August, 2015

Flour Mills Nig. Plc

We rate the counter **BUY**

Flourmill of Nig Plc ("FMN" or "the company") full year result 2015 showed a 5.25% y/y decline in revenue with a 5-year revenue CAGR of 7% (2011-2015). Whilst full year post-tax profit was up 57.66% y/y, it was a direct benefit from gains on partial disposal of the company's investment in UNICEM. Earnings Per Share therefore rose 80% y/y to its current level at N3.47 from N1.93 for FY2014.

- FMN is one of Nigeria's leading food and agro allied companies. Its primary businesses includes flour milling, production of pasta, noodles, edible oils and refined sugar, production of livestock feeds, farming and other agro-allied downstream activities, operation of terminal A and B at apapa port and recently branched into real estate investment.
- The company currently processes 140,000 metric tonnes of imported bulk brown rice and has commenced two rice growing projects in Niger state to supplement the raw material supply, in addition to a 4,500 hectare rice farm along the Niger River basin which will add to the rice production at Sunti rice farm.
- During the year, FMN introduced new products to the market and increased current production capacity through the commissioning of new mills in Apapa and Calabar and completion of upgrades on older mills (milling capacity of its subsidiary Niger Mills ,Calabar to 750MT per day).

Income Statement - Ratios

	FY'15	FY'14	Change
Gross Margin (%)	11.45	11.45	0.00%
Net Margin (%)	2.74	1.65	66.06%
EPS (Kobo)	3.47	1.93	79.79%

Source: NSE, Planet Capital Research

Balance Sheet - Ratios

	FY'15	FY'14	Change
Equity Multiplier (x)	3.92	3.55	10.42%
Asset Turnover (x)	0.90	1.10	(18.18%)
Debt/Equity (x)	2.16	2.60	(16.92%)
P/S	0.22	0.29	(24.13%)
P/E	7.29	20.31	(64.10%)
P/B	0.76	1.12	(32.14%)
PEG	0.32	-0.64	150.00%
ROE (%)	9.68	6.42	3.26
ROA (%)	2.47	1.81	0.66
Div Yield (%)	8.30	5.36	2.94

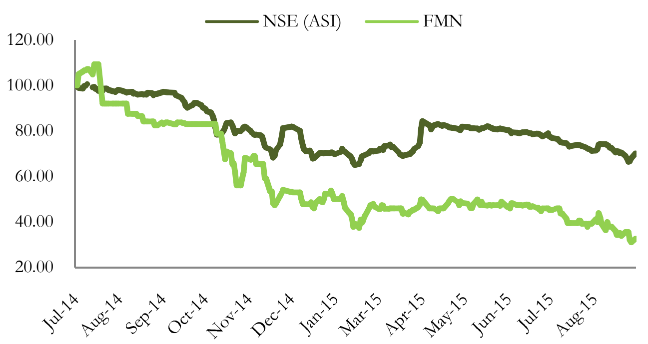
Source: NSE, Planet Capital Research

Stock Data

Ticker Symbol	
Full year end	March
52-week range	N24.15-N73.28
Price Mov'tYtD	(38.39%)
Average daily vol./val (Mn)	1.44/N55.26
Outstanding Share (Mn)	2,624.23
Market Cap.(N'm)	63,375.32
EPS (Kobo)	347
DPS(Kobo)	210

Source: Bloomberg, Planet Capital Research

Share Price 52 wk Movement (NSE vs. FMN)



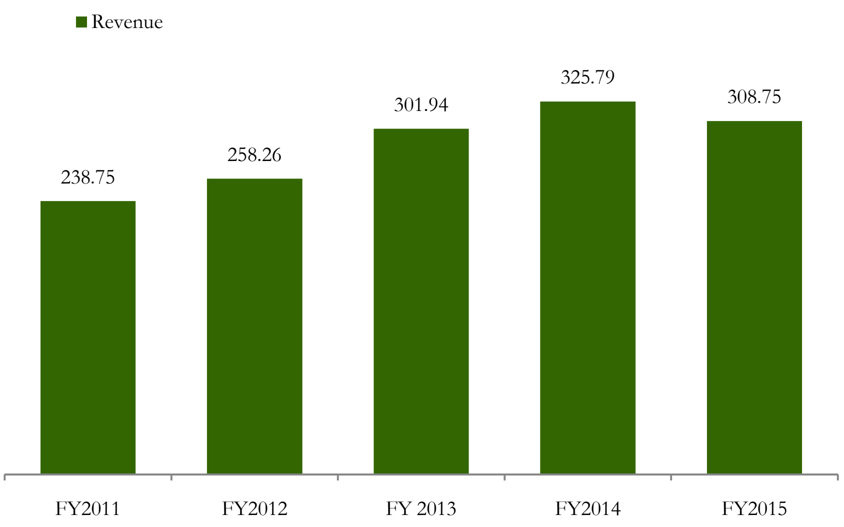
- A new range of products called “snacks” was successfully launched and the company commissioned an ultra-modern fully integrated edible oil refinery and margarine plant with installed capacity of 350,000 MT per annum, processing vegetable and soya oil products, as well as margarine.

Income Statement			
Revenue (N'm)	308,756.52	325,790.18	(5.23%)
Operating Profit (N'm)	10,215.76	13,022.80	(21.55%)
PAT (N'm)	8,463.06	5,367.87	57.66%

- In the core bread flour market, the company continues to maintain its market leadership despite price based competition. Wheat grinding capacity increased to over 8,000MT per day, while sugar refinery capacity increased to 750,000metric tonnes per annum to match demand as products serve both business-to-business and business-to-consumer customers.

