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Phibro Animal Health Corp. (PAHC)

Q2 2019 Earnings Call

CORPORATE PARTICIPANTS

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

OTHER PARTICIPANTS

David R. Risinger
Analyst, Morgan Stanley & Co. LLC

Erin Wilson Wright
Analyst, Credit Suisse Securities (USA) LLC

Balaji Prasad
Analyst, Barclays Capital, Inc.

Michael Ryskin
Analyst, Bank of America Merrill Lynch

David Westenberg
Analyst, Guggenheim Securities LLC

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Phibro Animal Health Corporation Q2 2019 Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions]

Thank you. I would now like to hand the conference over to your speaker today, Richard Johnson, Chief Financial Officer. Please go ahead.

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

Well, thank you, operator, and good morning, everyone. Welcome to the Phibro Animal Health earnings call for our second quarter ended December 2019. On the call today are Jack Bendheim, our Chief Executive Officer and myself, Richard Johnson. I'm the Chief Financial Officer. We'll provide an overview of our quarterly results and then we'll open the line for your questions.

Before we begin, let me remind you that the earnings press release and financial tables can be found on the Investors Section of our website at pahc.com. We're also providing a simultaneous webcast to this morning's call, which can be accessed on the website as well. Today's presentation slides and a replay and transcript of the call will also be available on the website later today.

Our remarks today will include forward-looking statements and actual results could differ materially from those projections. For a list and description of certain factors that could cause results to differ, I refer you to the forward-looking statements section on our earnings press release.

Our remarks today also include references to certain financial measures, which were not prepared in accordance with Generally Accepted Accounting Principles, or US GAAP. I refer you to the non-GAAP financial information section on our earnings press release for a discussion of these measures. Reconciliations of these non-GAAP financial measures to the most directly comparable US GAAP measures are included in the financial tables that accompany the press release.

Before we get into the numbers, we want to remind everyone that we present our results on a GAAP basis and on an adjusted basis. We present adjusted results that exclude acquisition-related items, unusual non-operational or non-recurring items, including stock-based compensation and restructuring costs, other income expenses separately reported in the consolidated statement of operations, including for example, foreign currency gains and losses, and the income tax effects related to any pre-tax adjustments, plus unusual or non-recurring income tax items.

So, first here is Jack Bendheim with some introductory comments.

Jack C. Bendheim

Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

Thanks, Dick. And thank you everyone for joining us today. I'm quite pleased that our core Animal Health segment returned to growth this past quarter. China's issues notwithstanding, our Vaccines and Nutritional Specialties products each grew with double-digit growth in the quarter, while as expected, our MFA and other performance was down 1% versus last year, driven by China. I expect the Animal Health segment to continue to show growth for the remainder of this fiscal year.

Just two examples, we're seeing a very strong demand for our poultry Vaccines in many international regions and the imminent launch of our next-generation OmniGen product looks to take advantage of the improving dairy market. As we have guided, our sales turnaround is accompanied by increased spend as we look to position ourselves for the years ahead.

The strategic growth initiatives we are undertaking are producing results. Just two examples, I've just returned from the IPPE, the annual poultry trade show in Atlanta and I can say without exaggeration that our pHi-Tech vaccination device was one of the major innovations presented at the show. We had integrators from around the world signing up for trials, and the trials that began a few months ago have gone exceedingly well and we have already signed up our first customers. I'm very confident pHi-Tech will meaningfully enhance our revenue and EBITDA beginning in our next fiscal year. Perhaps even more important, it is clear that producers that are introduced to pHi-Tech have begun to understand that Phibro is one of the market leaders in animal health technology. This is critical as we roll out our poultry vaccines through additional countries in South America and Asia.

I am similarly encouraged by the progress we are making with Rejensa, our first foray into the US pet market. We have begun rolling out Rejensa nationwide and today, we are in more than 500 vet clinics. We are working closely with our distribution partner, which is allowing us to limit our fixed expenses as we enter this extremely

competitive market, where we are receiving tremendous feedback both directly and indirectly through social media, and I'm excited to see our continued advancement here.

