PHIBRO ANIMAL HEALTH CORP
Form 10-Q
February 06, 2019
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2018
OR

TRANSITION REPORT PURSUANT TO SECTION 13 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____
Commission File Number: 001-36410

Phibro Animal Health Corporation
(Exact name of registrant as specified in its charter)

Delaware	13-1840497
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
Glenpointe Centre East, 3rd Floor 300 Frank W. Burr Boulevard, Suite 21 Teaneck, New Jersey (Address of Principal Executive Offices)	07666-6712 (Zip Code)

(201) 329-7300
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.) Yes No
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	

Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of January 30, 2019, there were 20,283,777 shares of the registrant's Class A common stock, par value $0.0001 per share, and 20,166,034 shares of the registrant's Class B common stock, par value $0.0001 per share, outstanding.

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

PHIBRO ANIMAL HEALTH CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
	(unaudited) (in thousands, except per share amounts)			
Net sales	$ 218,223	$ 205,876	$ 418,376	$ 399,288
Cost of goods sold	149,579	138,957	283,927	268,987
Gross profit	68,644	66,919	134,449	130,301
Selling, general and administrative expenses	42,938	42,981	85,890	83,976
Operating income	25,706	23,938	48,559	46,325
Interest expense, net	3,015	3,050	5,798	6,168
Foreign currency (gains) losses, net	2,617	(323)	(18)	2
Income before income taxes	20,074	21,211	42,779	40,155
Provision for income taxes	5,326	14,179	11,717	17,231
Net income	$ 14,748	$ 7,032	$ 31,062	$ 22,924
Net income per share				
basic	$ 0.37	$ 0.17	$ 0.77	$ 0.57
diluted	$ 0.36	$ 0.17	$ 0.77	$ 0.57
Weighted average common shares outstanding				
basic	40,383	40,186	40,376	40,065
diluted	40,523	40,364	40,523	40,329

The accompanying notes are an integral part of these consolidated financial statements

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PHIBRO ANIMAL HEALTH CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
	(unaudited) (in thousands)			
Net income	$ 14,748	$ 7,032	$ 31,062	$ 22,924
Change in fair value of derivative instruments	(2,243)	(276)	(1,702)	(898)
Foreign currency translation adjustment	4,163	(5,005)	(3,519)	(1,772)
Unrecognized net pension gains (losses)	124	95	232	226
(Provision) benefit for income taxes	527	809	365	996
Other comprehensive income (loss)	2,571	(4,377)	(4,624)	(1,448)
Comprehensive income	$ 17,319	$ 2,655	$ 26,438	$ 21,476

The accompanying notes are an integral part of these consolidated financial statements

PHIBRO ANIMAL HEALTH CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

As of	December 31, 2018	June 30, 2018
	(unaudited)	
	(in thousands, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	$ 31,336	$ 29,168
Short-term investments	49,000	50,000
Accounts receivable, net	144,050	135,742
Inventories, net	193,099	178,170
Other current assets	23,605	22,381
Total current assets	441,090	415,461
Property, plant and equipment, net	132,711	130,108
Intangibles, net	50,509	51,978
Goodwill	27,348	27,348
Other assets	45,634	46,784
Total assets	$ 697,292	$ 671,679
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current portion of long-term debt	$ 12,577	$ 12,579
Accounts payable	65,095	59,498
Accrued expenses and other current liabilities	58,157	71,144
Total current liabilities	135,829	143,221
Revolving credit facility	88,000	70,000
Long-term debt	223,699	229,802
Other liabilities	44,540	43,702
Total liabilities	492,068	486,725
Commitments and contingencies (Note 8)		
Common stock, par value $0.0001 per share; 300,000,000 Class A shares authorized, 20,220,534 and 19,992,204 shares issued and outstanding at December 31, 2018 and June 30, 2018, respectively; 30,000,000 Class B shares authorized, 20,166,034 and 20,365,504 shares issued and outstanding at December 31, 2018 and June 30, 2018, respectively	4	4
Preferred stock, par value $0.0001 per share; 16,000,000 shares authorized, no shares issued and outstanding	—	—
Paid-in capital	131,343	129,873
Retained earnings	154,984	131,560
Accumulated other comprehensive income (loss)	(81,107)	(76,483)
Total stockholders' equity	205,224	184,954
Total liabilities and stockholders' equity	$ 697,292	$ 671,679

The accompanying notes are an integral part of these consolidated financial statements

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PHIBRO ANIMAL HEALTH CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months	
For the Periods Ended December 31	2018	2017
	(unaudited) (in thousands)	
OPERATING ACTIVITIES		
Net income	$ 31,062	$ 22,924
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Depreciation and amortization	13,532	13,275
Amortization of debt issuance costs and debt discount	441	441
Stock-based compensation	1,129	—
Acquisition-related cost of goods sold	—	1,671
Acquisition-related accrued compensation	—	924
Acquisition-related accrued interest	—	505
Deferred income taxes	135	5,725
Foreign currency (gains) losses, net	12	11
Other	(1,071)	418
Changes in operating assets and liabilities, net of business acquisitions:		
Accounts receivable, net	(8,906)	(5,075)
Inventories, net	(16,278)	(10,845)
Other current assets	(3,616)	(4,751)
Other assets	866	664
Accounts payable	5,169	7,473
Accrued expenses and other liabilities	(5,839)	3,733
Net cash provided (used) by operating activities	16,636	37,093
INVESTING ACTIVITIES		
Purchases of short-term investments	(10,000)	(27,000)
Maturities of short-term investments	11,000	—
Capital expenditures	(12,117)	(8,851)
Business acquisitions	(9,838)	(15,000)
Other, net	27	(716)
Net cash provided (used) by investing activities	(20,928)	(51,567)
FINANCING ACTIVITIES		
Revolving credit facility borrowings	103,000	109,870
Revolving credit facility repayments	(85,000)	(103,870)
Payments of long-term debt, capital leases and other	(6,359)	(3,236)
Issuance of acquisition note payable	3,775	—
Proceeds from common shares issued	341	3,700
Dividends paid	(8,883)	(8,008)

Net cash provided (used) by financing activities	6,874	(1,544)
Effect of exchange rate changes on cash	(414)	120
Net increase (decrease) in cash and cash equivalents	2,168	(15,898)
Cash and cash equivalents at beginning of period	29,168	56,083
Cash and cash equivalents at end of period	$ 31,336	$ 40,185

The accompanying notes are an integral part of these consolidated financial statements
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except per share amounts)
(unaudited)

1.
Description of Business

Phibro Animal Health Corporation ("Phibro" or "PAHC") and its subsidiaries (together, the "Company") is a diversified global developer, manufacturer and marketer of a broad range of animal health and mineral nutrition products for food animals including poultry, swine, cattle, dairy and aquaculture. The Company is also a manufacturer and marketer of performance products for use in the personal care, industrial chemical and chemical catalyst industries. Unless otherwise indicated or the context requires otherwise, references in this report to "we," "our," "us," and similar expressions refer to Phibro and its subsidiaries.

The unaudited consolidated financial information for the three and six months ended December 31, 2018 and 2017, is presented on the same basis as the financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2018 (the "Annual Report"), filed with the Securities and Exchange Commission on August 27, 2018 (File no. 001-36410). In the opinion of management, these financial statements include all adjustments necessary for a fair statement of the financial position, results of operations and cash flows of the Company for the interim periods, and the adjustments are of a normal and recurring nature. The financial results for any interim period are not necessarily indicative of the results for the full year. The consolidated balance sheet information as of June 30, 2018, was derived from the audited consolidated financial statements, which include the accounts of Phibro and its consolidated subsidiaries, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("GAAP"). The unaudited consolidated financial information should be read in conjunction with the consolidated financial statements and notes thereto included in the Annual Report.

The consolidated financial statements include the accounts of Phibro and its consolidated subsidiaries. Intercompany balances and transactions have been eliminated in the consolidated financial statements. The decision whether or not to consolidate an entity requires consideration of majority voting interests, as well as effective control over the entity.

2.
Summary of Significant Accounting Policies and New Accounting Standards

Our significant accounting policies are described in the notes to the consolidated financial statements included in our Annual Report. We adopted Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers (Topic 606), effective July 1, 2018. See "New Accounting Standards" and "Statements of Operations—Additional Information." As of December 31, 2018, there have been no other material changes to our significant accounting policies

Revenue Recognition

We recognize revenue from product sales when control of the products has transferred to the customer, typically when title and risk of loss transfer to the customer. Certain of our businesses have terms where control of the underlying products transfers to the customer on shipment, while others have terms where control transfers to the customer on delivery.

Revenue reflects the total consideration to which we expect to be entitled, in exchange for delivery of products or services, net of variable consideration. Variable consideration includes customer programs and incentive offerings, including pricing arrangements, rebates and other volume-based incentives. We record reductions to revenue for estimated variable consideration at the time we record the sale. Our estimates for variable consideration primarily use the most-likely amount method. Such estimates are generally based on contractual terms and historical experience, and are adjusted to reflect future expectations as new information becomes available. Historically, we have not had significant adjustments to our estimates of customer incentives. Sales returns and product recalls have been insignificant and infrequent due to the nature of the products we sell.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Net sales include shipping and handling fees billed to customers. The associated costs are considered fulfillment activities, not additional promised services to the customer, and are included in costs of goods sold in the consolidated statements of operations when the related revenue is recognized. Net sales exclude value-added and other taxes based on sales.

