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Phibro Animal Health Corporation (PAHC)

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CORPORATEPARTICIPANTS

Jack Bendheim Phibro Animal Health Corporation - Chairman, CEO and President

Richard Johnson Phibro Animal Health Corporation - CFO

CONFERENCECALLPARTICIPANTS

Brett William Sprinces Wong Piper Jaffray Companies, Research Division - Principal and Senior Research Analyst

David Reed Risinger Morgan Stanley, Research Division - MD in Equity Research and United States Pharmaceuticals Analyst

Erin Elizabeth Wilson Wright Crédit Suisse AG, Research Division - Director & Senior Equity Research Analyst

Kevin Kedra G. Research, LLC - Research Analyst

Michael Leonidovich Ryskin BofA Merrill Lynch, Research Division - Associate

PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Phibro Fourth Quarter Financial Results Call. (Operator Instructions) I'd now like to introduce your host for today's conference, Mr. Richard Johnson, Chief Financial Officer. Sir, please go ahead.

Richard Johnson - Phibro Animal Health Corporation - CFO

Thank you, operator. Good morning, everyone, and welcome to the Phibro Animal Health earnings call for our fourth quarter and fiscal year ended June 2017. On the call today are Jack Bendheim, our Chief Executive Officer; and myself, the Chief Financial Officer. We will provide an overview of our quarterly and annual results for fiscal 2017, and then we'll discuss our fiscal year 2018 guidance. And then after that, we'll open it up for your questions.

Before we begin, the standard language, let me remind you that the earnings press release and financial tables can be found on the Investors section of our website at pahc.com. We're also providing a simultaneous webcast for this morning's call, which can be accessed on the website as well. Today's presentation slides and a replay and transcript of the call will also be available on the website later today. Our remarks today will include forward-looking statements, and actual results could differ materially from those projections. For a list and description of certain factors that could cause results to differ, I refer you to the forward-looking statements section in our earnings press release.

And our remarks today will also include references to certain financial measures, which were not prepared in accordance with generally accepted accounting principles or U.S. GAAP. I refer you to the non-GAAP financial information section on our earnings press release for a discussion of these measures. Reconciliations of these non-GAAP financial measures to the most directly comparable U.S. GAAP measures are included in the financial tables that accompany the earnings press release.

So with that out of the way, I'll turn it over to Jack Bendheim for some introductory comments. Jack?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

Thank you, Dick, and thank you everyone who is joining us today for this call. Our June quarter was a solid finish to our fiscal year. Our Animal Health business saw continued growth -- strong growth in nutritional specialties and vaccines. MFAs and other sales declined due to the ongoing reduction in United States sales of medically important antimicrobials and the continued challenging economic environment in Brazil. We continue and are increasingly investing in Animal Health product development and organizational capabilities to build the business for future growth.

Our Mineral Nutritional business completed the year with another strong quarter of income growth.

We are optimistic about our business in the broader animal health industry as we enter our new fiscal year. We have numerous opportunities to grow our business to add additional penetration, geographic expansion, new product introductions and acquisitions. We expect continued double-digit growth in nutritional specialties and vaccines. We see growth opportunities for MFAs and other products in international regions, and U.S. sales of medically important antimicrobials are expected to level out about midway through our fiscal year. We will continue to spend P&L dollars on Animal Health product development and organization as we build the business for the longer term.

I will now turn it back to Dick and look forward to our discussions after his prepared remarks.

Richard Johnson - Phibro Animal Health Corporation - CFO

Thanks, Jack. Well, before we get into numbers, there's one page in the slide that just talks a little more in depth about the GAAP and non-GAAP financial information. Just as a reminder, our adjusted numbers are adjusted to exclude all acquisition-related items in common parlance that would be purchase accounting or business combination accounting-type adjustments. We also exclude any unusual nonoperational or nonrecurring items. Over the course of this year, we've had things like pension settlement cost, a gain on an insurance settlement and a loss on extinguishment of debt. We also exclude the foreign currency gains and losses that we report separately. And then lastly, we adjust income tax expense to reflect any income tax related to the pretax adjustments and also to remove unusual or nonrecurring items that are in the GAAP income tax provision.

