Q1 2022: Flour Mills of Nigeria

Nigeria | Food Processing | Flour Mills of Nigeria   02 August 2021   **Equities**

Sailing through the Storm

Flourmills Nigeria Plc (FMN) released its Q1 2022 financial results showing a 51.2% y/y growth in Revenue to N233.73bn from N154.57bn in Q1 2021. The growth in Revenue was supported by growth across major business segments as Agro-Allied (Up 44.1% y/y to N47.69bn), Sugar (Up 24.0% y/y to N33.53bn) and Food (Up 61.4% y/y to N146.93bn) all recorded double digit growth in Q1 2022. Net Income was up 9.6% y/y to N5.44bn in Q1 2022 from N4.97bn in Q1 2021.

Going forward, while we forecast sustained Revenue growth across the company's major businesses, we expect the Food and Agro Allied businesses to be the growth drivers of the company's Revenue. The investment in B2C channels, launch of new discount-priced products and re-sizing of some products to lower SKUs are strategic moves that we expect to support Revenue in the near-term. That said, we forecast a Revenue growth of 6.8% y/y to N824.21bn in FY 2022. Similarly, we project a rise albeit marginal (up 1.8% y/y) in Net Income to N26.09bn in the period.

We raise our target price to N61.97/s from the N36.12/s previously, implying an 104.9% upside from Friday's closing price of N30.25/s. The increase in our target price was driven by a combination of the improving Net Income forecast, Revenue, and Cashflow outlook in the coming years – In summary the firm has significantly improved efficiency and we expect this to persist. Our valuation methodology is a single stage 5-Year Free Cash Flow to Firm (FCFF) model.

Growth across segments underlines topline performance

Based on the recently released scorecard in Q1 2022, Flourmills continued its trend of double-digit top-line growth (Up 51.2% y/y) to N233.73bn from N154.57bn in the corresponding period in 2021. This performance follows its FY 2021 performance, when Revenue grew significantly (Up 34.5% y/y) to N771.60bn amid a series of macro-economic headwinds. The Q1 2022 performance reflects the strategic efforts of the firm aimed at sustaining growth, as it continues to consolidate its position as a leading brand in the Nigerian consumer goods space. Growth was recorded across the food (up 61.4% y/y to N146.93bn), Agro-Allied (up 44.1% y/y to N47.69bn), Sugar (up 24.0% y/y to N33.53bn), and Support Services (up 63.3% to N5.56bn) segments of the business. The Agro-Allied segment continues to grow strongly, driven mainly by improved volume in the Edible Oil (up 9.0% y/y), and Fertilizer (up 16.0% y/y). We observe that despite volume growth, the company might be forced to hike prices on some of its products given the continued surge in the cost of input.

Material Cost pressures Gross Margin

Burdened by the continued surge in the cost of local input owing to logistics bottleneck and the foreign exchange pressure on its foreign input, Cost of Sales (adjusted for depreciation) grew 63.9% y/y to N202.83bn in Q1 2022 from N123.76bn in Q1 2021, outpacing Revenue growth of 51.2%. Material Cost which constitutes 92.1% of Cost of Sales was the main driver, up 77.8% in the period. Consequently,

Recommendation	**Buy**
Target Price	**N61.97**
Closing Price	**N30.25**

*Price as of 31 July

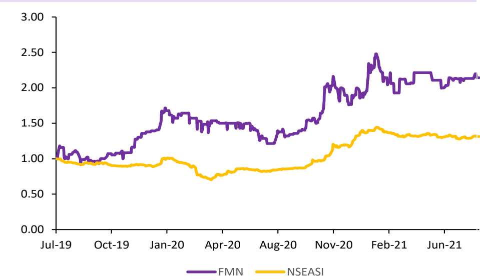
Key data

Year to March, Nbn

	2020	2021	2022e	2023e
Sales	573.8	771.6	824.2	869.1
EBITDA	57.1	76.3	74.6	98.5
Net Profits	11.6	25.6	23.3	38.5
EPS, N	2.86	6.03	5.45	9.17
PE Ratio	6.9x	3.3x	3.6x	2.1x
EV/EBITDA	2.9x	2.3x	2.4x	1.7x

Market cap.	N123.01bn (US$299.29m)
Free float	66.3%
Bloomberg	FLOURMIL NL
Reuters	FMNL.LG

Three-year graph



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Gross profit took a hit, up 0.2ppts to N30.87bn from N30.81bn in the corresponding of 2021 and Gross Margin shrank 6.7ppts to 13.2%.

