

Phibro Animal Health (PAHC)

\$24.79 (As of 12/27/19)

Price Target (6-12 Months): **\$26.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 11/04/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: C

Growth: F

Momentum: D

Summary

Phibro shares have underperformed its industry for the past six months. On a positive note, the company witnessed double-digit revenue growth in its Performance Products business. Strong international volume growth in dairy products contributed to the rise in Nutritional specialty product sales. The company is upbeat about its long-term prospects within the Animal Health segment and has invested in strategic acquisitions like Osprey Biotechnics. The launch of Rejensa, a supplemental chew for canine joint health, also instills optimism. Growth of Phibro's diversified portfolio also buoys optimism. On the flip side, the company reported revenues decline in two core segments and contraction in operating margin are headwinds. Fiscal 2019 was disappointing for the company as its earnings missed the consensus mark.

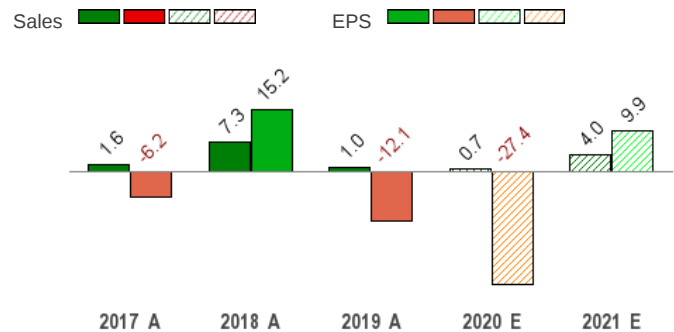
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$36.98 - \$20.00
20 Day Average Volume (sh)	167,261
Market Cap	\$1.0 B
YTD Price Change	-22.9%
Beta	0.82
Dividend / Div Yld	\$0.48 / 1.9%
Industry	Medical - Products
Zacks Industry Rank	Top 40% (102 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-13.6%
Last Sales Surprise	NA
EPS F1 Est- 4 week change	0.0%
Expected Report Date	02/05/2020
Earnings ESP	0.0%
P/E TTM	18.8
P/E F1	22.3
PEG F1	5.1
P/S TTM	1.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					867 E
2020	190 A				834 E
2019	200 A	218 A	206 A	204 A	828 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$1.22 E
2020	\$0.19 A	\$0.28 E	\$0.34 E	\$0.31 E	\$1.11 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 12/27/2019. The reports text is as of 12/30/2019.

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.

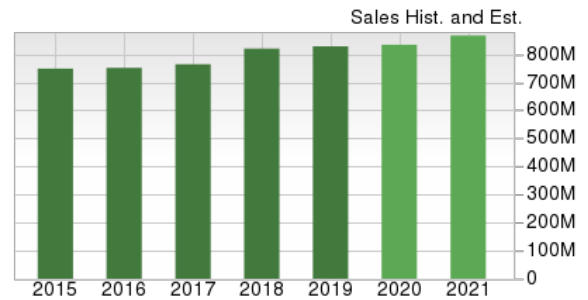
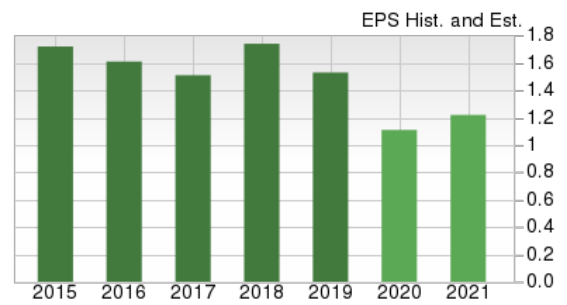
Currently, Phibro focuses on regions where the majority of livestock production is consolidated in large commercial farms such as the U.S., Brazil, China, Russia, Mexico, Australia, Turkey, Israel, Canada and Europe.

Business Segments

Animal Health (64.8% of total revenue in FY18) develops, manufactures and markets more than 550 product presentations including antibacterials, anticommodicals, nutritional specialty products and vaccines.

Mineral Nutrition (28.6% of total revenue in FY18) 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 (6.5% of total revenue in FY18) 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.

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 fiscal third quarter, the company projects full-year animal Health sales in the range of \$529 million and \$532 million, in line with the previous year.

- ▲ **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.

