

Flour Mills of Nig. Plc

Nigeria | Equities | Consumer Goods | February 2, 2022

PAC RESEARCH

Three Business Segments Record Over 50% Revenue Growth in Third Quarter of 2021/22

INVESTMENT SUMMARY

Flour Mills of Nigeria (FMN) reported another impressive financial results in nine-month to December 2021/22 as revenue grew significantly by 48.55% to ₦824.98 billion (vs. ₦555.34 billion in nine-month to December 2020/21), driven mainly by the strong volume growth across the board. Specifically, Food segment, Agro-allied segment and Support segment recorded over 50% growth in revenue during the period. This showed that FMN remains a market leader in Flour and Pasta manufacturing in Nigeria. However, the improved production volumes and higher input costs (domestic and imported inputs) resulted in higher cost of sales as it increased significantly by 54.23% to ₦744.76 billion in 9M'21/22 (vs. ₦482.90 billion in 9M'20/21). In addition, the administrative, selling and distribution expenses rose by 24.13% to ₦31.16 billion in 9M'21/22 (vs. ₦25.11 billion reported in 9M'20/21), driven by higher expenses on advertisement, sales and increased salaries & related staff costs, among others. Notwithstanding the higher operating expenses, the EBITDA of the company rose by 9.47% to ₦58.57 billion in 9M'21/22 (vs. ₦53.50 billion in 9M'20/21).

As a result of higher borrowings and lower finance income during the period, the net finance cost of the company grew by 30.92% to ₦15.19 billion in 9M'21/22, (vs. ₦9.13 billion in 9M'20/21). Despite the setback recorded in non-operating activities, the profit before tax grew by 6.97% to ₦25.26 billion in 9M'21/22 (vs. ₦23.61 billion in 9M'20/21). The company made a provision of ₦8.21 billion for tax in 9M'21/22 (vs. ₦8.03 billion in 9M'20/21). Consequently, profit after tax grew by 9.40% to ₦17.05 billion (vs. ₦15.58 billion in 9M'20/21) and this resulted in a 12-month trailing Earnings Per Share (EPS) of ₦6.63 in 9M'21/22. Based on the recent figures released, we hereby upgrade our target price slightly to ₦36.31 (Previous TP: ₦36.26) and maintain a **BUY** recommendation.

Fig. 1: Quarterly results highlights

	3Q2022	2Q2022	3Q2021	Q/q Δ	Y/y Δ
Revenue (₦mn)	302,159	289,118	200,530	+4.51%	+50.68%
Operating profit (₦mn)	16,389	12,540	11,478	+30.69%	+42.79%
Net profit (₦mn)	6,517	5,082	5,649	+28.24%	+15.37%

Source: FMN, PAC Research

February 2, 2022

Oluwole Adeyeye

oluwole.adeyeye@panafricancapitalholdings.com

Price:

- Current	₦28.85
- Target	₦36.31

Recommendation: **BUY**

* As at Tuesday February 1, 2022

Fig. 2: Stock data

FYE	March
Price Mov't: YtD / 52wk	+1.76%/-14.14%
52-week range	₦34.70 - ₦27.00
30-day Average vol.	527,211
Shares Outstanding (mn)	4,100.38
Market Cap. (₦bn)	118.30
EPS, ₦- 12months trailing	6.63
DPS, ₦- FY2021	1.65

Source: NGX, Company's Annual Reports, PAC Research

Fig. 3: Key ratios

	9M'22	9M'21
Gross profit margin	9.72%	13.05%
COS/Revenue	90.28%	86.95%
Net Profit Margin	2.07%	2.81%
Asset turnover	1.17	1.13

