Phibro Animal Health Corporation
Barclays Global Healthcare Conference
March 12, 2024

Balaji Prasad: Good afternoon, everyone. My name is Balaji Prasad. I'm the senior analyst for the spec pharma coverage for Barclays. And bringing up the final meeting of the day for the spec pharma track, last but not the least, we have Phibro and the management team from Phibro, including Glenn David, who many of you would know, the Chief Financial Officer, and Larry Miller, the Chief Operating Officer.

Glenn and Larry, thank you so much for joining us. I know that we have a hard stop for you to get to your flight. We'll get there.

So, let me, to just kickstart the proceedings, Glenn, you reported your 2Q results recently, your quarterly results. So, could you walk us through some of the key points there and how are things progressing now for the rest of the fiscal year.

Glenn David: My pleasure. So, starting with revenue. So, strong quarter in terms of revenue growth. We had 2% revenue growth.

But the real highlight for the quarter was our animal health business, and our animal health business grew 6%. And the star within the animal health business was our vaccine portfolio. So, our vaccine portfolio grew over 30% for the quarter. So, really pleased with the performance of our animal health business and, particularly, the vaccine segment as well.

And from an adjusted EBITDA perspective, while the adjusted EBITDA for the quarter was down about 5%, again the animal health portfolio really stood out, with growth of around 6% in adjusted EBITDA. The driver of the down adjusted EBITDA for the full business was really some particular issues within our performance products and our mineral and nutrition portfolios, which we do believe will improve as we go through the year.

So, strong revenue for the quarter. And also, for the first half of the year; we had revenue growth of about 1%, again with animal health leading the way, with 5% growth, and with vaccines growing over 20% for the first half of the year.

So, a good start to the year, particularly in the animal health segment.

Balaji Prasad: Wonderful. Maybe just thinking about, speaking about the momentum in the vaccines business, can you underline what's driving this momentum and how sustainable do you expect this to be and the key drivers for the vaccine segment overall?

Larry Miller: So, our vaccine businesses continue to grow over the last several years. Outside of the United States, it's largely driven by poultry vaccines. We had a launch last year at this time of an infectious bronchitis vaccine to address an outbreak that was happening in markets, particularly in South America. And that drove a lot of growth, particularly in a couple of specific states of Brazil. So, we expect continued use of that vaccine there.

And we do a lot of surveillance in all countries and follow the surveillance reports that governments issue from slaughter plants. And so, we continue to monitor very closely for this variant strain to see where it's coming next and to try and be there with a solution.

Balaji Prasad: Great. Maybe just taking that poultry segment a bit further, I think this is a segment where there is a fair amount of interest on innovation. I mean, Zoetis has in the past spoken about vector vaccines. Do you have anything in the pipeline again with regard to addressing the broader market opportunity within poultry vaccines?

Larry Miller: So, again, we continue to invest in things that the market doesn't have, whether that's different pathogens that we're trying to address or other facets of a vaccine, as far as administration as well. So, I can't go into our portfolio today, but assure that this is an area of focus. As Glenn said, it's been driving a lot of growth, an area we're really excited about. And our focus is on, again, identifying things where there's a market need and where we can bring some innovation to meet those needs.

Balaji Prasad: Thank you, Larry. Alongside poultry, maybe could you also discuss about the broader underlying demand trends within some of the other key livestock categories, be it dairy or swine, and what do you see there for the rest of the year?

Larry Miller: So, I'll take that. Poultry is – I think it's in the black, for sure. And volume and demand is what continues to drive that market.

The dairy is producing at about breakeven costs. So, perhaps some of the larger producers, particularly those associated with a processor or to a chain to market, are making profits.

Swine continues to be a challenging story, particularly in the U.S. here, for the rest of calendar year 2024. We've seen an 11% reduction in the sow population there. So, they've got some inventory to work through, and we're hopeful that next year the industry will be a little more positive.

Balaji Prasad: Eleven percent reduction in sow.

Larry Miller: In sow population, yes.

