

## Phibro Animal Health Corp.

### 3Q14: A Good Opening

**Phibro Animal Health Corp. made a solid debut with its initial earnings report after the April 11 IPO, matching our expectations for total revenues of \$173M and EBITDA of \$22M.** We see initial noise around net income and earnings per share as a function of the housekeeping variables that should stabilize near-term: effective share count, interest expense post IPO/debt refinancing, transaction costs, and tax rates. Reported GAAP EPS of \$0.21 excludes typical adjustments for amortization of intangibles, non-cash taxes, fx losses, etc. Removing these impacts we estimate 3Q operating EPS of \$0.28. **Phibro's management also offered an "adjusted pro forma" EPS number of \$0.36 that indicates what earnings would have been had the IPO/debt refinancing been effective as of January 1, reducing interest expense substantially and increasing the total share count.** We continue to focus on EBITDA as a measure of company performance and as our valuation metric.

**Operationally the company's growth was driven by the Animal Health division, with revenues up 15% y/y and EBITDA up 25%.** Management cited higher volumes as the dominant driver of the better top line, with each segment (MFAs, Nutritional Specialties, Vaccines) delivering double-digit percentage sales improvement. **Guidance for 4Q sales (\$174-\$177M) and EBITDA (\$23-\$24M) is in-line with our existing model,** with our EPS estimate lower on higher projected interest expense (refinancing impact not until later in the quarter). We also exclude \$6M in one-time tax items expected for 4Q – adding this to our numbers would bring EPS in-line with management's \$0.19-\$0.21 guidance range.

Near-term, domestic livestock production faces some headwinds as (1) the cattle herd undergoes the slow process of rebuilding post-drought, which took a toll on pasture land and feed costs, and (2) swine litters are impacted by the spread of PEDv. That said, **we continue to believe that the diversification of PAHC's business model across species, product, and region is a solid advantage.** We will watch in the quarters ahead for evidence of continued market penetration (Brazil, Europe) with key products (V-Max, OmniGen) as the company invests in its sales and support staff.

#### PAHC: Quarterly and Annual EPS (USD)

	2013		2014		2015		Change y/y		
FY Jun	Actual	Old	New	Cons	Old	New	Cons	2014	2015
Q1	0.07A	0.21A	0.21A	N/A	0.34E	0.34E	N/A	200%	62%
Q2	0.15A	0.27A	0.27A	N/A	0.36E	0.36E	N/A	80%	33%
Q3	0.18A	0.18E	0.28A	N/A	0.35E	0.35E	N/A	56%	25%
Q4	0.21A	0.32E	0.27E	N/A	0.37E	0.36E	N/A	29%	33%
Year	0.60A	0.98E	1.03E	N/A	1.42E	1.42E	N/A	72%	38%
P/E	29.7		17.3			12.6			

Source: Barclays Research. Consensus numbers are from Thomson Reuters

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 3.

#### Equity Research

Basic Industries | North America Fertilizers & Agriculture  
15 May 2014

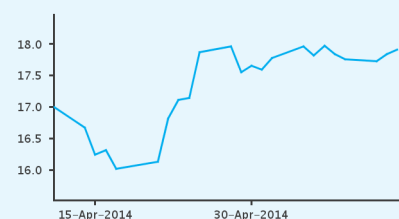
Stock Rating	<b>OVERWEIGHT</b> Unchanged
Industry View	<b>NEUTRAL</b> Unchanged
Price Target	<b>USD 21.00</b> Unchanged

Price (14-May-2014)	USD 17.91
Potential Upside/Downside	+17%
Tickers	PAHC

Market Cap (USD mn)	695
Shares Outstanding (mn)	38.79
Free Float (%)	100.00
52 Wk Avg Daily Volume (mn)	0.3
Dividend Yield (%)	N/A
Return on Equity TTM (%)	N/A
Current BVPS (USD)	-1.64

Source: Thomson Reuters

Price Performance	Exchange-Nasdaq
52 Week range	USD 18.50-15.10



[Link to Barclays Live for interactive charting](#)

#### North America Fertilizers & Agriculture

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## North America Fertilizers &amp; Agriculture

Industry View: NEUTRAL

## Phibro Animal Health Corp. (PAHC)

Stock Rating: OVERWEIGHT

Income statement (\$mn)	2013A	2014E	2015E	2016E	CAGR
Revenue	653	684	728	771	5.7%
EBITDA (adj)	76	90	100	110	13.3%
EBIT	57	69	79	89	16.4%
Pre-tax income	18	34	65	77	62.4%
Net income	25	18	52	53	28.5%
EPS (adj) (\$)	0.60	1.03	1.42	1.66	40.0%
Diluted shares (mn)	30.5	32.9	39.4	39.4	9.0%
DPS (\$)	0.00	0.46	0.39	0.39	N/A

Margin and return data	Average				
EBITDA (adj) margin (%)	11.6	13.2	13.7	14.3	13.2
EBIT margin (%)	8.7	10.1	10.9	11.6	10.3
Pre-tax margin (%)	2.7	5.0	8.9	9.9	6.6
Net margin (%)	3.8	2.6	7.1	6.9	5.1
ROIC (%)	5.5	9.6	15.6	14.7	11.3
ROA (%)	4.0	6.9	10.7	12.1	8.4
ROE (%)	-23.4	-201.6	104.1	71.9	-12.2