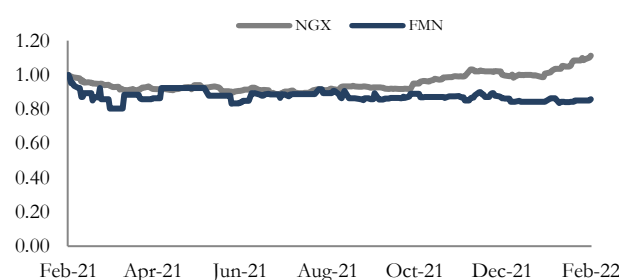
Source: NGX, PAC Research

Fig. 4: Valuations

	FY2020	FY2021	FY2022F	FY2023F
P/E(x)	10.40	4.60	4.17	3.22
P/B(x)	0.76	0.68	0.62	0.56
Div. Yield	4.85%	5.72%	5.72%	8.32%
Payout Ratio	50.46%	26.31%	23.85%	26.79%
Ev/Revenue	3.33	2.67	2.33	2.12
Rev Per Shr.	139.93	188.18	269.10	296.01
ROE	7.30%	14.73%	14.85%	17.48%
ROA	2.63%	4.72%	4.07%	4.79%

Source: NGX, PAC Research

Fig. 5: FMN vs NGX, 52-wk Movement (Rebased)



Source: Bloomberg, PAC Research

Revenue grows by 48.55% year-on-year, driven by strong volume growth: All the business segments of FMN witnessed various level of growth in nine-month to December 2021/22 due to improved demand during the period. The overall revenue of the company grew by 48.55% to ₦824.98 billion in 9M'21/22 (vs ₦555.34 billion reported in 9M'20/21). Precisely, revenue from the Food Segment, which contributed about 65% to the total revenue of the company, rose significantly by 55% to ₦534.5 billion in 9M'21/22 (vs ₦343.9 billion in 9M'20/21), driven by 24%, 8%, 7% and 3% growth in Flour, Noodles, Ball Foods and Pasta respectively. The Food segment also witnessed significant volume growth in Golden Vita, Amazing Day and Goat Meat Pepper Soup during the period. In addition, revenue from Agro-Allied business segment improved by 49% to ₦157.1 billion in 9M'21/22 (vs. ₦105.6 billion in 9M'20/21), driven by 48% revenue growth in the Oil and Fats value chain and 21% volume growth in fertilizers. The higher local demand, improvement in export operations and market penetration in the northern part of the country contributed to growth in Agro-Allied Segment.

Although the revenue from the Support Segment of the company is the least contributor to the overall revenue of the company, the segment grew faster than all the other segment during the period. Revenue from Support segment grew by 62% to ₦25.4 billion in 9M'21/22 (vs. ₦15.6 billion in 9M'20/21), driven mainly by increased demand in Bagco.

Mainly as a result of improved demand for Brown Sugar during the period, especially from industrial customers and northern part of the country, revenue from the Sugar business segment of FMN increased by 20% to ₦108.0 billion in 9M'21/22 (vs. ₦90.2 billion in 9M'20/21).

We maintained that the acquisition of about 72% majority shareholding in Honeywell Flour Mills Plc (HFMP), the installation of an additional noodles line, training of over 1,486 farmers, commencement of cassava production, among other, are expected to improve the company's revenue in the coming quarters.

...the acquisition of about 72% majority shareholding in Honeywell Flour Mills Plc (HFMP), the installation of an additional noodles line, training of over 1,486 farmers... are expected to improve the company's revenue in the coming quarters

Fig. 6: Revenue – 9M'21 – 12M'24F (Billion NGN)

