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Phibro Animal Health Corp. (PAHC)

Q3 2020 Earnings Call

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Jack C. Bendheim
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Kevin Kedra
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David Westenberg
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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Phibro Animal Health Corporation Q3 2020 Earnings Conference. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your host today, Mr. Richard Johnson. Sir, please go ahead.

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

Thank you, operator. Good morning, everyone. Welcome to our earnings call for our third quarter ended March 31, 2020. On the call today are Jack Bendheim, our Chief Executive Officer and myself, Richard Johnson, 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, a few housekeeping items, 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 of this morning's call, which can be accessed from 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 will 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.

Looking at page 3 of the webcast, and 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. Our adjusted results exclude acquisition-related items, unusual or non-operational or non-recurring items, certain other income or expense items and the income tax effects related to any of those pre-tax adjustments plus any unusual or non-recurring income tax items themselves.

So with that introduction, I'd like to turn it over to Jack Bendheim for his introductory comments. Jack?

Jack C. Bendheim

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

Thanks, Dick, and first and foremost we cannot overstate our gratitude for the medical professionals, first responders and many others who are at the frontline fighting COVID-19 and its effects on our family, friends and communities. I'd also like to acknowledge and thank all of those people such as supermarket workers, truck drivers, delivery people and food processing plant workers who, day-in and day-out, providing essential services without whom the world would not be able to practice the social distancing necessary to get ahead of this pandemic.

I'm immensely proud and heartened by the way the people of Phibro have responded to the biggest challenge we have faced as a company. Without missing a beat, our offices throughout the world have transformed to virtual ones and our manufacturing facilities, central to food production, have managed to continue producing at unchanged levels. We have maintained production despite numerous measures we have taken to safeguard our people's safety and significantly reduce the risks of infection. What this experience has made clear is the tremendous ingenuity and work ethic across our company, as we are getting our jobs done in ways that just 60 days ago would have seemed undoable.

Examples are numerous from figuring out which borders are open in order to deliver our products, to creating, in the span of weeks, a Phibro online forum that has hosted speakers on topics during in excess of a thousand global viewers, to meeting our customers in the field, with all participants safely staying in their pickups and sharing discussion and presentations via mobile hotspots.

For the quarter ended March, we're able to grow our sales in our core Animal Health segment by a healthy 8% despite the pandemic challenges and the lower sales in China that we have experienced all year. Our vaccines and nutritional specialties product continued to show double-digit growth. While there has been modest swine restocking in China, we did not see any sales of MFAs into China in the quarter due to regulatory changes that took effect January 1st. Included in the quarter was a minimal benefit from customers looking to build the inventory at the early stages of the global lockdown.

With regards to the various pipeline and newly introduced products and projects that I have been updating on a quarterly basis, one of the unfortunate truths of the current situation is it has become extremely difficult to launch products in the current environment. In those areas where we are incumbents, this is a benefit, but we have definitely seen a pause in the uptake of our OmniGen Pro, Provia Prime, Rejensa and pHi-Tech launches and customer adoptions.

We are hard at work building tools and processes that enable us to promote these new products and launches in the current environment and are optimistic that as the social distancing requirements are eased around the globe, we will resume the pace of success we were seeing, and perhaps accelerate it as the financial benefits to our customers may be even more apparent than they previously were.

For the upcoming quarter, we are seeing some softening due to unprecedented disruptions our customers are facing with their downstream demand and processing. We're also seeing an increase in costs as we look to navigate the logistics of disruptive supply chains as well as costs associated with reducing the risk of the virus to our manufacturing employees.

As a result, while our sales to-date have continued close to expectations, we anticipate a decline in demand for our products in the June quarter and we are, therefore, pulling our guidance for the fiscal year ending in June. The bottom line is that there are too many “unknown unknowns” for us to confidently predict that we will achieve our previous expectations for the business.

With that, I will hand it back to Dick and I look forward to answering any questions you may have after his remarks.

Richard G. Johnson

Chief Financial Officer, Phibro Animal Health Corp.

