

Phibro Animal Health (PAHC)

\$17.75 (As of 03/16/20)

Price Target (6-12 Months): **\$20.00**

Long Term: 6-12 Months

Zacks Recommendation:

Outperform

(Since: 02/10/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: D

Summary

Phibro witnessed revenue growth in its Animal Health segment. Strong international volume growth in domestic dairy products and the Osprey Biotechnics acquisition drove Nutritional specialty product sales. The company is upbeat about its long-term prospects within its Animal Health segment. The company continued benefiting from the launch of Rejensa, a supplemental chew for canine joint health. Growth of Phibro's diversified portfolio also buoys optimism. Phibro's second-quarter fiscal 2020 performance was impressive as it registered better-than-expected earnings. However, year-over-year decline in revenues as well as revenue decline in two of its core segments and contraction in operating margin are concerning. The lowered fiscal 2020 guidance is another cause of worry. Phibro shares have underperformed the industry in the past three months.

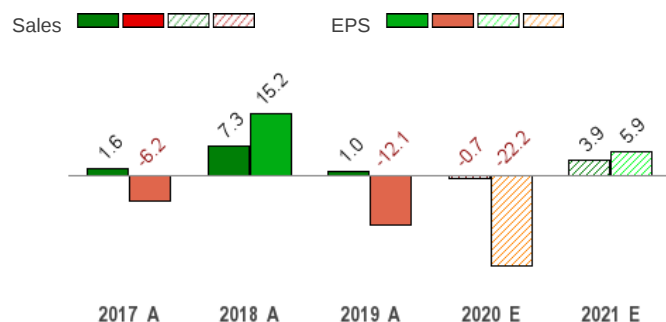
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$36.98 - \$17.63
20 Day Average Volume (sh)	207,533
Market Cap	\$718.0 M
YTD Price Change	-28.5%
Beta	0.43
Dividend / Div Yld	\$0.48 / 2.7%
Industry	Medical - Products
Zacks Industry Rank	Top 20% (51 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	21.4%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	0.0%
Expected Report Date	05/04/2020
Earnings ESP	0.0%
P/E TTM	14.2
P/E F1	14.9
PEG F1	3.4
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					854 E
2020	190 A	214 A			822 E
2019	200 A	218 A	206 A	204 A	828 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$1.26 E
2020	\$0.19 A	\$0.34 A	\$0.36 E	\$0.33 E	\$1.19 E
2019	\$0.39 A	\$0.41 A	\$0.39 A	\$0.33 A	\$1.53 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/16/2020. The reports text is as of 03/17/2020.

Overview

Headquartered in New Jersey, Phibro Animal Health Corporation is a leading global diversified animal health and mineral nutrition company. The company provides a broad range of products for food animals including poultry, swine, beef and dairy cattle and aquaculture. In addition to animal health and mineral nutrition products, Phibro manufactures and markets specific ingredients for use in the personal care, automotive, industrial chemical and chemical catalyst industries. At present, Phibro sells over 1,200 products in more than 65 countries.

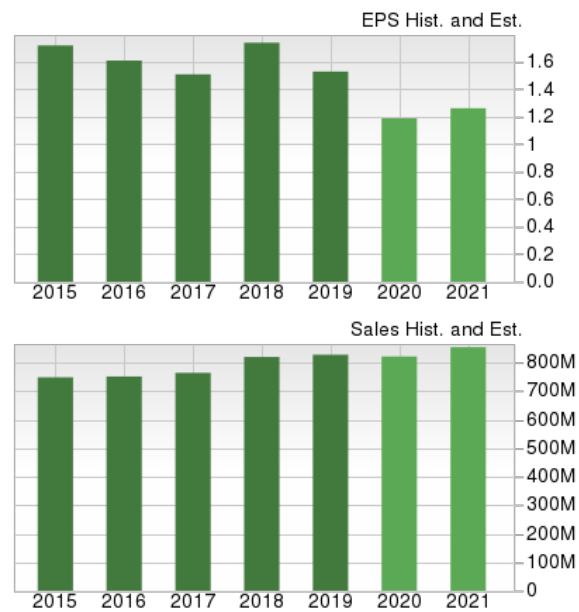
Currently, Phibro focuses on regions where the majority of livestock production is consolidated in large commercial farms such as the U.S., Brazil, China, Russia, Mexico, Australia, Turkey, Israel, Canada and Europe.

