

Flash Commentary: Antibiotics and Animal Health

Recent Data Points Highlight an Accelerating Move



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- **US markets moving away from antibiotics; our thesis remains intact.** In our October 5, 2015, report [Antibiotics and Animal Health: Value-Chain Implications in the US](#), we posited that consumer demand could push food supply chain companies to phase out antibiotics beyond the level required by FDA guidelines. We are seeing this play out as a growing number of producers, restaurants, and supermarkets announce antibiotic policies that are more restrictive than US regulatory guidelines. We believe these actions are accelerating the move away from antibiotics in US markets.
- **Weak US antibiotic sales evident in Phibro's earnings.** We previously highlighted stand-alone animal health company Phibro Animal Health as a gauge for how this theme is progressing. In its most recent quarter (fiscal 4Q16), Phibro reported that sales of medicated feed additives (MFAs—which contain antibiotics) increased 3%. The increase came after reporting declines in three of the last four quarters. If not for modest growth in the international market, the declines in the US market would be more readily observed. The company also expects MFAs to see a stable to single-digit decline in 2017 versus the prior year. In contrast, Phibro highlighted continued double-digit growth for nutritional specialties and vaccine products that we previously identified as antibiotic alternatives.
- **Sanderson Farms' antibiotic policy pushes back on consumer and industry trends.** In assessing poultry producers' antibiotics use policies, we highlighted Perdue Farms (private company) as a leading performer and Sanderson as lagging. Sanderson does not believe the antibiotic-free (ABF) movement is grounded in proper science and ethics, and believes competitors' efforts are a marketing gimmick aimed at charging higher prices. To this end, the company designed a marketing campaign against ABF chicken at a cost of \$2.5 million per month through at least the end of 2016. While Sanderson's view about strict ABF policies compromising animal welfare is worthy of examination, we question the company's strategy to combat shifting consumer demand. We believe CEO Joe Sanderson is also hedging his bet by suggesting that the company could transition away from antibiotics quickly. It took Perdue roughly a decade to transition about half of its chickens to "no antibiotics ever," so we believe Sanderson's view is overly optimistic.

- **Growth opportunities in nutritional feed additives and vaccines.** Recent company announcements reinforce our view that specialty and nutritional feed additives as well as vaccines have significant potential for growth. Pilgrim’s Pride said that it is working closely with a large agri-bio firm to develop customized probiotics for its chickens. Citing the promising long term outlook for animal health probiotics, Chr Hansen will continue to expand its presence in this area despite near-term headwinds related to the depressed agricultural sector. In July 2016, Evonik acquired the probiotics business of private Spanish feed ingredients company Norel. Evonik believes probiotics will be critical components of a line-up of possible antibiotic alternatives. As aforementioned, Phibro believes it is well positioned to benefit from adding vaccines and nutritional specialties to its product portfolio, and expects continued double-digit growth for these product lines.
- **Lastly, on September 21, the United Nations confirmed its Global Action Plan on Antimicrobial Resistance.** This is only the fourth time a health issue has been taken up by the UN General Assembly (the others were HIV, non-communicable diseases, such as strokes and heart attacks caused by obesity or smoking, and Ebola). The Plan cites the need for ‘effective and enforceable regulation...for antimicrobial medicines in human and animal health.’ We see this Action Plan as a potential catalyst for antibiotic regulation in other major meat-producing companies, and are watching key markets (Brazil, China, and Australia) closely. 🇺🇸

Stock prices as of September 23 close:

Chr Hansen	CHR	\$69.46
Evonik	EVK-GR	€30.39
Phibro Animal Health	PAHC	\$27.22
Pilgrim’s Pride	PPC	\$20.96
Sanderson Farms	SAFM	\$94.98



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