

Flour Mills of Nig. Plc

Impressive Performance across the Business Segments

INVESTMENT SUMMARY

Flour mills of Nigeria (FMN) has been consistently benefiting from the closure of the land borders since August 2019. However, in the middle of December 2020, the Federal Government of Nigeria opened the land borders at Seme, Illela, Maigatari and Mfun. As expected, the re-opening of the land borders had no adverse impact on the turnover of FMN as revenue increased by 31.14% to ₦555.34 billion in 9M'20/21 (vs. ₦423.48 billion in 9M'19/20). The improvement in the top-line may be attributed to the benefit derived from the border closure and improved Christmas demand, as all the business segments of the company grew by 25% plus. Mainly as a result of higher sales during the period, the cost of sales increased by 28.55% to ₦482.90 billion (vs. ₦375.65 billion in the corresponding period of previous year), and this translated to a lower cost-to-sales ratio of 86.95% (vs. 88.71% 9M'19/20). Mainly as a result of higher salaries, wages and other staff costs, the administrative expenses of the company rose by 6.28% to ₦18.35 billion in 9M'20/21 (vs. ₦17.26 billion reported in 9M'19/20). With the impressive operating performance, EBITDA improved by 64.84% to ₦66.08 billion in 9M'20/21 (vs. ₦40.09 billion in 9M'19/20).

In nine-month to December 2020/21, Flour Mills of Nigeria further optimised the cost of financing and debt levels as net finance costs declined by 6.36% to ₦11.60 billion (vs. ₦12.39 billion in 9M'19/20). With the impressive operating and non-operating performance, profit before tax improved significantly by 92.06% to ₦23.61 billion in 9M'20/21 (vs. ₦12.29 billion in 9M'19/20). However, the company made higher provision of ₦8.03 billion for tax in 9M'20/21 (vs. ₦4.13 billion in 9M'19/20). Consequently, profit after tax improved significantly by 90.94% to ₦15.58 billion (vs. ₦8.16 billion in 9M'19/20). Based on the recent figures released, we upgrade our target price to ₦30.63 (from ₦28.50 previously recommended) and maintain a **HOLD** recommendation.

Fig. 1: Quarterly results highlights

	3Q2021	2Q2021	3Q2020	Q/q Δ	Y/y Δ
Revenue (₦mn)	200,233	200,530	152,717	-0.15%	+31.11%
Operating profit (₦mn)	11,478	12,741	7,860	-9.91%	+46.03%
Net profit (₦mn)	5,649	4,962	2,257	+13.85%	+150.3%

Source: Bloomberg, PAC Research

February 12, 2021

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Price:

- Current	₦29.25
- Target	₦30.63
Recommendation:	HOLD

* As at Thursday February 11, 2021

Fig. 2: Stock data

FYE	March
Price Mov't: YtD / 52wk	+12.50% / +28.29%
52-week range	₦35.00 - ₦17.00
30-day Average vol.	3,834,161
Shares Outstanding (mn)	4,100.38
Market Cap. (₦bn)	119.94
EPS, ₦- 12months trailing	4.58
DPS, ₦- FY2020	1.40

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

Fig. 3: Key ratios

	9M'21	9M'20
Gross profit margin	13.05%	11.29%
COS/Revenue	86.95%	88.71%
Net Profit Margin	2.81%	1.93%
Asset turnover	1.13	1.05

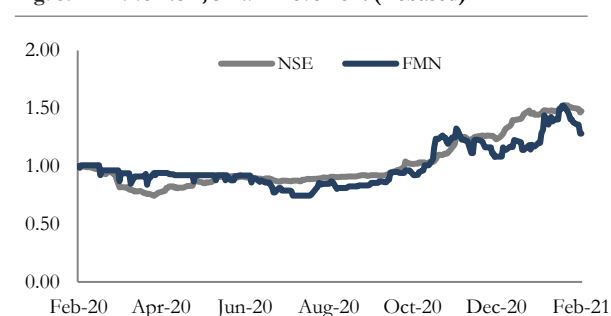
Source: NSE, PAC Research

Fig. 4: Valuations

	FY2019	FY2020	FY2021E	FY2022F
P/E(x)	29.98	10.54	5.87	4.69
P/B(x)	0.79	0.77	0.71	0.73
Div. Yield	4.10%	4.79%	7.52%	9.57%
Payout Ratio	123.01%	50.46%	44.15%	44.87%
Ev/Revenue	0.42	0.34	0.25	0.25
Rev Per Shr	128.62	139.93	181.91	191.01
ROE	2.65%	7.30%	12.15%	15.67%
ROA	0.96%	2.63%	4.01%	4.87%