Business Segments

Animal Health (64.3% of total revenue in FY19) develops, manufactures and markets more than 550 product presentations including antibacterials, anticommodicals, nutritional specialty products and vaccines.

Mineral Nutrition (28.2% of total revenue in FY19) manufactures and markets more than 400 formulations and concentrations of trace minerals such as zinc, manganese, copper, iron and other compounds, with special focus on customers in North America.

Performance Products (6.4% of total revenue in FY19) manufactures and markets a number of specialty ingredients for use in the personal care, automotive, industrial chemical and chemical catalyst industries, predominantly in the U.S.



Reasons To Buy:

- ▲ **Animal Health Market Growth Continues:** Phibro Health is well positioned in the fastest growing food animal species segment of the animal health market with significant presence in poultry and swine, which are projected by Vetnosis (a research and consulting firm specializing in global animal health and veterinary medicine) to grow globally at compound annual rates of 5.9% and 5%, respectively, between 2014 and 2019. With such optimistic trends prevailing in the market, Phibro's animal health business is doing well.

During the second quarter of fiscal 2020, Animal Health net sales grew 3% year over year. Within Animal Health, Nutritional specialty product sales rose 12% on increased volume in domestic poultry and dairy products. The recently-completed acquisition of Osprey Biotechnics also aided sales at the segment. Apart from this, net vaccine sales increased 10% year over year, driven by robust international demand and enhanced market penetration.

We are encouraged to note that, Phibro as a leading provider of Medicated Feed Additives (MFA) products, has the potential to best capture the huge and growing animal health market worldwide. Data by Vetnosis also supports our view with their projected CAGR (compound annual growth rate) of approximately 4% (from 2015–2020) for MFA products.

At the end of the second quarter of fiscal 2020, the company projected full-year animal Health sales in the range of \$537 million to \$557 million for fiscal 2020, suggesting a growth of 1-3% from year-ago reported figure.

- ▲ **Diversified Product Portfolio:** With rise in scarcity of natural resources, demand for efficient production of animal food such as poultry, swine and cattle have increased. By 2050, the world will need to double food production to feed an estimated global population of 9.1 billion (as per United Nations World Population Database). Meeting this need requires cost-effective production of safe, high-quality animal protein.

Phibro's key animal health products, including MFAs and nutritional specialty products facilitate in enhancing animal nutrition. Phibro's leading product franchise, Stafac/V-Max/Eskalin, is approved in more than 30 countries for use in poultry and swine and is regarded as one of the leading MFA products for livestock. Similarly, the company's nutritional product offerings, such as OmniGen-AF, are used increasingly in the global dairy industry. The company also manufactures vaccines which protect animals from both viral and bacterial disease challenges.

On the other hand, Phibro's mineral nutrition products strengthen an animal's diet and helps maintain its optimal health. Management believes the diversity of species and product categories enhances the company's sales mix and lowers sales concentration risk.

Currently, the company is focused on expanding its footprint in the poultry, swine and cattle industries in both domestic and international markets. The complementary nature of its animal health and mineral nutrition portfolio provides Phibro with unique cross-selling opportunities that can help reach out to new customers or strengthen relationships with existing ones. We believe such a diverse portfolio will allow the company to comfortably address the distinct growing conditions of livestock in different regions of the world.

- ▲ **Potential in Emerging Markets:** Phibro's existing operations and established sales, marketing and distribution network in over 65 countries, provides it ample scope to take advantage of global growth opportunities. Outside the United States, Phibro's global footprint extends to key high-growth regions (countries where the livestock production growth rate is expected to be higher than the average growth rate) including Brazil and other countries in South America, China, India and Asia Pacific, Russia and former CIS countries, Mexico, Turkey, Australia, Canada and South Africa and other countries in Africa.

Phibro has continued to invest in the Far East Asia where huge growth is expected in poultry and dairy industries. Currently, the company is expanding its dairy business in the markets of Australia, Brazil and Mexico. We believe given the turmoil that is currently prevailing in the economies of Russia, Greece, Brazil and China, Phibro has performed quite well of late and bears the potential to continue the healthy performance, going ahead.

