

Flour Mills of Nig. Plc

Nigeria | Equities | Consumer Goods | June 24, 2022

PAC RESEARCH

Solid Performance Across all the Business Segments as Revenue Grows by 51% in FY-2022

INVESTMENT SUMMARY

Flour Mills of Nigeria (FMN) remains the market leader in Flour and Pasta manufacturing in Nigeria as the company reported an outstanding revenue of ₦1.16 trillion in 2021/22, which is 50.83% higher than the revenue of ₦0.77 trillion recorded in 2020/21. The significant increase in the top-line is mainly attributed to the strong volume growth in all the business segments – Food Segment, Agro-Allied segment and Support segment recorded over 50% revenue growth each during the period. However, cost of sales accelerated by 58.79% to ₦1.06 trillion in FY'21/22 (vs. ₦0.66 trillion in FY'20/21), driven by improved production volumes, rising inflation and higher energy costs. The higher production volumes and rising inflation reflected in operating expenses as administrative, selling and distribution expenses increased by 4.21% to ₦42.86 billion in FY'21/22 (vs. ₦41.13 billion reported in FY'20/21). With the impressive operating performance, EBITDA improved by 11.66% to ₦87.61 billion in FY'21/22 (vs. ₦78.47 billion in FY'20/21).

To support and expand the operations during the period, the company increased the banks loans and overdraft by 81.67% to ₦17.96 billion in FY'21/22 (vs. ₦9.89 billion in FY'20/21). This resulted in higher net finance costs of ₦24.40 billion in FY'21/22, which is 62.60% higher than the ₦15.00 billion reported in FY'20/21. Despite the higher net finance costs, profit before tax rose by 10.55% to ₦41.12 billion in FY'21/22 (vs. ₦37.19 billion in FY'20/21). However, the company made higher provision of ₦13.10 billion for tax in FY'21/22 (vs. ₦11.48 billion in FY'20/21). Notwithstanding higher tax provision, net profit grew by 8.94% to ₦28.02 billion in FY'21/22 (vs. ₦25.72 billion in FY'20/21), translating to earnings per share of ₦6.26 (FY'20/21: ₦6.38). FMN recommended a dividend of ₦2.15 per share in FY'21/22 (FY'20/21: ₦1.65). Based on the figures released, we maintain a **BUY** rating on the stock at the current price of ₦32.75 as present forward estimate places the company's share price at ₦36.77 (Previous TP: ₦36.31).

Table 1: Quarterly results highlights

	4Q2022	3Q2022	4Q2021	Q/q Δ	Y/y Δ
Revenue (₦mn)	338,822	302,159	216,266	+12.13%	+56.67%
Operating profit (₦mn)	25,070	16,389	16,987	+52.97%	+47.58%
Net profit (₦mn)	10,970	6,517	10,135	+68.33%	+8.24%

Source: Bloomberg, PAC Research

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Price:

- Current	₦32.75
- Target	₦36.77
Recommendation:	BUY

* As at Thursday June 23, 2022

Table 2: Stock data

FYE	March
Price Mov't: YtD / 52wk	+15.52%/+9.90%
52-week range	₦41.45 - ₦27.50
30-day Average vol.	3,408,634
Shares Outstanding (mn)	4,100.38
Market Cap. (₦bn)	134.29
EPS, ₦- 12months trailing	6.26
DPS, ₦- FY2022	2.15

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

Tab 3: Key ratios

	FY'22	FY'21
Gross profit margin	9.29%	13.84%
COS/Revenue	90.71%	86.16%
Net Profit Margin	2.41%	3.33%
Asset turnover	1.74	1.42