Source: NSE, PAC Research

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

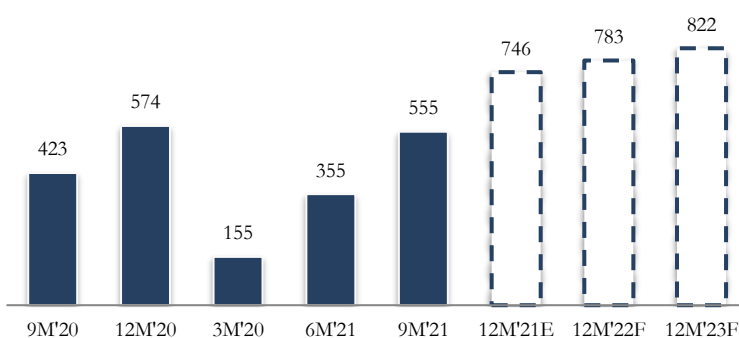


Source: Bloomberg, PAC Research

Revenue rises by 31.14% year-on-year, driven by improved demand: Fifteen days to the end of Flour Mills of Nigeria's third quarter, the Federal Government of Nigeria opened the land border, and as expected, this had no impact on the turnover of the company as revenue improved significantly by 31.14% to ₦555.34 billion (vs. ₦423.48 billion in 9M'19/20). The improvement in top line could be attributed to impressive performance across all the business segments. Revenue from the food segment improved significantly by 31.21% to ₦343.89 billion in 9M'20/21 (vs. ₦262.10 billion in 9M'19/20), due to improved volume growth in B2C segment, which translated to 20% volume growth in Pasta and 27% volume growth in Semovita and Golden Vita during the period. In addition, the revenue of the Sugar segment of the company increased by 33.41% to ₦90.21 billion in 9M'20/21 (vs. ₦67.62 billion in 9M'19/20), due to improved demand for local sugar. Agro-allied segment improved its revenue by 29.86% to ₦105.59 billion in 9M'20/21 (vs. ₦81.31 billion in 9M'19/20), largely driven by higher volumes in fertilizers and oils & fats. It should be noted that the export revenue from the Agro-allied segment grew by 23% during the period and we expect this to improve the diversification of revenue sources and mitigate FX exposures. The revenue of Support segment rose by 25.63% to ₦15.65 billion in 9M'20/21 (vs. ₦12.46 billion in 9M'19/20), driven by strong demand in ABTL (Apapa Bulk Terminal Limited) and Bagco with the scarcity of imported packaging in the market.

We do not expect the re-opening of the land borders to have adverse impact on the demand for the products of FMN in the next quarter due to restrictions on the importation of some goods into the country. Again, the company has positioned itself for possible competition from outside the country.

Fig. 6: Revenue – 9M'20-12M'23F (Billion NGN)



Source: NSE, PAC Research

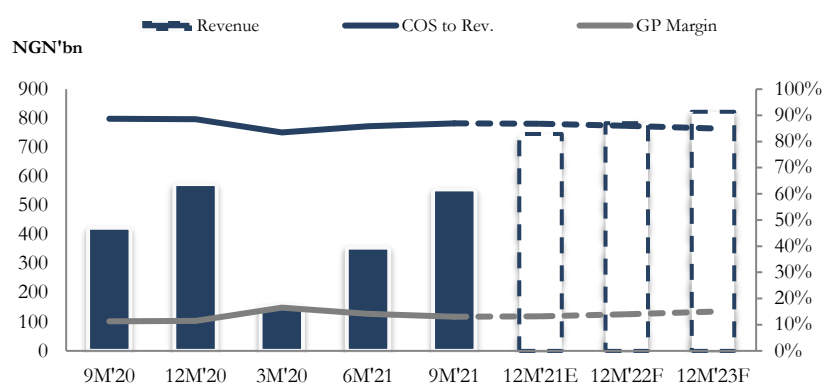
Cost of sales rises by 28.55% year-on-year due to higher production volumes: In nine-month to December 20/21, the cost of sales rose significantly by 28.55% to ₦482.90 billion (vs. ₦375.60 billion in nine-month to December 2019/20), driven by higher production volumes. The higher cost of sales during the period could be mainly attributed to higher material costs as it rose by 31.67% to ₦425.82 billion in 9M'20/21 (9M'19/20: ₦323.39 billion).

