

# Flour Mills of Nigeria Plc.

## Minutes from Meeting with Management

We met with the management of FLOURMILL earlier today ahead of our update following the release of second quarter result (July to September 2016). Summary of the feedback is that while Q3-17 performance is expected to be affected by the impact of seasonality, there is strong conviction that the company would close 2017F on an impressive note. Specific guidance for revenue and earnings growth was not provided, but both are expected to grow in line with H1-17.

Revenue growth in the Food (51% in H1) and Agro-Allied (34% in H1) divisions is expected to remain strong, while recovery in Packaging (-32% in H1) is dependent upon recovery in external demand (accounting for 50% of total sales). Volumes, thus far, have grown in low single-digit on average across product categories, confirming that revenue growth has largely been as a result of price increases (PIs). We understand that margins are now reviewed weekly and extra costs (where they arise) are passed to consumers monthly. No significant change is expected in this trend. Management's comment on sales is somewhat consistent with the feedback from our routine checks, where distributors confirmed stable demand across products such as Semovita, Noodles, Pasta and Sugar.

Management said that exports (of food and packaging products to South and North Africa, and commodities to Asia) contributed to revenue in Q2, although details were not disclosed in the latest filing. Short term plan is to generate about 10% of total forex requirement from exports and the proportion should increase to 50% in the medium to long term.

The significant increase in SD&A expenses in Q2 was as a result of increasing focus on sales as well as the impact of naira depreciation on USD denominated salaries.

Forex loss of N9.3 billion was reported in Q2 following revaluation of (1) account payables and (2) US\$20 million foreign loans. Each contributed equally to the forex loss. FLOURMILL benefits from the CBN's frequent intervention in the FX market, wherein the apex bank sells USD (in excess of US\$300 million) preferentially to manufacturers at subsidized rates. However, allocation is usually far insufficient (less than 5% of total demand). We estimate FLOURMILL's average USD purchase rate to be around N388/USD.

In addition to PIs, FX linked costs are controlled by increasing domestic sourcing of inputs that are available locally. Items like maize and soybean are now 100% sourced locally, but concerns is that more than 80% is from third party growers, most of whom prices often reflect international market prices. Wheat and Sugar are still wholly imported.

On debt, the slight q/q increase in Q2 was as a result of fresh long term loans taken during the period to fund the ongoing backward integration programme (BIP) in sugar. The management recently issued a commercial paper (CP) at a rate that mirrors the yield on short term government treasuries. In addition, there is plan to raise up to N100 billion through CPs (to refinance maturing short term loans) in tranches over the next two years.

We are overweight FLOURMILL. Forecasts are under review.

## BUY

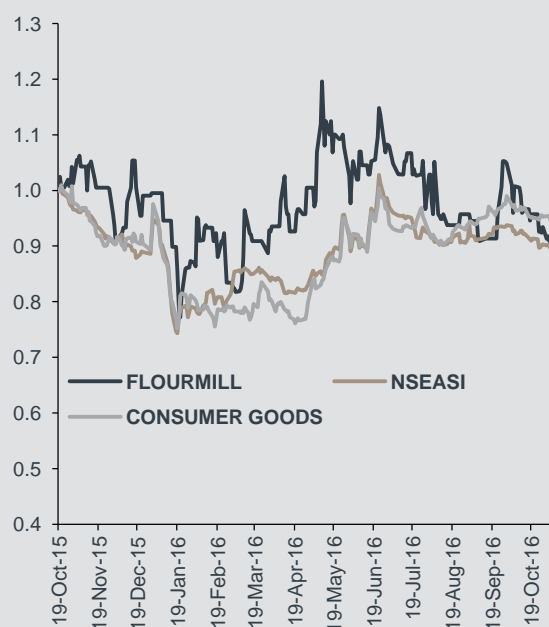
Target Price (N)	43.65
Current Price (N)	19.00
Implied Return (%)	136.59

### Company Data

NSE Code	FLOURMILL
Bloomberg Code	FLOURMILL:NL
Reuters Code	FLOURMIL.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	49.86
Free Float (%)	47.82

Ratios	9M-16	9M-15	2016FY
Gross margin	14.27%	10.27%	29.62%
Opex margin	3.58%	4.38%	24.26%
EBIT margin	7.52%	6.88%	5.37%
*PBT margin	3.45%	0.21%	2.23%
*PAT margin	2.53%	0.21%	18.13%
*EPS (N)	2.23	0.14	0.42

### Price movement (FLOURMILL vs. Benchmark Indices)



# Disclosures

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