Finally, we continue to make headway on our vaccine against African swine fever. To-date, the coronavirus outbreak has not affected our efforts, but this could change if the virus remains unchecked in the months ahead. We expect to trial our initial candidate in pigs later this spring, assuming no delay due to the coronavirus.

I will likely not have significant update to provide next quarter on this project, but certainly expect to have some result to share on this initial candidate later this year.

With that I look forward to your questions at the conclusion of the presentation and I will now hand it back to Dick.

Richard G. Johnson

Chief Financial Officer, Phibro Animal Health Corp.

Thanks, Jack. I'm looking at page 5 of the presentation. Consolidated sales were $214 million for the quarter. That was a 2% decline versus the same quarter last year. Increased sales in the Animal Health segment were more than offset by lower average selling prices in Mineral Nutrition and a slightly decreased volume in Performance Products. The increase in Animal Health sales was driven by our Nutritional Specialties and Vaccine products, partially offset by lower sales of MFAs and others. We'll get into further details regarding segment results later in the presentation.

On a reported basis, net income of $11.9 million declined $2.9 million due to increased operating expenses, including increased costs for strategic investments, as well as increased interest expense from a higher level of debt outstanding, partially offset by improved gross profit driven by product mix. On an earnings per share basis, diluted EPS was $0.29 per share for the current quarter, and that was $0.07 per share below the same quarter last year.

So now, let's look at adjusted results on the following page. Net sales overall, as I said, declined about $4 million. I'll discuss the change in net sales in more detail at the individual segment level. Overall, adjusted gross profit increased almost $1 million, or 1%, compared to the prior year. Animal Health volume growth in Nutritional Specialties and Vaccines was partially offset by reduced volumes in MFAs and others.

Mineral Nutrition gross profit decreased as average selling prices and unfavorable product mix more than offset lower raw material costs. And in Performance Products, gross profit decreased due to reduced volumes, partially offset by favorable product mix.

Operating expenses overall, or as we refer to them as selling, general and administrative, SG&A, increased $4.4 million, or 10%, driven by spending on strategic investments and key development projects to position ourselves for future growth, and in addition, the effects of the recent acquisition of the Osprey business.

Our adjusted net interest expense increased about $300,000 on higher debt level quarter-over-quarter. And from an adjusted income tax perspective, our effective tax rate for the current quarter was 28% as compared to 29% last year.

Looking more closely at the Animal Health business, net sales of almost $144 million increased about $4 million, or 3%, compared to the prior year. MFAs and other sales declined $1 million, or 1%. Increased US demand was

more than offset by lower volumes in China due to the effects of African swine fever. In the quarter, our customers in China did make some purchases at the end of the current quarter in advance of regulatory changes that became effective January 1, 2020.

In the Nutritional Specialties area, net sales were $33 million in the quarter, an increase of $3.6 million, or 12%. The recent Osprey acquisition accounted for approximately two-thirds of the sales growth in that category. We also experienced organic volume growth in our US dairy and poultry businesses, which was partially offset by timing of the sales in certain international markets. The increase in the domestic Poultry segment was driven by the introduction of a new product, Provia Prime, a direct fed microbial product that helps optimize the gut microbiome in poultry for improved health, immunity and productivity.

Vaccine net sales of $18.7 million, increased $1.6 million, or 10%, from last year, driven by strong international demand and increased market penetration. For the segment, adjusted EBITDA was $33.8 million and that was a decrease of about $2 million, or 6%, primarily due to increased SG&A cost, partially offset by the sales growth and increased gross profit. The SG&A increase was due to the investment in strategic growth initiatives and also the effect of the Osprey acquisition.

And now, looking at our other segments, Mineral Nutrition net sales were $55.7 million in the quarter and that was a decline on the top line of $6.6 million, or 11%. The decline was fundamentally due to lower average selling prices correlated with the movement of underlying raw material costs. We also saw slightly lower volumes this year compared with last year.

