

Flour Mills of Nig. Plc

Nigeria | Equities | Consumer Goods | August 6, 2021

PAC RESEARCH

Good Start to the Year as all the Business Segments Maintains Double Digit Growth

INVESTMENT SUMMARY

Flour Mills of Nigeria maintained a stellar performance in the first quarter of 2021/22 as revenue improved significantly by 51.19% to ₦233.70 billion (vs. ₦154.58 billion in the first quarter of 2020/21). The improvement recorded in the top-line was mainly driven by strong volume growth as all the business segments of the company maintained double digit growth during the period. However, the cost of sales increased significantly by 61.21% to ₦208.00 billion in Q1'21/22 (vs. ₦129.03 billion in Q1'20/21), mainly as result of improved production volumes and higher input costs (domestic and imported inputs) during the period. Also, the administrative, selling and distribution expenses increased by 39.66% to ₦9.66 billion in Q1'21/22 (vs. ₦6.92 billion reported in Q1'20/21) due to higher expenses on advertisement, sales, repairs & maintenance, salaries, wages & other staff costs, among others. Despite the higher cost of sales and other expenses, the operating profit improved by 4.77% to ₦11.52 billion in Q1'21/22 (vs. ₦10.99 billion in Q1'20/21).

As a result of replacement of expensive short-term facilities with long-term loans in the last financial year, the net finance costs of the company fell by 6.22% to ₦4.25 billion in Q1'21/22 (vs. ₦4.54 billion reported in Q1'20/21). With the impressive operating and non-operating performance during the period, profit before tax increased by 12.49% to ₦7.26 billion in Q1'21/22 (vs. ₦6.46 billion in Q1'20/21). The company made a provision of ₦1.82 billion for tax in Q1'21/22 (vs. ₦1.49 billion in Q1'20/21). Notwithstanding the higher tax provision, profit after tax improved by 9.57% to ₦5.45 billion (vs. ₦4.97 billion in Q1'20/21) and this resulted in 12-month trailing Earnings Per Share (EPS) of ₦6.39 in Q1'21/22 (Q1'20/21: ₦2.95). Based on the recent figures released, we upgrade our target price slightly to ₦31.73 (Previous TP: ₦31.48) and maintain a **HOLD** recommendation.

Fig. 1: Quarterly results highlights

	1Q2022	4Q2021	1Q2021	Q/q Δ	Y/y Δ
Revenue (₦mn)	233,703	216,266	154,579	+8.06%	+51.19%
Operating profit (₦mn)	11,515	16,987	10,991	-32.21%	+4.77%
Net profit (₦mn)	5,446	10,135	4,971	-46.27%	+9.56%

Source: Bloomberg, PAC Research

Oluwole Adeyeye

oluwole.adeyeye@panafricancapitalholdings.com

Price:

- Current	₦30.00
- Target	₦31.73
Recommendation:	HOLD

* As at Thursday August 5, 2021

Fig. 2: Stock data

FYE	March
Price Mov't: YtD / 52wk	+17.12% / +56.15%
52-week range	₦35.00 - ₦18.30
30-day Average vol.	2,274,772
Shares Outstanding (mn)	4,100.38
Market Cap. (₦bn)	123.01
EPS, ₦- 12months trailing	6.39
DPS, ₦- FY2021	1.65

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

Fig. 3: Key ratios

	Q1'22	Q1'21
Gross profit margin	11.00%	16.53%
COS/Revenue	89.00%	83.47%
Net Profit Margin	2.33%	3.22%
Asset turnover	0.43	0.32

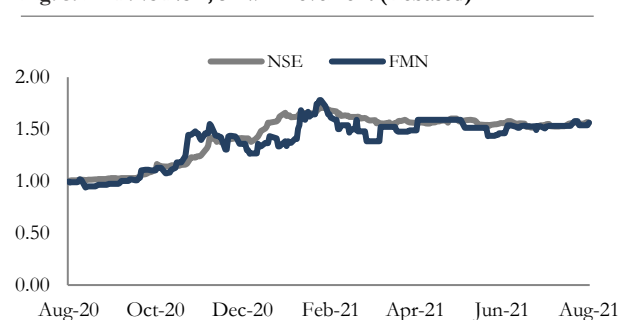
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2020	FY2021	FY2022F	FY2023F
P/E(x)	10.81	4.78	4.49	3.47
P/B(x)	0.79	0.70	0.69	0.66
Div. Yield	4.67%	5.50%	8.33%	10.67%
Payout Ratio	50.46%	26.31%	37.43%	36.99%
Ev/Revenue	3.72	2.28	2.35	2.08
Rev Per Shr.	139.93	188.18	218.29	229.20
ROE	7.30%	14.73%	15.45%	19.06%
ROA	2.63%	4.72%	4.75%	5.86%