Thank you, Jack. So let's start by reviewing the results for our March 2020 quarter. Consolidated sales were $211 million for the quarter, that was a $5 million or 2% increase versus the same quarter last year. Increased sales in the Animal Health business were partially offset by lower average selling prices in Mineral Nutrition and slightly decreased sales in Performance Products. The increase in Animal Health was driven by our nutritional specialties and vaccine products. We'll get into further details regarding segment results later in the presentation.

Reported net income of $13.5 million declined $1.3 million. Higher gross profit driven by volume growth in the Animal Health segment was more than offset by increased SG&A expenses across the business. Diluted earnings per share of $0.33 per share for the current quarter was $0.04 below the same quarter last year.

Let's discuss adjusted results on page 6. First, we will look at net sales in more detail at the individual segment level, but on a consolidated basis, adjusted gross profit increased $5 million or 8% when compared to the prior year, that was the same amount as the increase in sales. So overall, a favorable product mix effect for the company.
The gross profit increase was driven by sales growth in the Animal Health segment, primarily volume growth in nutritional specialty and vaccine products. We did see slightly lower volumes in MFAs and other products as a partial offset.

Gross profit in the Mineral Nutrition segment decreased, as lower average selling prices and unfavorable product mix more than offset lower raw material costs. Our Performance Products gross profit was comparable to the prior year.

For operating expenses, or what we refer to as selling, general and administrative, adjusted SG&A increased $5.5 million or 13% driven by strategic investments in key product development projects and in part, the effect of the recent Osprey acquisition and also the effect of variable compensation returning to more normalized levels.

Our adjusted net interest expense increased $300,000 year-over-year on higher debt levels, the higher debt levels were partially offset by the benefit of lower variable interest rates. And from an adjusted income tax perspective,

our effective income tax rate for the quarter was 26.3%. That was comparable to the prior year.

Looking more closely at the Animal Health business, net sales of $139 million increased almost $10 million or 8% compared to the same period last year. MFAs and other product net sales were $82.7 million, a decline of $1.4 million, or 2%. We saw very nice increased demand from our poultry and cattle customers in the United States and Latin America. This helped to largely offset lower volumes in China due to the effects of African swine fever and a phased regulatory change that began January 1, 2020.

Nutritional specialty products net sales were $34.6 million, an increase of $6.4 million, or 23%. We experienced organic volume growth in the domestic dairy and poultry markets. In addition, the recent Osprey acquisition accounted for approximately half of the year-over-year sales growth.

Net sales of vaccines were $21.7 million, an increase of $4.8 million, or 28% over last year, driven by strong international demand for poultry vaccines as well as growth in adjuvant products that we also produce.

For the segment, adjusted EBITDA was $34.6 million for the quarter, that was an increase $1.4 million, or 4%. The increase in gross profit from the strong volume growth at the sales level, particularly nutritional specialty and vaccine products, was offset by higher SG&A costs for strategic product development and marketing initiatives plus, in part, the effect of the Osprey acquisition. So, all-in-all that accounted for the increase in profitability in the quarter.

Looking at the other segments on page 8, Mineral Nutrition reported net sales of $56.2 million for the quarter. That was a decline of $4.5 million, or 7%, due to lower average selling prices. We did see some volume growth in the quarter compared to last year. The lower average selling prices are generally correlated with the movement of underlying raw material costs. However, gross profit declined $800,000 year-over-year as the decline in average selling prices and an unfavorable product mix more than offset the lower cost of goods. The gross profit decline, coupled with some increase in SG&A, led to a $1.2 million decline in segment EBITDA compared to last year.

Performance Products net sales were $15.6 million, slightly below last year. We saw a slight decline in sales of ingredients for personal care products, while gross profit was comparable to the prior year due to a favorable product mix. And as a result, segment adjusted EBITDA increased $200,000 over the prior year. Corporate expenses were $10.1 million in the quarter, a $200,000 increase over last year due among other reasons to increased public company costs.

Capitalization on page 9, our gross leverage ratio, debt-to-EBITDA, ratio at March 31st was 3.5 times with $368 million of total debt on our balance sheet and $105 million of trailing 12-month adjusted EBITDA. We had $82 million of cash and short-term investments on the balance sheet at quarter end. And for the March quarter, we generated $19 million of cash, excluding changes in short-term investments and before financing activities.