- ▲ **Prospering Vaccine Business:** Phibro is focusing on new developments along with incremental registrations and growing volumes of existing nutritional specialties and vaccine technologies. Last December, Phibro bought the assets of KoVax, an Israel-based developer and manufacturer of vaccines for the international aquaculture market. The buyout has widened Phibro's portfolio of aquaculture products.

Earlier, the company purchased MJ Biologic's swine vaccines in the United States. Further, Phibro had become the exclusive distributor of MJ Biologicals that works on research and development of animal health products. Both the firms are working on the joint development of certain animal vaccines. So far, the collaboration has helped expand Phibro's U.S. swine product offering to include specialized vaccines.

The company recently launched the pHi-Tech vaccination device. The initial trials have started delivering impressive results. The company has signed up its first customers for the trials and expects the product to contribute to its top line in the long term.

Phibro's diversified product portfolio, the benefits of the recent MJ Biologicals deal, and the company's significant presence in the emerging markets bolster our confidence in the stock.

Risks

- **Price Movement:** Phibro has underperformed its industry for the past three months. The stock has lost 27.2% compared with the industry's 19.2% fall. Revenues declined year over year owing to substantially lower sales in two segments — Performance Products and Mineral Nutrition. Contraction in operating margin is also concerning. The lowered fiscal 2020 guidance also dragged the share price down. Net sales at the Mineral Nutrition segment fell 11% year over year owing to lower average selling prices combined with lower overall unit volume.

Net sales at the Performance Products segment fell 10% owing to lower volume of copper-based products. Within Animal Health segment, the company saw a 1% year-over-year decline in sales of medicated feed additives (MFAs). This was on account of lower demand owing to the African swine fever outbreak in China.

Also, the company saw adverse economic conditions and unfavorable currency movements internationally.

- **Foreign Exchange Headwinds:** Phibro conducts operations globally, which entails transactions in a variety of currencies. Although a portion of Phibro's revenues are denominated in various currencies, the selling prices of the majority of its products outside the United States are referenced in U.S. dollars. As a result, Phibro's revenues are not significantly directly affected by currency movements. However, the company is subject to currency risk to the extent that its costs are denominated in currencies other than those in which the company earns revenues. Notably, Phibro manufactures some of its major products in Brazil and Israel, where production costs are largely denominated in local currencies, while selling prices are largely set in U.S. dollars. As such, the company is exposed to changes in cost of goods sold resulting from currency movements and may not be able to adjust its selling prices to offset such movements. In fact, management in particular believes that the current strong U.S. dollar is affecting the company's export market.
 - **Competitive Landscape:** Phibro is engaged in highly competitive industries. With respect to its major products, it thus faces threat from a substantial number of global and regional competitors. Phibro's competitive position is based principally on its product registrations, customer service and support, breadth of product line, product quality, manufacturing technology, facility location, and product prices. Some of the company's principal competitors, with greater financial, R&D, production and other resources, include Bayer AG, Ceva Santé Animale, Boehringer Ingelheim International GmbH, Eli Lilly and Company (Elanco Animal Health), Huvepharma Inc., Lallemand Inc., Merck & Co., Inc. (Merck Animal Health and MSD Animal Health), Pharmgate LLC, Southeastern Minerals, Inc., Virbac and Zoetis Inc. Moreover, consolidation continues to rise in the animal health market, which might work in favor of Phibro's competitors. Thus, the company faces a tough competitive scenario in nearly all the markets wherein it operates.
 - **Generic Pressure to Affect Growth:** Phibro also faces competition from generic alternatives of some of its products. The company depends primarily on trade secrets to provide management with competitive advantages for many of its products. The protection afforded is limited by the availability of new competitive products or generic versions of existing products that can successfully compete with Phibro's products. As a result, Phibro faces competition from such new competitive products or lower-priced generic alternatives. These days, generic competitors are becoming more aggressive in terms of pricing, and generic products form a considerable proportion of overall animal health sales in certain regions. If animal health customers increase their use of new or existing generic products, it will adversely affect Phibro's financial health and operational performance.
 - **African Swine Fever in China:** Presently, Phibro's food animal business is facing a huge setback in China as this country is currently dealing with the growing incidence of African swine fever which raises around 400 million pigs. The fever has also started to spread in the neighboring countries, which is another concern for Phibro. Through fiscal 2020, the company apprehends significantly weak animal health sales in China as African swine fever continues to reduce demand.
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Last Earnings Report

Phibro Q2 Earnings Top Estimates, Revenues Fall Y/Y

Phibro Animal Health Corporation reported adjusted earnings per share of 34 cents in the second quarter of fiscal 2020, reflecting a 17.1% fall from the year-ago 41 cents. The figure, however, beat the Zacks Consensus Estimate by 21.4%.