Marketing and staff cost drive OPEX surge

Operating Expenses (adjusted for depreciation) also grew significantly (up 45.0% y/y to N8.92bn) in the period as the firm intensified its marketing campaign aimed at introducing its most recent products into the market. Selling and Distribution Expense grew 53.0% y/y to N3.06bn from N2.00bn in Q1 2021. Administrative Expenses also grew strongly, spurred by a significant rise (73.0%) in salary, wages and other staff costs which increased to N5.86bn from N4.15bn in Q1 2021. Consequently, the firms Earnings Before Interest Tax, Depreciation and Amortization declined 11.0% y/y to N21.95bn, resulting in an EBITDA Margin of 9.4%, down from 16.0% in the corresponding period of 2021.

Net-Profit growth reflects pro-active debt management

Net Finance Cost continued to decline (down 6.2% y/y to N4.25bn), as the firm's strategic move to restructure its debt portfolio in 2021 continues to yield result. Both Finance Income (down 9.5% y/y to 0.28bn) and Finance Costs (down 6.4% y/y to N4.55bn) declined in the period, but the quantum of decline in Finance Costs outweighed the decline in Finance Income leaving the firm in a favourable Net Finance Income position. This supported an improvement in Pre-tax Profit (up 12.5% y/y) to N7.26bn from N6,45bn in Q1 2022. Nonetheless, pressured by the weight of a 22.3% y/y growth in Tax Expense, Net Profit grew moderately to N5.44bn from N4.97bn in the corresponding period of the 2021 accounting year.

Q1 2022, Nm

Nm, except where mentioned otherwise	Q1'22	Q1'21	y/y
Revenue	233,703	154,579	51.2%
Cost of Sales (Ex-Dep)	(202,829)	(123,759)	63.9%
Gross Profit	**30,874**	**30,819**	**0.2%**
Administrative Expenses (Ex-Dep)	(5,861)	(4,152)	41.2%
Selling and Distribution Expenses (Ex-Dep)	(3,062)	(2,001)	53.0%
EBITDA	**21,951**	**24,666**	**-11.0%**
Depreciation and Amortization	(5,911)	(6,033)	-2.0%
Operating Profit	**16,040**	**18,633**	**-13.9%**
Net Operating Gains & Losses	(4,525)	(7,643)	n/a
EBIT	**11,515**	**10,991**	**4.8%**
Net Finance Cost	(4,253)	(4,535)	-6.2%
Profit before tax	**7,261**	**6,455**	**12.5%**
Tax expense	(1,815)	(1,485)	22.3%
Net Profit	**5,446**	**4,971**	**9.6%**
Net income attributable to equity holders	**5,446**	**4,960**	**9.8%**
Earnings Per Share	**1.33**	**1.21**	**9.8%**
No of Outstanding Shares	4,100	4,100	
Margins:	**Q1'22**	**Q1'21**	**y/y**
Gross margin	13.2%	19.9%	-6.7ppts
EBITDA Margin	9.4%	16.0%	-6.6ppts
PBT Margin	3.1%	4.2%	-1.1ppts
Net margin	2.3%	3.2%	-0.9ppts

Source: Company, CSL Research.

Outlook and Forecasts

Growth drivers remain Agro-Allied & Sugar

Flour Mills has continued to leverage the current momentum to good effect, seen in the company's recent innovative ideas to meet consumers' need. We have seen the resizing of some ball food products (e.g., Semovita) to lower SKUs at lower price points, introduction of new products (Golden Penny jollof noodles, Golden Penny goat meat pepper soup Noodles, Golden Penny garri & damavita sorghum flour etc.)

at discount price points. Further investment in improving B2C channels has also contributed to Revenue growth recovery in the Food business. Agro-Allied also has continued to record decent performance.