Balaji Prasad: Got it. And you called about the opportunity with infectious bronchitis in Brazil. So, maybe just segueing towards the broader geography on the key important markets for you, could you discuss about the Beijing markets for you and the outlook that you're seeing there between China, Brazil, U.S., and any other OUS market that you would like to highlight?

Larry Miller: I would summarize it and say that we're expecting nice, continued growth in North America and in South America. Certainly, some challenges that the economy and the dairy industry in particular is facing in China.

Balaji Prasad: And what are your expectations, especially for China, as you think about the market there? I mean, there have been multiple macro pressures. So, it's pressured both the livestock side of the business and the companion animal side. And how do you expect the recovery there to pan out?

Larry Miller: It's a good question.

Glenn David: I mean, I think one of the key things for us is China isn't as big a portion of our overall business as it may be for some of our competitors, and we're actually larger in poultry than we are in swine. But we're building in that market. So, we're starting from a smaller base right now. So, we do think there's opportunities for us to grow off of the smaller base that we have there.

Balaji Prasad: Got it. And I think, last I recollected speaking with Donny about the registrations for the Chinese market, would you have an update on where you are with some of these commercial registrations?

Larry Miller: So, the products that we've been focused on recently in China specifically are in the dairy area. And we have a couple of our key products there. And we're just focusing on getting penetration with those products. And we're evaluating other opportunities for bringing other products in as we see market opportunities.

Balaji Prasad: Any particular areas of interest, Larry?

Larry Miller: It's going to be in nutrition and health.

Balaji Prasad: Okay. And maybe just thinking about the broader animal health business, as you said in your opening comments, Glenn, clearly outperforming the mineral and nutrition and performance products. How do you think about this dynamic? How much of this would be sustained because of, let's say, infectious bronchitis itself? Because that has an outsize contribution, right? And how do you expect that to pan out for the rest of the year?

Glenn David: So, as you look at the rest of the year and at the guidance, I think it's good to understand how we performed for the first half and the dynamics of that. So, we grew 1% revenue in the first half of the year and, as I mentioned, 5% growth in animal health. But we actually declined 19% in our performance products, and we declined 3% in mineral and nutrition.

So, as we look to the second half, we definitely see improving performance in both of those businesses. Particularly within performance products, a lot of that was inventory driven. Our customers had higher inventory at the end of our fiscal year-end. That's worked its way out in the first half of the year. So, we expect improving performance in the second half in those businesses.

And it also had a significant negative impact on EBITDA, because both mineral and nutrition and performance products declined in EBITDA for the first half. And again, we expect improving performance in the second half.

So, as you look at the guidance, the guidance would imply at a midpoint of the range about 2% growth for the overall Phibro business. So, if you look at 1% in the first half of the year, guiding at a midpoint to 2%, that would imply improved performance in the second half of the year.

And then if you look at an EBITDA perspective, it's even more impactful, as the first half of the year the EBITDA was negative 9%, and the guidance at a midpoint would imply about negative 3%. So, again, significantly better performance in the second half of the year than the first half of the year. And a lot of that is driven by a recovery in both mineral and nutrition and performance products.

Balaji Prasad: Understood. Thank you. I think one of the things that I get questions once in a while is about definitely on Mecadoxide (ph). And there has been now going on for a last couple of years. So, would love to get some color there on where does it stand currently. And again, I know that you provided a lot of safety data to the FDA on Mecadox and there's been multiple (inaudible) and proof back and forth with the FDA. What are your expectations there?

Larry Miller: Sure. So, the information I can share obviously is public information. We filed for a hearing in November, and then we submitted comprehensive data to support the Notice of Opportunity for Hearing. The CVM/FDA applied for an extension to review that, which they received a 90-day extension. And so, that's where we're at currently.

Balaji Prasad: Got it. And for those who are following the story now, can you help us understand the relative importance and size of Mecadox versus the overall business?

Larry Miller: So, it's an important product to the industry. For us, it's an important product, but it's not a material product.

Glenn David: It's less than a few percent of sales overall. But as Larry says, this is an important product for the industry.