So with that, let's first review the highlights for our June quarter. Consolidated sales were $195 million for the quarter, a 3% increase compared to last year. That increase was driven by volume growth in the Animal Health segment and also volume growth and some pricing in the Mineral Nutrition segment.

GAAP results included a $2.6 million pretax loss on extinguishment of debt related to the refinancing we completed in June 2017. GAAP results for the 2017 and 2016 quarters, the quarters each benefited from unusual or onetime items in the income tax provision. It was $2.5 million in the 2017 quarter and $2.9 million total in the same quarter a year earlier. And these were benefits from the release of a valuation allowance related to foreign operations; the exercise of employee stock options, sometimes known as a windfall tax benefit; and the recognition of previously unrecognized benefits.

The adjusted results, when we talk about those, exclude all of the items I've just talked about. We excluded the loss on debt extinguishment, and we exclude the favorable income tax items.

At the adjusted EBITDA line. Adjusted EBITDA was $29.4 million, up a little more than $1 million over last year. We'll get into that in more detail when we look at the segments in the coming slides. And our adjusted diluted EPS was $ 0.39 a share. That was up $0.07 or 22% above last year. That was driven by a number of positive factors, including improved adjusted EBITDA. We had lower depreciation expense in the quarter, reduced net interest expense and a lower adjusted effective tax rate. All of those items contributed to the adjusted net income and the EPS growth.

So turning to page 6. Looking at just selected line items from the P&L. Not a lot more to talk about here. You see consolidated sales grew 3%. And adjusted gross profit, which basically removes acquisition-related items, grew by 4%, grew faster than sales on favorable product mix. Adjusted SG&A increased $1.1 million in total. More than the entire increase was driven by the Animal Health segment to position ourselves for future growth. We continued to increase spending on product development and organizational capabilities.

And looking more closely at the Animal Health segment. We had sales of $128.6 million for the quarter. That was growth of $2.4 million or 2% over last year. We saw similar trends to what we've been seeing in recent quarters. The growth was driven by strong increases in nutritional specialties and vaccine product groups. We did see a decline in the MFAs and other category. Nutritional specialties of $28.1 million grew $3.4 million or 14% over last year. The same -- continuation of the same story, and that is volume growth of products for the U.S. poultry and dairy industries and a bit of geographic expansion of those products also.

Vaccine sales in the quarter were $16.3 million. That was growth of $1.2 million or 8% over last year. And that, again, was due to volume growth. I would say that our underlying vaccine demand remained strong, but timing of certain customer shipments resulted in a lower-than-typical growth rate in the quarter. For MFAs and others, sales were approximately $84 million in the quarter, a $2 million or a 7% decrease from last year. Sorry, that should be a 3% decrease from last year.

We saw continued reductions in sales of medically important antimicrobials in the U.S. due to regulatory and due to consumer preference factors. We saw a sales decline in Brazil, resulting from challenging economic conditions. However, we did have sales growth of other products in other regions that partially offset the declines I talked about above.

Adjusted EBITDA of $31.2 million for the quarter decreased $200,000 or 1%, just slightly below last year. Nice gross profit growth in the segment was offset by increased operating expenses, as we talked about.

In looking at our other segments for the quarter, Mineral Nutrition had a very nice quarter. Net sales were $53 million, up $2.5 million or 5% on volume growth and some commodity pricing. The nice part about this business was the $4.4 million of adjusted EBITDA, an increase of $700,000 over last year, well ahead of the sales growth. So good profit performance, as we've seen really all year from the Mineral Nutrition segment.