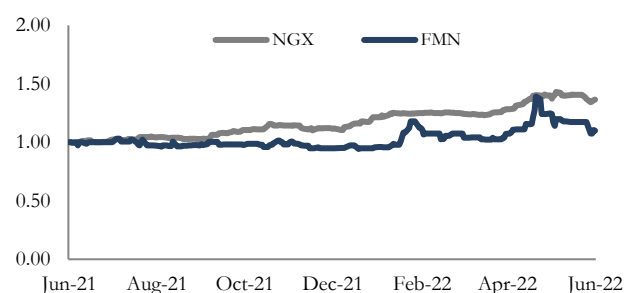
Source: NGX, PAC Research

Table 4: Valuations

	FY2020	FY2021	FY2022F	FY2023F
P/E(x)	5.22	4.79	4.21	3.72
P/B(x)	0.77	0.69	0.66	0.62
Div. Yield	5.04%	6.56%	7.63%	8.85%
Payout Ratio	26.31%	31.47%	32.12%	32.90%
Ev/Revenue	2.88	2.87	2.40	2.29
Rev Per Shr.	188.18	283.83	337.61	371.37
ROE	14.73%	14.30%	15.69%	16.76%
ROA	4.72%	4.20%	4.30%	4.47%

Source: NGX, PAC Research

Fig. 1: FMN vs NGX, 52-wk Movement (Rebased)



Source: Bloomberg, PAC Research

Revenue crosses ₦1 trillion for the first time, driven by strong growth in all the business segments: In the full year of 2021/22, FMN recorded impressive performance as revenue accelerated by 50.83% to ₦1.16 trillion (vs ₦0.66 trillion recorded in FY'20/21), driven by strong growth in all the business segments of the company – revenue of each business segment grew by over 50%, except for Agro-allied segment which grew by 25% in 2021/22. The revenue of the Food Segment increased significantly by 56.54% to ₦748.76 billion (vs. ₦478.33 billion in FY'20/21), driven by Business-to-Business (B2B) volume growth and Business-to-Consumer (B2C) redistribution infrastructure drive. Continued deepening of the B2C redistribution infrastructure drive with investments and roll out of 226 vans resulted in significant growth in Noodles and Ball Foods during the period. In addition, increased rural penetration, through the deployment of containers, tricycles and POS, contributed to the strong growth recorded in Food Segment. Flour product remained the largest contributor to Food Segment, with volume mix of 65%, followed by Pasta (18%), Ball Foods (10%) and Noodles (3%). Revenue from Agro-Allied Segment and Support Segment grew by 53.02% and 56.32% to ₦213.37 billion (FY'20/21: ₦139.44billion) and ₦45.64 billion (FY'20/21: ₦29.20 billion) respectively. The key drivers of Agro-Allied Segment in FY'21/22 are Oil and Fats business, Animal feeds business, Fertilizers business and Starch business as they recorded revenue growth of 58%, 49%, 21% and 46% respectively. The significant growth in Support Segment is attributed to the increased demand for locally produced packaging materials, strong growth in transportation logistics business and impressive performance of Apapa Bulk Terminal Limited (ABTL) (the port facilities business) during the period. Also, revenue from Sugar Segment grew by 25.18% to ₦156.02 billion in FY'21/22 (vs. ₦124.64 billion in FY'20/21), mainly driven by 21% growth in Sunti Brown Granulated Sugar, with notable increased demand from the Northern part of the country and other industrial customers.

We may likely see significant increase in the revenue of company in coming quarters as Honeywell Flour Mills Plc (HFMP) started operating under FMN from May 2022. In addition, the extension of blending plants and sales outlets, as well as expansion of fertilizers business into northern and eastern markets will continue to have positive impact on the overall revenue of the company.

Fig. 2: Revenue (Billion NGN) – FY'21 - FY'25F

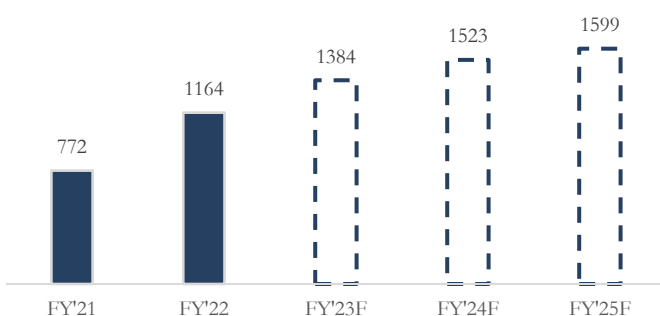
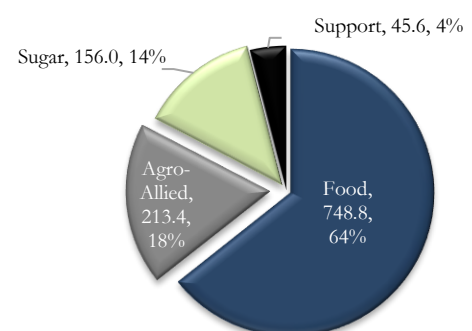


Fig. 3: Contribution to Revenue by Segment (Billion NGN) – FY'21/22



Flour product remained the largest contributor to Food Segment, with volume mix of 65%, followed by Pasta (18%), Ball Foods (10%) and Noodles (3%).

