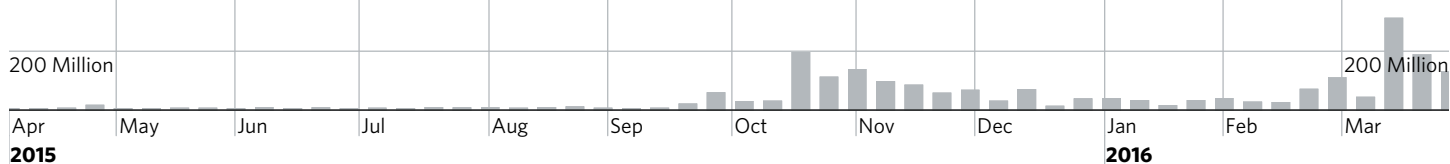
	Q4 2014	Q1 2015	Q2 2015	Q3 2015
OVERALL RATING	SELL	HOLD	SELL	SELL
EARNINGS QUALITY	STRONG	STRONG	WEAK	STRONG
CASH FLOW QUALITY	WEAKEST	WEAKEST	WEAKEST	WEAKEST
OPERATING EFFICIENCY	STRONG	STRONG	WEAK	WEAK
BALANCE SHEET	WEAK	STRONG	WEAKEST	WEAK
VALUATION	MOST RISK	MOST RISK	MOST RISK	LEAST RISK

PRICE TRENDS AND VALUATION

Price (AS OF 03/10/16)	\$66.20	MARKET CAP.	\$22.6 BILLION	PRICE/SALES	2.3
PRICE/EARNINGS	36.8	PRICE/EARNINGS GROWTH	NA	PRICE/CASH FLOW	7.9
PRICE/ADJUSTED EARNINGS	34.4	PRICE/ADJUSTED EARNINGS GROWTH	-563.9	PRICE/ADJUSTED CASH FLOW	-244.1



Average Weekly Volume



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OVERALL RATING FOR 3RD QUARTER 2015 **SELL**

EARNINGS QUALITY: STRONG

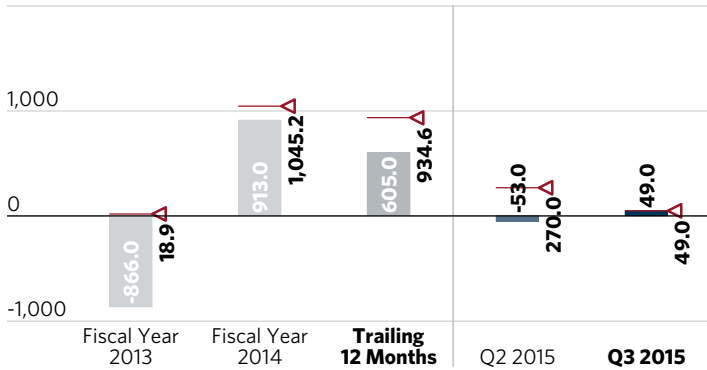
Earnings quality has long been analyzed and used by investors as a measure of the fundamental quality of the company and its future prospects. Companies may be including certain items that increase reported earnings and often the amount of cash flow supporting the earnings may be weak. Jefferson adjusts for these kinds of items and other anomalies to produce an adjusted earnings number that more accurately reflects ongoing business fundamentals at VALEANT PHARMACEUTICALS INTL. Reported earnings are compared to the Jefferson adjusted earnings as a means to gauge earnings quality. Also measured is the amount of cash flow that underpins earnings.

The earnings quality for VRX improved from WEAK to STRONG.

With a reported net income of \$49.0M in the last quarter that was equal to the adjusted number, VRX's quality of net income earnings is extremely high. However, operating cash flow rose in the current quarter to \$736.0M from \$410.0M, but the quality decreased as the ratio of operating cash flow to earnings declined.

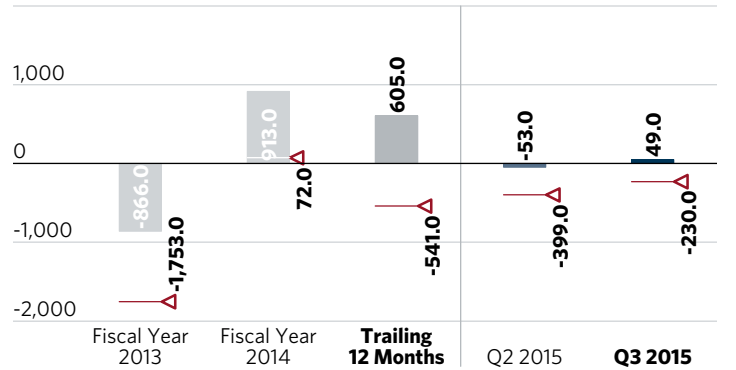
NET INCOME VS. ADJUSTED NET INCOME \$ IN MILLIONS
 ▲ Adjusted Net Income

Adjusted Net Income as a Percentage of Net Income
 102.2% 114.4% 154.5% 610.7% 100.0%