Balaji Prasad: Got it. Great. Shifting towards the companion animal side of the business, again cognizant that it's not a big part of the business, but this has been a strategic journey that the team's been undertaking for the last couple of years. So, speak to us a bit about your investments into the companion animal side of the business and how are you thinking about the pipeline. I know that recently they also added a couple of additions to the board from this aspect, too.

Glenn David: So, in terms of the additions to the board, Alejandro Bernal recently joined the board, but Alejandro has broad experience in animal health in both livestock and companion animal. And I had the pleasure of working with Alejandro for a number of years, myself in some previous roles. So, very glad to have Alejandro on part of the board. Obviously, his most recent experience has been more companion animal focused, but Alejandro is a veterinarian as well and has deep experience in livestock as well and I think will continue to be a great addition to the board.

In terms of the companion animal investments, currently we have a product in the market called Rejensa, and that's a chewable for joint care. That we have made available solely through the vet channel. It's been on the market for about five years now. It continues to perform well; it continues to grow. But as a product matures, obviously, those growth rates begin to slow. And that was sort of a starting point into the companion animal space.

But the company has also, as you mentioned, made continued strategic investments in research and development related to companion animal. And we do have molecules in some of the larger segments, such as dermatology, such as pain, such as oral care, as well, and those investments we are continuing. They have been sort of negative to our EBITDA growth with those incremental R&D investments, but we believe it's the right thing to do for the medium- and long-term growth of the company overall.

Balaji Prasad: I hear you, Glenn. As you think about these, any tentative timelines, or a horizon that you want to provide as we think about your expansion in this space and on the companion animal side?

Glenn David: So, the company, for competitive reasons, doesn't really disclose or hasn't disclosed at this point the timelines for those products. And as products get closer to market, that's when we'll start to disclose more of the timeline.

Balaji Prasad: Got it. So, would it be something like a one- to three-year thing? Or beyond three years?

Glenn David: As I said, we haven't discussed the timelines.

Balaji Prasad: Got it. So, we'll look forward to further updates from you on this at the right time.

Maybe shifting towards – again since we spoke about innovation in the companion animal side – also on the innovation on the livestock side. I mean, there's been a lot of focus around sustainability and all, and you know that some of your peers have come through with products like, of course, to reduce ammonia and methane. So, what are you doing towards the sustainability side of things on the livestock side? And how much are you investing, or do you plan to invest?

Larry Miller: So, at this stage, we do not have any products that directly compete or have a claim in this area. It is an interesting area to watch, for sure, and one that the industry is really, really looking at.

I guess the thing that I would remind us of all is our products basically promote animal health. And by doing that, healthy animals are more thrifty and they produce better. And so, all of our products for as long as they've been around have been about sustainability, keeping animals healthy so that they're basically performing at optimal rates.

Balaji Prasad: Okay. And similarly, I think as we think about other opportunities similar to the sustainability side of things, again on antibiotics, there's a growing amount of interest, especially with novel antibiotics, for livestock. So, can you share your thoughts on the broader livestock antibiotic market space, the market size, and again your thoughts on investing into the space, to the extent you can? I know that the industry tends to be holding the cards pretty close to the chest, but investors would like to know, too.

Glenn David: So, really, I think, as Larry mentioned, we've really been focused more on the vaccine space and nutritional specialties on the livestock side. In terms of our MFA business, a lot of that has been more focused on life cycle management. But in terms of new innovation, I think Phibro has been focused more on bringing new vaccines to the market, such as the success that we had in Latin America and Brazil that really helped drive our growth in the quarter and the half, and also on bringing new nutritional specialties to the markets as well. That's really where the investment in R&D has been focused, complemented obviously by what we talked about earlier in terms of the investment in the companion animal space.

Balaji Prasad: Got it. And maybe, Glenn, just stepping back, I know it's around four to five weeks for you in this role. I'd love to get your sense and thoughts around Phibro as a company and what excited you the most about the company and got you to join here. And expectations versus reality, how has that matched?