Source: NSE, PAC Research

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



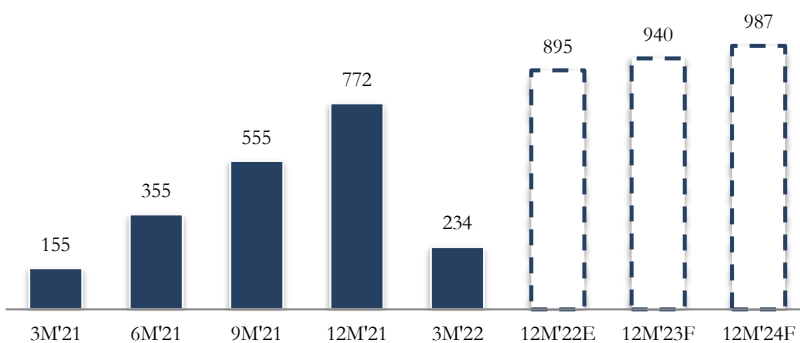
Source: Bloomberg, PAC Research

All the business segments maintained double digit growth as revenue improves by 51.19% year-on-year: Flour mills of Nigeria kicked off the financial year with impressive performance as revenue increased by 51.19% to ₦233.70 billion in the first quarter of 2021/22 (vs ₦154.58 billion reported in the first quarter of 2020/21), driven by strong volumes and revenue growth across all the business segments of the company. The revenue of Agro-Allied Segment improved by 20.41% to ₦47.70 billion in Q1'21/22 (vs. ₦33.10 billion in Q1'20/21) due to 9% revenue growth in the Oil and Fats (driven by 126% growth in export sales) and higher volumes in the Fertilizers business. In addition, the top-line of the Food Segment increased significantly by 62.86% to ₦146.90 billion in Q1'21/22 (vs. ₦61.43 billion Q1'20/21) due to 42% rise in Business-to-Business (B2B) and 12% growth in Business-to-Consumer (B2C) volumes, which translated to 18% growth in Semo, 17% growth in Noodles and 8% growth in Pasta. The revenue of Sugar Segment and Support Services Segment of the company increased by 24.07% and 64.71% to ₦33.50 billion (Q1'20/21: ₦27.00 billion) and ₦5.60 billion in Q1'21/22 (Q1'20/21: ₦3.40 billion) respectively, driven by improved volume growth in locally produced brown Sugar and increased demand in Bagco and sale of innovative products.

Going forward, we maintain that the extension of blending plants and sales outlets, as well as expansion of fertilizers business into northern and eastern markets will improve the revenue of the company. In addition, the strategic partnership with Flour Milling Association of Nigeria (FMAN), additional investment lines in Pasta, Semovita and Noodles (Food Segment) and Solid backward integration investment plans in the Sugar value chain are expected to boost the company's top-line in coming quarters.

Going forward, we maintain that the extension of blending plants and sales outlets, as well as expansion of fertilizers business into northern and eastern markets will improve the revenue...

Fig. 6: Revenue – 3M'21 – 12M'24F (Billion NGN)