EARNINGS VS. OPERATING CASH FLOW \$ IN MILLIONS
 ▲ Reported Operating Cash Flow

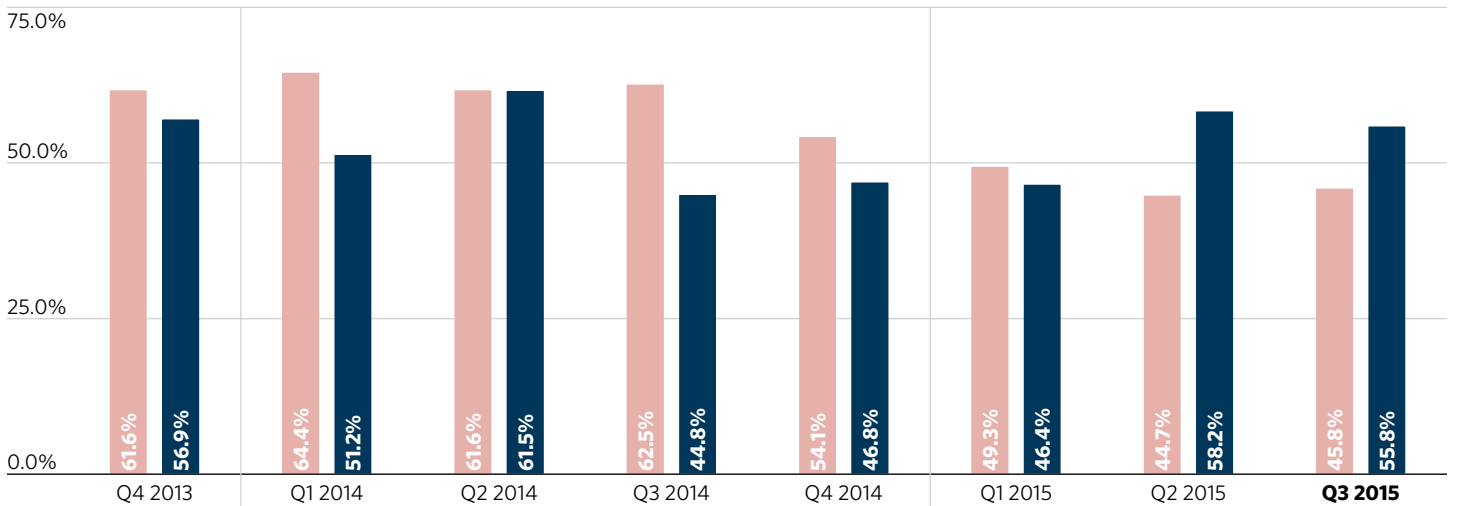
Operating Cash Flow as a Percentage of Earnings
 220.3% 251.2% 405.5% 874.5% 1487.7%



ACCRUALS

Actual Accruals Forcasted Accruals

% OF SALES



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OVERALL RATING FOR 3RD QUARTER 2015 **SELL**

CASH FLOW QUALITY: WEAKEST

Cash flow is considered by many investors to be the ultimate measure of company performance and more reliable than reported earnings. The Jefferson measurement eliminates items that are not part of recurring cash flow or the result of actual operations for VALEANT PHARMACEUTICALS INTL. These adjustments to cash flow provide a truer measure of cash flow and the resultant cash flow quality rating.

The cash flow quality rating for VRX remains WEAKEST as the operating cash flow quality year over year improved.

Even though the annual operating cash flow quality improved this fiscal year with a reported number of \$2,294M and an adjusted number that was 3.1% of reported, the decline in the quarter's free cash flow quality offset this with a reported number of \$685.0M and an adjusted number that was \$966.0M less than reported. This represents deterioration from the previous period when the reported number was closer to the adjusted number.