Turning to page 10, as Jack mentioned during his opening remarks, the animal production industry is currently facing unprecedented demand disruption and production impacts, including its ability to process animals, all as a direct result of the COVID-19 pandemic. Animal producers are rapidly adjusting the amount of animals and milk being produced and significant price declines at the producer level for all proteins have also contributed to reduced production levels.

We anticipate a decline in demand for our products during our quarter ended June 2020. And due to the uncertainties of the pandemic, we're unable to estimate the overall effects on our operations and financial results in the near-term. And as a result, we're withdrawing all previously issued financial guidance for our fiscal year

ended June 2020.

We believe the current difficult situation will begin to normalize in the second half of the calendar year and the industry gradually will return to typical operating levels. We believe we have the financial resources to weather a downturn in our business. We're actively monitoring the ever changing environment and stand ready to take additional operational actions as necessary to protect our financial position.

And that is the conclusion of my prepared remarks. So operator, if you would open it up for questions please?

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Balaji Prasad of Barclays.

Balaji Prasad
Analyst, Barclays Capital, Inc.

Q

Hi. Good morning. This is Balaji. Thanks for taking the questions. A couple of them from me. Firstly, can you help me understand what drove the distributor stocking variation which we have seen this quarter across the industry? There seems to be pretty wide variations between all those companies which have reported and you. How should we interpret this? Thanks.

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

A

Well, I think as we said quite often in the past, our businesses significantly differ from the other companies reporting in this industry. I mean, our segment in the companion animal business, which relies quite heavily on distributors is quite small. So, the amount of product in the pipeline that our competitors have with distributors, which has been very much affected by their lack of ability to call on customers, is different than ours. We call pretty much across the world directly. Where we use distributors, just for logistic reasons, so we don't have that much product in the pipeline. And I did mention we saw, as the lockdowns went into effect, we saw some of our distributors buying a little bit more but overall it was a small effect on our business.

Balaji Prasad
Analyst, Barclays Capital, Inc.

Q

Got it. Yeah. I was speaking of distributor stocking in livestock, but that's helpful. Secondly, are you seeing or do you expect to see an acceleration in the poultry vaccine demand that you have, which is already strong. And I am asking, as we seem to be seeing a strong shift towards cheaper proteins like poultry from the consumer side as that demand pattern shifts? And if you can segregate this between what are you seeing in the US market and the international markets? Thanks.

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

A

So I mean that is a great question and we are seeing some shifts. In many of our markets, the only protein of choice is really poultry, but those very, very same markets are affected by COVID in different ways, which is sort of interesting. A lot of the markets around the world rely – their businesses there rely on their people working in industries that rely on exporting, let's say the United States. And as we've been locked down here and not shopping, we're importing a lot fewer products, which means that the suppliers in the Far East are not working.

And if they're not working they're not paying, and if they're not paying, people are not going out to buy any protein, specifically protein, poultry.

So we're seeing those kind of gyrations, they're not major. In the United States, clearly this is about many of the protein products were prepared for restaurants. As you read that every day, you see that shift, so there are declines. And I would say a lot of this is not as affected by the fact of the damage COVID-19 has done to a few of the slaughterhouses where people have gotten sick and then had to shut them down and that's created a real back up.

Again, the poultry industry, as you've heard often this week, you can control that because if the cycle is under 30 days, that goes very, very quickly. In the cattle industry, you got room on the ranches to hold the cattle longer and the swine industry, you're stuck. You have to get the pigs to market at a certain weight and if they get heavier, it's a problem to be handled. So there, we're seeing depopulation. In this combination you don't know exactly where it's going to happen. You don't know exactly what slaughter plants are going to close tomorrow.
This is why so late in the cycle here we are into the first week of May, end of the quarter is less than eight weeks away. But since you don't know what slaughter plants are going to close and where the bottlenecks are going to come from and which of our customers are going to be affected, it's really become, as I said, unknowns on top of unknowns.

So, the bigger effect in United States I think is in the hog industry and then the cattle. There'll be slowing down the poultry industry around the world. You have effects just in terms of economic stagnation. If people don't have the money, they're just not going to buy chicken. Laid over all this stuff is the Chinese are still importing a lot of pigs and some chickens from around the world. So, it's complicated. It changes week-to-week. As this disease gets mitigated, we'll see it return to normal, but right now, literally, as I said, week-to-week, this is a surprise.