Meanwhile, without adjustments, reported earnings was 29 cents, down 19.4% from the year-ago count.

Quarter Ending **12/2019**

Report Date	Feb 03, 2020
Sales Surprise	NA
EPS Surprise	21.43%
Quarterly EPS	0.34
Annual EPS (TTM)	1.25

Net Sales

In the quarter under review, net sales totaled \$214 million, down 1.9% year over year owing to substantially lower sales at two core segments — Mineral Nutrition and Performance Products.

Segmental Sales Break-Up

During the second quarter, **Animal Health** net sales grew 3% to \$143.7 million. Within this segment, the company registered \$92 million in sales of medicated feed additives (MFAs) and other, reflecting a 1% year-over-year decline. This was on account of lower demand owing to African swine fever outbreak in China.

Within Animal Health, Nutritional specialty product sales rose 12% to \$33.1 million on volume growth in domestic poultry and dairy products. The recently-completed acquisition of Osprey Biotechnics also aided sales at the segment.

Apart from this, net vaccine sales totaled \$18.7 million, showing an increase of 10% year over year, driven by robust international demand and enhanced market penetration.

Net sales at the **Mineral Nutrition** segment fell 11% year over year to \$55.7 million owing to lower average selling prices combined with lower overall unit volume.

Net sales at the **Performance Products** segment fell 10% to \$14.6 million owing to lower volume of copper-based products.

Margins

Phibro's second-quarter gross profit rose 1% year over year to \$69.1 million. Also, gross margin expanded 85 basis points (bps) to 32.3%.

Selling, general and administrative expenses in the reported quarter were \$49.5 million, up 15.4% from the year-ago quarter.

Operating profit declined 23.7% year over year to \$20 million and operating margin contracted 262 bps to 9.2% in the quarter under review.

Financial Update

The company ended the second quarter of fiscal 2020 with cash and short-term investments on hand of \$75 million compared with \$79 million at the end of first-quarter fiscal 2020.

Cumulative net cash provided by operating activities at the end of the second quarter was \$28.5 million compared with the year-ago figure of \$16.6 million. Cumulative capital expenditure amounted to \$16.1 million at the end of the second quarter, reflecting an increase from the year-ago \$12.1 million.

FY20 Outlook

The company has lowered its guidance for fiscal 2020. The company has lowered the revenue outlook to \$812-828 million from the earlier-issued \$833-863 million. The Zacks Consensus Estimate for fiscal 2020 revenues is pegged at \$833.6 million, which is above the guided range.

Adjusted earnings per share is pegged at 88-95 cents, lower than the earlier-provided range of \$1.08-\$1.15. The Zacks Consensus Estimate for adjusted earnings per share is pegged at \$1.11, above the guided range.

Valuation

Phibro shares are down 28.5% in the year-to-date period and down 44.7% in the trailing 12-month period. Stocks in the Zacks sub-industry and Zacks Medical sector are down 17.5% and 12.8% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 14.8% and down 13.8%, respectively.

The S&P 500 index is down 15.9% in the year-to-date period and down 5.3% in the past year.

The stock is currently trading at 14.3X Forward 12-months earnings, which compares to 20.3X for the Zacks sub-industry, 17.9X for the Zacks sector and 15.7X for the S&P 500 index.

Over the past five years, the stock has traded as high as 28.1X and as low as 10.1X, with a 5-year median 19.4X. Our Outperform recommendation indicates that the stock will perform above the market. Our \$20 price target reflects 16.1X forward 12-months earnings.

The table below shows summary valuation data for PAHC.