Net Income per Share, Weighted Average Shares and Dividends per Share

Basic net income per share is calculated by dividing net income by the weighted average number of common shares outstanding during the reporting period.

Diluted net income per share is calculated by dividing net income by the weighted average number of common shares outstanding during the reporting period after giving effect to potential dilutive common shares resulting from the assumed exercise of stock options and vesting of restricted stock units. All common share equivalents were included in the calculation of diluted net income per share for all periods presented.

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
Net income	$ 14,748	$ 7,032	$ 31,062	$ 22,924
Weighted average number of shares – basic	40,383	40,186	40,376	40,065
Dilutive effect of stock options and restricted stock units	140	178	147	264
Weighted average number of shares – diluted	40,523	40,364	40,523	40,329
Net income per share				
basic	$ 0.37	$ 0.17	$ 0.77	$ 0.57
diluted	$ 0.36	$ 0.17	$ 0.77	$ 0.57
Dividends per share	$ 0.12	$ 0.10	$ 0.22	$ 0.20

New Accounting Standards

ASU 2018-14, Compensation—Retirement Benefits—Defined Benefit Plans—General (Topic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans, modifies existing disclosure requirements for defined benefit pension and other postretirement plans. This ASU is effective for fiscal years ending after December 15, 2020 and must be applied on a retrospective basis. We continue to evaluate the effect of adoption of this guidance on our consolidated financial statements.

ASU 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement, modifies existing disclosure requirements for fair value measurement. This ASU is effective for fiscal years beginning after December 15, 2019. We continue to evaluate the effect of adoption of this guidance on our consolidated financial statements.

ASU 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, allows reclassification from accumulated other comprehensive income to retained earnings of stranded tax effects related to adjustments resulting from the United States Tax Cuts and Jobs Act. This ASU is effective for annual reporting periods beginning after December 15, 2018. We do not expect adoption of this guidance to have a material effect on our consolidated financial statements.

ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, provides specific guidance for the classification of certain transactions within the statement of cash flows. We adopted this guidance during the three months ended September 30, 2018, and it did not have a material effect on our consolidated financial statements.

ASU 2016-02, Leases (Topic 842), supersedes the current lease accounting guidance, requires an entity to recognize assets and liabilities for both financing and operating leases on the balance sheet and requires additional qualitative and quantitative disclosures regarding leasing arrangements. This ASU and its amendments are effective for our consolidated financial statements beginning July 1, 2019. The new standard requires a modified retrospective method. We expect the adoption of this guidance will increase the assets and liabilities reported on our consolidated balance sheet. We continue to evaluate the effects of this guidance.

ASU 2014-09, Revenue from Contracts with Customers (Topic 606), establishes principles for the recognition of revenue from contracts with customers. The underlying principle is to identify the performance obligations of a contract, allocate the revenue to each performance obligation and then to recognize revenue when the company satisfies a specific performance obligation of the contract. We adopted ASU 2014-09 and its amendments effective July 1, 2018, using the modified retrospective method. Comparative prior period amounts were not restated and continue to be reported under the accounting standards in effect for those periods. The adoption of the new revenue standard did not have a material effect on reported net sales or retained earnings.

The total cumulative effect of initial adoption of the new standard resulted in the following changes to our consolidated balance sheet:

As of July 1, 2018	Effect of Adoption	Post-adoption
Other current assets	$ 2,100	$ 24,481
Other assets	2,325	49,109
Accrued expenses and other current liabilities	343	71,487
Other liabilities	2,837	46,539
Retained earnings	$ 1,245	$ 132,805

The current year effect of the adoption of the new standard resulted in the following changes to our consolidated balance sheet and consolidated statement of operations:

As of December 31. 2018	Effect of adoption	As reported
Other current assets	$ 100	$ 23,605
Other assets	125	45,634
Other liabilities	(108)	44,540
Retained earnings	$ 333	$ 154,984

	Three Months		Six Months	
For the Periods Ended December 31, 2018	Effect of adoption	As reported	Effect of adoption	As reported
Net sales	$ 198	$ 218,223	$ 396	$ 418,376
Provision for income taxes	32	5,326	63	11,717
Net income	$ 166	$ 14,748	$ 333	$ 31,062

For changes to our policy resulting from the adoption of ASU 2014-09, see "—Summary of Significant Accounting Policies and New Accounting Standards—Revenue Recognition." See "Statements of Operations—Additional Information" for our disclosures regarding disaggregated revenue, deferred revenue and customer payment terms.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

3.

Statements of Operations—Additional Information

Disaggregated revenue, deferred revenue and customer payment terms

We develop, manufacture and market products for a broad range of food animals including poultry, swine, beef and dairy cattle and aquaculture. The products help prevent, control and treat diseases, enhance nutrition to help improve health and contribute to balanced mineral nutrition. The animal health and mineral nutrition products are sold either directly to integrated poultry, swine and cattle integrators or through commercial animal feed manufacturers, wholesalers and distributors. The animal health industry and demand for many of the animal health products in a particular region are affected by changing disease pressures and by weather conditions, as product usage follows varying weather patterns and seasons. Our operations are primarily focused in regions where the majority of livestock production is consolidated in large commercial farms.

We have a diversified portfolio of products that are classified within our three business segments—Animal Health, Mineral Nutrition and Performance Products. Each segment has its own dedicated management and sales team.

Animal Health

The Animal Health business develops, manufactures and markets products in three main categories:

- MFAs and Other: The MFAs and other business primarily consists of concentrated medicated products that are administered through animal feeds, commonly referred to as Medicated Feed Additives (“MFAs”). Specific product classifications include antibacterials, which inhibit the growth of pathogenic bacteria that cause bacterial infections in animals; anticoccidials, which inhibit the growth of coccidia (parasites) that damage the intestinal tract of animals; and other related products.

- Nutritional Specialties: Nutritional specialty products enhance nutrition to help improve health and performance in areas such as immune system function and digestive health.

- Vaccines: Our vaccines are primarily focused on preventing diseases in poultry and swine. They protect animals from either viral or bacterial disease challenges. We also manufacture and distribute autogenous vaccine products and market adjuvants to vaccine manufacturers. We have developed an innovative and proprietary delivery platform for vaccines.

Mineral Nutrition

The Mineral Nutrition business is comprised of formulations and concentrations of trace minerals such as zinc, manganese, copper, iron and other compounds, with a focus on customers in North America. The customers use these products to fortify the daily feed requirements of their livestock’s diets and maintain an optimal balance of trace elements in each animal. Mineral nutrition products are manufactured and marketed for a broad range of food animals including poultry, swine and beef and dairy cattle.

Performance Products

The Performance Products business manufactures and markets a number of specialty ingredients for use in the personal care, industrial chemical and chemical catalyst industries, predominantly in the United States.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following tables present our revenues disaggregated by major product category and geographic region:
Net Sales by Product Type

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
Animal Health				
MFAs and other	$ 93,054	$ 82,018	$ 180,058	$ 161,621
Nutritional specialties	29,460	32,623	56,430	63,400
Vaccines	17,048	18,204	34,263	36,665
Total Animal Health	$ 139,562	$ 132,845	$ 270,751	$ 261,686
Mineral Nutrition	62,319	59,616	117,157	111,689
Performance Products	16,342	13,415	30,468	25,913
Total	$ 218,223	$ 205,876	$ 418,376	$ 399,288

Net Sales by Region

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
United States	$ 127,750	$ 129,379	$ 243,842	$ 242,548
Latin America and Canada	39,316	36,126	77,575	68,452
Europe, Middle East and Africa	26,181	27,672	51,040	53,054
Asia Pacific	24,976	12,699	45,919	35,234
Total	$ 218,223	$ 205,876	$ 418,376	$ 399,288

Net sales by region are based on country of destination.
Total deferred revenue was $6,416 and $4,530 as of December 31, 2018 and June 30, 2018, respectively. Accrued expenses and other current liabilities included $1,471 and $508 of the total deferred revenue as of December 31, 2018 and June 30, 2018, respectively. The deferred revenue resulted primarily from certain customer arrangements, including technology licensing fees and discounts on future product sales. The transaction price associated with our deferred revenue arrangements is generally based on the stand alone sales prices of the individual products or services.
Our customer payment terms generally range from 30 to 120 days globally and do not include any significant financing components. Payment terms vary based on industry and business practices within the regions in which we operate. Our average worldwide collection period for accounts receivable is approximately 60 days after the revenue is recognized.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Interest expense and Depreciation and amortization

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
Interest expense, net				
Term loan	$ 2,202	$ 2,110	$ 4,314	$ 4,143
Revolving credit facility	920	739	1,667	1,420
Amortization of debt issuance costs and debt discount	220	220	441	441
Acquisition-related accrued interest	—	252	—	505
Other	120	2	283	241
Interest expense	3,462	3,323	6,705	6,750
Interest (income)	(447)	(273)	(907)	(582)
	$ 3,015	$ 3,050	$ 5,798	$ 6,168
Depreciation and amortization				
Depreciation of property, plant and equipment	$ 5,308	$ 5,222	$ 10,496	$ 10,405
Amortization of intangible assets	1,521	1,397	3,012	2,846
Amortization of other assets	12	12	24	24
	$ 6,841	$ 6,631	$ 13,532	$ 13,275

4.
Balance Sheets—Additional Information

As of	December 31, 2018	June 30, 2018
Inventories		
Raw materials	$ 80,649	$ 62,373
Work-in-process	14,907	14,731
Finished goods	97,543	101,066
	$ 193,099	$ 178,170

We evaluate our investments in equity method investees for impairment if circumstances indicate that the fair value of the investment may be impaired. The assets underlying a $3,141 equity investment are currently idled; we have concluded the investment is not currently impaired, based on expected future operating cash flows and/or disposal value.