Our Performance Products net sales were about $13 million, slightly above last year. Adjusted EBITDA was also slightly ahead of last year, and corporate expenses were slightly favorable to last year.

So now if we look at Page 9, looking at a summary of our full fiscal year. Our net sales for the full year were $764 million. That was about $13 million of growth or 3%. And those sales generated growth in adjusted EBITDA of $7.4 million, and it -- and obviously, I mean, we've talked about this a number of times. Our gross profit grew faster than sales on favorable product mix and also, ongoing benefit of manufacturing cost efficiencies we've been seeing from some of the CapEx investments we've been making.

Adjusted SG&A across the entire company for the year increased $3.5 million, driven entirely by investments we're making in the Animal Health segment. Adjusted net interest expense was favorable due to interest income on deposits in foreign jurisdictions. The adjusted effective income tax rate for the year was 30.1%, up slightly compared to 29.5% last year. And that brings it all down to adjusted diluted EPS of $1.51 per share for the year, up $0.08 or 6% over the same period last year.

Looking at capitalization and capital allocation. Our leverage ratio, which is debt to adjusted EBITDA, was 2.6x on a gross basis at June 30. Our positive cash flow continues to improve the leverage ratio. We also had $56 million of cash on the balance sheet at year-end. For our June quarter, we generated $9 million of net cash flow before financing. And for the year, we generated $76 million of net cash flow before financing. And on the dividend front, we paid a routine quarterly dividend in the quarter and have declared the same amount per share to be paid in September.

So now turning to guidance on Page 11 and I guess, 12 and 13. You see the numbers on Slide 11. We've given guidance on both a GAAP and an adjusted basis. There's more detail in the press release on these numbers. These are some of the highlight numbers. We forecast Animal Health net sales at $500 million to $515 million. That's up to a 3% increase over last year at the top end of the range. We continue -- we expect that nutritional specialties and vaccines will continue to grow at double-digit rates. We expect MFAs and other sales will decline something in the single-digit neighborhood. We expect continued reduction in U.S. sales of medically important antimicrobials through the first half of our fiscal year, we do expect continued growth in international markets, which will be a partial offset to those declines. In Mineral Nutrition, we expect revenues to remain steady to a slight increase, with volume growth being offset by reduced pricing related to commodity prices. And Performance Products, we expect to remain stable or decline slightly.

And so that gives you, for the total company, consolidated net sales of between $765 million and $790 million expected next year, again, up to a 3% increase.

On a GAAP basis, we expect GAAP diluted earnings per share of $1.43 to $1.56. That's down from 2017, primarily due to a higher -- call it, more normalized GAAP effective tax rate. The 2017 effective tax rate and therefore, tax expense, included some unusual benefits that we do not expect to recur in fiscal 2018.

So looking now at adjusted EBITDA. We expect adjusted EBITDA for our fiscal 2018 to be in the $123 million to $126 million range. That's a 3% to 6% increase over 2017. We expect EBITDA margin or operating margin to improve by 30 to 40 basis points. And that will be driven by an improved gross profit ratio, really due to a favorable product mix. However, we will continue with increased spending on operating expenses for product development, which will partially offset the gross profit growth.

We expect adjusted EPS will be between $1.55 and $1.61. That's a 3% to 7% increase over the prior year. On -- the growth in adjusted EBITDA is really the primary driver of the growth in adjusted earnings per share. We expect adjusted EBITDA for our September and December quarters -- so the first 2 quarters, the first half of our fiscal year. We expect adjusted EBITDA for the first half will be approximately equal to the comparable quarter last year. So we expect that the growth in adjusted EBITDA will come primarily in the second half of our fiscal year. And finally, we expect positive cash flows and remain interested in acquisitions.

So that is the conclusion of my prepared remarks. So operator, if you would please open the line for questions.

Q U E S T I O N S A N D A N S W E R S

Operator

(Operator Instructions) Our first question comes from the line of Brett Wong with Piper Jaffray.