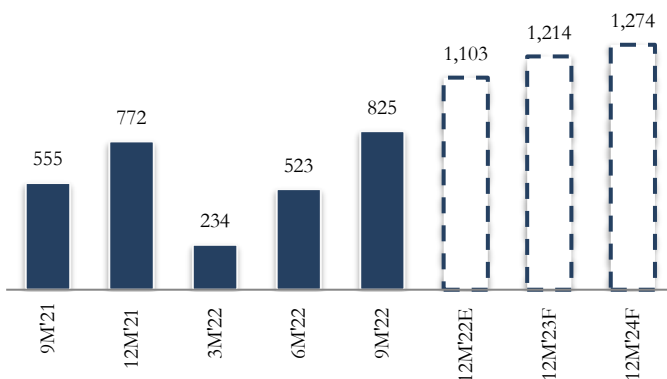
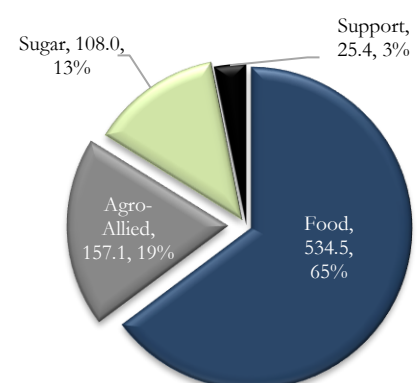


Fig. 7: Distribution of Revenue by Segments (Billion NGN) – 9M'21



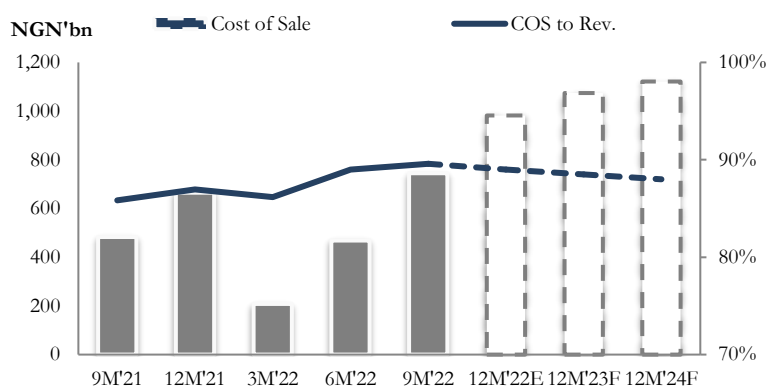
Source: NGX, FMN, PAC Research

higher production volumes and higher input costs results in 54.23% rise in cost of sales: Nine-month to December 2021/22 witnessed significant rise in demand and input costs, which raised the cost of sales of FMN during the period. The cost of sales accelerated by 54.23% to ₦744.76 billion in 9M'21/22, from ₦482.90 billion recorded in 9M'20/21. Specifically, the material costs, which constituted about 90% of the total cost of sales, increased by 58.11% to ₦673.26 billion in 9M'21/22 (9M'20/21: ₦425.82 billion), driven mainly by higher production volume and input costs. The higher cost of inputs reflected on the cost-to-sale margin which increased to 90.28% in 9M'21/22 from 86.95% in 9M'20/21, and this remains a major threat to the profitability of the company. We anticipate that the adoption of backward integration by FMN will address the high input costs in the coming quarters.

...the adoption of backward integration by FMN will address the high input costs in the coming quarters

In line with our projection, the administrative, selling and distribution expenses of the company increased by 24.13% to ₦31.16 billion in 9M'21/22 (vs. ₦25.11 billion reported in 9M'20/21), driven by higher expenses on advertisement, sales, salaries, wages and other staff costs, among others. With the expectation of improved production volumes and high inflation rate in the country, we may continue to see higher figure for selling, distribution, and administration expenses in the coming quarters.