As of	December 31, 2018	June 30, 2018
Accrued expenses and other current liabilities		
Employee related	$ 21,282	$ 27,333
Commissions and rebates	7,510	7,341
Insurance-related	1,563	1,168
Professional fees	4,599	4,350

Income and other taxes	4,122	3,610
Acquisition-related consideration	3,928	12,845
Other	15,153	14,497
	$ 58,157	$ 71,144

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In July 2018, we accelerated the closing date and completed the purchase of intellectual property and certain other assets comprising the MJ Biologics, Inc. ("MJB") business relating to animal vaccines. The Company and MJB had originally agreed to the purchase business combination in January 2015, with a contemplated final closing date in January 2021. The final amount due, net of previously paid amounts, was $12,775, including $9,000 paid in July 2018 and $3,775 paid in January 2019.

As of	December 31, 2018	June 30, 2018
Accumulated other comprehensive income (loss)		
Derivative instruments	$ 3,284	$ 4,986
Foreign currency translation adjustment	(70,617)	(67,098)
Unrecognized net pension gains (losses)	(17,981)	(18,213)
(Provision) benefit for income taxes on derivative instruments	(818)	(1,241)
(Provision) benefit for income taxes on long-term intercompany investments	8,166	8,166
(Provision) benefit for income taxes on pension gains (losses)	(3,141)	(3,083)
	$ (81,107)	$ (76,483)

5. Debt

Term Loans and Revolving Credit Facilities

Pursuant to a credit agreement (the "Credit Agreement"), we have a revolving credit facility (the "Revolver"), where we can borrow up to $250,000, subject to the terms of the agreement, and a term A loan with an aggregate initial principal amount of $250,000 (the "Term A Loan," and together with the Revolver, the "Credit Facilities"). The Credit Facilities have applicable margins equal to 2.00%, 1.75% or 1.50%, in the case of LIBOR and Eurodollar rate loans and 1.00%, 0.75% or 0.50%, in the case of base rate loans; the applicable margins are based on the First Lien Net Leverage Ratio, as defined in the Credit Agreement. The LIBOR rate is subject to a floor of 0.00%. The Credit Facilities mature on June 29, 2022.

The Credit Facilities require, among other things, the maintenance of (i) a maximum First Lien Net Leverage Ratio and (ii) a minimum consolidated interest coverage ratio, each calculated on a trailing four quarter basis, and contain an acceleration clause should an event of default (as defined in the agreement governing the Credit Facilities) occur. As of December 31, 2018, we were in compliance with the covenants of the Credit Facilities.

As of December 31, 2018, we had $88,000 in borrowings under the Revolver and had outstanding letters of credit of $4,191, leaving $157,809 available for borrowings and letters of credit under the Revolver. We obtain letters of credit in connection with certain regulatory and insurance obligations, inventory purchases and other contractual obligations. The terms of these letters of credit are one year or less.

As of December 31, 2018, the interest rates for the Revolver and the Term A Loan were 4.00% and 3.58%, respectively. The weighted-average interest rates for the outstanding revolving credit facilities were 3.71% and 3.01% for the six months ended December 31, 2018 and 2017, respectively. The weighted-average interest rates for the term loans were 3.47% and 3.29% for the six months ended December 31, 2018 and 2017, respectively.

In July 2017, we entered into an interest rate swap agreement on $150 million of notional principal that effectively converts the floating LIBOR or base rate portion of our interest obligation on that amount of debt, to a fixed interest rate of 1.8325% plus the applicable rate. The agreement matures concurrent with the Credit Agreement. The interest rate swap has been designated as a highly effective cash flow hedge. For additional details, see "—Derivatives."

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Long-Term Debt

As of	December 31, 2018	June 30, 2018
Term A Loan due June 2022	$ 237,500	$ 243,750
Capitalized lease obligations	77	118
	237,577	243,868
Unamortized debt issuance costs and debt discount	(1,301)	(1,487)
	236,276	242,381
Less: current maturities	(12,577)	(12,579)
	$ 223,699	$ 229,802

6.
Related Party Transactions

Certain relatives of Jack C. Bendheim, our Chairman, President and Chief Executive Officer, provided services to us as employees or consultants and received aggregate compensation and benefits of approximately $430 and $409 during the three months ended December 31, 2018 and 2017, respectively, and $1,213 and $1,129 during the six months ended December 31, 2018 and 2017, respectively. Mr. Bendheim has sole authority to vote shares of our stock owned by BFI Co., LLC, an investment vehicle of the Bendheim family.

7.
Income Taxes

In December 2017, the United States government enacted comprehensive income tax legislation (the “Tax Act”). The Tax Act makes broad and complex changes to United States income tax law and includes numerous elements that affect the Company, including a reduced federal corporate income tax rate from 35% to 21%, creating a territorial tax system that includes a one-time mandatory transition tax on previously deferred foreign earnings and changes to business-related exclusions, deductions and credits. The Tax Act also has consequences related to our international operations.

We have elected to record Global Intangible Low-Taxed Income (GILTI) aspects of the comprehensive U.S. income tax legislation as a current period expense. The provision for income taxes for the three and six months ended December 31, 2018, included $315 and $672 of expense, respectively, from the effects of GILTI.

During the three months ended December 31, 2018, we completed our analysis and accounting for the Tax Act and recorded a $715 reduction in the provision for income taxes, related to the previously recorded one-time mandatory toll charge on the deemed repatriation of undistributed earnings of foreign subsidiaries.

8.
Commitments and Contingencies

Environmental

Our operations and properties are subject to extensive federal, state, local and foreign laws and regulations, including those governing pollution; protection of the environment; the use, management, and release of hazardous materials, substances and wastes; air emissions; greenhouse gas emissions; water use, supply and discharges; the investigation and remediation of contamination; the manufacture, distribution, and sale of regulated materials, including pesticides; the importing, exporting and transportation of products; and the health and safety of our employees (collectively, “Environmental Laws”). As such, the nature of our current and former operations exposes us to the risk of claims with respect to such matters, including fines, penalties, and remediation obligations that may be imposed by regulatory authorities. Under certain circumstances, we might be required to curtail operations until a particular problem is remedied. Known costs and expenses under Environmental Laws incidental to ongoing operations, including the cost of litigation proceedings relating to environmental matters, are included within operating results. Potential costs and expenses may also be incurred in connection with the repair or upgrade of facilities to meet existing or new requirements under Environmental Laws or to investigate or remediate potential or actual contamination and from time to time we establish reserves for such contemplated investigation and remediation costs. In many instances, the ultimate costs under Environmental Laws and the time period during which such costs are likely to be incurred are difficult to predict.

While we believe that our operations are currently in material compliance with Environmental Laws, we have, from time to time, received notices of violation from governmental authorities, and have been involved in civil or criminal action for such violations. Additionally, at various sites, our subsidiaries are engaged in continuing investigation, remediation and/or monitoring efforts to address contamination associated with historic operations of the sites. We devote considerable resources to complying with Environmental Laws and managing environmental liabilities. We have developed programs to identify requirements under, and maintain compliance with Environmental Laws; however, we cannot predict with certainty the effect of increased and more stringent regulation on our operations, future capital expenditure requirements, or the cost of compliance.

The nature of our current and former operations exposes us to the risk of claims with respect to environmental matters and we cannot assure we will not incur material costs and liabilities in connection with such claims. Based upon our experience to date, we believe that the future cost of compliance with existing Environmental Laws, and liabilities for known environmental claims pursuant to such Environmental Laws, will not have a material adverse effect on our financial position, results of operations, cash flows or liquidity.

The United States Environmental Protection Agency (the “EPA”) is investigating and planning for the remediation of offsite contaminated groundwater that has migrated from the Omega Chemical Corporation Superfund Site (“Omega Chemical Site”), which is upgradient of Phibro-Tech’s Santa Fe Springs, California facility. The EPA has named Phibro-Tech and certain other subsidiaries of PAHC as potentially responsible parties (“PRPs”) due to groundwater contamination from Phibro-Tech’s Santa Fe Springs facility that has allegedly commingled with contaminated groundwater from the Omega Chemical Site. In September 2012, the EPA notified approximately 140 PRPs, including Phibro-Tech and the other subsidiaries, that they have been identified as potentially responsible for remedial action for the groundwater plume affected by the Omega Chemical Site and for EPA oversight and response costs. Phibro-Tech contends that any groundwater contamination at its site is localized and due to historical operations that pre-date Phibro-Tech and/or contaminated groundwater that has migrated from upgradient properties. In addition, a successor to a prior owner of the Phibro-Tech site has asserted that PAHC and Phibro-Tech are obligated to provide indemnification for its potential liability and defense costs relating to the groundwater plume affected by the Omega Chemical Site. Phibro-Tech has vigorously contested this position and has asserted that the successor to the prior owner is required to indemnify Phibro-Tech for its potential liability and defense costs. Furthermore, a group of companies that sent chemicals to the Omega Chemical Site for processing and recycling has filed a complaint under CERCLA and RCRA in the United States District Court for the Central District of California against many of the PRPs allegedly associated with the groundwater plume affected by the Omega Chemical Site (including Phibro-Tech) for contribution toward past and future costs associated with the investigation and remediation of the groundwater plume affected by the Omega Chemical Site. Due to the ongoing nature of the EPA’s investigation, the preliminary stage of the ongoing litigation and Phibro-Tech’s dispute with the prior owner’s successor, at this time we cannot predict with any degree of certainty what, if any, liability Phibro-Tech or the other subsidiaries may ultimately have for investigation, remediation and the EPA oversight and response costs associated with the affected groundwater plume.