Brett William Sprinces Wong - Piper Jaffray Companies, Research Division - Principal and Senior Research Analyst

First, just looking at your guidance. What's driving your expectations or confidence of double-digit growth next fiscal in vaccines given the more difficult comps that we already started to see this recent quarter?

Richard Johnson - Phibro Animal Health Corporation - CFO Go ahead.

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

It's probably a global footprint. We are increasing our penetration of some markets in the Far East, where we're seeing sort of dynamic growth in protein. One on the consumption side, but more importantly is the countries there are more concerned about food safety. They're getting their arms around treating animals to make sure that healthy animals enter into the food supply. So we're seeing increase in -- on both the vaccine side as well as on various MFA sides in those markets. That's confidence. And the other side of it is, as part of -- as we've discussed on past, as we sit here, what we need is, in a way, for our business, is we need -- we're controlling diseases, so we are expecting a normal run of both poultry and swine diseases around the world. And that's on a normal expectation, so that's what's driving our guidance.

Richard Johnson - Phibro Animal Health Corporation - CFO

Yes. And I'd add to that, Brett. We're out there, I'll call it, prospecting in the market, presenting our products to potential customers. And I think we see good, strong interest in our products in -- with a number of both customers and segments of the industry and geographies, where we're very -- where we're optimistic about turning some of that customer interest into sales in the coming year.

Brett William Sprinces Wong - Piper Jaffray Companies, Research Division - Principal and Senior Research Analyst

Okay, that's helpful. And then just kind of looking at the MFA side with your expectations of ongoing declines in the first half of the year. Can you provide a little more detail around your thoughts for the back half? What's factored into that expectation of stabilization or improvement and what could result in that back half, either declining again or proving to be more optimistic?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

I think it's mostly driven by the fact that we're lapping this year. The U.S. regulatory changes went into effect at the beginning of 2017. So we saw last year sort of in the back half of 2016 calendar sort of an increase in sales as people put some more inventory in. They will either use up some inventory they had on hand, but then the game changed. So we're going to get through that 6 months over the first 6 months of our fiscal year, all right, the back half of the calendar year. And then starting next year, we're in the new world that we've been in now, so we think things will stabilize. I mean, in the U.S., the customers, especially in the poultry side, have broken down into 3 worlds. There've been -- the customers who are -- well, they call themselves, NAEs, or No Antibiotics Ever. So there's no antibiotics, literally, from hatchery through processing. And then there are customers who are raising antibiotic-free birds that has to do with the U.S. government's list of medically important antibiotics, but they are using a range of antibiotics to control diseases. And then there are customers who are just doing conventional birds, who are saying that, logically, as long as the animals are sick, the best way to treat them are using the products -- the best products available that happen to be antibiotics. And that's not saying that the other customers are not treating their animals. Everyone's treating their animals, but everyone's treating their animals in different ways with different products, which is why our nutritional specialties business, have grown because we have entered into those markets with a new range of products that are taking hold. But they'll take a while because this is, again, a new world for everybody. So that's how we view the world. The rest of the world -- while the influence in the U.S. about using less antibiotics, clearly, is built around the world, it's more than offset by the fact that I have mentioned earlier, is that, as customers around the world, being driven heavily by China, but that's the biggest influence there in the Far East, are very concerned about food safety, and this is -- I think you – may be heavily written about, the smaller farms, the backyard farms are being shut down or are closing down. And people are concerned in that the animals are moving to more commercial farms, where you control -- you can control what they eat. They even control the health and the well-being of the animals. And in those kind of markets, we find that our product ranges and our products, from MFAs through vaccines through nutritional specialties, have a greater acceptance. So that's the balance of the business that we see for this coming year and as we see out into the future.