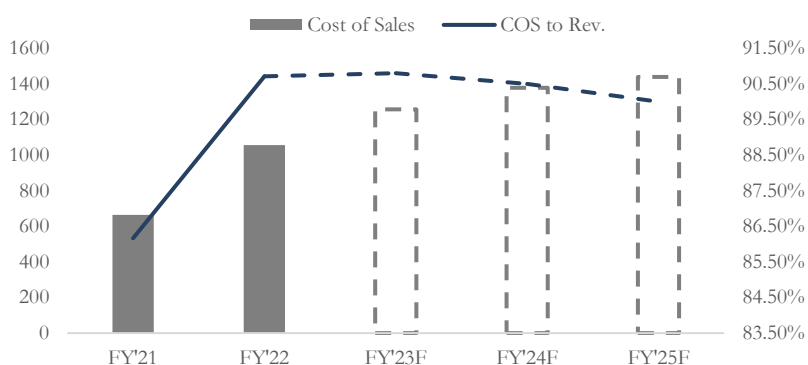
Cost of sales rises by 59% year-on-year, driven by improved production volume, higher energy prices and rising inflation: The ongoing war between Russia and Ukraine, which had negative impact on agricultural commodity prices and energy costs, resulted in high cost of inputs in the full year of 2021/22. In addition to the high cost of input, high production volume raised the company's cost of sales significantly by 58.79% to ₦1.06 trillion (vs. ₦0.66 trillion in full year of 2020/21). Specifically, cost of raw and packing materials, which constitutes about 91% of the total cost of sales, increased by 64.14% to ₦957.96 billion in FY'21/22 (FY'20/21: ₦583.62 billion). The higher energy cost and rising inflation mirrored in the cost-to-sales margin which increased by 455 basis point to 90.71% in FY'21/22 (FY'20/21: 86.16%).

Also, the operating expenses (OPEX), which comprises of administrative, selling and distribution expenses, increased by 4.21% to ₦42.86 billion in FY'21/22 (vs. ₦41.13 billion reported in FY'20/21). The increase in the operating expenses of the company is attributed to higher employee costs, elevated bank charges, higher expenses on fuel, gas & oil, increased travelling expenses, among others. Although, the company witnessed a surge of 4.21% in the OPEX during the period, the inflation rate of 15.92% in March 2022 is 1171 basis point higher the 4.21% increase in OPEX of the company. This showed the efforts of the management in upholding cost-minimisation strategy during the period.

Going forward, the rising inflation rate is expected to have negative impact on the operating expenses of the company. Meanwhile, the acquisition of HFMP will result in cost synergies – improved economies of scale (by streamlining the supply chain and operations of HCMP and FMN) and savings from improved and efficient distribution and marketing channels. The cost synergies is expected offset the adverse impact of the rising inflation on the operating expenses in coming quarters.

Although the company witnessed a surge of 4.21% in the OPEX during the period, the inflation rate of 15.92% in March 2022 is 1171 basis point higher the 4.21% increase in OPEX of the company.