Based upon information available, to the extent such costs can be estimated with reasonable certainty, we estimated the cost for further investigation and remediation of identified soil and groundwater problems at operating sites, closed sites and third-party sites, and closure costs for closed sites, to be approximately $6,598 and $6,833 at December 31, 2018 and June 30, 2018, respectively, which is included in current and long-term liabilities on the consolidated balance sheets. However, future events, such as new information, changes in existing Environmental Laws or their interpretation, and more vigorous enforcement policies of regulatory agencies, may give rise to additional expenditures or liabilities that could

be material. For all purposes of the discussion under this caption and elsewhere in this report, it should be noted that we take and have taken the position that neither PAHC nor any of our subsidiaries is liable for environmental or other claims made against one or more of our other subsidiaries or for which any of such other subsidiaries may ultimately be responsible.

Claims and Litigation

PAHC and its subsidiaries are party to a number of claims and lawsuits arising out of the normal course of business including product liabilities, payment disputes and governmental regulation. Certain of these actions seek damages in various amounts. In many cases, our insurance policies will cover such claims. We believe that none of the claims or pending lawsuits, either individually or in the aggregate, will have a material adverse effect on our financial position, results of operations, cash flows or liquidity.

9.
Derivatives

We monitor our exposure to foreign currency exchange rates and interest rates and from time-to-time use derivatives to manage certain of these risks. We designate derivatives as a hedge of a forecasted transaction or of the variability of the cash flows to be received or paid in the future related to a recognized asset or liability (cash flow hedge). All changes in the fair value of a highly effective cash flow hedge are recorded as an asset or liability with a corresponding amount recorded in accumulated other comprehensive income (loss).

We routinely assess whether the derivatives used to hedge transactions are effective. If we determine a derivative ceases to be an effective hedge, we discontinue hedge accounting in the period of the assessment for that derivative, and immediately recognize any unrealized gains or losses related to the fair value of that derivative in the consolidated statements of operations.

We record derivatives at fair value in the consolidated balance sheets. For additional details regarding fair value, see “—Fair Value Measurements.”

We entered into an interest rate swap agreement on $150,000 of notional principal that effectively converts the floating LIBOR or base rate portion of our interest obligation on that amount of debt, to a fixed interest rate of 1.8325% plus the applicable rate. The agreement matures concurrent with the Credit Agreement. The forecasted transactions are probable of occurring, and the interest rate swap has been designated as a highly effective cash flow hedge.

We entered into foreign currency option contracts to hedge cash flows related to monthly inventory purchases. The individual option contracts mature monthly through June 2020. The forecasted inventory purchases are probable of occurring and the individual option contracts were designated as highly effective cash flow hedges.

The following table summarizes the outstanding derivatives that are designated and effective as cash flow hedges as of December 31, 2018:

Instrument	Hedge	Notional Amount at December 31, 2018	Consolidated Balance Sheet	Fair value as of December 31, 2018	Fair value as of June 30, 2018
Options	Brazilian Real calls	R$75,000	(1)	$ 551	$ 71
Options	Brazilian Real puts	R$75,000	(1)	$ (146)	$ —
Swap	Interest rate swap	$150,000	Other assets	$ 2,972	$ 5,078

(1)
We record the net fair values of our outstanding foreign currency option contracts within the respective balance sheet line item based on the net financial position and maturity date of the individual contracts as of the balance sheet date. The net fair values of $405 and $71 were included in other current assets as of December 31, 2018 and June 30, 2018, respectively.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following tables show the effects of derivatives on the consolidated statements of operations and other comprehensive income for the three and six months ended December 31, 2018 and 2017.

For the Three Months Ended December 31

Instrument	Hedge	Gain (Loss) recorded in OCI		Gain (Loss) recognized in consolidated statements of operations			Consolidated Statement of Operations Line Item Total	
		2018	2017	Consolidated Statement of Operations	2018	2017	2018	2017
Options	Brazilian Real puts and calls	$ 513	$ (1,781)	Cost of goods sold	$ —	$ 517	$ 149,579	$ 138,957
Swap	Interest rate swap	$ (2,756)	$ 1,505	Interest expense, net	$ —	$ —	$ 3,015	$ 3,050

For the Six Months Ended December 31

Instrument	Hedge	Gain (Loss) recorded in OCI		Gain (Loss) recognized in consolidated statements of operations			Consolidated Statement of Operations Line Item Total	
		2018	2017	Consolidated Statement of Operations	2018	2017	2018	2017
Options	Brazilian Real puts and calls	$ 404	$ (2,686)	Cost of goods sold	$ 1,084	$ 703	$ 283,927	$ 268,987
Swap	Interest rate swap	$ (2,106)	$ 1,788	Interest expense, net	$ —	$ —	$ 5,798	$ 6,168

We recognize gains (losses) related to these foreign currency derivatives as a component of cost of goods sold at the time the hedged item is sold. Realized net gains of $1,084 related to matured contracts were recorded as a component of inventory as of June 30, 2018 and were fully recognized as an offset to costs of goods sold during the three months ended September 30, 2018.

10.

Fair Value Measurements

Short-term investments

As of December 31, 2018, our short-term investments consist of cash deposits held at financial institutions. We consider the carrying amounts of these short-term investments to be representative of their fair value.

Derivatives

We determine the fair value of derivative instruments based upon pricing models using observable market inputs for these types of financial instruments, such as spot and forward currency translation rates, and interest rate curves.

Fair Value of Assets (Liabilities)

As of	December 31, 2018	June 30, 2018

	Level 1	Level 2	Level 1	Level 2
Short-term investments	$ 49,000	$ —	$ 50,000	$ —
Derivatives asset (liability)	$ —	$ 405	$ —	$ 71
Interest rate swap	$ —	$ 2,972	$ —	$ 5,078

There were no Level 3 fair value measurements as of the periods presented.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

11.
Business Segments

We evaluate performance and allocate resources based on the Animal Health, Mineral Nutrition and Performance Products segments. Certain of our costs and assets are not directly attributable to these segments and we refer to these items as Corporate. We do not allocate Corporate costs or assets to the segments because they are not used to evaluate the segments' operating results or financial position. Corporate costs include certain costs related to executive management, business technology, legal, finance, human resources and business development. Corporate assets include cash and cash equivalents, certain debt issue costs, income tax related assets and certain other assets.
We evaluate performance of our segments based on Adjusted EBITDA. We define Adjusted EBITDA as income before income taxes plus (a) interest expense, net, (b) depreciation and amortization, (c) (income) loss from, and disposal of, discontinued operations, (d) other expense or less other income, as separately reported on our consolidated statements of operations, including foreign currency gains and losses and loss on extinguishment of debt, and (e) certain items that we consider to be unusual, non-operational or non-recurring.
The accounting policies of our segments are the same as those described in the summary of significant accounting policies included herein.

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
Net sales				
Animal Health	$ 139,562	$ 132,845	$ 270,751	$ 261,686
Mineral Nutrition	62,319	59,616	117,157	111,689
Performance Products	16,342	13,415	30,468	25,913
Total segments	$ 218,223	$ 205,876	$ 418,376	$ 399,288
Depreciation and amortization				
Animal Health	$ 5,493	$ 5,265	$ 10,849	$ 10,519
Mineral Nutrition	616	584	1,213	1,169
Performance Products	279	259	552	505
Total segments	$ 6,388	$ 6,108	$ 12,614	$ 12,193
Adjusted EBITDA				
Animal Health	$ 35,925	$ 35,036	$ 71,641	$ 68,778
Mineral Nutrition	4,084	5,614	6,647	9,330
Performance Products	1,514	264	2,230	512
Total segments	$ 41,523	$ 40,914	$ 80,518	$ 78,620

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

	Three Months		Six Months	
For the Periods Ended December 31	2018	2017	2018	2017
Reconciliation of income before income taxes to Adjusted EBITDA				
Income before income taxes	$ 20,074	$ 21,211	$ 42,779	$ 40,155
Interest expense, net	3,015	3,050	5,798	6,168
Depreciation and amortization – Total segments	6,388	6,108	12,614	12,193
Depreciation and amortization – Corporate	453	523	918	1,082
Corporate costs	9,918	8,436	18,804	16,025
Stock-based compensation	564	—	1,129	—
Acquisition-related cost of goods sold	—	1,422	—	1,671
Acquisition-related accrued compensation	—	487	—	924
Acquisition-related transaction costs	—	—	—	400
Other, net	(1,506)	—	(1,506)	—
Foreign currency (gains) losses, net	2,617	(323)	(18)	2
Adjusted EBITDA – Total segments	$ 41,523	$ 40,914	$ 80,518	$ 78,620

As of	December 31, 2018	June 30, 2018
Identifiable assets		
Animal Health	$ 472,534	$ 455,704
Mineral Nutrition	77,351	69,779
Performance Products	32,430	24,040
Total segments	582,315	549,523
Corporate	114,977	122,156
Total	$ 697,292	$ 671,679

The Animal Health segment includes all goodwill of the Company. The Animal Health segment includes advances to and investment in an equity method investee of $3,141 and $3,432 as of December 31, 2018 and June 30, 2018, respectively. The Performance Products segment includes an investment in an equity method investee of $629 and $437 as of December 31, 2018 and June 30, 2018, respectively. Corporate assets include cash and cash equivalents, short-term investments, certain debt issuance costs, income tax related assets and certain other assets.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Introduction

Our management’s discussion and analysis of financial condition and results of operations (“MD&A”) is provided to assist readers in understanding our performance, as reflected in the results of our operations, our financial condition and our cash flows. The following discussion summarizes the significant factors affecting our consolidated operating results, financial condition, liquidity and cash flows as of and for the periods presented below. This MD&A should be read in conjunction with our consolidated financial statements and related notes thereto included elsewhere in this Quarterly Report on Form 10-Q. Our future results could differ materially from our historical performance as a result of various factors such as those discussed in “Risk Factors” and “Forward-Looking Statements.”