Balaji Prasad
Analyst, Barclays Capital, Inc.

Q

Thank you, Jack.

Operator: Our next question is from Kevin Kedra of G.Research.

Kevin Kedra
Analyst, G.Research LLC

Q

All right, thanks for taking the questions. Jack, I'm sorry, I missed some of your comments on China. So was wondering if you could just speak to kind of what you're seeing there, not only in terms of African swine fever, but also how the country seems to be emerging from COVID.

And then secondly, just want to get a sense, if you see any long-term changes to the livestock industry coming out of COVID-19 or should we think of most of what we're seeing as simply being kind of transitory and reverting back to normal full scale as we get into 2021 or so?

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

A

Let me take the second first. I think long-term we will see things returning to normal pretty much as we knew it. There will be changes in survivors of this disease. Some of the people right now raising animals will not be able to afford some of the losses they're having and that's heavily in the swine business. So – we'll see consolidation, but overall, as you can – as you well understand, animals are being produced, they are being

consumed. And if someone doesn't produce them, someone else will produce them. So there might be movement around the world, maybe moving around the various countries. But overall, the amount of animals being raised, I think will stay the same and we'll go back to the growth pattern we've seen tied to economic growth. This is a disruption, which is not in anyone's model, right, Kevin, you're a smart guy, this is never – it's not have been in any of your models. So we'll see how people will adjust to this. So people will come out, no one will come out stronger, but – and no one really comes out smarter, because there's nothing you can do.

Then I think maybe the changes will be the slaughterhouses will – in terms of going forward, there will be a heightened awareness of what can happen. There might be different ways of keeping people further apart. Maybe more robotics, maybe fewer people in these plants. That will be the changes, but the volumes I think will return to normal.

As far as China goes, people in China calling this they're living through two pandemics. So, they have effects of the coronavirus, which they're starting to come out of. People, just this week, are now allowed to fly from Shanghai to Beijing and not go into quarantine in Beijing. And that's only been lifted this past week. So, they're starting to come out of it, people are slowly going back in, where the economy is being affected, then there's less money available in families. And so, they're buying less. But it is slowly coming back. As I said earlier, there is some restocking of pork, but it's going slowly because African swine fever is very still very much there. So, you have these combination of two things.

As far as it affects us, we are set back in our development of our attempt to make a vaccine for African swine fever because of the coronavirus, because people are not been able to get to the laboratories. The government has taken over every single testing facility to work on a cure for the COVID-19. So for them, internationally it's greater importance than African swine fever. Even though, I think, economically, African swine fever is higher. So there is a setback but everything eventually, whether it's going to be month, two months or three months will start moving forward again.

Kevin Kedra
Analyst, G.Research LLC

Q

Great. Thanks for the color.

Operator: Our next question is from Michael Ryskin of Bank of America.

Michael Ryskin
Analyst, BofA Securities, Inc.

Q

Hi, Mike Ryskin here. Jack, I want to follow up on some of your earlier comments on sort of the medium and long-term impact to the domestic livestock industry in the US, primarily focusing on dairy and swine, as you indicated those seem to be the hardest hit here. Are you having any changes in terms of conversations with your customers where they're becoming so pressured by this outbreak that they're changing their purchasing patterns. They are either becoming more price sensitive or they are outright reducing their medicalization of animals. And we understand that the products you provide, the vaccines and the nutritional specialties, they're critical to the health and well-being here, but it's some degree when the futures prices are down 30% to 40% for these products and schools are closed, restaurants are closed, there is just an economic consideration to be had. So are you seeing any meaningful shift in terms of purchase patterns, behaviors of customers? I'm just wondering could that have a slightly more long-term impact. As you said, there is going to be disruption here and turnover in your customer base. So it may take a while for that to come back.