From a gross profit perspective, overall, at the bottom line, Mineral Nutrition reported $3.7 million of adjusted EBITDA. That was $400,000 decline compared to the same quarter last year.

Performance Products net sales of $14.6 million declined $1.7 million, or 10%. We saw some volume declines in copper-based products with a partial offset from continued growth in ingredients for personal care products. Segment EBITDA decreased slightly by about $100,000.

Corporate expenses were $10.5 million. That was an increase of $600,000 over last year, again primarily due to increased costs of strategic initiatives and in addition, increased investment in public company costs.

Looking at our capitalization, our gross leverage ratio of debt to adjusted EBITDA was 3.6 times at the end of December with $374 million of total debt and on a trailing 12-month basis, $105 million of adjusted EBITDA. We had $75 million of cash and short-term investments on hand on the balance sheet at quarter-end. So, on a net leverage basis, that gave us a net leverage of just under 3 times.

We had a strong cash flow in the quarter. We generated $23 million source of cash in the quarter before financing and excluding changes in short-term investments.

And we updated our guidance for our full fiscal year, really not major changes to our guidance. At the key adjusted EBITDA line, we kept that unchanged at $103 million to $107 million of EBITDA for the full year.

On the net sales level, we brought down overall consolidated net sales expectations, reflecting lower pricing in the Mineral Nutrition business primarily, which was related to the underlying raw material costs. We also tightened the range on our Animal Health segment.

On an earnings per share basis, adjusted earnings per share, we now expect $1.15 to $1.22 for the full year, a decline from the prior year, but an improvement from our previous expectations. Our expectations now is for less interest expense than we had originally projected and guided to. So, the improvement in earnings per share is really all related to improved interest expense.

And with that, that's the end of my prepared remarks. So, operator, if you would open it up for questions, please.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from the line of David Risinger from Morgan Stanley. Your line is open.

David R. Risinger
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks very much and good morning, Jack and Dick, and congrats on the performance. I have a couple of questions. First, maybe it'd be helpful, Jack, if you could just help us better understand the competitive marketplace that OmniGen competes in, who the key competitors are, how much of an inflection for OmniGen this is going to be that you're launching a next generation? So that would be very helpful.

And then, Dick, if you could comment, please, on the MFA growth, excluding China, so we have a better sense for the growth ex-China in the quarter. And also, if you could comment on the outlook for MFA growth prospects, ex-China, going forward. Thanks very much.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

A

David, hi. Thank you. Thank you for those questions. So, I think, as we've talked in the past, OmniGen was an extremely successful product where most of our customers were smaller dairies, dairies of say, 500 cows or less, which was the predominant dairies in the United States 10 years ago. But that has shifted very, very dramatically in these last 10 years. So, the total amount of dairy cows in United States is about the same as it's been 10 years ago, about 9.2 million cows, but it shifted from smaller dairies to larger dairies.

So, we needed to do something with OmniGen, which was a very successful product on the smaller dairies. It was a successful product where the dairy man got out and saw the – basically, physically saw the health of the animal and was able to see the results of OmniGen, which had a lot to do with immune – strength and immune health. So, we reformulated the product to add some other components to it and really, we manufacture, just not a blending, and concentrating a bit more now on milk production, which becomes more important when you have 5,000 head, 10,000 head in some of these farms in the United States. They go as large as over 20,000.

So for us, it's taking the product relatively to new markets. Some of the same producers we saw or we knew when they ran 500 dairies, we are calling on now with bigger dairies, their needs are slightly different. So they know the product works immune health and now, we're introducing it as well with this new added function which is going to increase milk production.

So it's sort of a wide open field. There's always competition. There's no end to competition in United States at every level. But we have a good history. We have a great sales team, and we're very confident we are going to grow this business, grow the segment.