Overview of our business

Phibro Animal Health Corporation is a global diversified animal health and mineral nutrition company. We develop, manufacture and market products for a broad range of food animals including poultry, swine, beef and dairy cattle and aquaculture. Our products help prevent, control and treat diseases, enhance nutrition to help improve health and performance and contribute to balanced mineral nutrition. In addition to animal health and mineral nutrition products, we manufacture and market specific ingredients for use in the personal care, industrial chemical and chemical catalyst industries.

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Analysis of the consolidated statements of operations

Summary Results of Operations

For the Periods Ended December 31	Three Months 2018	2017	Change		Six Months 2018	2017	Change	
	(in thousands, except per share amounts and percentages)							
Net sales	$ 218,223	$ 205,876	$ 12,347	6%	$ 418,376	$ 399,288	$ 19,088	5%
Gross profit	68,644	66,919	1,725	3%	134,449	130,301	4,148	3%
Selling, general and administrative expenses	42,938	42,981	(43)	(0)%	85,890	83,976	1,914	2%
Operating income	25,706	23,938	1,768	7%	48,559	46,325	2,234	5%
Interest expense, net	3,015	3,050	(35)	(1)%	5,798	6,168	(370)	(6)%
Foreign currency (gains) losses, net	2,617	(323)	2,940	*	(18)	2	(20)	*
Income before income taxes	20,074	21,211	(1,137)	(5)%	42,779	40,155	2,624	7%
Provision for income taxes	5,326	14,179	(8,853)	(62)%	11,717	17,231	(5,514)	(32)%
Net income	$ 14,748	$ 7,032	$ 7,716	110%	$ 31,062	$ 22,924	$ 8,138	35%
Net income per share								
basic	$ 0.37	$ 0.17	$ 0.20		$ 0.77	$ 0.57	$ 0.20	
diluted	$ 0.36	$ 0.17	$ 0.19		$ 0.77	$ 0.57	$ 0.20	
Weighted average number of shares outstanding								
basic	40,383	40,186			40,376	40,065		
diluted	40,523	40,364			40,523	40,329		
Ratio to net sales								
Gross profit	31.5%	32.5%			32.1%	32.6%		
Selling, general and administrative expenses	19.7%	20.9%			20.5%	21.0%		
	11.8%	11.6%			11.6%	11.6%		

Operating income					
Income before income taxes	9.2%	10.3%		10.2%	10.1%
Net income	6.8%	3.4%		7.4%	5.7%
Effective tax rate	26.5%	66.8%		27.4%	42.9%

Certain amounts and percentages may reflect rounding adjustments.
*
Calculation not meaningful

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Net sales, Adjusted EBITDA and reconciliation of GAAP net income to Adjusted EBITDA

We report Net sales and Adjusted EBITDA by segment to understand the operating performance of each segment. This enables us to monitor changes in net sales, costs and other actionable operating metrics at the segment level. See "—General description of non-GAAP financial measures."

Segment net sales and Adjusted EBITDA:

	Three Months				Six Months			
For the Periods Ended December 31	2018	2017	Change		2018	2017	Change	
	(in thousands, except percentages)							
Net sales								
MFAs and other	$ 93,054	$ 82,018	$ 11,036	13%	$ 180,058	$ 161,621	$ 18,437	11%
Nutritional specialties	29,460	32,623	(3,163)	(10)%	56,430	63,400	(6,970)	(11)%
Vaccines	17,048	18,204	(1,156)	(6)%	34,263	36,665	(2,402)	(7)%
Animal Health	139,562	132,845	6,717	5%	270,751	261,686	9,065	3%
Mineral Nutrition	62,319	59,616	2,703	5%	117,157	111,689	5,468	5%
Performance Products	16,342	13,415	2,927	22%	30,468	25,913	4,555	18%
Total	$ 218,223	$ 205,876	$ 12,347	6%	$ 418,376	$ 399,288	$ 19,088	5%
Adjusted EBITDA								
Animal Health	$ 35,925	$ 35,036	$ 889	3%	$ 71,641	$ 68,778	$ 2,863	4%
Mineral Nutrition	4,084	5,614	(1,530)	(27)%	6,647	9,330	(2,683)	(29)%
Performance Products	1,514	264	1,250	*	2,230	512	1,718	*
Corporate	(9,918)	(8,436)	(1,482)	*	(18,804)	(16,025)	(2,779)	*
Total	$ 31,605	$ 32,478	$ (873)	(3)%	$ 61,714	$ 62,595	$ (881)	(1)%
Adjusted EBITDA ratio to segment net sales								
Animal Health	25.7%	26.4%			26.5%	26.3%		
Mineral Nutrition	6.6%	9.4%			5.7%	8.4%		
Performance Products	9.3%	2.0%			7.3%	2.0%		

Corporate(1)	(4.5)%	(4.1)%	(4.5)%	(4.0)%
Total(1)	14.5%	15.8%	14.8%	15.7%

(1)
reflects ratio to total net sales

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The table below sets forth a reconciliation of net income, as reported under GAAP, to Adjusted EBITDA:

For the Periods Ended December 31	Three Months 2018	Three Months 2017	Change		Six Months 2018	Six Months 2017	Change	
	(in thousands, except percentages)							
Net income	$ 14,748	$ 7,032	$ 7,716	110%	$ 31,062	$ 22,924	$ 8,138	35%
Interest expense, net	3,015	3,050	(35)	(1)%	5,798	6,168	(370)	(6)%
Provision for income taxes	5,326	14,179	(8,853)	(62)%	11,717	17,231	(5,514)	(32)%
Depreciation and amortization	6,841	6,631	210	3%	13,532	13,275	257	2%
EBITDA	29,930	30,892	(962)	(3)%	62,109	59,598	2,511	4%
Stock-based compensation	564	—	564	*	1,129	—	1,129	*
Acquisition-related cost of goods sold	—	1,422	(1,422)	*	—	1,671	(1,671)	*
Acquisition-related accrued compensation	—	487	(487)	*	—	924	(924)	*
Acquisition-related transaction cost	—	—	—	*	—	400	(400)	*
Other, net	(1,506)	—	(1,506)	*	(1,506)	—	(1,506)	*
Foreign currency (gains) losses, net	2,617	(323)	2,940	*	(18)	2	(20)	*
Adjusted EBITDA	$ 31,605	$ 32,478	$ (873)	(3)%	$ 61,714	$ 62,595	$ (881)	(1)%

Certain amounts and percentages may reflect rounding adjustments.

*

Calculation not meaningful

Comparison of three months ended December 31, 2018 and 2017

Net sales

Net sales of $218.2 million for the three months ended December 31, 2018, increased $12.3 million, or 6%, as compared to the three months ended December 31, 2017. Animal Health, Mineral Nutrition and Performance Products grew $6.7 million, $2.7 million and $2.9 million, respectively.

Animal Health

Net sales of $139.6 million for the three months ended December 31, 2018, increased $6.7 million, or 5%. Net sales of MFAs and other increased $11.0 million, or 13%, driven by continued international volume growth, particularly in the Asia Pacific and Latin America regions. Reduced selling prices in certain countries due to unfavorable exchange rate movements partially offset the international growth. Net sales of domestic MFAs and other declined slightly from the prior year. Net sales of nutritional specialty products declined by $3.2 million, or 10%, due to volume declines from continued negative dairy industry conditions and reduced demand from poultry customers. Net sales of vaccines declined $1.2 million, or 6%, due to turbulent economic conditions in certain international countries and the loss of a domestic distribution arrangement; volume growth in other international markets partially offset the reductions.

Mineral Nutrition

Net sales of $62.3 million for the three months ended December 31, 2018, increased $2.7 million, or 5%. Higher average selling prices, plus increased volumes, were the drivers of the increase. Our selling prices of mineral nutrition products generally move in direct correlation with the underlying commodity costs.

Performance Products

Net sales of $16.3 million for the three months ended December 31, 2018, increased $2.9 million, or 22%, due to volume growth of copper-based and personal care products.