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

A

So I think the answer – the short answer is, I don't think there will be a long-term impact. A little bit longer answer is that let's analyze what's happening. So you invested in dairy and these are very productive animals and they need to be fed every day and they need to be kept healthy. The problem is one of volume. So, can you limit your herd, I mean, it doesn't make any sense whether it was dairy or pigs or cattle to keep investing in the animal, and you already put a lot of money into that animal. And then to lose money, so again, milk is one thing, but look at the pig business, you're investing so much money and yet at the – you paid already with losses when – to sell it to the packing house. So the answer is no.

But you're not going to go ahead and destroy your big investment just because you're losing some short-term money. What you're going to do is you're going to slow growth and that effects, so you will change what you're feeding, you will change. I mean the products that we and our competitors sell, enhance the ability of the animal to stay healthy and to grow faster and to be more productive.

Now, if you're losing money, why spend money to do that. I mean you don't need more animals coming out of the gate, because that's not helping you right now. So you're going to do everything you can to lower your cost and to slow growth. So you'll change what you put in, so that's not a long-term answer. Your long-term ability to make money in this business is to keep your animals as productive as possible. So again, it's short-term, if I'm losing $15 an animal, do I want to lose $16 or $17 or I would try lose $14 or $13. So I think that's the thinking.

Our customers are very smart, and they've been in this business for long time. They have never seen anything like this as we haven't, you haven't. So they'll adjust, but this is a short-term adjustment. They will depopulate, we're seeing that across chickens, we're seeing that definitely across the hog industry, that's seen in a little bit in some markets around the cattle industry. But then they will come back and as it always does.

Michael Ryskin
Analyst, BofA Securities, Inc.

Q

Great. Really appreciate that. Can I ask sort of a similar big picture question on international markets outside of the US, I think a lot of the news we've seen with slaughterhouse closures, as sort of some of those near term impacts really primarily focused in the US, you're not seeing the same news in internationally, I think it has a lot to do with the sort of the state and the makeup of the OUS livestock industry sort of, especially in the LatAm and in Western Europe. Are you seeing any or do you anticipate seeing any impacts there beyond, sort of the economic conditions and recessionary impact? Or is it fair to say that market has held up pretty well, at least better than the US has?

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

A

I think you're seeing some disruptions. I think the US, while not early to this COVID game, I think it's definitely earlier than South America is. So you're seeing some of the similar effects down there, I think some of the advantages, let's say Brazil is one of the biggest exports of poultry and hogs, as well as Mexico of hogs, is that China keeps buying, China has bought more this year than they bought last year. And the inventories in China, frozen inventories are running out. So China has stepped up its purchases, especially as they come out of COVID. So some of their exports is better. On the other hand, when you have this kind of shutdown which you had across the world, people don't earn money. I mean it's not what we're talking in the United States, as we see it in the papers, its unemployment is up to this, but people are getting paid with unemployment insurance.

That is not the case around the world. So you have less money, you're still going to eat, but you're going to eat less and definitely going to eat less of the expensive food. So there is effects, typical economic recession like effects, right?

And the faster that these people get back to work, the faster that they're going to go back to eating. So that's a little bit again of the unknown unknown here. How long the recession is going to be in these countries, how quickly the US comes back. The US is the economic driver of the world as the Chinese are on the other side. So these are all – you have to do modeling, these are all the hard modeling. You got to figure out, but it's – but again the strong companies will survive and overall, we will come back to the norm and I think we will come back to the growth.
This is going to be maybe a little bit longer than we expected.

Michael Ryskin
Analyst, BofA Securities, Inc.
Q

Great. Thanks. Can I squeeze in one last one for Richard? Can just comment quickly on sort of the balance sheet and your thoughts going forward? I know you recognized this, there's a lot of moving pieces in the environment and how you want to sort of control spend? But any comments you can make on the leverage, and the balance sheet and also your commitment to the dividend?

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

I'm going to pass it back to Dick, okay? As you can imagine, we're not in the same room here.

Michael Ryskin
Analyst, BofA Securities, Inc.
Q

Yeah.

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

So, Dick you want to pick up some of that?

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

Yeah. I got it. Right. We're comfortable with our liquidity. We have – at the end of March, we had between bank liquidity and cash on the balance sheet, we had something in the $150 million range, so a very adequate liquidity where we are conserving cash wherever possible. At the same time, we're continuing to run our operations more or less normally. And we've announced just a couple of days ago, the routine dividend payable later in June. So we are committed to the dividend, subject of course to future developments, but committed to the dividend. And capital spending, we'll continue to spend on the very high priority items. We'll throttle back where we can, where it doesn't slowdown the growth of the business.