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.
A

Yeah, David. And to your second question, sort of on the numbers around MFAs. In the second quarter, just to reiterate, we saw overall MFAs down about $1 million, or 1%. If we, ex the China MFA effect, we did see growth. We saw growth within the, probably 3% range year-over-year. On a full-year basis, we're expecting MFAs ex-China to be somewhere around, I'll call it, breakeven to a slightly positive number, as we'll continue to overlap the effect of not having much, if any, China sales for really all of the year.

David R. Risinger
Analyst, Morgan Stanley & Co. LLC
Q

Great. Thank you.

Operator: Your next question comes from the line of Erin Wright from Credit Suisse. Your line is open.

Erin Wilson Wright
Analyst, Credit Suisse Securities (USA) LLC
Q

Great. Thanks. A follow-up on China. How big was that stocking dynamic in terms of the purchasing ahead of the regulatory changes? And can you just describe what that's all related to, in terms of that purchasing dynamic? And should we anticipate then a pullback kind of in the next period here in terms of destocks? I guess any color you can give there would be helpful. Thanks.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.
A

So, Erin, as we sort of had forecasted, we didn't expect to do any business in China this fiscal year. Our distributors – our customers really in China, had inventory which we expected them to sell down with the old registration. The old registration was a growth promotion registration and we have been working for last many years, two, three years, on – as we've done in most markets in the world now, to change their registration from growth promotion to a therapeutic claim. And we've been successful [in other markets.]

Part of the problem with African swine fever in China was, obviously, well, the pigs aren't there, so the market was declining. And this is going to be little long to answer your question, but bear with me. So, the pigs aren't there, but it's also the government was not allowing us or anybody to move pigs around for testing. So, our ability to test on farms and to show either we need to do for the therapeutic claim was slowed down. So, that's really where we were, going forward on a therapeutic claim. But in the meanwhile, the price of pigs in China rose so high that people felt, even though some pigs were going to die from African swine fever, it still pays to grow pigs, because even if you only had a 30%, 40% yield, you can make more than enough money to cover the loss.

So, our customers there saw a big increase and with the calculation they had made to have enough inventory to get through the first six months 2020, they felt they were wrong and they know they had to get material in before the end of the year by Chinese regulations. So, that was the spur. It was not a huge bump. It was a bump, a couple of million dollars and that's done.

Erin Wilson Wright
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. Great. That's really helpful. And then, can you give us an update on just the US market across the species groups here, US poultry, swine, and dairy markets? I guess, in particular, I'd be curious around if you're seeing really a stabilization across dairy markets as well? But, yeah, if you could give us some color on where we stand today in the industry, that will be great. Thanks.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

A

I think, generally, we are seeing a stabilization in at least what we hear back – feedback from our customers. It depends where you are in the market. I think, if you're still out there with a farm of 100, 150 cows, you're under pressure, you're in trouble, and you will most likely be out of the business. But I think, for the larger dairies, they are making money at these levels.

And, again, part of it is because China is looking for a source of protein. And so, somehow that affects directly or indirectly, all the big producers around the world of any protein.

Erin Wilson Wright
Analyst, Credit Suisse Securities (USA) LLC

Q

Okay. All right. Thank you.

Operator: Your next question comes from line of Balaji Prasad from Barclays. Your line is open.

Balaji Prasad
Analyst, Barclays Capital, Inc.

Q

Hi. Thank you and good morning, everyone. So, coming back to the subject on ASF, I had couple of questions on there. Firstly, as you may have seen from the recent USDA report of global pork exports had increased by 10%. And of course you mentioned that you have some registration changes underway to be able to sell more. I wanted to understand, which of the export markets would you be able to target and what are the timelines that you can see in a recovery year?

And secondly, specifically, also from a re-herding prospect, how would that play into your Animal Health growth?