We see Food and Agro-Allied businesses as the Revenue growth drivers for FY 2022. The Agro-Allied business has benefitted from the increased traction from B2C channels. We forecast Food, Sugar & Agro-Allied Revenue growth of 8.0%, 5.0% and 10.0% respectively. Overall, we forecast Revenue growth of 6.8% y/y to N824.21bn in FY 2022.

Shrinking Margin to persist

Over the past eighteen (18) months, Flour Mills has continued to invest in restructuring its businesses and improving production processes. The company is now focused on improving the proportion of locally sourced raw materials in its raw material mix. The continued surge in Cost of Input both local and imported however, continues to pressure margins. That said, we note the recent directive by of the CBN allowing only three sugar refining companies, with considerable progress in achieving an agreed backward integration plan to source FX from the official window, to import sugar into the country would create some support in an otherwise unstable FX environment. In this light, we forecast a 1.4ppts contraction in Gross margin leading to a 1.9% decline in Gross Profit to N125.19bn in FY 2022.

Operating Expenses to weigh on profitability

We anticipate the company's Operating Costs will continue to rise, following rising local prices, and the firm's quest to increase awareness of its products. We however expect this to be under control relative to peers, given the firm's conscious efforts at taming expenses. Consequently, we model Operating Expenses growth rate of 19.4% y/y (excluding Receivables Impairment Charges). We forecast a reduction in other operating loss. As a backdrop, we forecast 1.9% y/y and 4.4% y/y decline in EBITDA and Operating Profit to N74.81bn and N50.48bn respectively in the period.

Restructured debt book to support profit growth

Flour Mills took a huge step in tapering its Finance Cost in FY 2021 issuing long term bonds at single-digit rates. As a result, the firm's debt mix is tilted towards longer and cheaper debts which now constitute 78% of total debt mix, driving down Interest Expense at the end of Q1 2022. The upcoming repayment of bonds totaling N11.00bn by the firm leaves room for an improved loan book, which should ultimately result in lower Interest Expense. In this light, we project a marginal (down 2.3% y/y) decline in Interest Expense to N18.22bn in FY 2022 while we expect the improved yield environment alongside the robust cash flow of the firm to jointly support Investment Income. Consequently, we forecast Net Finance Cost would decline by 8.4% y/y.

Valuation: Despite a higher Cost of Equity, we retain a BUY on the stock

We raise our target price to N61.97/s from the N36.12/s previously, implying a 104.9% upside from current market price of N30.25/s. In addition, we anticipate a sustained Revenue growth and Profits over our forecast years. Our valuation methodology is a Single stage 5-Year FCFF model.

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March year-end; Nm (unless otherwise stated)

Income Statement	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**	**2025E**
Revenues	542,670	573,774	771,608	824,211	869,088	913,938	959,918
Cost of Sales*	(459,082)	(487,944)	(643,245)	(698,542)	(734,060)	(772,270)	(811,468)
Gross Profit	**83,588**	**85,831**	**128,363**	**125,668**	**135,028**	**141,668**	**148,450**
Operating Expenses (Opex)*	(23,493)	(33,597)	(36,568)	(46,156)	(45,193)	(47,525)	(49,916)
EBITDA	**66,038**	**57,139**	**76,266**	**74,567**	**98,526**	**103,283**	**108,133**
Depreciation and Amortisation	(17,615)	(22,060)	(24,070)	(24,036)	(25,129)	(26,281)	(27,491)
Other Income	-	-	-	-	-	-	-
EBIT	**48,423**	**35,080**	**52,197**	**50,531**	**73,397**	**77,002**	**80,643**
PBT before exceptional items	16,542	17,497	37,194	33,224	55,021	58,075	61,992
Exceptional items	-	-	-	-	-	-	-
PBT	**16,542**	**17,497**	**37,194**	**33,224**	**55,021**	**58,075**	**61,992**
Taxation	(2,926)	(5,877)	(11,568)	(9,967)	(16,506)	(17,422)	(18,598)
Net Profits	**13,616**	**11,620**	**25,626**	**23,257**	**38,515**	**40,652**	**43,394**
Minority interest	940	(108)	909	909	909	909	909
EPS, N	4.83	2.86	6.03	5.45	9.17	9.69	10.36
DPS, N	1.00	1.20	1.40	2.73	4.59	4.85	5.18
Payout ratio	21%	42%	23%	50%	50%	50%	50%
Dividend sum	2,624	4,920	5,741	11,174	18,803	19,872	21,243
Number of shares outstanding, m	**2,624**	**4,100**	**4,100**	**4,100**	**4,100**	**4,100**	**4,100**