Glenn David: So, as you said, it's five weeks in, but the reality has been very positive in terms of expectations. And I think what excited me – obviously, I have a passion for the industry, right? It's a very solid industry with strong fundamentals, strong future growth, and serves a key need for health. So, obviously, very passionate about the industry.

And Phibro has performed very well in the industry, particularly in the livestock space, and has been able to grow in line with the market or faster than the market within the livestock space. So, great opportunities there.

And then also very excited about the areas of investment – the investments in vaccines, the investments in companion animal – which I think could drive good medium- to long-term growth as well.

But most of all, I was also very impressed with the people that I met during the interview process, their deep knowledge of the industry, and I felt that my experience could really help complement where the company is looking to move forward.

So, so far, it's been a great five weeks, but look forward to learning more and getting more familiar with the company as well.

Balaji Prasad: Fantastic. For what it's worth, I mean, every time I speak to Jack and Donny, I come out significantly wiser. I mean, Jack's insights on the industry is exceptional, in my view.

But again, it kind of leads to my next question. I know it's, as I said, five weeks. So, as you look at the company's financials and as you think about your role as the CFO, speak to us about your thoughts around capital expenditures, capital allocation. How do you plan to balance these? And where do you think there's scope for significant improvement?

Glenn David: So, I think there are a number of areas. And again, five weeks in, but as I get more and more familiar with the company. Capital allocation obviously starts with putting your expenses and your OpEx to the areas of highest growth. So, really working with the management team to understand where our OpEx is being driven. And I think the company has made some really good decisions in terms of not just investing in the short term, but also investing in the long term, with some of the more strategic investments in companion animal, in vaccines, in the aquaculture area as well. So, making sure that we continue to put our OpEx behind the areas of highest growth.

Obviously, also then working through some of the working capital areas, understanding what the appropriate levels of inventory are, is there opportunity to reduce inventory to drive some additional working capital and additional cash for either investment or to pay down debt levels overall, which I know is a plan for the company to continue to work down debt levels overall.

So, those are some of the areas that I get up to speed, really want to understand what are the opportunities for a working capital perspective, with inventory in particular. As I look at the company's AR and DSOs, they're pretty much in line with or even above most of the industry. So, I think the company has done a really good job from an AR perspective. So, it's really more along the inventory lines and then other areas that we continue to generate additional cash to continue to work down debt and bring down the leverage ratios.

Balaji Prasad: Got it. Maybe I'll follow up further on that in terms of leverage ratios. So, you're at around 4x to 4.5x leverage ratio. And obviously, I think considering the rate environment and market focus, especially last year, on levered companies, I'm sure you'll have further plans for de-levering. So, what is the leverage that you'll be most comfortable with and that would be a goal for you?

Glenn David: So, we haven't set a target, either gross leverage ratio or net leverage ratio. Typically, we've been in that 4x to 4.5x range in terms of gross leverage. When you look at it on a net basis, you can take away almost a turn, as we have close to $100 million of cash and short-term investments on the balance sheet. So, the intention would be to work that down. I want to get a better understanding of the company, what our cash needs are, moving forward, before we share a specific target or goal with the street. But obviously, an area of focus to bring that net leverage ratio down. We're fortunate that a good portion of our debt is fixed at a very favorable rate for the near term. But as we move forward, it'd be beneficial for us to continue to work down the overall debt levels.

Balaji Prasad: Fantastic. So, as far as now, it's around $300 million of your approximately $470 million is fixed rate.

Glenn David: Yes.

Balaji Prasad: Okay. The focus will be on the other part of the leverage ratio. Great.

So– I know that you have a flight to catch, as I said. We have a couple of minutes left, but I'll leave it up to you for any closing comments, and hope you get your flight.

Glenn David: Just really appreciate your time. It was great to join you again.

Balaji Prasad: Larry and Glenn, thank you so much for joining us today, and I hope you had a productive day at the conference. So, thank you again, and we'll continue our conversation.

Larry Miller: Thank you.

Glenn David: Thank you so much, Balaji.