Fig. 8: Cost of Sale and COS to Revenue – 9M'21 – 12M'24F



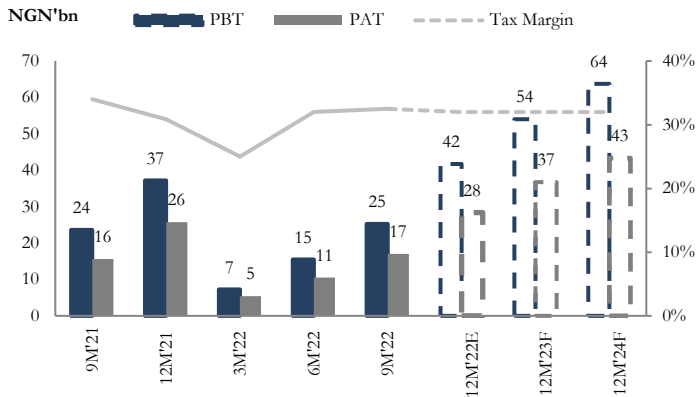
Source: NGX, PAC Research

PBT improves by 6.97% year-on-year, despite the setback recorded in the non-operating activities: Although, FMN reported improved operating performance during the period, there was a setback in non-operating activities of the company, especially from both finance cost & investment income. The net finance costs of the company declined by 30.92% to ₦15.19 billion in 9M'21/22 (vs. ₦11.60 billion in 9M'20/21), mainly driven by higher loans and borrowings during the period.

Notwithstanding the setback recorded in non-operating activities during the period, the profit before tax improved by 6.97% to ₦25.26 billion in 9M'21/22 (vs. ₦23.61 billion in 9M'20/21).

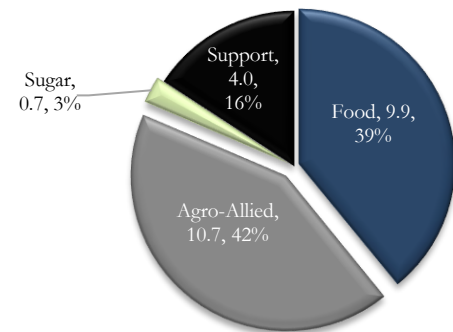
The company made a provision of ₦8.21 billion for tax in nine-month to December 2021/22 (vs. ₦8.03 billion in nine-month to December 2020/21). Consequently, profit after tax improved by 9.40% to ₦17.05 billion in 9M'21/22 (vs. ₦15.58 billion reported in 9M'20/21) and this translated to a 12-month trailing Earnings Per Share (EPS) of ₦6.63 in 9M'21/22

Fig. 9: PBT, PAT and Tax Margin – 9M'21 - 12M'24F



Source: NGX, FMN, PAC Research

Fig. 10: Distribution of PBT (Billion NGN) – 9M'21



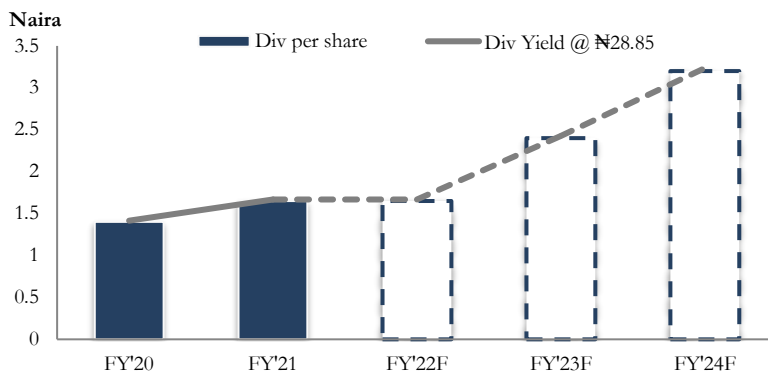
Robust balance sheet signals dividend payment in FY'21/22: Flour Mills of Nigeria continued with a robust balance sheet in the third quarter of 2021/22 as the total assets of the company improved by 42.53% to ₦702.91 billion (vs. ₦493.16 billion in the third quarter of 2020/21), as a result of improvement in both the current and non-current assets. The current assets of the company improved by 75.84% to ₦449.69 billion in Q3'21/22 (vs. ₦255.73 billion in Q3'20/21), driven by 128% increase in inventory and 229% increase in prepayment & deposit for import during the period. In addition, the total non-current assets of the company improved by 6.65% to ₦253.22 billion in Q3'21/22 (vs. ₦237.43 billion in Q3'20/21), mainly as a result of higher deferred tax assets during the period.