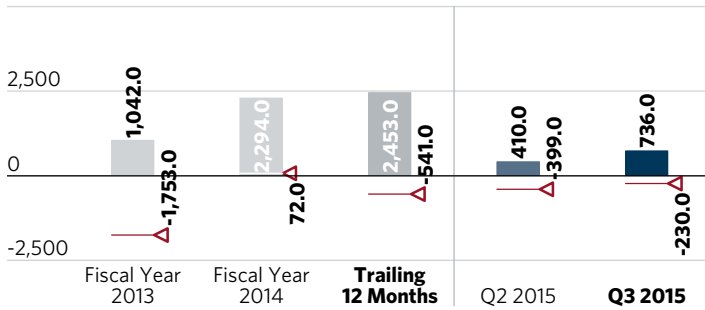
OPERATING CASH FLOW

\$ IN MILLIONS

▲ Adjusted Operating Cash Flow

Adjusted Operating Cash Flow as a Percentage of Operating Cash Flow

-168.3% 3.1% -22.1% -97.2% -31.3%



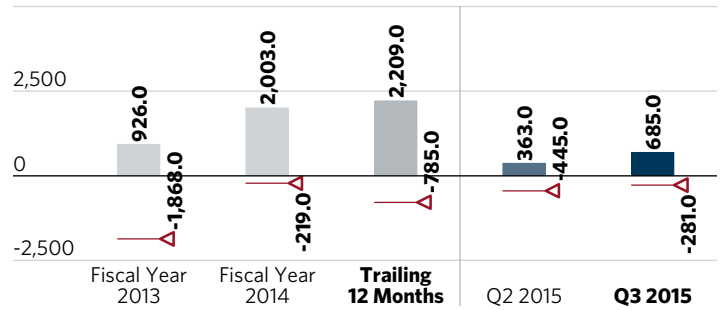
FREE CASH FLOW

\$ IN MILLIONS

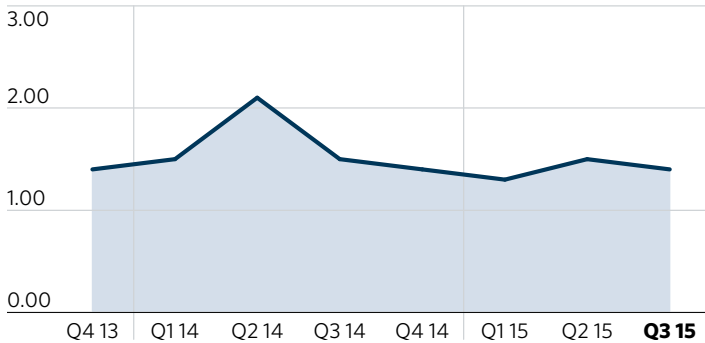
▲ Adjusted Free Cash Flow

Adjusted Free Cash Flow as a Percentage of Free Cash Flow

-201.7% -11.0% -35.5% -122.6% -41.0%

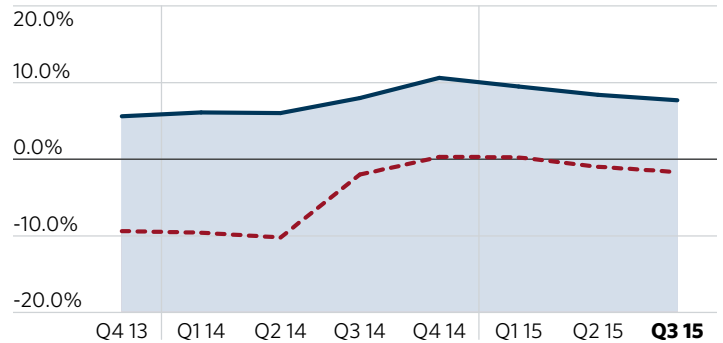


FLOW RATIO



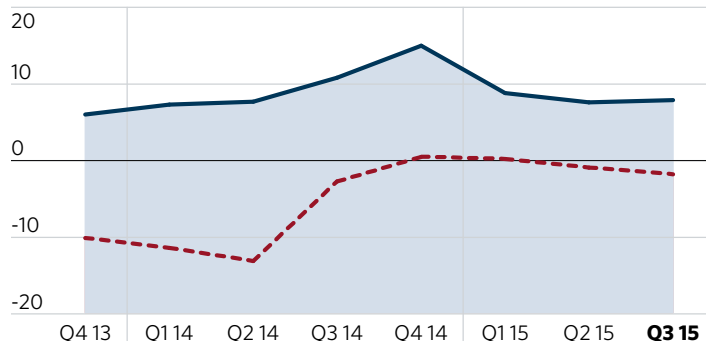
CASH FLOW ROI

--- Adjusted Cash Flow ROI



DEBT COVERAGE

--- Adjusted Debt Coverage



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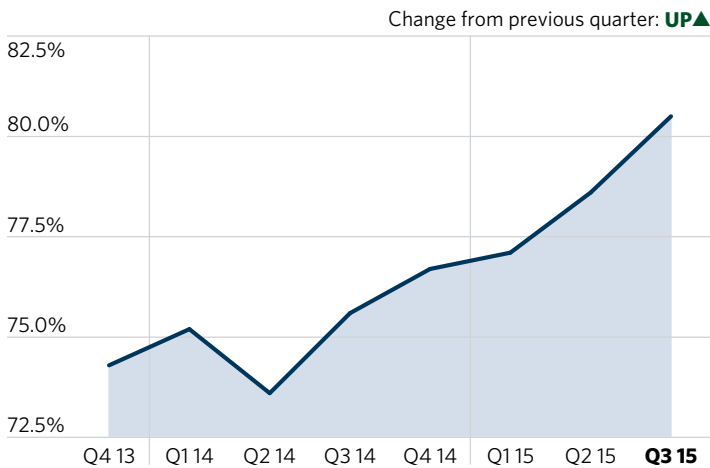
OPERATING EFFICIENCY: WEAK

The ability of VALEANT PHARMACEUTICALS INTL to earn a profit is in part the result of how rapidly it converts its collection of assets into revenues and the resulting earnings and cash flow margins available. Operating Efficiency is measured by a combination of factors including: return on invested capital (ROIC), gross margin, EBIT margin, asset turnover, equity turnover, and lastly Staff, General, and Administrative costs as a percentage of sales (SGA).

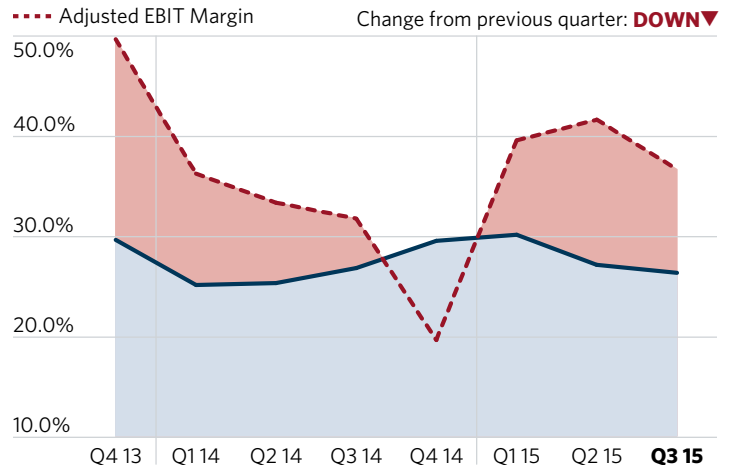
The operating efficiency rating for VRX remains WEAK as the gross margin and SGA costs strengthened over the last quarter, while at the same time the ROIC and EBIT margin weakened.

Even though the gross margin improved from 78.6% to 80.5%, the decline in ROIC offset this, deteriorating from 3.2% to 2.0%. The lower ROIC indicates that VRX is producing less profit per dollar of capital invested in the business.