Balance sheet and cash flow (\$mn)	CAGR				
Tangible fixed assets	104	107	106	105	0.3%
Intangible fixed assets	35	31	31	31	-3.7%
Cash and equivalents	27	49	57	65	33.2%
Total assets	474	510	530	548	5.0%
Short and long-term debt	366	296	271	241	-12.9%
Other long-term liabilities	62	62	62	62	0.1%
Total liabilities	543	475	458	439	-6.9%
Net debt/(funds)	338	247	215	177	-19.4%
Shareholders' equity	-69	35	72	110	N/A
Change in working capital	-35	-22	-5	-9	N/A
Cash flow from operations	0	27	68	73	460.1%
Capital expenditure	-20	-19	-20	-20	N/A
Free cash flow	-20	8	48	53	N/A

Valuation and leverage metrics	Average				
EV/EBITDA (adj) (x)	21.0	16.7	14.7	13.0	16.4
P/E (adj) (x)	29.7	17.3	12.6	10.8	17.6
FCF yield (%)	-3.6	1.4	6.8	7.5	3.0
P/Sales (x)	1.9	1.8	1.7	1.6	1.8
P/BV (x)	-7.9	16.6	9.7	6.3	6.2
Dividend yield (%)	0.0	2.6	2.2	2.2	1.7
Total debt/capital (%)	123.2	89.4	79.1	68.8	90.1

## Selected operating metrics

Source: Company data, Barclays Research  
Note: FY End Jun

Price (14-May-2014) USD 17.91  
Price Target USD 21.00

**Why Overweight?** We see PAHC shares as a unique way to gain exposure to the strong underlying protein demand trends supporting agribusiness, and we believe that its potential for additional Animal Health market penetration with both existing and new products should support above-industry revenue growth and solid margin expansion.

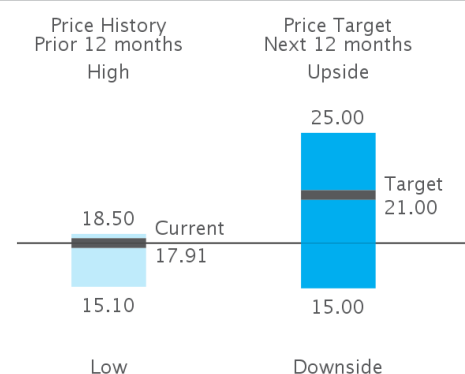
**Upside case** USD 25.00

Our upside case of \$25 assumes a slightly higher multiple applied to a est 2015 EBITDA of \$105M + a modestly higher long-term growth rate in our cash flow model. This EBITDA value results from assuming better top line growth and slight margin expansion relative to our base case.

**Downside case** USD 15.00

Our downside case of \$15 assumes a slightly lower multiple applied to a est 2015 EBITDA of \$89M + a modestly lower long-term growth rate in our cash flow model. This EBITDA value results from assuming slower top line growth and slight margin compression relative to our base case.

## Upside/Downside scenarios



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### Primary Stocks (Ticker, Date, Price)

Phibro Animal Health Corp. (PAHC, 14-May-2014, USD 17.91), Overweight/Neutral, A/C/D/I/L

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**Neutral** - industry coverage universe fundamentals/valuations are steady, neither improving nor deteriorating.

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Agrium Inc. (AGU)	Bunge Limited (BG)	CF Industries Holdings (CF)
CVR Partners (UAN)	Ingredion Inc. (INGR)	Intrepid Potash Inc. (IPI)
Phibro Animal Health Corp. (PAHC)	Potash Corporation of Saskatchewan (POT)	The Mosaic Company (MOS)

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A high/low Quality score indicates financial statement strength/weakness. Measures of quality include ROIC and corporate default probability.

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Phibro Animal Health Corp. (PAHC)

USD 17.91 (14-May-2014)

Stock Rating

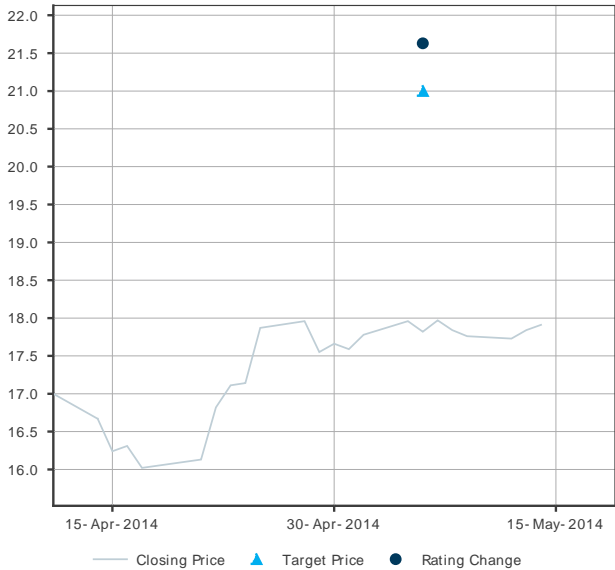
**OVERWEIGHT**

Industry View

**NEUTRAL**

Rating and Price Target Chart - USD (as of 14-May-2014)

Currency=USD



Date	Closing Price	Rating	Adjusted Price Target
06-May-2014	17.82	Overweight	21.00

Source: Thomson Reuters, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

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**Valuation Methodology:** In our view, an appropriate valuation for PAHC stock is to give the company a small but substantial discount to the trading level of ZTS stock, in accordance with PAHC's smaller revenue and lower margins – largely stemming from PAHC's lower-margin Mineral Nutrition and Performance Product divisions – and higher debt level. We set our price target for PAHC at \$21, reflecting an average of two valuation methodologies: (1) using a multiple of 10.25x our projected 2015 EBITDA of \$100M and (2) a discounted cash flow model assuming an 8.2% discount rate and a long-term growth rate of 3.0%

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