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

Reasons To Sell:

- ▼ **Price Movement:** Phibro has underperformed its industry for the past six months. The stock has lost 21.6% against the industry's 3% rise. Phibro exhibited a disappointing performance in the fiscal 2019. Revenues declined year over year owing to substantially lower sales in two core segments — Animal Health and Mineral Nutrition. Contraction in operating margin is also concerning. According to Phibro, lower demand owing to African swine fever outbreak in China in Animal Health business along with unfavorable product mix in Mineral Nutrition have resulted in the reduced gross profit. Also, the company saw adverse economic conditions and unfavorable currency movements internationally.
- Customer consolidation can adversely affect Phibro's revenues. Moreover, headwinds such as unfavorable currency movement and tough competitive scenario continue to pose threats.
- ▼ **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. In fiscal 2019, the company apprehends significantly weak animal health sales in China as African swine fever reduces demand.
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Last Earnings Report

Phibro's Q4 Earnings Miss Estimates

Phibro Animal Health Corporation reported adjusted earnings per share of 33 cents in the fourth quarter of fiscal 2019, showing a 28% drop from the year-ago number. The figure missed the Zacks Consensus Estimate by 2.9%.

Meanwhile, without adjustments, reported (or GAAP) earnings per share was 22 cents, reflecting a fall of 60% from the year-ago count.

For fiscal 2019, adjusted earnings per share came in at \$1.53, down 12% from the year-ago figure. The metric beat the consensus mark by 0.7%.

Quarter Ending **09/2019**

Report Date	Nov 04, 2019
Sales Surprise	NA
EPS Surprise	-13.64%
Quarterly EPS	0.19
Annual EPS (TTM)	1.32

Net Sales

In the quarter under review, net sales totaled \$203.9 million, down 3.7% year over year owing to substantially lower sales at two core segments — Animal Health and Mineral Nutrition.

For 2019, net sales totaled \$828 million, up 1% from the year-ago tally. However, the figure missed the Zacks Consensus Estimate by 0.2%.

Segmental Sales Break-Up

During the fourth quarter, Animal Health net sales declined 4% to \$132 million. Within this segment, the company registered \$86.3 million in sales, reflecting a 6% decline in medicated feed additives (MFAs). This was on account of lower demand owing to African swine fever outbreak in China and consistently lower domestic demand from the poultry and swine sectors. Nutritional specialty product sales rose 1% to \$28.6 million, asconsistently dismal domestic dairy conditions and lowered demand from poultry customers was offset by international volume growth in dairy products. Apart from this, net vaccine sales totaled \$17.2 million, showing a drop of 1% year over year due to the loss of a domestic distribution arrangement and the continued impact of turbulent economic conditions in certain foreign markets.

Net sales at the Mineral Nutrition segment fell 7% year over year to \$56 million owing to unfavorable product mix and lower average selling prices.

Net sales at the Performance Products segment rose 15% to \$15.9 million backed by higher volumes of personal care products.

Operational Update

Phibro's fourth-quarter gross profit declined 3.3% year over year to \$65.3 million. Gross margin expanded 16 basis points (bps) to 32%.

Selling, general and administrative expenses in the reported quarter came in at \$53.2 million, up 28.5% from the year-ago quarter.

Operating profit declined 53.6% year over year to \$12.1 million and operating margin contracted 639 bps to 5.9% in the quarter under review.

Financial Update

The company exited fiscal 2019 with net cash used by operating activities of \$14.1 million, down from the year-ago \$84.6 million. Capital expenditure amounted to \$10.1 million in this quarter, reflecting an increase from \$5.5 million in the prior-year quarter.

FY20 Outlook

The company has initiated its guidance for fiscal 2020. Net sales are projected in the range of \$833-863 million (an increase of 1-4%). Adjusted earnings per share is estimated in the band of \$1.08-1.15.

The Zacks Consensus Estimate for fiscal revenues 2019 is pegged at \$862.6 million, within the guided range. The same for adjusted earnings per share is pegged at \$1.61, above the guided range.

Valuation

Phibro's shares are down 22.9% in the year-to-date and the trailing 12-month periods. Stocks in the Zacks sub-industry are up 16.8% in the year-to-date period and over the past year. The Zacks Medical sector is up 8.9% in the year-to-date period and over the past year.

The S&P 500 index is up 27.9% in the year-to-date period and in the past year.