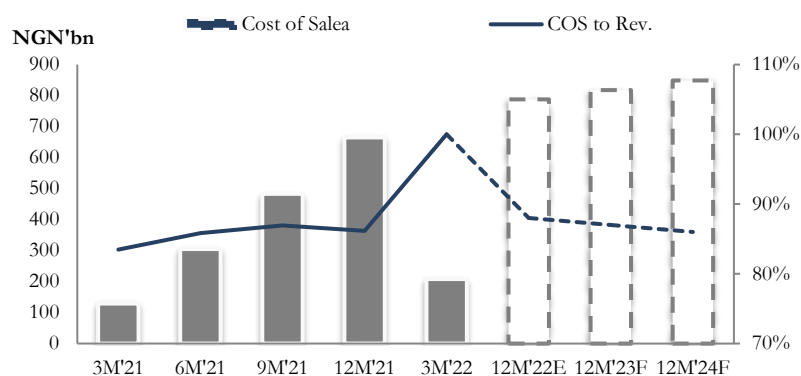


Source: NSE, PAC Research

Cost of sales rises by 61.21% year-on-year, driven by higher production volumes and higher input costs: In the first quarter of 2021/22, the cost of sales rose significantly by 61.21% to ₦208.00 billion (vs. ₦129.03 billion in the first quarter of 2020/21), driven by higher production volumes and higher input costs during the period. Specifically, the cost of raw and packing materials, which constitutes about 89% of the total cost of sales, increased by 40.72% to ₦186.03 billion in Q1'21/22 (Q1'20/19: ₦110.28 billion). Although the improved volume growth and higher input costs contributed to the overall rise in the cost of sales, the cost-to-sales margin, which increased significantly to 89.00% in Q1'21/22 (from 83.47% in Q1'20/21), remains a major threat to the profitability of the company. To achieve outstanding bottom-line going forward, FMN needs to strengthen its cost-minimization strategy by improving the cost-to-sales margin in the coming quarters.

The administrative, selling and distribution expenses of FMN increased by 39.66% to ₦9.66 billion in Q1'21/22 (vs. ₦6.92 billion reported in Q1'20/21), due to higher expenses on advertisement, sales, repairs & maintenance, salaries, wages & other staff costs, among others. With the relatively higher inflation rate in the country, we may likely see further increase in the expenses on selling, distribution, and administration in the coming quarters.

Fig. 7: Cost of Sale and COS to Revenue – 3M'21 – 12M'24F



Source: NSE, PAC Research

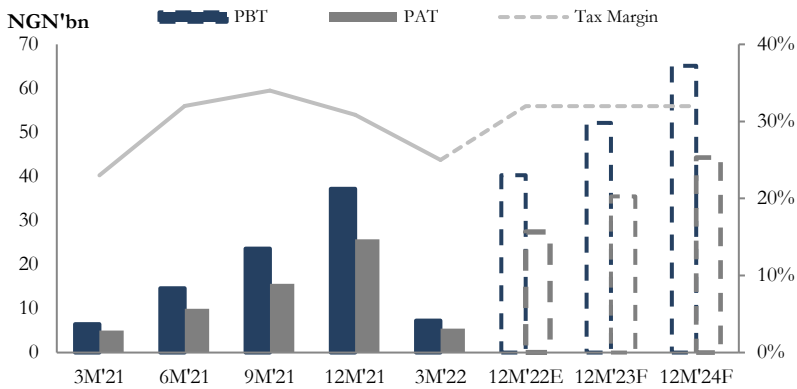
With Stellar operating and non-operating performance, PBT improves by 12.49% year-on-year: The decision of FMN to replace the expensive short-term facilities with long-term loans in the last financial year yielded positive in the first quarter of 2021/22 as net finance costs fell by 6.22% to ₦4.25 billion in Q1'21/22 (vs. ₦4.54 billion in Q1'20/21).

With the impressive performance recorded across board, the profit before tax improved by 12.49% to ₦7.26 billion in Q1'21/22 (vs. ₦6.45 billion in Q1'20/21). Meanwhile, the company made a higher provision of ₦1.82 billion for tax in the first quarter of 2021/22 (vs. ₦1.49 billion in the first quarter of 2020/21).

To achieve outstanding bottom-line going forward, FMN needs to strengthen its cost-minimization strategy by improving the cost-to-sales margin in the coming quarters.

Despite the higher provision for tax during the period, profit after tax increased by 9.57% to ₦5.45 billion, from ₦4.97 billion reported in the corresponding quarter of the previous year.