Brett William Sprinces Wong - Piper Jaffray Companies, Research Division - Principal and Senior Research Analyst

That's really great. And then just one last one for me. Just wondering if you can provide a little more color around potential M&A in the space. And do you think there will be any consolidation from large players with the tuck-ins that you're looking at, how valuation -- all that good stuff.

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

Valuations are high, thank you, and so it makes sort of larger acquisitions for us difficult. I mean, while we have a very strong balance sheet, it's not strong enough to do very, very large acquisitions. We do see continued consolidations in the industry, though, nonetheless. We see people sort of rightsizing their portfolios. There's some very, very big players. So we anticipate, as things go forward, they might decide to concentrate on one aspect of the business and divest other aspects. And this business is the same before. We -- internationally, we might be seeing more opportunities with some very, very small players there sort of feeling the heat of larger companies come in and looking to possibly sell. So it's all those things that we're looking at. I mean, there are a lot of deals in the market, and we constantly look. So that drives our optimism about acquisitions.

Operator

Our next question comes from the line of David Risinger with Morgan Stanley.

David Reed Risinger - Morgan Stanley, Research Division - MD in Equity Research and United States Pharmaceuticals Analyst

I have, I guess, a couple of questions. First, with respect to vaccines, Jack, maybe you can speak to how you see the underlying growth rate. Obviously, it was abnormally depressed at about 8% this quarter, but it would be helpful to understand how you see the underlying growth trend. And then my second product-related question is, could you just talk about how you see consumer preferences continuing to impact MFAs long term? I just don't know how to gauge how depressing the organic trend will be and how much it will constrain MFAs longer term. And then 2 quick questions. Well, actually, I'll pause there. I've got a couple of quick financial questions for Dick as well.

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

You don't want Dick to answer these questions? Anyway, Dave, I think, first of all, we have -- our business has been -- vaccines grew up double digits. And I think the last quarter is just a question of timing of shipment. So I wouldn't read anything more into that. What we're seeing again, in the U.S., with the movement away from how we raised birds historically -- you and I have spoken about this quite often. It's nice to have a regulation. It's nice to have consumer preferences. Someone will have to tell that to the animals, the viruses, the bacteria. At the end, the disease pressures remain. Now clearly, people prefer if you can come up with a vaccine, which, literally, will help make the animals stronger, prevent diseases. That is a preference. You got to balance that with cost. You have to balance that with some of the side effects. But we have seen -- because of that, people looking -- in the U.S. and where we are, we're both in the poultry and the swine business here. One, we are increasing our sales and penetration of certain poultry vaccines. And we're seeing customers who, historically, have not looked beginning to look. We're a very small player. Obviously, it's a big potential. On the swine side, the vaccines we sell are autogenous. So basically, we go out to the farms, we pick up the viruses, we take them back to the lab and we make, effectively, a custom vaccine. This is -- this will never be the largest part of the business because it's not one size fitting all. It's more bespoke. Then it's going to be -- I wouldn't see it as -- find a good example -- but just, Amazon. But what we do is that the vaccines, because they -- looking at the viruses on the farms, yes, they're more expensive, but they also work effectively against the viruses that are on those farms. So we are continuing to see, in the changing environment, that's quite effective, and we continue to see growth in that business. So that's our approach in the U.S. Our poultry vaccine business out of Israel are more general vaccines. And we sort of follow diseases around, and we see a continued growth in that business. And as I said, the Far East is a big opportunity there. The organic pressure, I think, is a slow growth. I mean, it's easy to put organic or any kind of label or no label on a bottle, on a package. It's hard to raise animals, and it's quite expensive. So yes, in the U.S., yes, we'll see a growth. But still, the amount of truly organic poultry in the United States, our estimate, is less than 3%, 4%. The amount of animals -- poultry that's raised with reduced level of antibiotics is quite high. That could be 60%. In that environment, we do quite well, all right? Because it's a combination of MFAs. Yes, we'll see a decline. But we'll also an increase in the nutritional specialties as well as vaccines. So it's -- the business we're in, if we need -- we want to see lots of animals being raised with our products, we continue to be -- and that's the goal of our business over the next 5 years or longer, to be totally agnostic of what the animal will use or what the grower will use with our products to raise those animals. As long as they're raising those animals and we have a product available that will let them have, in case of birds or pigs or cattle or dairy, that they'll have a healthy animal that will produce to its maximum ability, whether it's weight gain, product quality, milk production, we won't care -- we don't care. That's how we're driving our business. So while we're in this, every month, every quarter, category of MFA, nutritional specialty, vaccines, believe me, if it wasn't for the account, I'd love to get away from that. Because we like to look at our business as an Animal Health business and not really care what the -- what people are buying. We still report that way. But over time, it will become less important to us and hopefully, to you.