However, the total liabilities of the company grew by 58.15% to ₦517.94 billion in Q3'21/22 (vs. ₦327.50 billion in Q3'20/21), due to 93% increase in trade & other payables, 25% rise in total borrowings, 34% increase in lease liabilities, among others. Impressively, the improvement in the total assets outweighed the increase in the total liabilities of the company during the period. As a result, the net assets improved by 11.66% to ₦184.97 billion in Q3'21/22 (vs. ₦165.66 billion in Q3'20/21), which translated to a net assets per share (NAPS) of ₦45.11 (Q3'20/21: ₦40.40).

We may not see positive growth in dividend payment in FY'21/22 as we expect the acquisition of 71.69% majority shareholding in Honeywell Flour Mills Plc (HFMP) to have impact on the balance sheet of the company.

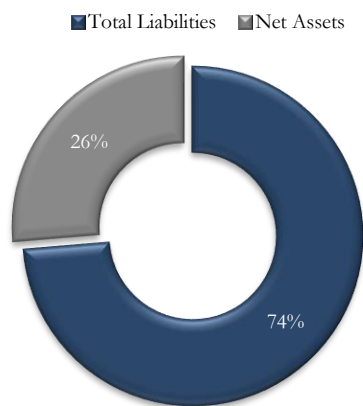
We may not see positive growth in dividend payment in FY'21/22 as we expect the acquisition of 71.69% majority shareholding in Honeywell Flour Mills Plc (HFMP) to have impact on the balance sheet of the company.

Fig. 11: Dividend Per Share and Dividend Yield – FY'20-FY'24F



Source: NGX, PAC Research

Fig. 12: Total Liabilities Vs Net Asset in Q3'21/22



Source: NGX, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦36.31, representing an increase of 25.86% from the current market price of ₦28.85. In arriving at the target price, we employed dividend discount valuation methodology. Consequently, we maintained a **BUY** recommendation on the stock of the company. Our valuation and forecasts considered several factors (both quantitative and qualitative) among which are: the previous financial reports of the company, the current figures released by the company, acquisition of 71.69% majority shareholding in Honeywell Flour Mills Plc (HFMP) and the outlook from the management.

Our valuation puts the target price of the stock at ₦36.31, representing an increase of 25.86% from the current market price of ₦28.85.

Fig. 13: Share Price History (Naira)



Source: Bloomberg, PAC Research

Fig. 14: Statement of Profit or Loss, N'mn

	2020	2021	2022E	2023F
Revenue	573,774	771,608	1,103,399	1,213,735
<i>Change</i>		<i>34.48%</i>	<i>43.00%</i>	<i>10.00%</i>
Cost of sales	-507,987	-664,851	-982,025	-1,074,15
<i>Change</i>		<i>30.88%</i>	<i>47.71%</i>	<i>9.38%</i>
Gross profit	65,787	106,757	121,374	139,580
<i>Change</i>		<i>62.28%</i>	<i>13.69%</i>	<i>15.00%</i>
Selling and distr exp.	-9,278	-12,080	-16,551	-17,599
<i>Change</i>		<i>30.19%</i>	<i>37.02%</i>	<i>6.33%</i>
Administrative exp.	-23,346	-29,046	-33,102	-36,412
<i>Change</i>		<i>24.41%</i>	<i>13.96%</i>	<i>10.00%</i>
Net Op. gains (losses)	4,906	-15,528	-9,931	-16,992
<i>Change</i>		<i>-416.54%</i>	<i>-36.05%</i>	<i>71.11%</i>
Operating profit	35,080	52,197	61,239	71,853
<i>Change</i>		<i>48.79%</i>	<i>17.32%</i>	<i>17.33%</i>
investment income	2,393	3,652	1,434	5,219
<i>Change</i>		<i>52.64%</i>	<i>-60.72%</i>	<i>263.85%</i>
Profit Before Tax	17,497	37,194	41,708	54,011
<i>Change</i>		<i>112.57%</i>	<i>12.14%</i>	<i>29.50%</i>
Taxation	-6,120	-11,477	-13,347	-17,284
<i>Change</i>		<i>87.53%</i>	<i>16.29%</i>	<i>29.50%</i>
Profit After Tax	11,377	25,717	28,362	36,728
<i>Change</i>		<i>126.05%</i>	<i>10.28%</i>	<i>29.50%</i>