The stock is currently trading at 21.3X Forward 12-months earnings, which compares to 25X for the Zacks sub-industry, 21.5X for the Zacks sector and 18.8X 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 19.3X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$26 price target reflects 22.3x 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	21.28	25.02	21.48	18.75
	5-Year High	28.10	25.37	21.48	19.33
	5-Year Low	10.12	17.02	15.91	15.16
	5-Year Median	19.28	19.53	18.97	17.43
P/S F12M	Current	1.18	3.89	2.87	3.41
	5-Year High	2.53	3.93	3.80	3.41
	5-Year Low	0.91	2.88	2.42	2.54
	5-Year Median	1.54	3.22	2.94	3.00
P/B TTM	Current	4.85	3.12	4.61	4.42
	5-Year High	63.41	4.30	5.01	4.42
	5-Year Low	3.81	2.21	3.42	2.85
	5-Year Median	9.73	2.77	4.27	3.60

As of 12/27/2019

Industry Analysis Zacks Industry Rank: Top 40% (102 out of 252)



Top Peers

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

Industry Comparison Industry: Medical - Products				Industry Peers		
	PAHC Neutral	X Industry	S&P 500	LLY Outperform	MRK Outperform	ZTS Neutral
VGM Score	D	-	-	D	A	B
Market Cap	1.00 B	337.82 M	23.80 B	126.28 B	232.96 B	63.47 B
# of Analysts	3	2	13	5	5	10
Dividend Yield	1.94%	0.00%	1.78%	1.96%	2.67%	0.49%
Value Score	C	-	-	C	B	D
Cash/Price	0.08	0.08	0.04	0.01	0.03	0.03
EV/EBITDA	11.67	0.53	13.88	25.61	18.70	30.92
PEG Ratio	5.06	2.71	2.13	2.00	1.99	3.19
Price/Book (P/B)	4.85	4.20	3.33	36.47	8.70	23.76
Price/Cash Flow (P/CF)	11.07	20.36	13.55	18.89	14.72	34.87
P/E (F1)	22.35	26.77	19.62	22.66	17.76	37.00
Price/Sales (P/S)	1.23	5.38	2.66	5.58	5.07	10.32
Earnings Yield	4.48%	-0.01%	5.09%	4.41%	5.63%	2.70%
Debt/Equity	1.84	0.11	0.71	4.09	0.84	2.47
Cash Flow (\$/share)	2.24	-0.00	6.94	6.94	6.21	3.82
Growth Score	F	-	-	F	A	B
Hist. EPS Growth (3-5 yrs)	0.03%	9.58%	10.48%	16.65%	7.23%	19.65%
Proj. EPS Growth (F1/F0)	-27.45%	3.10%	6.14%	4.58%	18.71%	15.05%
Curr. Cash Flow Growth	-7.92%	5.10%	14.75%	20.58%	3.40%	28.45%
Hist. Cash Flow Growth (3-5 yrs)	4.96%	9.87%	8.93%	4.33%	-1.53%	14.83%
Current Ratio	3.21	2.78	1.24	1.17	1.26	4.39
Debt/Capital	64.83%	15.02%	42.92%	80.34%	45.72%	71.19%
Net Margin	4.99%	-11.16%	11.06%	35.10%	20.26%	23.76%
Return on Equity	25.52%	-4.59%	17.10%	107.99%	48.16%	70.78%
Sales/Assets	1.12	0.60	0.54	0.57	0.55	0.56
Proj. Sales Growth (F1/F0)	0.68%	1.01%	2.49%	-9.22%	11.12%	6.99%
Momentum Score	D	-	-	B	C	B
Daily Price Chg	0.08%	0.00%	0.21%	0.02%	-0.11%	0.08%
1 Week Price Chg	2.30%	0.29%	1.46%	8.97%	2.68%	6.61%
4 Week Price Chg	1.35%	2.33%	1.98%	11.67%	4.26%	9.37%
12 Week Price Chg	16.05%	2.92%	9.78%	22.23%	10.39%	7.04%
52 Week Price Chg	-21.75%	7.94%	28.47%	16.17%	21.17%	57.75%
20 Day Average Volume	167,261	158,956	1,778,443	3,360,937	7,353,546	1,930,115
(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%	0.00%	0.21%	0.00%	0.00%
(F1) EPS Est 12 week change	-1.94%	-0.87%	0.12%	1.26%	4.77%	0.81%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	-0.88%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	C
Growth Score	F
Momentum Score	D
VGM Score	D

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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