Fig. 8: PBT, PAT and Tax Margin – 3M'21 - 12M'24F



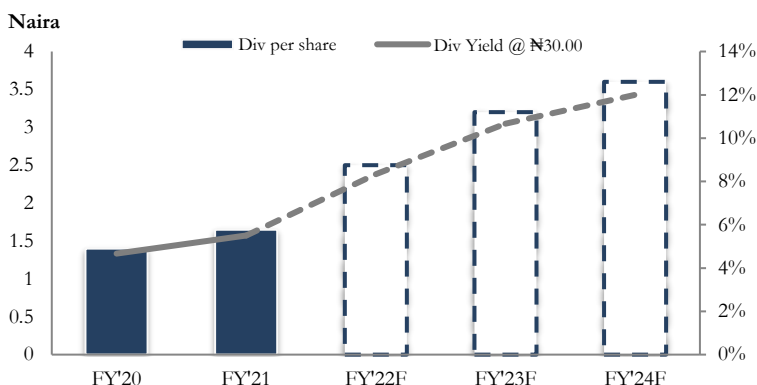
Source: NSE, PAC Research

Balance sheet remains solid: Expectation of improved dividend payment in FY'21/22: Flour Mills of Nigeria continue to maintain a strong balance sheet as the total assets of the company improved by 13.62% to ₦540.41 billion in first quarter of 2021/22 (vs. ₦475.65 billion in first quarter of 2020/21), driven mainly by improvement in the current assets of the company. The current assets improved by 27.69% to ₦301.77 billion in Q1'21/22 (vs. ₦236.32 billion in Q1'20/21) as a result of 59.30% increase in inventory and 77.57% increase in prepayment and deposit for import. However, the total liabilities of the company rose by 14.44% to ₦360.35 billion in Q1'21/22 (vs. ₦314.87 billion in Q1'20/21), due to notable increase in customer deposits, long term borrowing, current tax payables, among others. Consequently, the net assets increased by 11.99% to ₦180.06 billion in Q1'21/22 (vs. ₦160.78 billion in Q1'20/21) and this resulted in net assets per share (NAPS) of ₦43.91 (Q1'20/21: ₦39.21).

With the impressive operating growth, non-operating performance, robust balance sheet and positive outlook from the management, we expect improved dividend payment in FY'21/22.

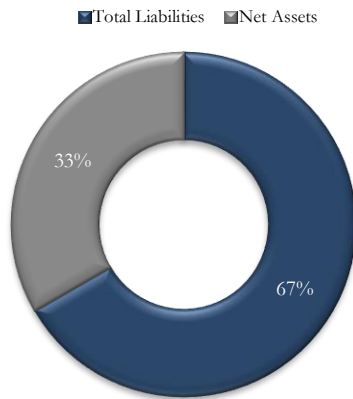
With the impressive operating growth, non-operating performance, robust balance sheet and positive outlook from the management, we expect improved dividend payment in FY'21/22.

Fig. 9: Dividend Per Share and Dividend Yield – FY'20-FY'24F



Source: NSE, PAC Research

Fig. 10: Total Liabilities Vs Net Asset in Q1'21/22



Source: NSE, PAC Research

Valuation

Our valuation puts the target price of the stock at ₦31.73, representing an increase of 5.78% from the current market price of ₦30.00. In arriving at the target price, we employed discounted free cash flow methodology. Consequently, we maintain a **HOLD** 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 and the outlook from the management.

Our valuation puts the target price of the stock at ₦31.73, representing an increase of 5.78% from the current market price of ₦30.00.