Fig. 15: Statement of Financial Position, N'mn

	2020	2021	2022E	2023F
Property plant and equip.	216,890	208,721	220,680	242,748
Investment property	1,633	1,533	1,986	2,185
Goodwill	4,148	4,148	5,738	6,311
Deferred tax	3,578	6,974	7,503	8,253
Long term receivables	359	39	331	364
Inventories	115,596	195,449	275,850	303,435
Biological assets	148	376	1,655	1,821
Trade and other rec.	25,731	25,826	25,378	27,916
Total Assets	432,454	544,732	696,501	766,149
Bank overdraft	5,543	4,001	47,446	52,191
Trade & other payables	83,614	120,152	172,130	189,343
Borrowings	23,344	26,913	27,585	30,343
Retirement benefit oblig.	7,135	10,397	15,448	16,992
Long service award	2,738	3,713	3,972	4,369
deferred tax	11,849	16,857	21,516	23,668
Total liabilities	276,646	370,119	505,500	556,050
Net Assets	155,808	174,613	191,001	210,098

Fig. 16: Profitability Ratio

	2020	2021	2022E	2023F
Gross profit margin	11.47%	13.84%	11.00%	11.50%
Net Profit Margin	1.98%	3.33%	2.57%	3.03%
operating profit margin	6.11%	6.76%	0.00%	0.00%
Return on Equity	7.30%	14.73%	14.85%	17.48%
Return on Assets	2.63%	4.72%	4.07%	4.79%
ROCE	0.84%	1.09%	0.37%	1.22%

Fig. 17: Asset Utilisation

	2020	2021	2022E	2023F
cash/sales	0.03	0.06	0.07	0.07
Sales to inventory (x)	4.96	3.95	4.00	4.00
Sales to total assets (x)	1.33	1.42	1.58	1.58
sales/EBITDA	9.73	9.83	12.12	11.60
Sales to total fixed assets	2.65	3.70	5.00	5.00
Equity multiplier	2.78	3.12	3.65	3.65

Fig. 18: Liquidity Ratios

	2020	2021	2022E	2023F
Quick ratio	0.50	0.53	0.53	0.53
Current ratio	1.28	1.46	1.42	1.42
Cash ratio	0.12	0.22	0.26	0.26
Interest Coverage	0.88	1.99	1.99	2.34
Operating Cash Flow Ratio	0.00	0.00	0.00	0.00
Debt/net income	7.58	4.11	5.95	5.06
Debt/operating profit	36.03	28.96	117.69	35.58
Debt to asset	0.20	0.19	0.24	0.24
Debt to equity	0.55	0.61	0.88	0.88
Total liabilities/equity	1.78	2.12	2.65	2.65
Inventory turnover days	83.06	107.30	102.53	103.11
Account receivable days	16.37	12.22	8.40	0.55
Account payable days	60.08	65.96	63.98	64.34

Fig. 19: Shareholders' Investment Ratios

	2020	2021	2022E	2023F
Earnings per share	2.77	6.27	6.92	8.96
DiV per share	1.40	1.65	1.65	2.40
NAVPS	38.00	42.58	46.58	51.24
Earnings yield	9.62%	21.74%	23.98%	31.05%
P/S ratio	0.206	0.153	0.107	0.097

Source: Company's Annual Reports, PAC Research

Equity research methodology employed in this report

Views documented in this equity research report stem from conclusions reached through the use of multiple valuation methodologies, industry-wide knowledge, company specific information and our near to medium term expectations of industry and company performance, as well as market outlook. Our forecasts are based on a combination of top down and bottom up analysis, alongside historical trends in industry and company financials. Where appropriate, we factored in available forecasts and business direction provided by company management.