We do not expect the re-opening of the land borders to have adverse impact on the demand for the products of FMN in the next quarter due to restrictions on the importation of some goods into the country.

Although, the cost of sales increased by 28.55%, cost-to-sales margin declined to 86.95% in 9M'20/21 (9M'19/20: 88.71) and this showed an improvement in the cost minimization strategy of the company. The improvement in the cost-to-sales margin may be attributed to improved participation of FMN in partnership with Flour Milling Association of Nigeria (FMAN), successful implementation of the various programs such as farmers centre program and seed production program, as well as improved farmer engagement (478 farmers) and pre-season training completed for 2,100 wheat farmers across 15 target LGAs in Kano, Jigawa and Kebbi. We expect the partnership of FMN with FMAN and farmers to continue to boost the country self-sufficiency in wheat production, thereby improving cost-margin going forward.

Mainly as a result of higher salaries, wages and other staff costs during the period, selling & distribution and administrative expenses increased by 5.53% and 6.28% to ₦6.76 billion (9M'19/20: ₦6.40 billion) and ₦18.35 billion (9M'19/20: ₦17.62 billion) respectively in 9M'20/21.

Fig. 7: Revenue, COS to Rev. and GP Margin – 9M'20 - 12M'23F



Source: NSE, PAC Research

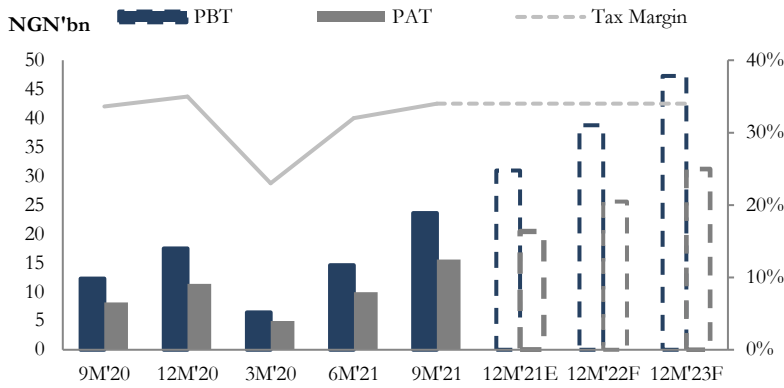
With impressive performance across board, PBT improves significantly by 92.06% year-on-year: During the period under review, FMN Plc reported impressive figures for non-operating activity as net finance costs fell by 6.36% to ₦11.60 billion (vs. ₦12.39 billion in corresponding period of previous year), as FMN continue to optimize the cost of financing and debt levels.

With impressive performance in operating and non-operating activities of the company, profit before tax improved significantly by 92.06% to ₦23.61 billion in 9M'20/21 (vs. ₦12.29 billion in 9M'19/20). However, the company made a higher provision of ₦8.03 billion for tax during the period (vs. ₦4.13 billion reported in the corresponding period of previous year). Consequently, profit after tax increased by 90.94% to ₦15.58 billion in 9M'20/21, from ₦8.16 billion recorded in 9M'19/20, and this translated to a trailing EPS of ₦4.58 during the period.

We expect the partnership of FMN with FMAN and farmers to continue to boost the country self-sufficiency in wheat production, thereby improving cost-margin going forward.