Gross profit
Gross profit of $68.6 million for the three months ended December 31, 2018, increased $1.7 million, or 3%, as compared to the three months ended December 31, 2017. Gross profit decreased to 31.5% of net sales for the three months ended December 31, 2018, as compared to 32.5% for the three months ended December 31, 2017. Gross profit for the three months ended December 31, 2017 included $1.4 million of acquisition-related cost of goods sold. Animal Health gross profit increased $0.8 million due to volume growth of MFAs and other, mostly offset by volume declines in the nutritional specialty and vaccine categories and increased vaccine manufacturing costs. Mineral Nutrition gross profit decreased $1.5 million, primarily due to unfavorable product mix and constrained pricing in a competitive environment. Performance Products gross profit increased $1.0 million, primarily due to volume growth. Gross profit increased $1.4 million due to acquisition-related cost of goods sold included in the three months ended December 31, 2017.
Selling, general and administrative expenses
Selling, general and administrative expenses ("SG&A") of $42.9 million for the three months ended December 31, 2018, was approximately equal to the three months ended December 31, 2017. SG&A for the three months ended December 31, 2018, included $0.6 million of stock-based compensation and a $1.5 million benefit from the cancellation of a certain business arrangement. SG&A for the three months ended December 31, 2017, included $0.5 million in acquisition-related compensation costs. Excluding the effects of these costs, SG&A increased $1.4 million, or 3%.
Animal Health, Mineral Nutrition and Performance Products SG&A were each little changed from the prior year. Corporate costs increased $1.4 million due to increased business development expenses. The stock-based compensation, cancellation of the business arrangement and acquisition-related compensation costs resulted in a $1.4 million reduction in SG&A.
Interest expense, net
Interest expense, net of $3.0 million for the three months ended December 31, 2018, was approximately equal to the three months ended December 31, 2017.
Foreign currency (gains) losses, net
Foreign currency (gains) losses, net for the three months ended December 31, 2018, amounted to net losses of $2.6 million, as compared to $0.3 million in net gains for the three months ended December 31, 2017. Foreign currency net losses for the three months ended December 31, 2018, were primarily due to the movement of the Turkish and Brazilian currencies relative to the U.S. dollar. Foreign currency gains and losses primarily arose from cash and intercompany balances.
Provision for income taxes
The provision for income taxes was $5.3 million and $14.2 million for the three months ended December 31, 2018 and 2017, respectively. The effective income tax rate was 26.5% and 66.8% for the three months ended December 31, 2018 and 2017, respectively. The provision for income taxes for the three months ended December 31, 2018 included a $0.7 million benefit from an adjustment to the previously recorded mandatory toll charge on deemed repatriation of undistributed earnings of foreign subsidiaries and a $0.1 million benefit from the exercise of employee stock options. The effective income tax rate, without these benefits, would have been 30.5% for the three months ended December 31, 2018, including a $0.3 million provision for the U.S. federal Global Intangible Low-Taxed Income (GILTI) aspects of the comprehensive U.S. income tax legislation. The effective income tax rate reflects the statutory 21% U.S. federal income tax rate.

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The effective income tax rate for the three months ended December 31, 2017, would have been 26.2% without the discrete items listed below. This effective rate for the three months ended December 31, 2017, included the benefit of adjusting the year-to-date income tax provision to reflect the statutory 28.1% weighted-average U.S. federal income tax rate. The provision for income taxes for the three months ended December 31, 2017, included the effects of the Tax Act and other discrete items:

- a $2.5 million provision for the remeasurement of deferred tax assets and liabilities to reflect the reduced U.S. federal income tax rate;
- a $4.2 million provision to reflect the mandatory toll charge on the deemed repatriation of undistributed earnings of foreign subsidiaries;
- a $0.5 million provision to eliminate the income taxes remaining in accumulated other comprehensive income ("AOCI") after all related foreign currency derivatives had matured and were completely cleared from AOCI;
- a $1.0 million provision for the remeasurement of deferred tax assets to reflect a reduced income tax rate in certain international jurisdictions;
- a $0.4 million net provision from the exercise of employee stock options, including a $0.5 million provision to adjust the benefit recognized in the three months ended September 30, 2017, to the reduced income tax rate.

Net income

Net income of $14.8 million for the three months ended December 31, 2018, increased $7.7 million, as compared to net income of $7.0 million for the three months ended December 31, 2017. A $2.9 million increase in foreign currency losses offset a $1.8 million improvement in operating income, resulting in a $1.1 million decrease in income before income taxes. The provision for income taxes decreased by $8.9 million, primarily because the three months ended December 31, 2017 included additional expense from the initial application of the comprehensive U.S. income tax legislation and other discrete items.

Adjusted EBITDA

Adjusted EBITDA of $31.6 million for the three months ended December 31, 2018, decreased $0.9 million or 3%, as compared to the three months ended December 31, 2017. Mineral Nutrition Adjusted EBITDA decreased $1.5 million, or 27%, due to the effect of unfavorable product mix and constrained pricing in a competitive environment. Corporate expenses increased $1.5 million due to increased business development expenses. Performance Products and Animal Health Adjusted EBITDA increased $1.2 million and $0.9 million, respectively, due to sales growth and increased gross profit.

Comparison of six months ended December 31, 2018 and 2017

Net sales

Net sales of $418.4 million for the six months ended December 31, 2018, increased $19.1 million, or 5%, as compared to the six months ended December 31, 2017. Animal Health, Mineral Nutrition and Performance Products grew $9.1 million, $5.5 million and $4.5 million, respectively.

Animal Health

Net sales of $270.8 million for the six months ended December 31, 2018, increased $9.1 million, or 3%. Net sales of MFAs and other increased $18.4 million, or 11%, driven by continued international volume growth, particularly in the Asia Pacific and Latin America regions. Reduced selling prices in certain countries due to unfavorable exchange rate movements partially offset the international growth. Net sales of domestic MFAs and other were approximately equal to the prior year. Net sales of nutritional specialty products declined by $7.0 million, or 11%, primarily due to volume

declines from the continued negative
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dairy industry conditions and reduced demand from poultry customers. Net sales of vaccines declined $2.4 million, or 7%, due to turbulent economic conditions in certain international countries and the loss of a domestic distribution arrangement; volume growth in other international markets partially offset the reductions.

Mineral Nutrition

Net sales of $117.2 million for the six months ended December 31, 2018, increased $5.5 million, or 5%. Higher average selling prices were the primary driver of the increased revenue, while volumes were approximately level with the prior year. Our selling prices of mineral nutrition products generally move in direct correlation with the underlying commodity costs.

Performance Products

Net sales of $30.5 million for the six months ended December 31, 2018, increased $4.5 million, or 18%, due to volume growth of copper-based products, coupled with higher average selling prices of certain industrial chemical products.

Gross profit

Gross profit of $134.4 million for the six months ended December 31, 2018, increased $4.1 million, or 3%, as compared to the six months ended December 31, 2017. Gross profit decreased to 32.1% of net sales for the six months ended December 31, 2018, as compared to 32.6% for the six months ended December 31, 2017. Gross profit for the six months ended December 31, 2017 included $1.7 million of acquisition-related cost of goods sold.

Animal Health gross profit increased $3.8 million due to volume growth and favorable unit costs and product mix in MFAs and other, partially offset by volume declines in both the nutritional specialty and vaccine categories and increased vaccine manufacturing costs. Mineral Nutrition gross profit decreased $2.7 million, primarily due to unfavorable product mix and constrained pricing in a competitive environment. Performance Products gross profit increased $1.4 million, primarily due to volume growth. Gross profit increased $1.7 million due to acquisition-related cost of goods sold included in the three months ended December 31, 2017.

Selling, general and administrative expenses

Selling, general and administrative expenses ("SG&A") of $85.9 million for the six months ended December 31, 2018, increased $1.9 million, or 2%, as compared to the six months ended December 31, 2017. SG&A for the six months ended December 31, 2018, included $1.1 million of stock-based compensation and a $1.5 million benefit from the cancellation of a certain business arrangement. SG&A for the six months ended December 31, 2017, included $0.4 million in acquisition-related transaction costs and $0.9 million in acquisition-related compensation costs. Excluding the effects of these costs, SG&A increased $3.6 million, or 4%.

Animal Health SG&A increased $1.3 million, driven by sales force expansion and increased investments in marketing and product development. Mineral Nutrition and Performance Products SG&A were each little changed from the prior year. Corporate costs increased $2.6 million due to higher business development expenses and professional fees. The stock-based compensation, cancellation of the business arrangement, acquisition-related transaction costs and acquisition-related compensation costs resulted in a $1.7 million reduction in SG&A.

Interest expense, net

Interest expense, net of $5.8 million for the six months ended December 31, 2018, decreased $0.4 million, or 6%, as compared to the six months ended December 31, 2017, primarily due to increased interest earnings on short-term investments.

Foreign currency (gains) losses, net

Foreign currency (gains) losses, net were insignificant for the six-month periods ended December 31, 2018 and 2017.

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Provision for income taxes

The provision for income taxes was $11.7 million and $17.2 million for the six months ended December 31, 2018 and 2017, respectively. The effective income tax rate was 27.4% and 42.9% for the six months ended December 31, 2018 and 2017, respectively. The provision for income taxes for the six months ended December 31, 2018 included a $0.7 million benefit from an adjustment to the previously recorded mandatory toll charge on deemed repatriation of undistributed earnings of foreign subsidiaries and a $0.2 million benefit from the exercise of employee stock options. The effective income tax rate, without these benefits, would have been 29.6% for the six months ended December 31, 2018, including a $0.7 million provision for the U.S. federal Global Intangible Low-Taxed Income (GILTI) aspects of the comprehensive U.S. income tax legislation. The effective income tax rate reflects the statutory 21% U.S. federal income tax rate.

The effective income tax rate for the six months ended December 31, 2017, would have been 28.3% without the discrete items listed below. The provision for income taxes for the six months ended December 31, 2017 included the effects of the Tax Act and other discrete items:

- a $2.5 million provision for the remeasurement of deferred tax assets and liabilities to reflect the reduced income tax rate;
- a $4.2 million provision to reflect the mandatory toll charge on the deemed repatriation of undistributed earnings of foreign subsidiaries;
- a $0.5 million provision to eliminate the income taxes remaining in AOCI after all related foreign currency derivatives had matured and were completely cleared from AOCI;
- a $1.0 million provision for the remeasurement of deferred tax assets to reflect a reduced income tax rate in certain international jurisdictions;
- a $2.4 million net provision from the exercise of employee stock options, including a $0.5 million provision to adjust the benefit recognized in the three months ended September 30, 2017, to the reduced income tax rate.