**Cost of Sales and Opex adjusted for Depreciation and Amortisation*

Balance Sheet	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**	**2025E**
Fixed Assets	217,901	216,890	208,721	210,906	204,892	198,802	192,612
Investments	1,864	1,661	1,560	1,580	1,499	1,418	1,337
Intangible Assets	1,095	954	646	587	220	-147	-515
Long Term Debtors and Prepayments	944	359	39	39	39	39	39
Non-Current Assets	**234,102**	**242,722**	**238,729**	**254,711**	**246,989**	**239,015**	**230,752**
Stocks	111,373	115,596	195,449	209,563	220,218	231,681	243,440
Debtors and Prepayments	-	-	-	-	-	-	-
Amount Due From Related Companies	-	-	-	-	-	-	-
Cash and Cash Equivalents	22,245	26,211	37,163	16,205	31,523	37,944	50,951
Current Assets	**174,246**	**189,732**	**306,005**	**292,703**	**322,266**	**343,738**	**372,183**
Total Assets	**408,348**	**432,454**	**544,734**	**547,413**	**569,255**	**582,753**	**602,935**
Trade Creditors	56,994	83,614	120,152	118,752	117,450	108,118	105,491
Current Portion of Loan Term	103,923	23,344	26,913	24,008	24,764	25,214	25,359
Other Creditors and Accruals	-	-	-	-	-	-	-
Amount Due to Related Companies	-	-	-	-	-	-	-
Current Portion of Bond	-	2,654.09	1,919.72	1,919.72	1,919.72	1,919.72	1,919.72
Taxation	3,151	5,531	9,482	9,482	9,482	9,482	9,482
Dividend Payable	2,006	3,985	4,208	4,208	4,208	4,208	4,208
Bank Overdraft	19,934	5,543	4,001	4,001	4,001	4,001	4,001
Total current liabilities	**199,788**	**148,758**	**209,697**	**205,392**	**204,844**	**195,963**	**193,481**
Non-current liabilities	**70,844**	**127,888**	**160,424**	**143,780**	**146,457**	**148,056**	**148,568**
Total Liabilities	**270,632**	**276,646**	**370,121**	**349,171**	**351,302**	**344,019**	**342,049**
Share Capital	2,050	2,050	2,050	2,050	2,050	2,050	2,050
Share Premium	75,377	75,377	75,377	75,377	75,377	75,377	75,377
Capital Reserve	- 72.56	- 113.02	- 107.92	- 113.02	- 113.02	- 113.02	- 113.02
Retained Earnings	67,904	71,630	90,906	82,804	101,607	121,478	142,721
Minority Interest (MI)	5,358	6,863	6,389	7,772	8,681	9,590	10,500
Shareholders' funds (Ex MI)	**145,259**	**148,944**	**168,225**	**160,118**	**178,921**	**198,793**	**220,035**

Cash Flow Statement	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**	**2025E**
Operating Cash Flow	84,592	67,578	35,477	65,511	82,978	78,900	90,069
Investing Cash Flow	(17,832)	(24,989)	(13,793)	(15,699)	(15,832)	(16,788)	(17,189)
Financing Cash Flow	(56,182)	(42,012)	(39,841)	(24,182)	(35,322)	(38,268)	(41,275)
Free Cash Flow	**63,194**	**41,355**	**19,260**	**50,675**	**67,335**	**62,449**	**72,790**