The second comment of my question was on the ASF vaccines. I would love to hear your thoughts on the various developmental programs currently ongoing, including the progress at USDA, and specifically from Phibro's perspective, can you help me understand how your epitope-based development compares to the vaccine now targeting the I177L gene that the USDA is working on. Does this make any difference from a commercial or a timeline perspective? Thank you.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

A

Do you have an hour? So, let's talk first about overall dynamics of protein and sort of call the pig protein versus the effect of African swine fever in China. So, I mean, as we sit here right now, there is no vaccine that will control African swine fever. And the effect of this, as we've seen, it sort of played out slowly, is in excess of 50%, maybe

even up to 70% of pigs have gone missing. And that doesn't mean pigs necessarily who've gotten the virus and died. It means that people see, they put pigs down, they get the virus, they die. So, I'm not going to put new pigs on the market, it doesn't pay overall.

So that has affected a huge shortage of protein. pig protein in China, and they're out there, all over the world, looking to buy all sorts of protein from every market. So, yes, we are seeing our sales into customers raising, again, all proteins specifically, yes, pig protein, but chicken protein, fish protein, cattle protein around the world, all those customers are doing better.

Now, in the US, it's a little bit [ ], I don't want to get into it because of the continuation on the trade war and the tariffs, it's not clear. But, I think that will get clear. But the business around the world, our business is getting better. Can you make up for the loss of, I don't know, 500 million pigs in a world that only is currently raising 250 million pigs? The answer is no. It could take a long time, if ever.

But, I think, there's some point where there will be and that comes through the second question, where there will be a point where there will be a vaccine developed that will be able to slow or to control some of the ASF, where there'll be a meeting point, where the Chinese will be able to start growing pigs again at decent prices, good prices, economic prices, and the world will grow, producing more pig meat, and it would all be – meet somewhere happily in the middle.

We've taken an approach on our vaccine, we've taken an approach different than what we see and what the USDA – what we see coming out of Plum Island. We're working mostly with the proteins that are found in the virus and we're not working to attenuate a virus.

So to that extent, as I said it – often I'll say it again, we don't know yet if our vaccine is going to work. We're doing a lot of work and there are some positive indications, but I don't want anyone to listen to this and think we're saying that it works. We have work to do and we will have a better indication as I said earlier in my remarks by late spring.

But it's a different approach. So, the historic approach to making vaccines is you basically attenuate a virus, you make the virus sort of softer. You then can – you can vaccinate the virus, the pigs' own immune system starts acting and it will protect the pig against whatever the disease is, in this case, the African swine fever.

The initial work on attenuated viruses was not successful. They were unable to do it. And now, with this USDA out of Plum Island, it looks like they have a candidate that could be very effective. So that's great. I think, we're in the business of making sure people have protein and are successful and live a long time, so that we are 100% behind that.

Our approach is a different approach. And there is some logic to say since we're not absolutely injecting, vaccinating the virus, that our approach might be safer and if it's safer then it might get to market faster than the approach which attenuates the virus. So that's a different approach. And again, remember, there were 800 million pigs in China. That's a huge market. Hopefully, everyone would be successful.

Balaji Prasad
Analyst, Barclays Capital, Inc.

Q

Thank you.

Operator: Your next question comes from the line of Michael Ryskin from Bank of America. Your line is open.

Michael Ryskin
Analyst, Bank of America Merrill Lynch

Q

Hey, guys. Thanks for taking the question. I want to follow up on a couple things. I think, people walked through a lot of the market implications, so I'll sort of try to dig it on to the guidance comments. First, on revenue guide, it looks like, I can see that most of the update did come from Mineral Nutrition, you've talked about how that sort of flows through from the underlying commodity prices. But also you did trim the top line for Animal Health, the high end of the guide by about $10 million, from $557 million to $547 million. So, I'm curious if that had anything to do with Nutritional Specialties and Vaccines and more specifically with Osprey, because I think by my prior notes, I had Osprey in at about a $20 million contribution for the year. By my math for the quarter, it goes only about $2.5 million. So, first question is, is that where the delta is coming in? Is it Osprey – is not contributing quite as much as you thought or sort of where is that in the numbers?