David Reed Risinger - Morgan Stanley, Research Division - MD in Equity Research and United States Pharmaceuticals Analyst Okay,

that's extremely helpful. Can you still hear me?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President Sure, yes.

David Reed Risinger - Morgan Stanley, Research Division - MD in Equity Research and United States Pharmaceuticals Analyst

Great. So Dick, with respect to cash flow from operations, it was quite strong in '17. It seemed to benefit a little bit from investments in inventory moderating and a swing in accrued expenses. So could you just discuss that? Talk about the outlook for cash flow from operations in 2018. And then my final question is just how should we think about the tax rate longer term?

Richard Johnson - Phibro Animal Health Corporation - CFO

Yes. So cash flow, I would say, we've said we expect positive cash flow in 2018. In the working capital component specifically, I think we will see some cash being used by working capital. As we grow sales, we're going to need to grow accounts receivable. We may need to grow inventories. Slightly, we'll get a little offset on the liability side of the balance sheet. The -- part of the performance in 2017 was bringing inventories back in the line after putting a lot of cash into inventory the prior year. So I think we'll see good control over working capital in 2018, but we'll see some cash going into working capital. On the longer term, effective tax rate, our 2018 guidance is an adjusted effective tax rate of about 30.5%. Over time, I would see that staying fairly stable, perhaps ticking up slightly. It'll depend on the mix of our profitability and basically, in the U.S. versus international locations. But I don't -- barring whatever, if any, effect of tax reform, but given status quo tax laws, I think we're in that low 30% range going forward.

Operator

Our next question comes from Erin Wright with Crédit Suisse.

Erin Elizabeth Wilson Wright - Crédit Suisse AG, Research Division - Director & Senior Equity Research Analyst

Can you speak to the U.S. dairy market trends and how that's impacting the overall sales of OmniGen? And have you historically -- I guess you've historically mentioned some market share for OmniGen and OmniGen in terms of, I guess, utilization across dairy cows. Where does that utilization, I guess, stand now? And can you comment on the competitive landscape across nutritional specialty?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

Thanks, Erin. So as we're seeing out there and what we're hearing as well, the dairy business is in somewhat a recovery. It's coming off a pretty bad couple of years. It hasn't returned across the board to the profitable business it was 2, 3 years ago. But it's starting -- our customers are starting to make more money. And as such, we're starting to see after sort of a leveling out or maybe a slight decline in the U.S. in the use of OmniGen, we're starting to see growth again in OmniGen, Animate and the other products we're selling to the dairy industry. Plus, our penetration around the world is starting to increase. We made efforts over the last bunch of years to enter into Europe, and that's growing month-to-month, quarter-to-quarter. And we even began and started making sales in China, which is something, again, I think we started speaking about over 2 years ago. So all that's happening in a positive way. With the ability to -- even a shift in the marketplace -- we assumed our market share. Basically, our headcount is about the same, maybe slightly above. It's sort of hard to keep track of that. We had some numbers in the past, but we assume that our market share still to be about in the low 20s percent of the market. But we're optimistic that we will continue to grow as our customers make money. Our products really help them make more money. So -- and they recognize it, so we're quite optimistic about that product line.