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Fig. 8: PBT, PAT and Tax Margin – 9M'20-12M'23F



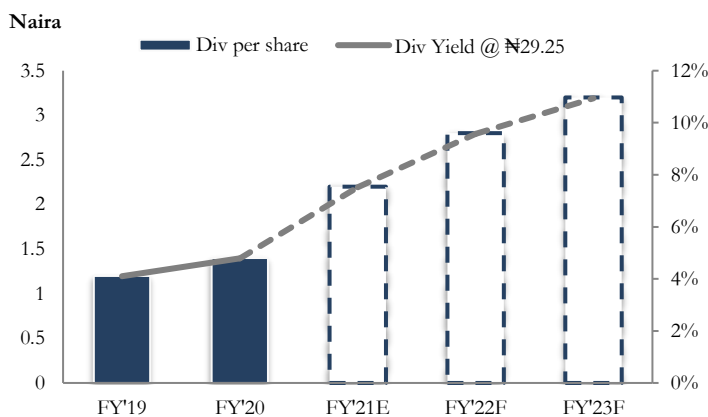
Source: NSE, PAC Research

Balance sheet remains strong and solid; Expectation of improved dividend

in FY'21: FMN Plc continued with impressive balance sheet in the third quarter of 20/21 as net assets increased by 7.43% to ₦165.66 billion (vs. ₦154.21 in the second quarter of 2019/20). This was majorly boosted by the significant improvement in the total assets of the company, which improved by 21.75% to ₦493.16 billion in third quarter of 2020/21 (vs. ₦405.04 billion in second quarter of 2019/20). The improvement in total asset was mainly driven by the significant increase in cash & cash equivalents and inventories. The increase in cash & cash equivalents could be attributed to the issuance of the N30bn bond in December 2020. However, the total liabilities of the company rose by 30.56% to ₦327.50 billion in Q3'20/21 (vs. ₦250.84 billion in Q2'19/20), due to notable increase in long term borrowing, customer deposits, trades & other payables, among others. Consequently, the net assets per share (NAPS) improved to ₦40.40 in Q3'20/21 (vs. ₦37.61 in Q2'19/20). With the improved balance sheet and impressive operating performance, we expect improved dividend payment (see fig. 9) from the company in full year of 2021.

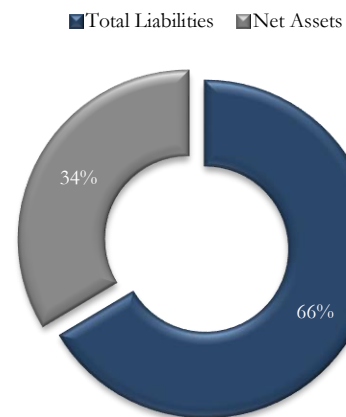
With the improved balance sheet and impressive operating performance, we expect improved dividend payment (see fig. 9) from the company in full year of 2021.

Fig. 9: Dividend Per Share and Dividend Yield – FY'19-FY'23F



Source: NSE, PAC Research

Fig. 10: Total Liabilities Vs Net Asset in Q3'20/21

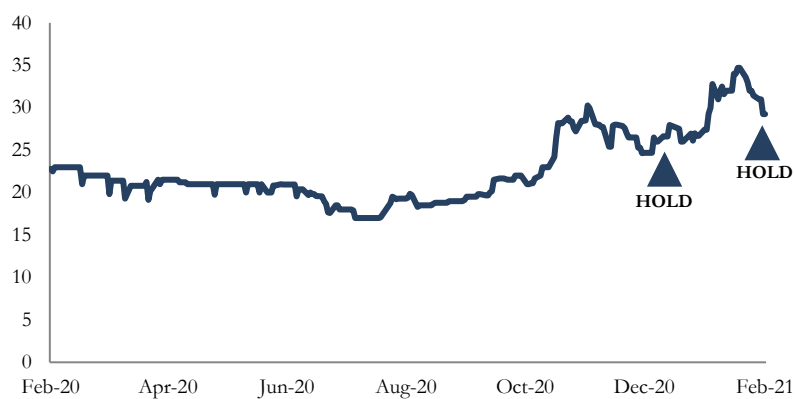


Valuation

Our valuation puts the target price of the stock at ₦30.63, representing an increase of 4.70% from the current market price of ₦29.25. 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 ₦30.63, representing an increase of 4.70% from the current market price of ₦29.25.