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

A

Yeah. Yeah, all your numbers make sense, Mike. This is Dick. Yeah, I think, we trimmed the top end of the Animal Health number for a variety of factors. I would say, just in terms of expectations and we continue, I think, our strongest growth expectations are going to be in the Vaccine product area, then followed by Nutritional Specialties.

Yes, we're seeing some customer order patterns in Osprey where those may reverse themselves later in the year. We'll have to see. But Nutritional Specialties, otherwise, we've talked a lot about dairy, we talked about products that are going into poultry and those are all doing well. And now MFAs, really outside of China, are holding their own. So, not a huge modification, I think, to the sales guidance overall, but that gives you a little more color.

Michael Ryskin
Analyst, Bank of America Merrill Lynch

Q

Got it. Appreciate the bridge there. And then, a follow-up sort of similar line on the P&L. The delta in the SG&A, I mean, you talked consistently about 2020 or fiscal 2020 as an investment year, both in sales force and R&D, the companion animal product, a lot of your investment in R&D for livestock as well, including the ASF vaccine. You still trimmed the SG&A guidance pretty meaningfully, by about $7 million to $10 million.

Just curious where is that extra spend coming from? Is that flexible spend you can take out of Mineral Nutrition, because of the lowered expectations there or sort of is it on the sales forces, on the R&D line? Just trying to get a better sense of where the delta comes in there.

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

A

I think the trimming comes into place as some of these strategic investments are – the timing of the spend is driven by a lot of factors that we can't necessarily control exactly the timing. So, some of these spend on is strategic initiatives has been extended out a little longer than we initially expected. We've also just reduced our expectation for the base spend on operating expenses. Maybe specifically, it's really not around Minerals, this spend is – the bulk of the business is the Animal Health segment and so when you're talking about changes in spending, you're really fundamentally talking about changes in the Animal Health business.

Michael Ryskin
Analyst, Bank of America Merrill Lynch

Q

Okay. Appreciate that. And then sort of one last one along that line, if I may. You talked about ASF vaccine, you talked about the OmniGen expansion. I would say the third product that in terms of innovation has gotten a lot of attention, a lot of focus is the companion animal, sort of direction you're moving into. Can you give us an update there, how that's trending, sort of continued feedback, and how you see that progressing in the next couple of years?

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

A

Yeah. So, we'll give you two answers. I'll give you a number answer. It's – the numbers in the P&L are still small, we don't break them out and they're not at this point really meaningful to trends. And we're – I think where this go is, is still open to question. We're optimistic at what we're seeing and with that, I'll turn it over to Jack for more of the color.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

A

Right. So, there are 25,000 vet clinics in the United States and we have successfully gotten Rejensa, our one product, into 500 clinics. We are adding more clinics every week, so we're still spending money. We are very optimistic and this product is a great product, and with the feedback, we see sort of unpaid for, from the customers on social media is really exciting. So, if anyone listening to this call has a dog which is a little bit old and in some trouble, arthritic trouble, I think go to the site and go buy some products.

But – so, we're still spending money and we might be – if this continues on the trend that it is on, we'll spend more money next year. And I think that's generally true. We haven't got – no one asked that question, but I want to get ahead of it. So that companion animal product is looking good and I think will expand and will be a profitable product, and will be a significant number in our numbers next year, when we get to over 1,000 or 1,500 or 2,000 clinics.

The Vaccines that Dick spoke earlier about it, is we're doing really well where our products are well-accepted in multiple markets and we're spending money, we're clearly spending money to get our new facility in Sligo up and running. We're still 18 months away, which will give us the capacity to sell more, because right now, we're butting up against the capacity at our Beit Shemesh facility.

I think, OmniGen Pro we just launched, we had a big launch meeting last month and looking good. We expect the growth there. African swine fever, we're spending money, don't know. The crazy thing about spending money, looking at this thing from sort of an analyst's numbers, you won't spend money if the product is not successful, and I go, my God, then our EBITDA goes up. But in reality, if it is successful, oh, my, it's a great potential and we'll continue spending money. So we're around that in all of these products. We're, many of you know me, I mean, if you know me, we're not wasting any money here. There are – none of these products are boondoggles. All these are all serious products with serious opportunities for the company. So, we remain excited about the opportunities here of the new products and obviously about the company.