Fig. 4: Cost of Sale and COS to Revenue – FY'21 - FY'25F (Billion NGN)



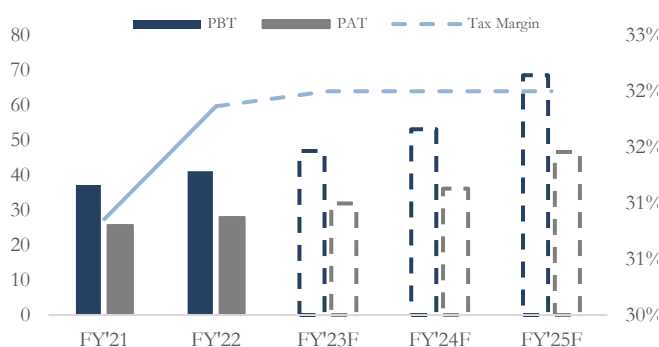
Source: NGX, PAC Research

Despite the setback in non-operating activities, pre-tax income rises by 11% year-on-year: The net finance costs of FMN increased by 62.60% to ₦24.40 billion in FY'21/22 (vs. ₦15.00 billion in FY'20/21) as the company increase its leverage to support the rising demand in various business segment during the period. Precisely, the key driver of net finance cost is interest on bank loans and overdrafts which increased significantly by 81.67% to ₦17.96 billion in FY'21/22 (vs. ₦9.89 billion reported in FY'20/21).

Meanwhile, the impressive operating activities overrode the setback recorded in the non-operating activities of the company during the period. Consequently, profit before tax grew by 10.55% to ₦41.12 billion in FY'21/22 (vs. ₦37.19 billion in FY'20/21). However, the company made a provision of ₦13.10 billion for tax in FY'21/22, which is 14.17% higher than ₦11.48 billion reported in FY'20/21. Notwithstanding the higher tax provision, profit after tax improved by 8.94% to ₦28.02 billion in FY'21/22 (vs. ₦25.72 billion reported in FY'20/21) and this resulted in earnings per share (EPS) of ₦6.26 (FY'20/21: ₦6.38).

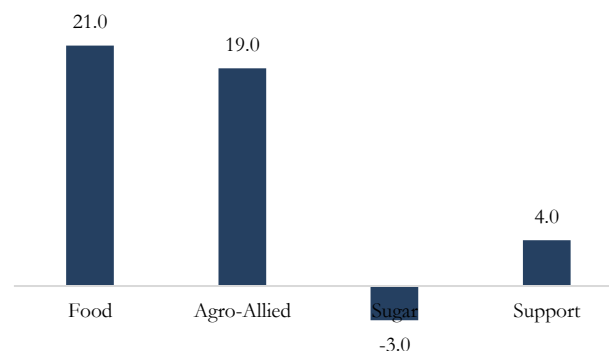
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Fig. 5: PBT, PAT and Tax Margin – FY'21-FY'25F (Billion NGN)



Source: NGX, PAC Research

Fig. 6: Distribution of PBT (Billion NGN) – FY'21/22



Balance sheet remains strong and healthy as FMN rewards shareholders

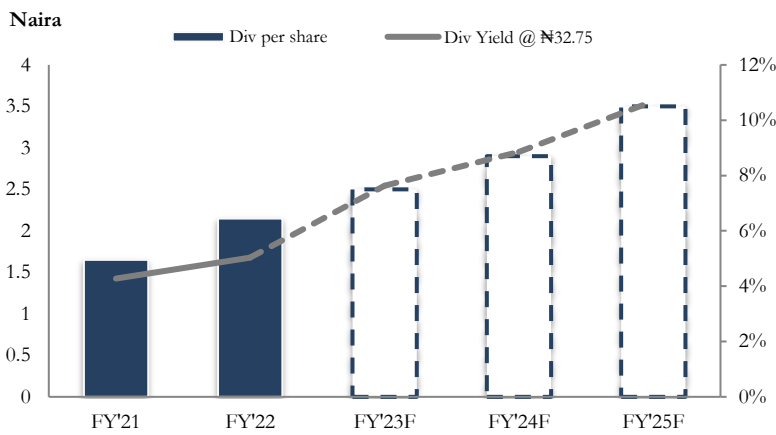
with ₦2.15 per share: FMN maintained a strong and healthy financial position in the period under review as total assets of the company increased by 22.45% to ₦667.01 billion in the full year of 2021/22 (vs. ₦544.73 billion in the full year of 2020/21), driven by strong growth in current assets and non-current assets of the company. As a result of 46% increase in inventory, 55% rise in trade and other receivables and 19% increase in prepayment and deposit for import, the current assets improved by 34.68% to ₦412.12 billion in FY'21/22 (vs. ₦306.01 billion in FY'20/21). In addition, the non-current assets of the company rose by 6.77% to ₦254.90 billion in FY'21/22 (vs. ₦238.73 billion in FY'20/21), driven mainly by additional investment to property, plant and equipment.