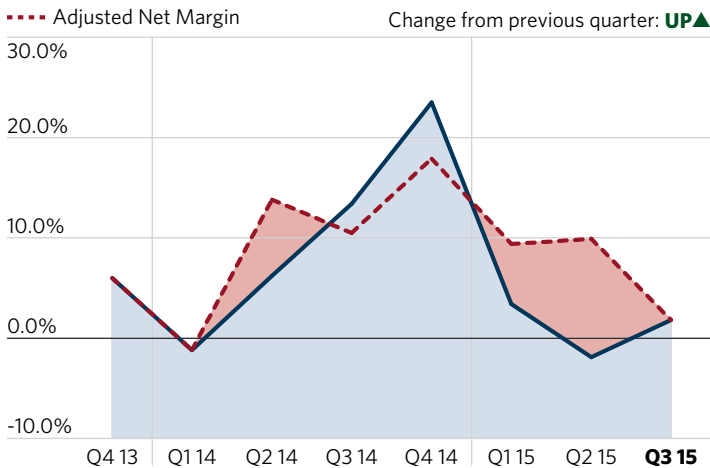
GROSS MARGIN



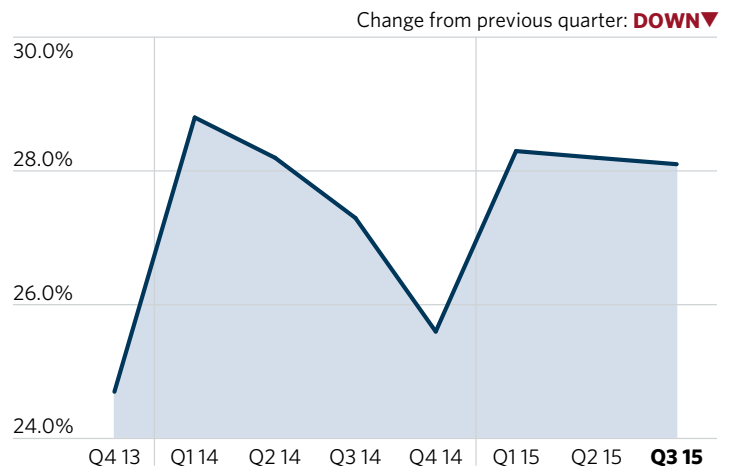
EBIT MARGIN



NET MARGIN



SG&A AS A PERCENTAGE OF SALES



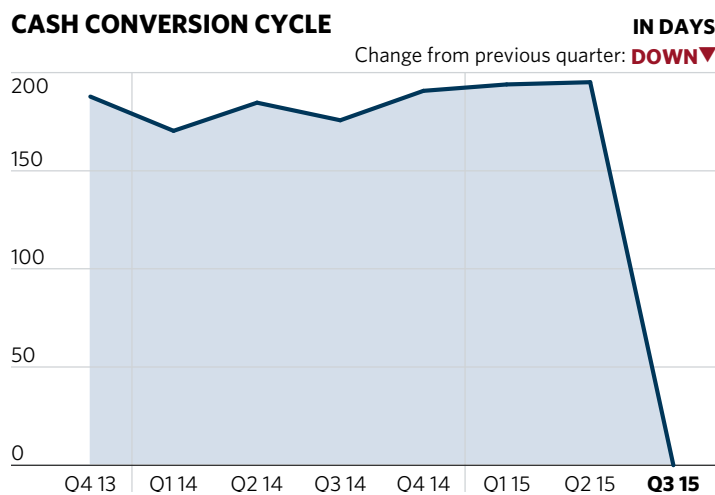
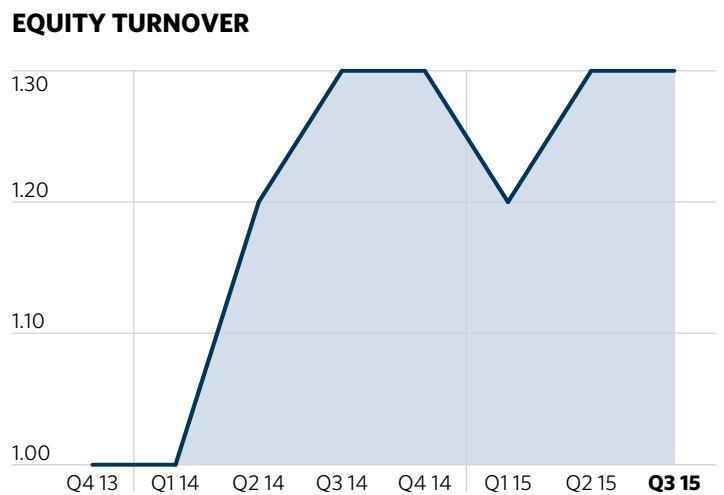
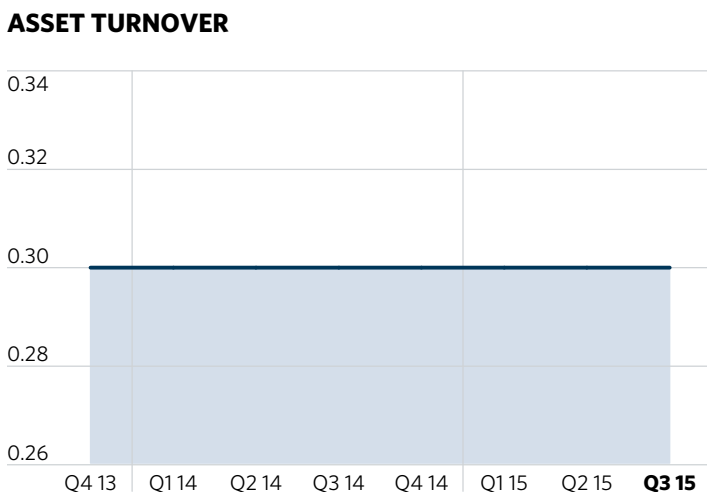
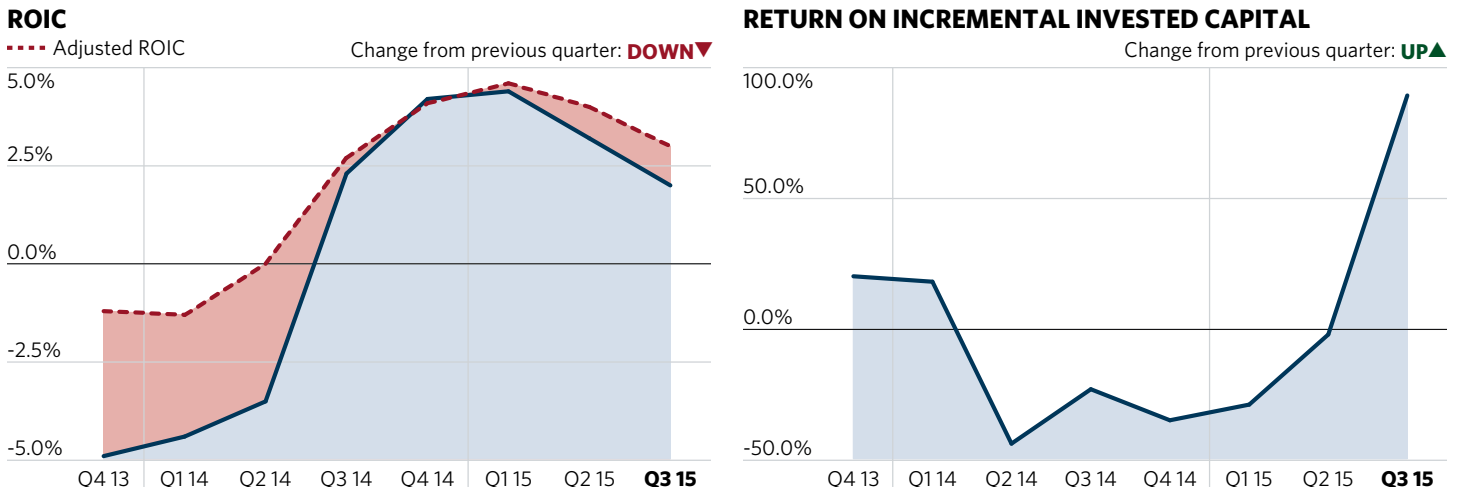
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OVERALL RATING FOR 3RD QUARTER 2015 **SELL**