Valuation Multiples - PAHC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	14.29	20.27	17.94	15.72
	5-Year High	28.10	25.36	21.08	19.34
	5-Year Low	10.12	17.01	15.81	15.18
	5-Year Median	19.42	19.62	18.73	17.42
P/S F12M	Current	0.85	3.25	2.44	2.90
	5-Year High	2.53	3.98	3.84	3.43
	5-Year Low	0.85	2.88	2.44	2.54
	5-Year Median	1.53	3.22	2.96	3.00
P/B TTM	Current	3.30	2.56	3.59	3.64
	5-Year High	63.41	4.30	5.05	4.55
	5-Year Low	3.30	2.21	3.45	2.85
	5-Year Median	9.54	2.77	4.32	3.63

As of 03/16/2020

Industry Analysis Zacks Industry Rank: Top 20% (51 out of 253)



Top Peers

Patterson Companies, Inc. (PDCO)	Outperform
Cardiovascular Systems, Inc. (CSII)	Neutral
Elanco Animal Health Incorporated (ELAN)	Neutral
IDEXX Laboratories, Inc. (IDXX)	Neutral
Eli Lilly and Company (LLY)	Neutral
Merck & Co., Inc. (MRK)	Neutral
Neogen Corporation (NEOG)	Neutral
Zoetis Inc. (ZTS)	Neutral

Industry Comparison Industry: Medical - Products				Industry Peers		
	PAHC Outperform	X Industry	S&P 500	LLY Neutral	MRK Neutral	ZTS Neutral
VGM Score	B	-	-	D	B	B
Market Cap	718.04 M	234.83 M	16.36 B	123.74 B	177.34 B	50.84 B
# of Analysts	3	2	13	6	7	11
Dividend Yield	2.70%	0.00%	2.63%	2.29%	3.49%	0.75%
Value Score	B	-	-	C	C	D
Cash/Price	0.08	0.11	0.06	0.02	0.05	0.03
EV/EBITDA	8.95	0.61	10.54	20.87	12.54	22.58
PEG Ratio	3.37	2.13	1.46	1.62	1.78	2.39
Price/Book (P/B)	3.30	2.40	2.26	46.02	6.85	18.83
Price/Cash Flow (P/CF)	7.94	13.74	8.80	18.27	10.45	23.53
P/E (F1)	14.92	22.10	13.18	19.11	12.22	27.10
Price/Sales (P/S)	0.88	3.67	1.78	5.54	3.79	8.12
Earnings Yield	6.70%	0.41%	7.56%	5.23%	8.18%	3.69%
Debt/Equity	1.64	0.10	0.70	5.30	0.87	2.26
Cash Flow (\$/share)	2.24	-0.00	7.01	7.08	6.69	4.55
Growth Score	C	-	-	D	B	B
Hist. EPS Growth (3-5 yrs)	-1.92%	11.68%	10.85%	16.64%	8.10%	20.29%
Proj. EPS Growth (F1/F0)	-22.22%	10.05%	5.72%	12.09%	10.24%	8.52%
Curr. Cash Flow Growth	-7.92%	2.12%	6.15%	-7.51%	5.54%	18.22%
Hist. Cash Flow Growth (3-5 yrs)	4.96%	8.20%	8.55%	9.27%	0.15%	16.87%
Current Ratio	3.03	2.72	1.24	1.16	1.24	2.63
Debt/Capital	62.18%	14.28%	42.57%	84.13%	46.65%	69.29%
Net Margin	4.67%	-12.35%	11.64%	37.27%	21.01%	23.96%
Return on Equity	23.94%	-9.59%	16.74%	192.27%	49.41%	69.41%
Sales/Assets	1.08	0.60	0.54	0.58	0.56	0.56
Proj. Sales Growth (F1/F0)	-0.75%	6.41%	3.50%	7.94%	6.36%	7.79%
Momentum Score	D	-	-	C	C	C
Daily Price Chg	-19.79%	-8.00%	-12.67%	-7.17%	-8.90%	-14.70%
1 Week Price Chg	-15.47%	-16.67%	-11.01%	-1.48%	-6.63%	-8.44%
4 Week Price Chg	-34.41%	-31.14%	-32.63%	-8.32%	-15.40%	-25.75%
12 Week Price Chg	-27.67%	-29.46%	-30.17%	-1.35%	-23.79%	-19.14%
52 Week Price Chg	-44.65%	-32.52%	-23.26%	3.31%	-14.05%	9.48%
20 Day Average Volume	207,533	209,319	3,457,426	5,577,443	15,820,834	2,972,451
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	-0.48%	0.00%	0.00%	-0.11%
(F1) EPS Est 12 week change	7.76%	-1.13%	-0.93%	-0.25%	4.22%	-1.03%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	-0.60%	-0.61%	0.00%	0.20%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	C
Momentum Score	D
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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