Net income

Net income of $31.1 million for the six months ended December 31, 2018, increased $8.1 million, as compared to net income of $22.9 million for the six months ended December 31, 2017. Increased operating income of $2.2 million and lower interest expense of $0.4 million resulted in a $2.6 million increase in income before income taxes. The provision for income taxes decreased by $5.5 million, primarily because the six months ended December 31, 2017 included additional expense from the initial application of the comprehensive U.S. income tax legislation and other discrete items.

Adjusted EBITDA

Adjusted EBITDA of $61.7 million for the six months ended December 31, 2018, decreased $0.9 million, or 1% as compared to the six months ended December 31, 2017. Animal Health Adjusted EBITDA increased $2.9 million, or 4%, due to sales growth and increased gross profit, partially offset by increased SG&A for investments in organization and business development. Mineral Nutrition Adjusted EBITDA decreased $2.7 million, or 29%, due to the effect of unfavorable product mix and constrained pricing in a competitive environment. Performance Products Adjusted EBITDA increased $1.7 million, primarily due to sales growth and increased gross profit. Corporate expenses increased $2.8 million due to higher business development expenses and professional fees.

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Analysis of financial condition, liquidity and capital resources

Net increase (decrease) in cash and cash equivalents was:

	Six Months		
For the Periods Ended December 31	2018	2017	Change
	(in thousands)		
Cash provided by/(used in):			
Operating activities	$ 16,636	$ 37,093	$ (20,457)
Investing activities	(20,928)	(51,567)	30,639
Financing activities	6,874	(1,544)	8,418
Effect of exchange-rate changes on cash and cash equivalents	(414)	120	(534)
Net increase/(decrease) in cash and cash equivalents	$ 2,168	$ (15,898)	$ 18,066

Certain amounts may reflect rounding adjustments.

Net cash provided (used) by operating activities was comprised of:

	Six Months		
For the Periods Ended December 31	2018	2017	Change
	(in thousands)		
EBITDA	$ 62,109	$ 59,598	$ 2,511
Adjustments			
Stock-based compensation	1,129	—	1,129
Acquisition-related cost of goods sold	—	1,671	(1,671)
Acquisition-related accrued compensation	—	924	(924)
Acquisition-related transaction costs	—	400	(400)
Other, net	(1,506)	—	(1,506)
Foreign currency (gains) losses, net	(18)	2	(20)
Interest paid	(5,874)	(5,595)	(279)
Income taxes paid	(10,490)	(9,708)	(782)
Changes in operating assets and liabilities and other items	(28,714)	(9,799)	(18,915)
Cash used for acquisition-related transaction costs	—	(400)	400
Net cash provided (used) by operating activities	$ 16,636	$ 37,093	$ (20,457)

Certain amounts may reflect rounding adjustments.

Operating activities

Net cash provided by operating activities was $16.6 million for the six months ended December 31, 2018. Cash provided by net income and non-cash items, including depreciation and amortization, was partially offset by $28.7 million of cash used in the ordinary course of business for changes in operating assets and liabilities and other items. Increased inventories used $16.3 million of cash due to the timing of sales, purchases and production. Accounts receivable used $8.9 million of cash due to the timing of sales and collections in international regions.

Investing activities

Net cash used in investing activities was $20.9 million for the six months ended December 31, 2018. Capital expenditures were $12.1 million as we continued to invest in our existing asset base and for capacity expansion and productivity improvements. Cash used for business acquisitions was $9.8 million. The use of cash was partially offset by $1.0 million of net proceeds provided by short-term investments.

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Financing activities
Net cash provided by financing activities was $6.9 million for the six months ended December 31, 2018. Net borrowings on our Revolver provided $18.0 million. We partially financed an acquisition of a business through the issuance of a $3.8 million short-term note payable. We received $0.3 million from the issuance of common shares related to the exercise of stock options. We paid $8.9 million in dividends to holders of our Class A and Class B common stock. We paid $6.3 million in scheduled debt and other requirements.
Liquidity and capital resources
We believe our cash on hand, our operating cash flows and our financing arrangements, including the availability of borrowings under the Revolver and foreign credit lines, will be sufficient to support our future cash needs. Our operating plan projects adequate liquidity throughout the year. However, we can provide no assurance that our liquidity and capital resources will be adequate for future funding requirements. We believe we will be able to comply with the terms of the covenants under the Credit Facilities and foreign credit lines based on our operating plan. In the event of adverse operating results and/or violation of covenants under the facilities, there can be no assurance we would be able to obtain waivers or amendments. Other risks to our meeting future funding requirements include global economic conditions and macroeconomic, business and financial disruptions that could arise. There can be no assurance that a challenging economic environment or an economic downturn would not affect our liquidity or our ability to obtain future financing. In addition, our debt covenants may restrict our ability to invest.
Certain relevant measures of our liquidity and capital resources follow:

As of	December 31, 2018	June 30, 2018	Change
	(in thousands, except ratios)		
Cash and cash equivalents and short-term investments	$ 80,336	$ 79,168	$ 1,168
Working capital	237,502	205,651	31,851
Ratio of current assets to current liabilities	2.93:1	2.57:1	

We define working capital as total current assets (excluding cash and cash equivalents and short-term investments) less total current liabilities (excluding the current portion of long-term debt). We calculate the ratio of current assets to current liabilities based on this definition.
At December 31, 2018, we had $88.0 million in outstanding borrowings under the Revolver. We had outstanding letters of credit and other commitments of $4.2 million, leaving $157.8 million available for borrowings and letters of credit.
On February 6, 2019, our Board of Directors declared a cash dividend of $0.12 per share on each share of our Class A and Class B common stock outstanding on the record date of March 6, 2019, payable on March 27, 2019. The quarterly dividend declared on February 6, 2019 and the quarterly dividend paid in December 2018 represent a 20% increase over the $0.10 per share quarterly dividend declared and paid during previous quarters. We expect to pay future quarterly dividends of $0.12 per share on our Class A and Class B common stock, representing approximately $19.4 million annually, subject to approval from the Board of Directors.
At December 31, 2018, our cash and cash equivalents and short-term investments included $78.1 million held by our international subsidiaries. There are no restrictions on cash distributions to PAHC from our international subsidiaries.
Contractual obligations
As of December 31, 2018, there were no material changes in payments due under contractual obligations from those disclosed in the Annual Report on Form 10-K for the year ended June 30, 2018.

Off-balance sheet arrangements

We do not currently use off-balance sheet arrangements for the purpose of credit enhancement, hedging transactions, investment or other financial purposes.

In the ordinary course of business, we may indemnify our counterparties against certain liabilities that may arise. These indemnifications typically pertain to environmental matters. If the indemnified party were to make a successful claim pursuant to the terms of the indemnification, we would be required to reimburse the loss. These indemnifications generally are subject to certain restrictions and limitations.

General description of non-GAAP financial measures

Adjusted EBITDA

Adjusted EBITDA is an alternative view of performance used by management as our primary operating measure, and we believe that investors' understanding of our performance is enhanced by disclosing this performance measure. We report Adjusted EBITDA to portray the results of our operations prior to considering certain income statement elements. We have defined EBITDA as net income (loss) plus (i) interest expense, net, (ii) provision for income taxes or less benefit for income taxes, and (iii) depreciation and amortization. We have defined Adjusted EBITDA as EBITDA plus (a) (income) loss from, and disposal of, discontinued operations, (b) other expense or less other income, as separately reported on our consolidated statements of operations, including foreign currency gains and losses and loss on extinguishment of debt, and (c) certain items that we consider to be unusual, non-operational or non-recurring. The Adjusted EBITDA measure is not, and should not be viewed as, a substitute for GAAP reported net income.

The Adjusted EBITDA measure is an important internal measurement for us. We measure our overall performance on this basis in conjunction with other performance metrics. The following are examples of how our Adjusted EBITDA measure is utilized:

- senior management receives a monthly analysis of our operating results that is prepared on an Adjusted EBITDA basis;
- our annual budgets are prepared on an Adjusted EBITDA basis; and
- other goal setting and performance measurements are prepared on an Adjusted EBITDA basis.

Despite the importance of this measure to management in goal setting and performance measurement, Adjusted EBITDA is a non-GAAP financial measure that has no standardized meaning prescribed by GAAP and, therefore, has limits in its usefulness to investors. Because of its non-standardized definition, Adjusted EBITDA, unlike GAAP net income, may not be comparable to the calculation of similar measures of other companies. Adjusted EBITDA is presented to permit investors to more fully understand how management assesses performance.

We also recognize that, as an internal measure of performance, the Adjusted EBITDA measure has limitations, and we do not restrict our performance management process solely to this metric. A limitation of the Adjusted EBITDA measure is that it provides a view of our operations without including all events during a period, such as the depreciation of property, plant and equipment or amortization of purchased intangibles, and does not provide a comparable view of our performance to other companies.