OPERATING EFFICIENCY: **WEAK**



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BALANCE SHEET QUALITY: **WEAK**

The balance sheet shows the ability of VALEANT PHARMACEUTICALS INTL to pay its bills and fund future growth. It also provides clues to aggressive accounting since reported earnings that do not generate cash flow generally end up somewhere on the balance sheet. The following are analyzed in determining balance sheet quality: quick ratio, current ratio, cash position, accounts receivable days sales outstanding (AR DSOs), and number of days inventory is held prior to sale to customers (Inv Days).

The balance sheet rating for VRX strengthened from WEAKEST to WEAK as the cash position, quick ratio, Inv Days, and debt/assets improved over the last quarter.

The cash position increased from \$958.0M to \$1,420M. With more cash on hand VRX will be better able to meet financial obligations. In addition, the quick ratio improved from 0.8X to 0.9X. The higher quick ratio indicates that VRX has increased the amount of liquid assets relative to current liabilities.

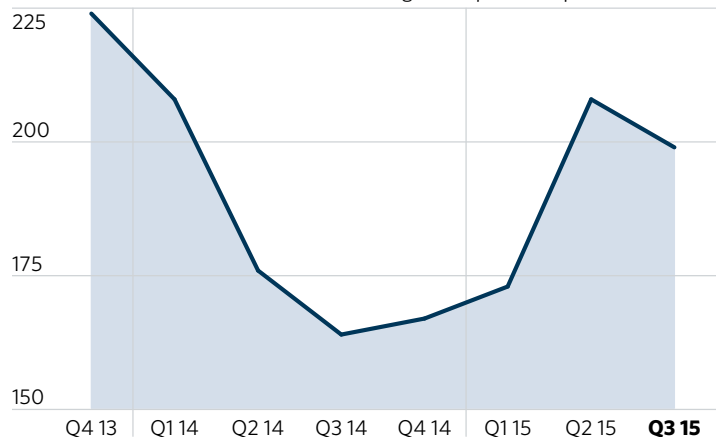
RECEIVABLES DAYS OUT