Fig. 11: Share Price History



Source: NSE, PAC Research

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

	2019	2020	2021E	2022F
Revenue	527,405	573,774	745,907	783,202
Change	-2.81%	8.79%	30.00%	5.00%
Cost of sales	-474,057	-507,987	-647,447	-673,554
Change	0.03%	7.16%	27.45%	4.03%
Gross profit	53,348	65,787	98,460	109,648
Change	-22.43%	23.32%	49.66%	11.36%
Selling and distr exp.	-8,166	-9,278	-9,697	-10,182
Change	32.13%	13.63%	4.51%	5.00%
Administrative exp.	-19,424	-23,346	-24,615	-25,846
Change	0.00%	20.19%	5.43%	5.00%
Net Op. gains (losses)	6,211	4,906	-16,783	-17,622
Change	4.51%	-21.02%	-442.11%	5.00%
Operating profit	32,297	35,080	47,365	55,999
Change	-33.30%	8.62%	35.02%	18.23%
investment income	769	2,393	4,475	4,699
Change	-5.85%	211.30%	87.05%	5.00%
Profit Before Tax	10,174	17,497	30,955	38,768
Change	-38.49%	71.97%	76.92%	25.24%
Taxation	-6,174	-6,120	-10,525	-13,181
Change	111.01%	-0.88%	71.97%	25.24%
Profit After Tax	4,000	11,377	20,430	25,587
Change	-70.62%	184.41%	79.58%	25.24%

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

	2019	2020	2021E	2022F
Property plant and equip.	221,465	216,890	212,583	223,213
Investment property	1,738	1,633	1,566	1,645
Goodwill	4,148	4,148	4,314	4,347
Deferred tax	3,964	3,578	4,102	4,229
Long term receivables	1,402	359	373	392
Inventories	118,867	115,596	123,075	129,228
Biological assets	18	148	149	157
Trade and other rec.	26,085	25,731	28,344	28,195
Total Assets	416,822	432,454	509,964	525,019
Bank overdraft	9,651	5,543	1,492	3,916
Trade & other payables	79,040	83,614	91,747	97,900
Borrowings	71,053	23,344	44,754	46,992
Retirement benefit oblig.	5,848	7,135	8,205	7,832
Long service award	2,183	2,738	2,685	2,820
deferred tax	10,588	11,849	15,962	16,761
Total liabilities	265,849	276,646	341,849	361,683
Net Assets	150,972	155,808	168,115	163,337

Fig. 14: Profitability Ratio

	2019	2020	2021E	2022F
Gross profit margin	10.12%	11.47%	13.20%	14.00%
Net Profit Margin	0.76%	1.98%	2.74%	3.27%
operating profit margin	6.12%	6.11%	6.70%	6.70%
Return on Equity	2.65%	7.30%	12.15%	15.67%
Return on Assets	0.96%	2.63%	4.01%	4.87%
ROCE	0.33%	0.84%	1.36%	1.42%

Fig. 15: Asset Utilisation

	2019	2020	2021E	2022F
cash/sales	0.03	0.03	0.04	0.03
Sales to inventory (x)	4.44	4.96	6.06	6.06
Sales to total assets (x)	1.27	1.33	1.46	1.49
sales/EBITDA	11.24	11.30	7.94	7.46
Sales to total fixed assets	2.38	2.65	3.51	3.51
Equity multiplier	2.76	2.78	3.03	3.21

Fig. 16: Liquidity Ratios

	2019	2020	2021E	2022F
Quick ratio	0.33	0.50	0.79	0.72
Current ratio	0.98	1.28	1.47	1.39
Cash ratio	0.10	0.12	0.14	0.14
Interest Coverage	0.44	0.88	1.48	1.77
Operating Cash Flow Ratio	0.00	0.00	0.00	0.00
Debt/net income	13.97	7.58	5.18	4.44
Debt/operating profit	72.71	36.03	23.67	24.17
Debt to asset	0.13	0.20	0.21	0.22
Debt to equity	0.84	0.55	0.63	0.70
Total liabilities/equity	1.76	1.78	2.03	2.21
Inventory turnover days	91.52	83.06	69.38	70.03
Account receivable days	18.05	16.37	13.87	13.14
Account payable days	60.86	60.08	51.72	53.05

Fig. 17: Shareholders' Investment Ratios

	2019	2020	2021E	2022F
Earnings per share	0.98	2.77	4.98	6.24
DiV per share	1.20	1.40	2.20	2.80
NAVPS	36.82	38.00	41.00	39.83
Earnings yield	3.34%	9.49%	17.03%	21.33%
P/S ratio	0.227	0.209	0.161	0.153

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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