Our recommendation tends towards value investing. Therefore, our investment rank gauge—a customized scale we use to judge how well a firm under coverage has performed—is determined using major value parameters as well as relevant ratios and multiples computed with figures from the company’s most recent financials.

The variables used to arrive at the company’s investment rank cover a wide range of measures which characterize liquidity, operational efficiency, profitability, profit margins, growth, economic viability, gearing, relative valuation ratios, capital structure and management performance. Our investment recommendation is underpinned by the upside or downside potential of a stock under coverage. This potential is estimated by comparing the stock’s current market price to its price target and fair value, on a percentage increase or decrease basis as summarized below:

Deviation from current price	Recommendation
>30%	STRONG BUY
10% to < 30%	BUY
-10% to < 10%	HOLD
<-10%	SELL

IMPORTANT DISCLOSURES

This research report has been prepared by the analyst(s), whose name(s) appear on the front page of this document, to provide background information about the issues which are the subject matter of this report. It is given for information purposes only.

Each analyst hereby certifies that with respect to the issues discussed herein, all the views expressed in this document are his or her own and reflect his or her personal views about any and all of such matters. These views are not necessarily held or shared by PanAfrican Capital Holdings or any of its affiliate companies. The analyst(s) views herein are expressed in good faith and every effort has been made to base our opinion on reliable comprehensive information but no representation is made as to its accuracy or completeness. The opinions and information contained in this report are subject to change and neither the analysts nor PanAfrican Capital Holdings is under any obligation to notify you or make public any announcement with respect to such change.

This report is produced independently of PanAfrican Capital Holdings and the recommendations (if any), forecasts, opinions, estimates, expectations and views contained herein are entirely those of the analysts. While all reasonable care has been taken to ensure that the facts stated herein are accurate and that the recommendations, forecasts, opinions, estimates, expectations and views contained herein are fair and reasonable, none of the analysts, PanAfrican Capital Holding nor any of its directors, officers or employees has verified the contents hereof and accordingly, none of the analysts, PanAfrican Capital Holding nor any of its respective directors, officers or employees, shall be in any way responsible for the contents hereof.

With the exception of information regarding PanAfrican Capital Holdings, reports prepared by PanAfrican Capital Holdings analysts are based on public information. Facts and views presented in this report have not been reviewed and may not reflect information known to professionals on other PanAfrican Capital Holdings business areas including investment banking. This report does not provide individually tailored investment advice. Reports are prepared without regard to individual financial circumstances and objectives of persons who receive it. The securities discussed in this report may not be suitable for all investors. It is recommended that investors independently evaluate particular investments and strategies. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances or objectives. Neither the analyst(s), PanAfrican Capital Holdings, any of its respective directors, officers nor employees accepts any liability whatsoever for any loss so ever arising from any use of this report or its contents or otherwise arising in connection therewith. Each analyst and/or any person connected with any analyst may have acted upon or used the information herein contained, or the research or analysis on which it is based prior to its publication date. This document may not be relied upon by any of its recipients or any other person in making investment decisions.

Each research analyst certifies that no part of his or her compensation was, or will be directly or indirectly related to the specific recommendations (if any), opinions, forecasts, estimates or views in this report. Analysts' compensation is based upon activities and services intended to benefit clients of PanAfrican Capital Holdings. As with other employees of PanAfrican Capital Holdings, analysts' compensation is impacted by the overall profitability of PanAfrican Capital Holdings, which includes revenues from all business areas of PanAfrican Capital Holdings.

PanAfrican Capital Holdings Ltd

8A, Elsie Femi Pearse Street

Victoria Island

Lagos, Nigeria

Tel: +234 (1) 2716899, 2718630

www.panafricancapitalholdings.com