Change from previous quarter: **UP▲**

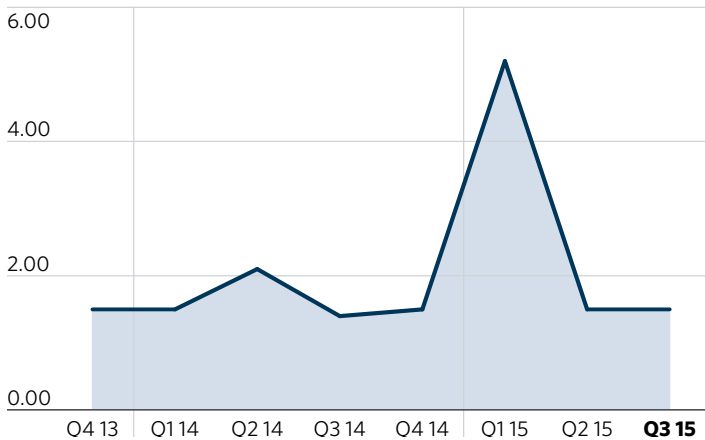


INVENTORY DAYS OUT

Change from previous quarter: **DOWN▼**

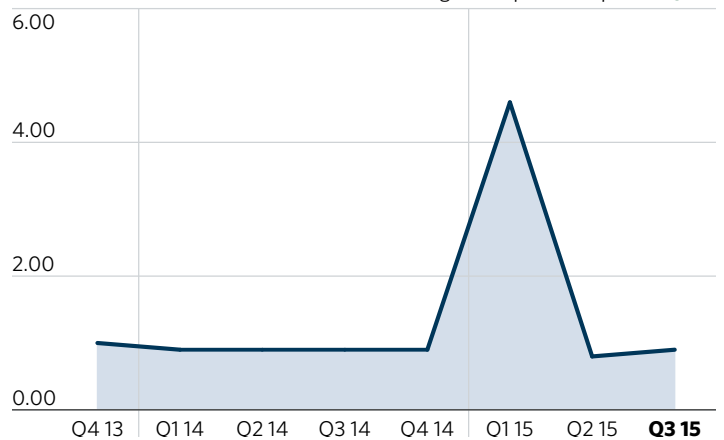


CURRENT RATIO



QUICK RATIO

Change from previous quarter: **UP▲**



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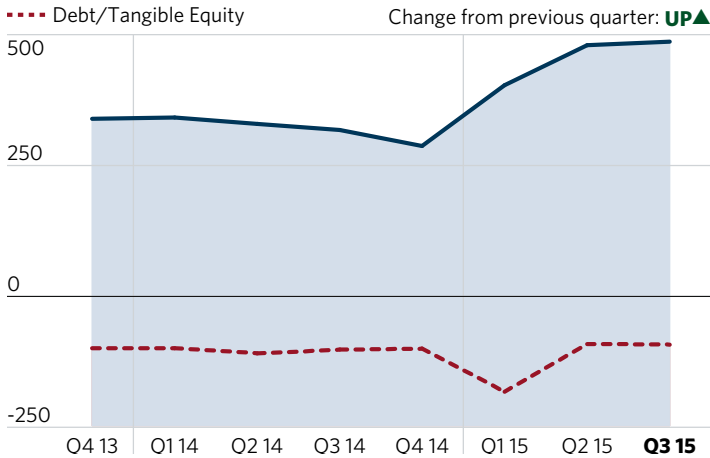
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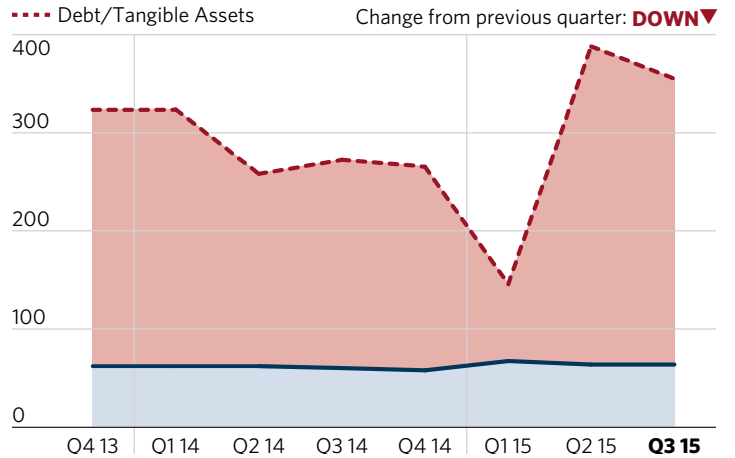
OVERALL RATING FOR 3RD QUARTER 2015 **SELL**

BALANCE SHEET QUALITY: WEAK

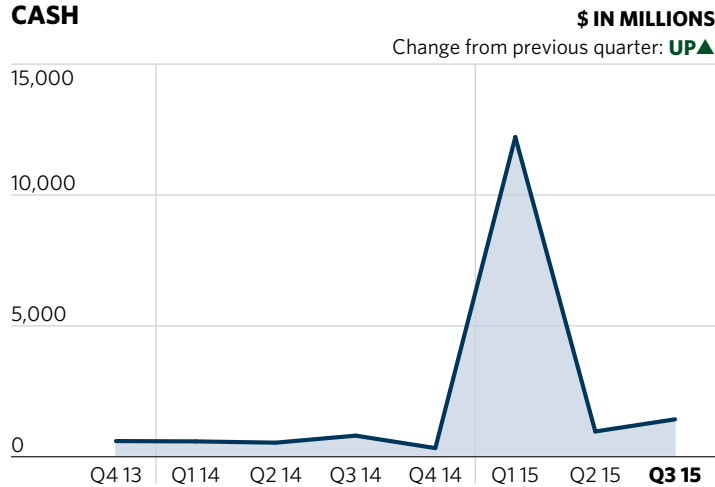
DEBT/EQUITY



DEBT/ASSETS



CASH



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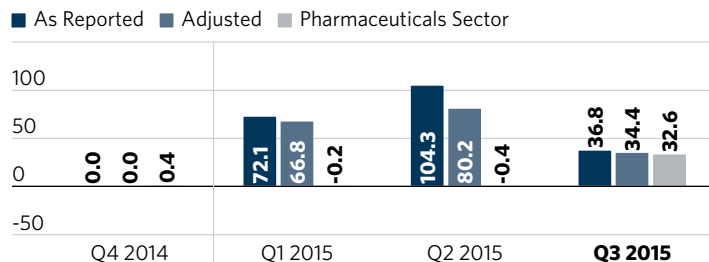
VALUATION: LEAST RISK

A favorable valuation (a LEAST RISK or LOW RISK rating) implies lower potential downward price risk that is evidenced by a company price multiple that is lower than the corresponding sector average. The valuation rating is based on both absolute and relative levels at VALEANT PHARMACEUTICALS INTL compared to its peers within its sector based on price to earnings (PE), price to earnings growth (PEG), price to sales (PS), and price to cash flow (PCF).