Operator: Our next question is from Erin Wright of Credit Suisse.

Haley Christofides
Analyst, Credit Suisse Securities (USA) LLC
Q

Great. Thank you. This is Haley on for Erin this morning. I was wondering, you touched on this a bit earlier, but if you could give a little more color into the impact across your relevant animal health businesses or business lines as it relates to the closure of the meat processing facilities, and when you think this can realistically be resolved. This is tough question to answer. And also my second question, could you speak to how your businesses, particularly across MFAs, have performed in past recessionary environments and how quickly you typically see a recovery? Thank you.

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

A

So we're reading what you're reading, some of these processing plants are reopening now. It's a question of them getting labor in. That is not sick and willing to come in. But we're starting to see some of these factories reopen that will remove the bottleneck. But the problem is you can imagine is if you are taking in – just invent some plants, but taking in 10,000 pigs a day, you don't do that for two weeks. What happens with all those pigs, what is the back up to? And there is no catching up. So, that has created the problem and dislocation for many of our customers. But we do see, as these plants reopen, prices normalizing for them and it's starting to flow through.

So, it really depends on control of a disease that no one seems to be able to control. So, I can't predict when there is going to be a vaccine, but till then, all these factories and they have to monitor their employees very closely, then we have to segregate duties as well as I can, they may have to look at how they – what they're doing and how they're doing it and it's going to take time but there are enough slaughter plants in United States and this thing doesn't go to zero and it keeps moving around. And I think that's – I mean that's – so that's – sorry what was your second question again?

Haley Christofides
Analyst, Credit Suisse Securities (USA) LLC

Q

I was wondering if could speak to how your businesses have performed in recessionary environments in the past and how quickly you typically see a recovery, particularly across MFAs?

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

A

So, our business has always performed sort of on a continuingly, sort of well line. We're an essential business. So you think of yourself. I mean, things are dynamic. Lot of people are being laid off in the financial markets et cetera, et cetera but you have a job and you're continuing to buy, have you cut back in the choice of meat you're eating, have you maybe experimented with some non-meat alternatives, some vegetable meat, yeah you might try that, but it's more expensive.

So I think in a recession, people will return to the basics and they like to eat meat. People tend not to try to go backwards and yes, you will downgrade, maybe instead of having steak, you'll have some pig instead of having that, you'll have poultry, but that sort of floats in between. So I think there might be a dip depending on what countries around the world, but I think that will come back as the recession sort of subsides, I mean, going forward here. So I'm optimistic on the industry, I'm optimistic on our position in the industry and this is a big hiccup and again I'd say the non-foreseen hiccup, but we will get through it.

Haley Christofides
Analyst, Credit Suisse Securities (USA) LLC

Q

Great. Thank you so much. That's helpful.

Operator: Our next question is from David Westenberg of Guggenheim Securities.

David Westenberg
Analyst, Guggenheim Securities LLC

Q

Hi. Thanks for taking the question. So there is – I realized there's a lot of moving parts with COVID here. So I just want to kind of ask on the supply chain dynamics, you have school closures, restaurant closures, meat packing plants being closing down. Is there any specific spot in those that's maybe more important than others in the supply chain that we need to worry about. So for example, if we say restaurant and meat packings are going well, but schools are still closed or restaurants are still closed, but meat packing is still going on. What's the parts that are more sensitive than maybe others?

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

A

You know if you sort of breakthrough, with schools closed, there's less liquid milk being consumed. That doesn't mean there's less liquid milk being produced, right? You got the cow and you're milking it every day. So, some of that is going to be converted to cheese, some that is going to be converted to milk powder and some of that's bought by the government and will be given out. I mean, the fact is that milk in schools is part of a very, very important nutritional package and we need to worry about that. We need to worry about kids getting meals. So, I think that will be – that's a blip and that could be expensive for the producer. But the producer has, in a way, no choice. They can depopulate. They could send more dairy cows into hamburgers, but they overall are not going to really change what they do, which is feed the cows and they produce milk.