Michael Ryskin
Analyst, Bank of America Merrill Lynch

Q

Thanks so much. Appreciate all the color from both you guys. Thank you.

Operator: [Operator Instructions] Your next question comes from the line of David Westenberg from Guggenheim Securities. Your line is open.

David Westenberg
Analyst, Guggenheim Securities LLC

Q

Hi. Thanks for taking the question. So, most of mine have already been answered, so mine will be pretty short. So, first on the Mineral Nutrition business, I know it's very susceptible to input prices. Now can you remind us if you're maintaining gross margin or if you're maintaining gross profit? I'm just trying to figure out the distinction between the two. As prices go up and down, what the objective is in terms of maintaining?

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

A

David, so we have two objectives. One is, on the traditional sort of base business, we are looking to make a profit for every unit we handle and we talk in terms of tons in the Mineral business. So, we're looking to make X dollars per ton, so whether the selling price is higher or lower, we want to make a certain amount of money on every ton we handle and get paid for the value we add, which is blending, sourcing, warehousing, logistics, et cetera. We are also adding over time and continue to add, more differentiated, higher value-added and therefore higher margin products into the Minerals business. And we're seeing some early success in that. We've – frankly, against our expectations, it's not so much against last year, but against our expectation, we've been seeing the bite of some of the tariffs, because some of these raw materials, many of the raw materials, come from China and have been subject to 25% tariffs. So, depending on the competitive situation of – in some cases, we've not been able to pass those costs through. So that's been something we've been dealing with lately.

David Westenberg
Analyst, Guggenheim Securities LLC

A

That was actually very – that was very helpful. So, back on to the pHi-Tech vaccination device. So it looks like kind of one of those products that could have maybe a portfolio effect. So, is that indeed the case? And could you see this contribute to better sales of the overall portfolio and not just vaccines, but kind of one of those things where it could have a halo effect on other source of businesses.

And then, just in generally and speaking on that pHi-Tech device, are there any maybe comps for us to look at it in terms of peak sales and sales ramp? I mean, is it Embrex from Zoetis, I mean, how can we look at that? That's all my questions. Thank you.

Jack C. Bendheim
Chairman, President & Chief Executive Officer, Phibro Animal Health Corp.

A

That's really a great question. So, I don't know if you can compare this. I think, we're the first in the market with this type of machine and it's not so much the fact that we've replaced finger power on a vaccine device to a battery-powered machine that you just pull and your fingers are protected, so on, so forth. The main thing here is the amount of information, the growers, the producer will get from what's going on. In other words, not just in terms of human resources, like, who's doing the right job, but at what temperature are the vaccines to be put in, where – what percentage of the birds are getting vaccine and what not, et cetera, et cetera. That makes us very powerful. That's why this was a very, very exciting addition at the poultry show last week.

So, we don't have the full range of vaccines that growers use to go through these things. So, right now, it's totally neutral. I mean, when Embrex started many, many years ago, they tried to control the vaccines. They went through it. And I mean, they leased the equipment, but you had to use their vaccines. That is no longer the case because they have competition.

So, we're not even starting there. I don't think that's important. But at the end, we are building solid relationships with poultry producers around the world. And if you build those kind of relationships, then eventually, it enhances our relationships and then they will look at our vaccines like they look at anyone else's vaccine.

David Westenberg
Analyst, Guggenheim Securities LLC

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All right. Thank you.

Operator: There are no further questions at this time. Mr. Johnson, I turn the call back over to you.

Richard G. Johnson
Chief Financial Officer, Phibro Animal Health Corp.

All right. We appreciate everyone listening and thank you for your questions. We'll talk again next quarter. Thank you and bye now.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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