The valuation rating for VRX improved from a MOST RISK to a LEAST RISK

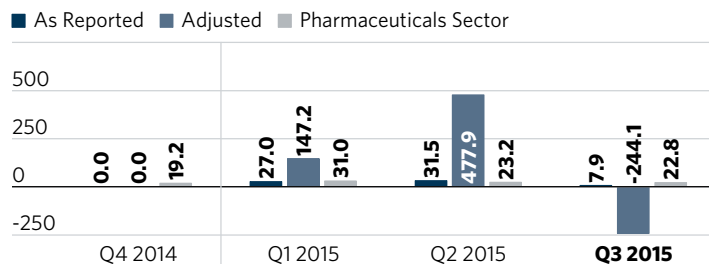
PRICE/EARNINGS

LAST 2 YEARS	RANGE		AVERAGE
	LOW	HIGH	
Reported Price/Earnings	0.00	104.30	60.38
Adjusted Price/Earnings	-223.90	59046.80	7364.59
Sector Price/Earnings	24.40	36.90	28.79



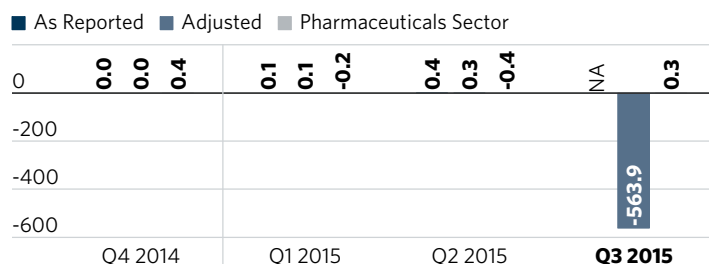
PRICE/CASH FLOW

LAST 2 YEARS	RANGE		AVERAGE
	LOW	HIGH	
Reported Price/Cash Flow	0.00	42.00	24.08
Adjusted Price/Cash Flow	-1422.10	477.90	-138.70
Sector Price/Cash Flow	12.60	31.00	20.53



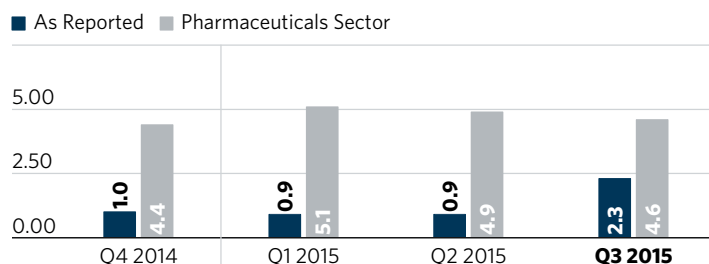
PRICE/EARNINGS GROWTH

LAST 2 YEARS	RANGE		AVERAGE
	LOW	HIGH	
Reported Price/Earnings Growth	0.00	0.40	0.17
Adjusted Price/Earnings Growth	-563.90	0.30	-140.87
Sector Price/Earnings Growth	-3.30	2.70	-0.22



PRICE/SALES

LAST 2 YEARS	RANGE		AVERAGE
	LOW	HIGH	
Reported Price/Sales	0.90	2.30	1.20
Sector Price/Sales	3.80	5.10	4.38



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PEER VALUATION COMPARISON

TICKER	COMPANY	MARKET CAP.	PRICE ON 03/31/16	PRICE/ EARNINGS	PRICE/ SALES	PRICE/ CASH FLOW	PRICE/ EARNINGS GROWTH	VALUATION RATING
TEVA	TEVA PHARMACEUTICAL INDS-ADR	\$54.7 B	\$53.50	29.1	2.6	17.4	NA	LEAST RISK
SHPG	SHIRE PLC -ADR	\$34.0 B	\$171.90	0.0	4.8	15.6	NA	LOW RISK
MYL	MYLAN NV	\$22.7 B	\$46.40	38.0	2.3	12.0	NA	LEAST RISK
VRX	VALEANT PHARMACEUTICALS INTL	\$22.6 B	\$66.20	36.8	2.3	7.9	NA	LEAST RISK
ZTS	ZOETIS INC	\$22.0 B	\$44.30	65.2	4.3	38.0	5.2	MEDIUM RISK
PRGO	PERRIGO CO PLC	\$18.3 B	\$127.90	131.9	3.4	30.6	NA	LOW RISK
JAZZ	JAZZ PHARMACEUTICALS PLC	\$8.0 B	\$130.60	24.3	5.6	17.0	1.0	LOW RISK
PHARMACEUTICALS SECTOR		\$36.2 B	—	32.6	4.6	22.8	0.3	—

PEER OPERATING COMPARISON

TICKER	COMPANY	MARKET CAP.	GROSS MARGIN (%)	EBIT MARGIN (%)	NET MARGIN (%)	ROIC (%)	CASH CONVERSION CYCLE (DAYS)	OPERATING EFFICIENCY RATING
TEVA	TEVA PHARMACEUTICAL INDS-ADR	\$54.7 B	65.0	24.5	10.2	4.8	124.0	MEDIUM RISK
SHPG	SHIRE PLC -ADR	\$34.0 B	86.6	35.7	16.5	14.4	192.0	MOST RISK
MYL	MYLAN NV	\$22.7 B	58.4	19.7	7.8	5.8	157.0	MEDIUM RISK
VRX	VALEANT PHARMACEUTICALS INTL	\$22.6 B	80.5	26.4	1.8	2.0	0.0	MEDIUM RISK
ZTS	ZOETIS INC	\$22.0 B	66.6	23.4	1.7	7.2	308.0	MEDIUM RISK
PRGO	PERRIGO CO PLC	\$18.3 B	50.0	15.8	-7.5	-0.2	0.0	MOST RISK
JAZZ	JAZZ PHARMACEUTICALS PLC	\$8.0 B	93.8	45.8	24.3	12.1	-35.0	LOW RISK

DEFINITIONS

Adjusted Net Income: Adjusted Net Income is a company's reported net income less adjustments for one-time and non-operating items yielding a more realistic picture of a company's ongoing earnings.