Fig. 11: Share Price History



Source: NSE, PAC Research

Fig. 12: Statement of Profit or Loss, N'mn

	2020	2021	2022E	2023F
Revenue	573,774	771,608	895,065	939,818
<i>Change</i>		<i>34.48%</i>	<i>16.00%</i>	<i>5.00%</i>
Cost of sales	-507,987	-664,851	-787,657	-817,642
<i>Change</i>		<i>30.88%</i>	<i>18.47%</i>	<i>3.81%</i>
Gross profit	65,787	106,757	107,408	122,176
<i>Change</i>		<i>62.28%</i>	<i>0.61%</i>	<i>13.75%</i>
Selling and distr exp.	-9,278	-12,080	-13,426	-13,627
<i>Change</i>		<i>30.19%</i>	<i>11.15%</i>	<i>1.50%</i>
Administrative exp.	-23,346	-29,046	-32,222	-33,833
<i>Change</i>		<i>24.41%</i>	<i>10.94%</i>	<i>5.00%</i>
Net Op. gains (losses)	4,906	-15,528	-10,741	-11,278
<i>Change</i>		<i>-416.54%</i>	<i>-30.83%</i>	<i>5.00%</i>
Operating profit	35,080	52,197	53,435	65,975
<i>Change</i>		<i>48.79%</i>	<i>2.37%</i>	<i>23.47%</i>
investment income	2,393	3,652	3,849	4,041
<i>Change</i>		<i>52.64%</i>	<i>5.38%</i>	<i>5.00%</i>
Profit Before Tax	17,497	37,194	40,278	52,160
<i>Change</i>		<i>112.57%</i>	<i>8.29%</i>	<i>29.50%</i>
Taxation	-6,120	-11,477	-12,889	-16,691
<i>Change</i>		<i>87.53%</i>	<i>12.30%</i>	<i>29.50%</i>
Profit After Tax	11,377	25,717	27,389	35,469
<i>Change</i>		<i>126.05%</i>	<i>6.50%</i>	<i>29.50%</i>

Fig. 13: Statement of Financial Position, N'mn

	2020	2021	2022E	2023F
Property plant and equip.	216,890	208,721	214,816	225,556
Investment property	1,633	1,533	1,880	1,880
Goodwill	4,148	4,148	4,654	4,887
Deferred tax	3,578	6,974	8,056	8,458
Long term receivables	359	39	269	282
Inventories	115,596	195,449	187,964	197,362
Biological assets	148	376	448	470
Trade and other rec.	25,731	25,826	29,090	30,544
Total Assets	432,454	544,732	576,093	604,801
Bank overdraft	5,543	4,001	1,343	1,410
Trade & other payables	83,614	120,152	116,358	122,176
Borrowings	23,344	26,913	28,642	30,074
Retirement benefit oblig.	7,135	10,397	12,531	13,157
Long service award	2,738	3,713	3,222	3,383
deferred tax	11,849	16,857	19,154	20,112
Total liabilities	276,646	370,119	398,778	418,717
Net Assets	155,808	174,613	177,314	186,084

Fig. 14: Profitability Ratio

	2020	2021	2022E	2023F
Gross profit margin	11.47%	13.84%	12.00%	13.00%
Net Profit Margin	1.98%	3.33%	3.06%	3.77%
operating profit margin	6.11%	6.76%	0.00%	0.00%
Return on Equity	7.30%	14.73%	15.45%	19.06%
Return on Assets	2.63%	4.72%	4.75%	5.86%
ROCE	0.84%	1.09%	1.08%	1.08%

Fig. 15: Asset Utilisation

	2020	2021	2022E	2023F
cash/sales	0.03	0.06	0.07	0.07
Sales to inventory (x)	4.96	3.95	4.76	4.76
Sales to total assets (x)	1.33	1.42	1.55	1.55
sales/EBITDA	10.61	8.21	9.61	8.73
Sales to total fixed assets	2.65	3.70	4.17	4.17
Equity multiplier	2.78	3.12	3.25	3.25

Fig. 16: Liquidity Ratios

	2020	2021	2022E	2023F
Quick ratio	0.50	0.53	0.63	0.63
Current ratio	1.28	1.46	1.48	1.48
Cash ratio	0.12	0.22	0.29	0.29
Interest Coverage	0.88	1.99	2.37	2.92
Operating Cash Flow Ratio	0.00	0.00	0.00	0.00
Debt/net income	7.58	4.11	4.13	3.35
Debt/operating profit	36.03	28.96	29.42	29.42
Debt to asset	0.20	0.19	0.20	0.20
Debt to equity	0.55	0.61	0.64	0.64
Total liabilities/equity	1.78	2.12	2.25	2.25
Inventory turnover days	83.06	107.30	87.10	88.10
Account receivable days	16.37	12.22	11.86	0.18
Account payable days	60.08	65.96	53.92	54.54

Fig. 17: Shareholders' Investment Ratios

	2020	2021	2022E	2023F
Earnings per share	2.77	6.27	6.68	8.65
DiV per share	1.40	1.65	2.50	3.20
NAVPS	38.00	42.58	43.24	45.38
Earnings yield	9.25%	20.91%	22.27%	28.83%
P/S ratio	0.214	0.159	0.137	0.131

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