

Flour Mills of Nigeria Plc.

First Glance: Q2-17/18 PAT; FX Gains Spur Earnings Growth

FLOURMILL just published Q2-17/18 and H1-17/18 results showing high double-digit growth in post-tax profit. The primary driver of the profit growth (as was the case in Q1) is a net operating gain of N1.92 billion, against a loss reported in Q2-16. That aside, gross profit was down 14% y/y while opex and finance costs increased by 13% y/y and 31% y/y respectively.

Net operating gain increased from N3.15 billion in Q1-17/18 to N1.92 billion in the review period, reflecting continued gains from FX hedges, on the backdrop of improved dollar liquidity and consequent strengthening of the naira.

Revenue grew by 9.8% y/y, the slowest pace since Q4-15/16, as pricing effect continues to taper. Coming off 2016/17, management said – in obvious acknowledgement of the little room for price increases – it will leverage on increased sales volumes and marketing activities to boost top-line going forward. While salient, we note that efforts in this regard continue to face challenges associated with both the gridlock in Apapa (which negatively affects both the movement of goods out FLOURMILL's factory and customers' access to the factory) and the consequent congestion of the seaport. The slower revenue growth also reflects sugar price discounting (we estimate 5%) initiated by the market leader on the back of increased illegal imports following improved access to dollars. All divisions of the business, save for ports operations, reported y/y revenue growth.

The y/y decline in gross profit was on the backdrop of faster increase in cost of sales (14.1%) and 331 bps contraction of gross margin (GM). FLOURMILL has reported lower gross margins in each of the two quarters of the current year, thus bringing GM over H1 to 11.9% (vs. 14.3% in H1-16/17). Given the relative stability of the naira in recent months, we would attribute the lower margins to price discounting (as in the case of sugar above) and unfavourable products mix.

Operating expenses increased by 12.6% y/y and 9.4% q/q, with the margins also rising by c.10 bps and 32 bps respectively. Admin expenses remain the driver of opex growth, although we note the slow growth from Q1's 52% (which management attributed to one-off charges). Increasing competition and the Apapa traffic situation are yet to reflect in marketing and distribution costs (-14% y/y).

Finance costs are higher by 31% y/y, but compared to Q1, they are lower by c.18%. While the y/y increase in finance costs reflects the still relatively higher gross debt (N188.2 billion vs. N155.4 billion), the continued q/q moderation mirrors the reducing debt balance since March ending 2017 (by 53.4 billion). Improved liquidity in the currency market and reduction in the tenor of CBN's forward contract to 2 months (previously 5 months) have enabled FLOURMILL reduce its LC-induced borrowings (-53% deposit for imports YTD).

Overall, declining revenue growth and weaker gross margin, amidst still high fixed financing and operating costs, in the absence of FX revaluation gains, portend risks to FLOURMILL's earnings. That said, we expect upward revision to 2018F estimates on higher annualized net profit of N17 billion, compared to consensus' N11.7 billion. Our estimates are under review.

HOLD

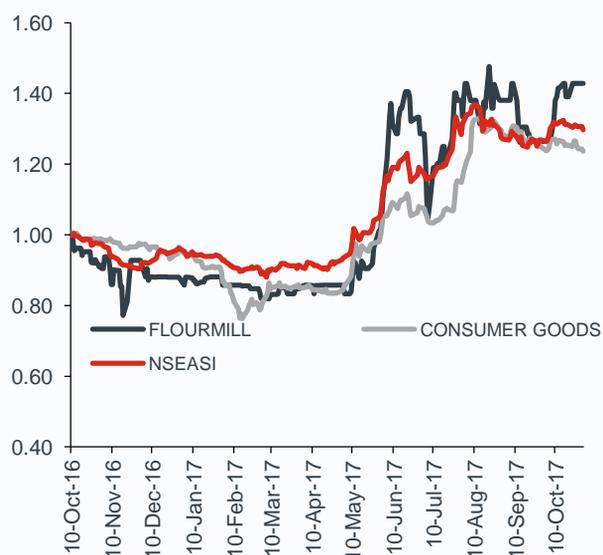
Target Price (N)	28.80
Current Price (N)	30.00
Implied Return (%)	-4.01