However, the total liabilities of the company rose by 27.29% to ₦471.11 billion in FY'21/22 (vs. ₦370.12 billion in FY20/21), due to notable increase in borrowings, bank overdraft, trades & other payables, deferred income, among others.

The improvement in total assets outweighed the increase in total liabilities during the period. Consequently, net assets increased by 12.19% to ₦195.91 in FY'21/22 (vs. ₦174.61 billion in FY'20/21), translated to a net assets per share (NAPS) of ₦47.78 (FY'20/21 ₦42.58). With the improved operating performance and robust balance sheet, FMN rewarded the shareholders with improved dividend of ₦2.15 per share in the full year of 2021/22 (vs. ₦1.65 recorded in the full year of 2020/21). With recent acquisition of HFMP and expectation of improved demand in all the business segment, we anticipate impressive operating performance and solid balance sheet in coming quarters. Hence, we forecast significant growth in the dividend payment in full year of 2022/23.

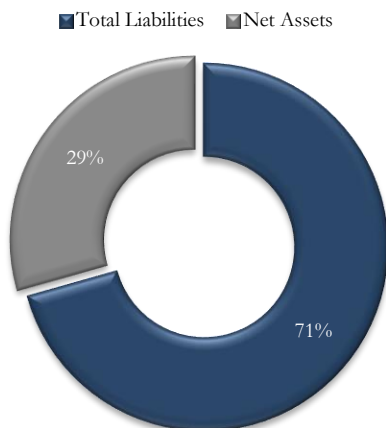
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Fig. 7: Dividend Per Share and Dividend Yield – FY'21-FY'25F



Source: NGX, PAC Research

Fig. 8: Total Liabilities Vs Net Asset in FY'21/22



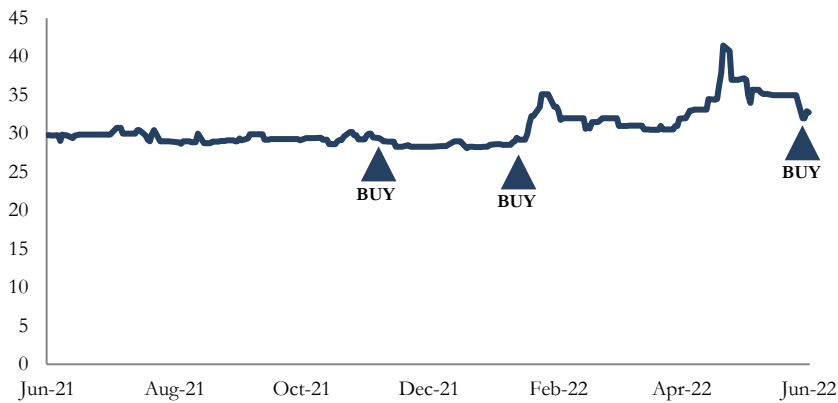
Source: NGX, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦36.77, representing an increase of 12.29% from the current market price of ₦32.90. In arriving at the target price, we employed dividend discount valuation methodology. Consequently, we maintain 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, the synergies from acquisition of HFMP and the outlook from the management.

Our valuation puts the target price of the stock at ₦36.77, representing an increase of 12.29% from the current market price of ₦32.90.

Fig. 9: Share Price History (in Naira)