Beyond that there is changes and if you built your business – your packing house business that was serving only food chain and not the supermarkets, you're hustling right now because you don't know how long this is going to last, but you will repackage, you will come up with ways of getting more cuts that will work well and could sell well into supermarkets because people are buying more – preparing more foods at home. So there's an adjustment. As I said earlier, there is no bunch of smarter people than farmers. They're great customers. They're great people and they will find ways of modifying what they're doing, want to supply their products to the customers and get through this.

David Westenberg
Analyst, Guggenheim Securities LLC

Q

Okay. So is it fair to say that on the value chain of animal to plate, there maybe is no specific one that scares you more than others? Is that fair to say? They're all kind of equally involved in the – as it pertains to your business?

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

A

Well, again, it pertains to everyone's business. I think the species and the industry that's most affected here, because the way it works in the United States, and you have no choices, is the hog industry. So, I think they're suffering the most. Everybody else has the ability to lower production or to depopulate or to hold on to animals and to get through the same for months and months.

David Westenberg
Analyst, Guggenheim Securities LLC

Q

Okay. So then maybe can you talk about the life cycles of animals in terms of a return to normalcy? I mean, we are looking at COVID playing out for maybe six months – or the summer might have a little bit of a return to normalcy. Maybe may be not, who knows? We, overall, are trying to figure that thing out. But the life cycles of the different animals are different. I mean, I can imagine that poultry is going to come back quite quickly. Do we need to look at maybe cattle – beef cattle as being something that's a little bit more, something we need to worry about to play into 2021, just given the fact that a cow is probably a couple years before it's slaughtered. So just kind of – if you can help us think about life cycle of the animal and how this kind of disruption might play into the next year.

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

So, I mean you're absolutely right. So if you make a decision to produce less poultry now, you can correct that in five weeks – four to five weeks. You can make a decision if you want to depopulate your hog production that could be changed in five to six months. If you want to make decision that you want to depopulate and have fewer animals coming into your feedlot in the cattle business, that's something that's going to affect your production for two years from now. So it's not so much, it's partly the short-term, but it's partly the result of when does this come back and then will you be in position to supply.

I think what all this tells me because we don't know when there will be a fast enough solution to COVID, is – and everyone is guessing that overall – the results of all this, I believe, is that the consumer price for protein is going to go up, because of the losses because of the way things are going to change, because there's going to be fewer animals available to satisfy that demand a year or two years from now.

David Westenberg Q
Analyst, Guggenheim Securities LLC

Okay. And then just the last one. I think in the prepared comments, you said it's good for the incumbents. When we talk to food producers, we do find that there is a very formulaic approach to the way they buy. So I'm a little bit – and, I guess Mike already asked this in a different kind of way, but I'm still a little bit unclear on why would always help the incumbent given the fact that they're so formulaic in the way that they approach medicine. So I would think on a lower price, you would actually see a swap out in product. So just a tiny bit more clarity there.

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

I think, so what I was trying to say is that let's assume you develop a new product, as we do, as all of us do all the time. And you have to get it to the field, you want someone to try it on 5,000, 10,000 animals. So you got to – you have to get into the field, has to be explained, you have to get the nutritionist and the vets involved. Well, you can't do that right now because you can make the sales calls, you can make the presentations. So it is formulaic...

David Westenberg Q
Analyst, Guggenheim Securities LLC

Got it.

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

...people are buying what they know and when they know it works for them. But they have the inability to go look at new things that will work better for them.

David Westenberg
Analyst, Guggenheim Securities LLC

Q

Got it, okay, it's more on line of testing new products, okay. Thank you very much.

Operator: [Operator Instructions] And we have no further questions at this time. Do you have any closing remarks?

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

Dick?

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

We'll just say thank you to everyone on the call this morning. Thank you for listening and we look forward to talking again when we update you on our year-end results which will be right about the end of August. I don't believe we have a specific date yet but there about. So until then, everyone be well, stay safe and thank you again for listening.

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

And I'll add in, everyone stay healthy and take care of yourself.

Operator: Ladies and gentlemen, this concludes today's program. You may now disconnect.

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