Company Data

NSE Code	FLOURMILL
Bloomberg Code	FLOURMILL:NL
Reuters Code	FLOURMILL.LG
Sector	CONSUMER GOODS
Market Cap. (N'bn)	78.73
Free Float (%)	47.82

Ratios	Q2-18	Q2-17	2017FY
Gross margin	12.23%	15.54%	12.72%
Opex margin	3.89%	3.79%	4.53%
EBIT margin	9.63%	6.04%	7.90%
PAT margin	3.23%	1.51%	1.68%
RoAE	10.18	-6.31%	7.83%
EPS (N)	1.63	0.64	3.03

Price movement (FLOURMILL vs. Benchmark Indices)



Source: NSE, Bloomberg, Cordros research

INCOME STATEMENT (N'bn)	30-Sep-17	30-Sep-16	% Δ	Q2 Sep 17	Q2 y/y	Q2 q/q	Q1 Jun 17	Q4-Mar 17	Q3 Dec 16	Q2 Sep 16
Revenue	298.44	255.30	16.9%	149.47	9.8%	0.3%	148.98	134.52	134.64	136.10
Cost of sales	-262.93	-218.88	20.1%	-131.19	14.1%	-0.4%	-131.74	-121.33	-117.57	-114.95
Gross profit	35.51	36.42	-2.5%	18.27	-13.6%	6.0%	17.24	13.19	17.07	21.15
S&D	-2.77	-2.94	-5.8%	-1.51	-14.1%	20.4%	-1.26	-0.91	-1.36	-1.76
Admin	-8.35	-6.21	34.5%	-4.30	26.4%	6.0%	-4.05	-8.38	-3.97	-3.40
Net operating gain/(loss)	5.08	-8.08	-162.8%	1.92	124.8%	-39.0%	3.15	10.27	-3.67	-7.76
EBIT	29.47	19.20	53.5%	14.39	74.9%	-4.6%	15.08	14.18	8.06	8.23
Finance costs	-16.27	-10.93	48.9%	-7.34	31.4%	-17.8%	-8.93	-14.83	-6.77	-5.59
Finance income	0.27	0.53	-48.3%	0.23	-18.9%	513.2%	0.04	0.84	0.20	0.29
PBT	13.48	8.80	53.1%	7.28	148.6%	17.6%	6.19	0.18	1.49	2.93
Taxation	-4.12	-2.33	76.7%	-2.46	181.6%	47.9%	-1.66	1.26	-0.56	-0.87
Profit/ (loss) from continued op.	9.36	6.47	44.6%	4.82	134.6%	6.4%	4.53	1.44	0.93	2.06
Profit for the year/period	9.34	6.46	44.4%	4.78	133.2%	4.9%	4.56	1.44	0.94	2.05
Profit to owners	8.33	5.85		4.27	155.0%	4.9%	4.07	1.40	0.71	1.67

RATIOS										
COS margin	88.10%	85.73%		87.77%			88.43%	90.19%	87.32%	84.46%
Gross profit margin	11.90%	14.27%		12.23%			11.57%	9.81%	12.68%	15.54%
OPEX margin	3.73%	3.58%		3.89%			3.56%	6.90%	3.96%	3.79%
Interest cover	1.81x	1.76x		1.96x			1.69x	0.96x	1.19x	1.47x
EBIT margin	9.88%	7.52%		9.63%			10.12%	10.54%	5.99%	6.04%
PBT margin	4.52%	3.45%		4.87%			4.16%	0.13%	1.11%	2.15%
PAT margin	3.13%	2.53%		3.23%			3.04%	1.07%	0.69%	1.51%
Tax	-30.58%	-26.50%		-33.77%			-26.84%	701.97%	-37.61%	-29.81%
EPS	3.17	2.23		1.63			0.15	0.53	0.27	0.64

Source: Company accounts, Cordros research estimates

Disclosures

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