Certain significant items

Adjusted EBITDA is calculated prior to considering certain items. We evaluate such items on an individual basis. Such evaluation considers both the quantitative and the qualitative aspect of their unusual or non-operational nature. Unusual, in this context, may represent items that are not part of our ongoing business; items that, either as a result of their nature or size, we would not expect to occur as part of our normal business on a regular basis. We consider foreign currency gains and losses to be non-operational because they arise principally from intercompany transactions and are largely non-cash in nature.

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New accounting standards

For discussion of new accounting standards, see "Notes to Consolidated Financial Statements—Summary of Significant Accounting Policies and New Accounting Standards."

Critical Accounting Policies

Critical accounting policies are those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Not all of these significant accounting policies require management to make difficult, subjective or complex judgments or estimates. However, management is required to make certain estimates and assumptions during the preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. Significant estimates include depreciation and amortization periods of long-lived and intangible assets, recoverability of long-lived and intangible assets and goodwill, realizability of deferred income tax and value-added tax assets, legal and environmental matters and actuarial assumptions related to our pension plans. These estimates and assumptions impact the reported amount of assets and liabilities and disclosures of contingent assets and liabilities as of the date of the consolidated financial statements. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the period they are determined to be necessary. Actual results could differ from those estimates. Our significant accounting policies are described in the notes to the consolidated financial statements included in the Annual Report. As of December 31, 2018, there have been no material changes to any of the critical accounting policies contained therein, except for the adoption of the new standard related to revenue recognition. See "Notes to Consolidated Financial Statements—Summary of Significant Accounting Policies and New Accounting Standards" for the changes made to our revenue recognition policy, following the adoption of Financial Accounting Standards Board Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606).

Forward-Looking Statements

This report contains forward-looking statements that are subject to risks and uncertainties. All statements other than statements of historical or current fact included in this report are forward-looking statements. Forward-looking statements discuss our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. These statements may include words such as "aim," "anticipate," "believe," "estimate," "expect," "forecast," "outlook," "potential," "project," "projection," "plan," "intend," "seek," "believe," "may," "c "should," "can," "can have," "likely," the negatives thereof and other words and terms of similar meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events. For example, all statements we make relating to our estimated and projected earnings, revenues, costs, expenditures, cash flows, growth rates and financial results, our plans and objectives for future operations, growth or initiatives, strategies, or the expected outcome or impact of pending or threatened litigation are forward-looking statements. All forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those that we expected. Examples of such risks and uncertainties include:

- perceived adverse effects on human health linked to the consumption of food derived from animals that utilize our products could cause a decline in the sales of those products;
- restrictions on the use of antibacterials in food-producing animals may become more prevalent;
- a material portion of our sales and gross profits are generated by antibacterials and other related products;
- competition in each of our markets from a number of large and small companies, some of which have greater financial, research and development ("R&D"), production and other resources than we have;

- outbreaks of animal diseases could significantly reduce demand for our products;
- our business may be negatively affected by weather conditions and the availability of natural resources;
- the continuing trend toward consolidation of certain customer groups as well as the emergence of large buying groups;
- our ability to control costs and expenses;
- any unforeseen material loss or casualty;
- exposure relating to rising costs and reduced customer income;
- competition deriving from advances in veterinary medical practices and animal health technologies;
- unanticipated safety or efficacy concerns;
- our dependence on suppliers having current regulatory approvals;
- our raw materials are subject to price fluctuations and their availability can be limited;
- natural and man-made disasters, including but not limited to fire, snow and ice storms, flood, hail, hurricanes and earthquakes;
- terrorist attacks, particularly attacks on or within markets in which we operate;
- our ability to successfully implement our strategic initiatives;
- our reliance on the continued operation of our manufacturing facilities and application of our intellectual property;
- adverse U.S. and international economic market conditions, including currency fluctuations;
- failure of our product approval, R&D, acquisition and licensing efforts to generate new products;
-

the risks of product liability claims, legal proceedings and general litigation expenses;

•
the impact of current and future laws and regulatory changes;

•
modification of foreign trade policy may harm our food animal product customers

•
our dependence on our Israeli and Brazilian operations;

•
our substantial level of indebtedness and related debt-service obligations;

•
restrictions imposed by covenants in our debt agreements;

•
the risk of work stoppages; and

•
other factors as described in “Risk Factors” in Item 1A. of our Annual Report.

While we believe that our assumptions are reasonable, we caution that it is very difficult to predict the impact of known factors, and it is impossible for us to anticipate all factors that could affect our actual results. Important factors that could cause actual results to differ materially from our expectations, or cautionary statements, are disclosed under “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” All forward-looking statements are expressly qualified in their entirety by these cautionary statements. You should evaluate all forward-looking statements made in this report in the context of these risks and uncertainties.
We caution you that the important factors referenced above may not contain all of the factors that are important to you. In addition, we cannot assure you that we will realize the results or developments we expect or anticipate or, even if substantially realized, that they will result in the consequences we anticipate or affect us or our operations in the way we expect. The forward-looking statements included in this report are made only as of the date hereof. We undertake no obligation to publicly update or revise any

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forward-looking statement as a result of new information, future events or otherwise, except as otherwise required by law. If we do update one or more forward-looking statements, no inference should be made that we will make additional updates with respect to those or other forward-looking statements.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

In the normal course of operations, we are exposed to market risks arising from adverse changes in interest rates, foreign currency exchange rates and commodity prices. As a result, future earnings, cash flows and fair values of assets and liabilities are subject to uncertainty. We use, from time to time, foreign currency contracts and interest rate swaps as a means of hedging exposure to foreign currency risks and fluctuating interest rates, respectively. We also utilize, on a limited basis, certain commodity derivatives, primarily on copper used in manufacturing processes, to hedge the cost of anticipated purchase or supply requirements. We do not utilize derivative instruments for trading or speculative purposes. We do not hedge our exposure to market risks in a manner that completely eliminates the effects of changing market conditions on earnings, cash flows and fair values. We monitor the financial stability and credit standing of our major counterparties.

For financial market risks related to changes in interest rates, foreign currency exchange rates and commodity prices, reference is made to the "Management's Discussion and Analysis of Financial Condition and Results of Operations—Qualitative and Quantitative Disclosures about Market Risk" section in the Annual Report and to the notes to the consolidated financial statements included therein. There were no material changes in the Company's financial market risks from the risks disclosed in the Annual Report.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation was carried out under the supervision and with the participation of the Company's management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based upon that evaluation as of December 31, 2018, our Chief Executive Officer and Chief Financial Officer each concluded that, as of the end of such period, our disclosure controls and procedures were not effective because of material weaknesses in our internal control over financial reporting, as described in Management's Report on Internal Control over Financial Reporting in "Item 9A. Controls and Procedures" in the Annual Report on Form 10-K for the year ended June 30, 2018.

Material Weakness Remediation Efforts

We continue to make further progress in implementing a broad range of changes to strengthen our internal control over financial reporting and to remediate the material weaknesses that existed as of June 30, 2018. Our actions to address material weaknesses have included the design and implementation of additional formal accounting policies and procedures to ensure transactions are properly initiated, recorded, processed, reported, appropriately authorized and approved. Also, our efforts to ensure maintenance of the appropriate level of segregation of duties includes restricting access to key financial systems and records to appropriate users. We have decreased the level of segregation of duties conflicts and continue to determine the extent it is necessary to limit access and modify responsibilities of certain personnel, as well as designing and implementing additional user access controls and compensating controls. We will continue to build on the progress we have made in our remediation plan. We cannot determine when our remediation plan will be fully completed, and we cannot provide any assurance that these remediation efforts will be successful or that our internal control over financial reporting will be effective as a result of these efforts.

Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting during the three months ended December 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II—OTHER INFORMATION

Item 1.
Legal Proceedings

Information required by this Item is incorporated herein by reference to "Notes to the Consolidated Financial Statements—Commitments and Contingencies" in Part I, Item 1, of this Quarterly Report on Form 10-Q.

Item 1A.
Risk Factors

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in the "Risk Factors" section in the Annual Report, which could materially affect our business, financial condition or future results.

There were no material changes in the Company's risk factors from the risks disclosed in the Annual Report.

Item 2.
Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3.
Defaults Upon Senior Securities

None.

Item 4.
Mine Safety Disclosures

None.

Item 5.
Other Information

None.

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Item 6.
Exhibits

Exhibit 31.1 Chief Executive Officer—Certification pursuant to Sarbanes-Oxley Act of 2002 Section 302

Exhibit 31.2 Chief Financial Officer—Certification pursuant to Sarbanes-Oxley Act of 2002 Section 302

Exhibit 32.1 Chief Executive Officer—Certification pursuant to Sarbanes-Oxley Act of 2002 Section 906

Exhibit 32.2 Chief Financial Officer—Certification pursuant to Sarbanes-Oxley Act of 2002 Section 906

Exhibit 101.INS* XBRL Instance Document

Exhibit 101.SCH* XBRL Taxonomy Extension Schema Document

Exhibit 101.CAL* XBRL Taxonomy Extension Calculation Linkbase Document

Exhibit 101.DEF* XBRL Taxonomy Extension Definition Linkbase Document

Exhibit 101.LAB* XBRL Taxonomy Extension Label Linkbase Document

Exhibit 101.PRE* XBRL Taxonomy Extension Presentation Linkbase Document

*
Furnished with this Quarterly Report. Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933 and are deemed not filed for purposes of section 18 of the Exchange Act.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

		Phibro Animal Health Corporation
February 6, 2019	By:	/s/ Jack C. Bendheim Jack C. Bendheim Chairman, President and Chief Executive Officer
February 6, 2019	By:	/s/ Richard G. Johnson Richard G. Johnson Chief Financial Officer