Source: Company, CSL estimates

FMN

Profitability Ratios	2019	2020	2021	2022E	2023E	2024E	2025E
Gross Profit Margin	15.4%	15.0%	16.6%	15.2%	15.5%	15.5%	15.5%
EBITDA Margin	12.2%	10.0%	9.9%	9.0%	11.3%	11.3%	11.3%
Operating Profit Margin	8.9%	6.1%	6.8%	6.1%	8.4%	8.4%	8.4%
PBT Margin	3.0%	3.0%	4.8%	4.0%	6.3%	6.4%	6.5%
Net Profit Margin	2.5%	2.0%	3.3%	2.8%	4.4%	4.4%	4.5%
ROAA	3.1%	2.8%	5.2%	4.3%	6.9%	7.1%	7.3%
ROCE	19.6%	17.9%	26.6%	24.4%	35.3%	35.4%	35.4%
ROAE	11.2%	7.9%	16.2%	14.2%	22.7%	21.5%	20.7%
Dividend Yield	5.1%	6.1%	7.1%	13.9%	23.3%	24.7%	26.4%
Opex/Sales	4.2%	5.3%	5.0%	5.6%	5.2%	5.2%	5.2%

Activity Ratios	2019	2020	2021	2022E	2023E	2024E	2025E
Total Asset Turnover	1.2x	1.4x	1.6x	1.5x	1.6x	1.6x	1.6x
Fixed Asset Turnover	2.5x	2.6x	3.6x	3.9x	4.2x	4.5x	4.9x
Current Asset Turnover	2.5x	3.2x	3.1x	2.8x	2.8x	2.7x	2.7x
Inventory Turnover	4.0x	4.3x	4.1x	3.4x	3.4x	3.4x	3.4x
Cash Turnover	16.1x	23.7x	24.4x	30.9x	36.4x	26.3x	21.6x

Liquidity Ratios	2019	2020	2021	2022E	2023E	2024E	2025E
Current Ratio	0.9x	1.3x	1.5x	1.4x	1.6x	1.8x	1.9x
Quick Ratio	0.2x	0.3x	0.3x	0.3x	0.3x	0.4x	0.5x
Cash Ratio	0.1x	0.2x	0.2x	0.1x	0.2x	0.2x	0.3x

Solvency Ratios	2019	2020	2021	2022E	2023E	2024E	2025E
Net Debt-to-Equity Ratio	90%	58%	58%	62%	49%	42%	32%
Debt-to-Capital Ratio	50%	42%	44%	41%	39%	37%	34%
Debt-to-Equity Ratio	102%	72%	77%	69%	63%	58%	53%
Debt-to-Assets Ratio	38%	26%	25%	21%	21%	21%	20%
Leverage	2.7x	2.8x	3.1x	3.3x	3.0x	2.8x	2.6x

Valuation Multiples	2019	2020	2021	2022E	2023E	2024E	2025E
EV / Sales	0.3x	0.3x	0.2x	0.2x	0.2x	0.2x	0.2x
EV / EBITDA	2.8x	2.9x	2.3x	2.4x	1.7x	1.6x	1.4x
EV / EBIT	3.8x	4.7x	3.4x	3.6x	2.3x	2.1x	1.9x
EV / CE	0.6x	0.6x	0.6x	0.6x	0.5x	0.5x	0.4x
Price to Earnings	4.1x	6.9x	3.3x	3.6x	2.1x	2.0x	1.9x
Price to Book Value	0.3x	0.5x	0.5x	0.5x	0.4x	0.4x	0.3x
Earnings Yield	0.2x	0.1x	0.3x	0.3x	0.5x	0.5x	0.5x