Erin Elizabeth Wilson Wright - Crédit Suisse AG, Research Division - Director & Senior Equity Research Analyst

Great. And you mentioned incremental cost associated with the product development initiatives. I guess what initiatives are currently in place? And what new initiatives are you implementing in 2018? And how should we think about the quarterly progression, I guess, of those efforts and associated expenses?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

So we had discussions here sort of like yesterday. It's how you look at a business. Basically, I mean, I view the business in terms of the steps, right? You build, and then you get the next rise, and you build and arise. And when you do that, it's great to graph. So you graph. It always looks like it's increasing day-to-day, week-to-week, month-to-month. I mean, that's literally how analysts look at a business. But we're in a -- we're right now in the sort of the first part of building that step before we get to the riser. And we're doing it by adding product development people, we're adding research people, we're putting more animals on our farm, we're looking at new species, we're looking at geographic growth. We're doing all of that. And we're doing that partly because we know there's a big market out there and a changing market. Hard to say right now which of those efforts is gonna produce the riser or the step sooner than another one, so we're doing all of that. So we're spending money. So we -- it limits our EBITDA growth. It sort of makes the curve -- we're still on a rising curve, but I think we've tempered the curve. But we're doing that because we see amazing amount of opportunities out there. Again, geographic species, product changes, et cetera, et cetera. So -- and that's how we want to run our business, which is -- and it's our plan to run the business.

Richard Johnson - Phibro Animal Health Corporation - CFO

And I -- it's implied, but most of our investment -- maybe all of our investment is really behind the faster-growing product categories that we've been talking about. So nutritional specialties, whether it's taking an existing product and expanding it to a new species or a new geography or developing, which is largely in-licensing efforts, developing additional nutritional specialty products. And on the vaccine side, it's somewhat the same thing. It's expanding our portfolio to take on more diseases, to upgrade to the latest version of a disease so that we have the most effective product on the market and can gain market share that way.

Operator

Our next question comes from the line of Derik De Bruin with Bank of America Merrill Lynch.

Michael Leonidovich Ryskin - BofA Merrill Lynch, Research Division - Associate

It's actually Mike Ryskin on for Derik. I had a couple quick questions. A lot's already been covered. But in the -- on the Animal Health side, this quarter, you posted some really strong numbers in MFAs from outside the U.S., a growth of $5.2 million if I'm not mistaken. Can you talk a little bit about what you saw there, particularly in APAC, this is the big number going off that base, and what your expectations are for 2018 OUS, particularly in that segment?

Richard Johnson - Phibro Animal Health Corporation - CFO

Yes. So I would -- again, in some markets, our customer purchases and therefore, our revenues can be a little bit lumpy just depending on timing of customer orders. So be a little bit cautious with reading too much into 1 quarter in one smaller part of the world. But in the broader sense, we continue to be optimistic and to expect growth in international markets of MFAs. There's no question. So -- and it's mostly the markets we're in today. So we're in -- we're pretty much throughout Latin America, Brazil, Mexico, other major countries. We're in various countries in Asia, China, down through the Southeast Asia countries, Australia, New Zealand, et cetera. So tempered by what Jack said earlier, which is the world pays attention to what's going on in the United States as far as antibiotics and pressure on antibiotics. But you have to, at the same time, balance that with the desire for and the need for healthy, affordable, good-quality food. And that's what we're seeing out there.

Michael Leonidovich Ryskin - BofA Merrill Lynch, Research Division - Associate

All right. And then one other point. You saw a very nice bump up in gross margins this quarter, over 100 bps when you adjust the gross margin. You attributed that to some favorable mix, but also to some operational improvements. How do you see the runway there going into 2018 and beyond, both with mix just continuing to move around your portfolio as you discuss the change in MFAs, but also with the steps you're taking operationally?