Source: NGX, PAC Research

Table 5: Statement of Profit or Loss, N'mn

	2021	2022	2023F	2024F
Revenue	771,608	1,163,803	1,384,343	1,522,778
<i>Change</i>		50.83%	18.95%	10.00%
Cost of sales	-664,851	-1,055,713	-1,256,984	-1,378,111
<i>Change</i>		58.79%	19.06%	9.64%
Gross profit	106,757	108,090	127,360	144,664
<i>Change</i>		1.25%	17.83%	13.59%
Selling and distr exp.	-12,080	-11,080	-13,843	-22,080
<i>Change</i>		-8.27%	24.94%	59.50%
Administrative exp.	-29,046	-31,776	-35,993	-36,547
<i>Change</i>		9.40%	13.27%	1.54%
Net Op. gains (losses)	-15,528	-136	-1,384	-1,523
<i>Change</i>		-99.12%	918.76%	10.00%
Operating profit	52,197	65,513	75,308	83,601
<i>Change</i>		25.51%	14.95%	11.01%
investment income	3,652	1,086	2,077	3,046
<i>Change</i>		-70.25%	91.13%	46.67%
Profit Before Tax	37,194	41,118	46,929	53,145
<i>Change</i>		10.55%	14.13%	13.24%
Taxation	-11,477	-13,103	-15,017	-17,006
<i>Change</i>		14.17%	14.61%	13.24%
Profit After Tax	25,717	28,015	31,912	36,139
<i>Change</i>		8.94%	13.91%	13.24%

Table 6: Statement of Financial Position, N'mn

	2021	2022	2023F	2024F
Property plant and equip.	208,721	226,840	242,260	258,872
Investment property	1,533	1,427	1,661	1,827
Goodwill	4,148	4,148	4,153	4,568
Deferred tax	6,974	6,245	6,922	7,614
Long term receivables	39	38	14	15
Inventories	195,449	284,463	319,922	351,914
Biological assets	376	757	692	761
Trade and other rec.	25,826	39,901	47,068	51,774
Total Assets	544,733	667,012	742,327	808,945
Bank overdraft	4,001	9,938	12,459	13,705
Trade & other payables	120,152	194,592	214,573	236,031
Borrowings	26,913	34,017	34,609	38,069
Retirement benefit oblig.	10,397	10,269	11,075	12,182
Long service award	3,713	3,591	5,676	6,243
deferred tax	16,857	15,023	26,995	29,694
Total liabilities	370,119	471,107	538,925	593,274
Net Assets	174,614	195,905	203,402	215,671

Table 7: Profitability Ratio

	2021	2022	2023F	2024F
Gross profit margin	13.84%	9.29%	9.20%	9.50%
Net Profit Margin	3.33%	2.41%	2.31%	2.37%
operating profit margin	6.76%	5.63%	0.00%	0.00%
Return on Equity	14.73%	14.30%	15.69%	16.76%
Return on Assets	4.72%	4.20%	4.30%	4.47%
ROCE	1.09%	0.29%	0.50%	0.68%

Table 8: Asset Utilisation

	2021	2022	2023F	2024F
cash/sales	0.06	0.05	0.05	0.05
Sales to inventory (x)	3.95	4.09	4.33	4.33
Sales to total assets (x)	1.42	1.74	1.86	1.88
sales/EBITDA	9.83	13.28	12.82	12.85
Sales to total fixed assets	3.70	5.13	5.71	5.88
Equity multiplier	3.12	3.40	3.65	3.75

Table 9: Liquidity Ratios

	2020	2021	2022F	2023F
Quick ratio	0.53	0.43	0.46	0.46
Current ratio	1.46	1.40	1.43	1.43
Cash ratio	0.22	0.19	0.20	0.20
Interest Coverage	1.99	1.61	1.54	1.59
Operating Cash Flow Ratio	0.00	0.00	0.00	0.00
Debt/net income	4.11	4.45	4.38	4.26
Debt/operating profit	28.96	114.83	67.33	50.50
Debt to asset	0.19	0.19	0.19	0.19
Debt to equity	0.61	0.64	0.69	0.71
Total liabilities/equity	2.12	2.40	2.65	2.75
Inventory turnover days	107.30	98.35	92.90	93.21
Account receivable days	12.22	12.51	12.41	0.18
Account payable days	65.96	67.28	62.31	62.51

Table 10: Shareholders' Investment Ratios

	2021	2022	2023F	2024F
Earnings per share	6.27	6.83	7.78	8.81
DiV per share	1.65	2.15	2.50	2.90
NAVPS	42.58	47.78	49.61	52.60
Earnings yield	19.15%	20.86%	23.76%	26.91%
P/S ratio	0.174	0.115	0.097	0.088

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

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