Y/y growth	2019	2020	2021	2022E	2023E	2024E	2025E
Revenues	3%	6%	34%	7%	5%	5%	5%
Gross Profit	5.2%	2.7%	49.6%	-2.1%	7.4%	4.9%	4.8%
Distribution and Selling Expenses	15.7%	50.1%	30.2%	9.2%	5.4%	5.2%	5.0%
Administrative Expenses	3.6%	28.3%	24.6%	24.0%	-5.1%	5.2%	5.0%
EBITDA	16.7%	-13.5%	33.5%	-2.2%	32.1%	4.8%	4.7%
EBIT	16.9%	-27.6%	48.8%	-3.2%	45.3%	4.9%	4.7%
PBT	57.9%	5.8%	112.6%	-10.7%	65.6%	5.5%	6.7%
Net Profits ex. MI	54.1%	-14.7%	120.5%	-9.2%	65.6%	5.5%	6.7%
EPS	59.2%	-40.8%	110.7%	-9.6%	68.3%	5.7%	6.9%
DPS	0.0%	20.0%	16.7%	94.6%	68.3%	5.7%	6.9%

Source: Company, CSL estimates

Analyst Certification

Each research analyst(s) principally responsible for the preparation and content of all or any identified portion of this research report hereby certifies that all of the views expressed in this research report accurately reflect their personal views about those issuer(s) or securities that the research analyst covers in this research report. Each research analyst(s) also certify that no part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this research report.

Important disclosures

Ratings and Target Price History

Flour Mills Nigeria

Date	Price (N)	Old Target (N)	New Price Target (N)	Old recommendation	New recommendation
19-Dec-13	86.6	106.3	106.3	Buy	Buy
24-Jan-14	88.0	106.3	106.3	Buy	Buy
10-Feb-14	83.1	106.3	106.3	Buy	Buy
27-Aug-14	68.1	106.3	106.3	Buy	Buy
2-Dec-14	45.3	106.3	54.8	Buy	Hold
4-Feb-15	38.0	54.8	54.8	Hold	Hold
11-Jun-15	35.0	54.8	40.7	Hold	Hold
10-Feb-16	19.0	40.7	16.6	Hold	Hold
8-Aug-16	22.0	16.6	15.8	Hold	Sell
1-Feb-17	18.0	15.8	24.9	Sell	Buy
2-Nov-17	33.7	24.9	30.8	Buy	Hold
15-Jan-18	33.4	30.8	36.7	Hold	Hold
12-Jul-18	30.8	36.7	40.8	Hold	Buy
28-Jan-19	19.5	40.8	28.7	Buy	Hold
6-Feb-19	18.5	28.7	26.4	Hold	Hold
26-Nov-19	18.20	26.4	23.7	Hold	Buy
24-Feb-20	23.00	23.7	25.9	Buy	Buy
21-Sep-20	19.65	25.9	36.1	Buy	Buy
2-Aug-21	30.25	36.1	61.9	Buy	Buy

CSL Research Ratings Distribution

	BUY	HOLD	SELL	Not Rated	Total
Coverage universe	16	11	3	3	33
% distribution	48%	33%	9%	9%	
Investment banking clients	0	1	1	0	2
% distribution	0%	50%	50%	0%	

Explanation of CSL Research's equity research rating system

Buy:	The analyst expects the stock to outperform the Benchmark over the next 12 months or the stated investment horizon.
Hold:	The analyst expects the stock to perform in line with the Benchmark over the next 12 months or the stated investment horizon.
Sell:	The analyst expects the stock to underperform the Benchmark over the next 12 months or the stated investment horizon.
Not Rated:	The rating and price target have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when FCMB Bank UK or the Group is acting in an advisory capacity in a merger or strategic transaction involving the company or due to factors which limits the analysts ability to provide forecasts for the company in question.
Benchmark:	The benchmark is the trailing three-year average yield of the 12-month T-Bill plus one standard deviation rounded to the nearest percent.
Price targets:	Price targets, if discussed, reflect in part the analyst's estimates for the company's earnings. The achievement of any price target may be impeded by general market and macroeconomic trends, and by other risks related to the company or the market and may not occur if the company's earnings fall short of estimates.
Asset allocation:	Asset allocation is the responsibility of the strategy team. The recommended weight (Buy, Hold and Sell) for equities, cash and fixed income instruments is based on a number of metrics and does not relate to a particular size change in one variable.

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