Accruals – Forecasted and Actual: The comparison of forecasted and actual accruals identifies a discretionary build not attributable to a company's sales growth, and could be a sign of poor earnings quality. For our purposes, the forecasted accrual component is an aggregate measurement of total accruals (short-term balance sheet accounts) that distinguishes between "normalized" and "extraordinary" accruals. The normalized accruals are based on historical relationships between sales and accruals and are dynamically adjusted over time to account for changes in the ratio between these two variables. Normally, short term accruals will grow as sales grow – i.e., the "normalized" measure. Discretionary accruals are the portion of accruals that are in excess of the base factor and therefore exceed the normal and are "extraordinary".

Adjusted Operating Cash Flow: Adjusted Operating Cash Flow is reported operating cash flow less adjustments for one-time and non-operating items yielding a more realistic picture of a company's ongoing cash flow from operations.

Adjusted Free Cash Flow: Adjusted Free Cash Flow is reported operating cash flow less adjustments for one-time, non-operating items and capital expenditures. This provides a more realistic picture of a company's ongoing cash generation from operations after capital investments.

Flow Ratio: The Flow Ratio is a measurement of management's effectiveness in managing its working capital to maximize the company's cash flows. The measure is a ratio of a company's non-cash current assets to its non-interest bearing short-term liabilities.– These non-cash assets include items such as accounts receivable (which are essentially interest-free loans to customers) and inventory (which is subject to obsolescence or spoilage). The non-interest bearing liabilities are essentially interest-free loans to the company. A lower ratio implies tighter cash management for a company as it has less cash tied up in non-cash current assets and is able to utilize interest free loans from suppliers.

Cash Flow Return on Investment: Cash Flow ROI is a measure of a company's ability to generate operating cash flow from its invested capital. Many analysts consider this measure preferable to an earnings return measure such as ROE since cash flow is considered a more reliable measure.

Adjusted Cash Flow Return on Investment: Adjusted Cash Flow ROI is a measure of the ability to generate operating cash flow from its investment in capital calculated using a company's adjusted cash flow.

Debt Coverage: Debt Coverage is a measure of a company's ability to cover its debt obligations with cash flow it generated from continuing operations.

Adjusted Debt Coverage: Adjusted Debt Coverage is a measure of a company's ability to cover its debt obligations with cash flow it generated from continuing operations, calculated using a company's adjusted cash flow.

Adjusted Return on Invested Capital: Adjusted ROIC assesses a company's efficiency at allocating the capital to profitable investments using a company's adjusted net income (see above) yielding a measure of how well a company is using its capital to generate returns.

Adjusted EBIT Margin: Adjusted EBIT Margin is a measure of a company's earnings before interest and income taxes less adjustments for one-time and non-operating items divided by a company's sales.

Adjusted Net Margin: Adjusted Net Margin is a measure of a company's net income less adjustments for one-time and non-operating items divided by a company's sales.

Return on Incremental Invested Capital: ROIC measures the relationship between incremental investment and incremental net operating profit after tax. This provides a measure of the returns a company is earning on recent investments rather than all investments as measured by ROIC.

Cash Conversion Cycle: The Cash Conversion Cycle measures the number of days working capital is tied up from the date of purchase of raw materials until the collection of cash from the sale of the product.

Debt to Tangible Equity: Debt to Tangible Equity is a ratio of a company's debt to equity less adjustments for goodwill and other intangible assets yielding tangible equity.

Debt to Tangible Assets: Debt to Tangible Assets is a ratio of a company's debt to total assets less adjustments for goodwill and other intangible assets.

Price/Adjusted Earnings: Adjusted Price/Earnings is a relative valuation measure comparing a company's share price to its adjusted net income.

Price/Adjusted Cash Flow: Adjusted Price/Cash Flow is a relative valuation measure comparing a company's share price to its adjusted cash flow.

Price/Adjusted Earnings Growth: Adjusted Price/Earnings Growth is a relative valuation measure comparing a company's share price to its growth in adjusted earnings.

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OVERALL RATING FOR 3RD QUARTER 2015 **SELL****ABOUT THE FINANCIAL SONAR™ REPORT & METHODOLOGY**

The Jefferson Financial Sonar™ ratings system classifies companies into three categories: Buy, Hold and Sell. The Financial Sonar rating is the result of a point scoring system derived from the five main criteria. The more negative the rating, the more likely the overall rating will be a Sell. More positive criteria will support an Overall Rating of Buy.

Jefferson Research & Management has developed the Financial Sonar™ Rating System which is based upon five analytical criteria: Earnings Quality, Cash Flow, Operating Efficiency, Balance Sheet, and Valuation. The first four criteria are rated in one of four categories (best to worst): Strongest, Strong, Weak, Weakest. Valuation is also rated in one of four categories (best to worst): Least Risk, Low Risk, Medium Risk, Most Risk.

ABOUT JEFFERSON RESEARCH & MANAGEMENT

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