Richard Johnson - Phibro Animal Health Corporation - CFO

Yes. I think most of -- in 2018, I think most of our gross profit improvement is going to come from mix and driving favorable product mix. We'll continue to get some cost efficiencies -- manufacturing cost efficiencies. It will be the smaller part of the equation in 2018.

Operator

(Operator Instructions) Our next question comes from the line of Kevin Kedra with Gabelli.

Kevin Kedra - G. Research, LLC - Research Analyst

Most of mine have been asked and answered, so I just wanted to ask about Mineral Nutrition. You saw a pretty good bump up not just for the quarter but for the year on the EBITDA margins there, I think around 8%. How should we be thinking about the margins for that business going forward? Do you have a lot more room for leverage there? Or are we getting near the top for the margins on that business?

Richard Johnson - Phibro Animal Health Corporation - CFO

Yes. I think we've got more room for -- this is going to be kind of an arithmetic answer. We've got a lot more room for profit growth. The margins are -- could move around depending on commodity pricing. So if commodity prices take off, we may actually see the percentage margin dip. But what our -- what we watch in the minerals business and what we expect long term is that we're going to be able to drive continued growth in the bottom line.

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

Yes. So I think the math answer -- I mean, what Dick has said, [wouldn't exactly] outweigh anything we try to do. But we concentrate on what we can control, right? We can't control the prices of zinc and copper and manganese, et cetera, et cetera, et cetera. But what we try to control is our product mix, is our concentration on our customer mix. And to that end, obviously, we're driving to try to increase our margins to put our specialty products where we'll be less -- those products are less affected by commodity moves. But overall, in that business, if zinc goes up $100 a ton, it's going to have a lot bigger effect on the dollars than on anything else we can do.

Richard Johnson - Phibro Animal Health Corporation - CFO

I just would repeat, we are fundamentally not exposed to commodity prices. This is a transparent pass-through business. And so when the price of copper goes up or goes down, our prices to our cost of goods and our prices to our customer goes down very quickly, very proportionately. So this is -- some people are concerned that we're exposed to commodity fluctuations, and that's not the nature of our minerals business.

Operator

We have a follow-up question from the line of Erin Wright from Crédit Suisse.

Erin Elizabeth Wilson Wright - Crédit Suisse AG, Research Division - Director & Senior Equity Research Analyst

Great, just 2 quick follow-ups. Can you give an update on aquaculture, the initiatives there? How big of an opportunity that could be as a faster-growing species segment? And then also, any sort of incremental efforts to deemphasize the Performance Products business at all?

Jack Bendheim - Phibro Animal Health Corporation - Chairman, CEO and President

So on the Performance Products side, we -- as we said in the past, we always look -- we are looking to deemphasize that business. We saw some increases in this last quarter, but we look for opportunities to get out a piece of that business. That business is made up of a lot of smaller pieces. And we keep our antenna out enough to see for ways to step away from some of those businesses. So that's an ongoing effort. On the aquaculture side, we continue stepping forward. This is a business that literally is a relative -- compared to all the other parts of the animal production, Animal Health business, it's a relatively new business, which means that products -- there are a few products out there that are registered, but most of these products are not. So we have to go through a long registration step. Years of products have been on the market maybe 30, 40 years in other species. But because this is a new species and because the government only grows, there are more hoops and more steps and more people to see. So we are making progress in the key markets registering products, and we are investing in putting people on the ground and starting the sales. But it hardly appears in our sales mix right now, but this is something that, over the next -- over the future -- near future, we will see growth over time.

Operator

I'm showing no further questions at this time. I'd like to turn the call back to Mr. Johnson for any closing remarks.

Richard Johnson - Phibro Animal Health Corporation - CFO

Well, thanks, everyone, again, for your time and listening in on the call this morning, and we'll talk to you again when we release our September quarter numbers. So until then, take care. Bye, everybody.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes the program, and you may now disconnect. Everyone, have a great day.