- **Core segment slowed revenue** – Revenue fell 5.2% y/y to N305.75billion, compared with N325.79billion in FY2014. Decline in revenue was due to a 6.08% y/y and 12.21% y/y decrease in Foods and Agro-Allied respectively. These segments accounted for 77.10% and 16.37% respectively of the group’s total revenue in FY 2015, down from 77.80% and 17.67% in FY 2014.

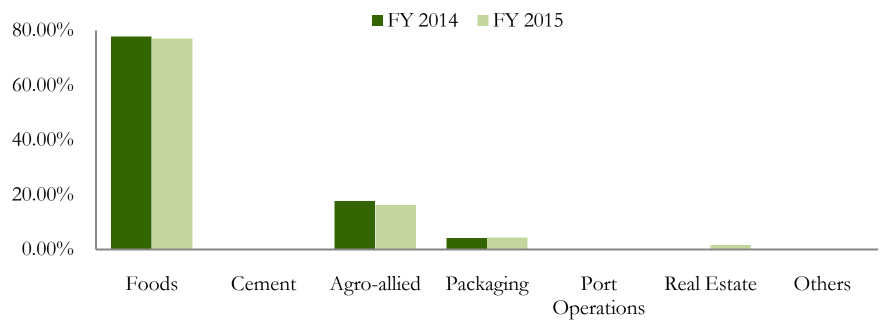
Revenue (N’billion)



- Growth from animal and aqua feed business was partly offset by lower revenue coming from fertilizer and rice. The contribution of packaging and real estate to total revenue increased to 4.51% and 1.73% from 4.17% and 0% in FY2014.

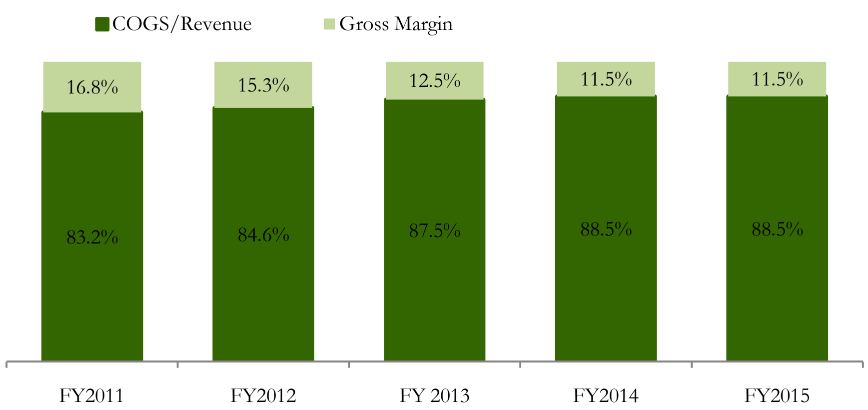
- The Company experienced a slowdown in the volume of its core business in Apapa, Iganmu and Agbara as a result of power issues arising from prolonged interruptions to gas supply, coupled with difficult logistics at apapadue to severe traffic congestions which hindered product evacuation by customers.

Revenue by Business Segments (%)



- COGS to sales ratio remains high in line with historical levels, stabilizing at 88.55% same as the prior year. FMN incurred higher input costs due toForeign Exchange losses from currency devaluation during the period as the company relies on imported raw materials for business.This was partly offset by an increase in selling price and lower commodity costs (global price of raw materials such as wheat softened in the year). The 5.23% y/y decline in COGS can be attributed to dwindling sales as it is a direct variable cost. Hence, gross profit margin remained at 11.45% same as prior year, with gross profit of N35.36billion, a decline of 5.19% y/y.

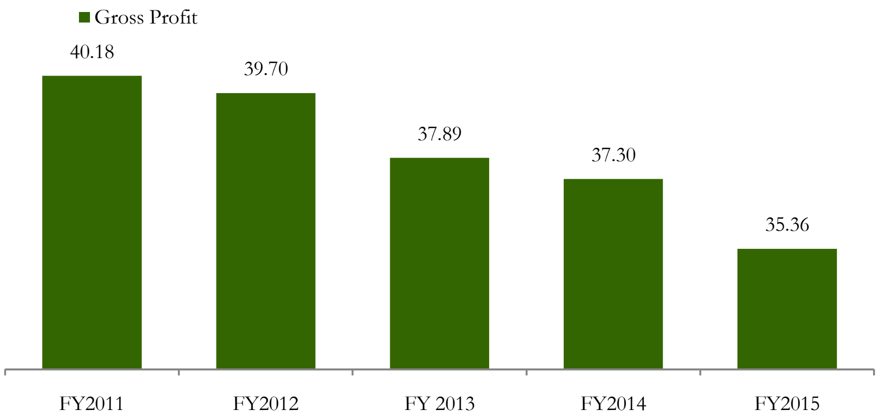
Yearly COGS/revenue ratio and Gross margins



- The AGRO ALLIED business operating environment is characterized by volatile commodity prices arising from unpredictable changes in global supply and demand in addition to limited access to foreign exchange and excessive tariffs, the combination of which have made reliance on imported raw materials for food processing facilities risky, expensive and unsustainable. The group is currently embarking on strategies to reduce dependence on imported raw materials thereby strengthening operating margins.

- FMN recently commissioned a large automated animal feed mill plant at Ibadan with an installed capacity of 370,000MT per annum with plans to expand the animal feed business using soybean meal and maize from its agricultural operations. The company is also pursuing the backward integration program for sugar, by cultivating 10,000 hectares of sugar cane at Sunti farm in Niger state using an agro allied subsidiary.

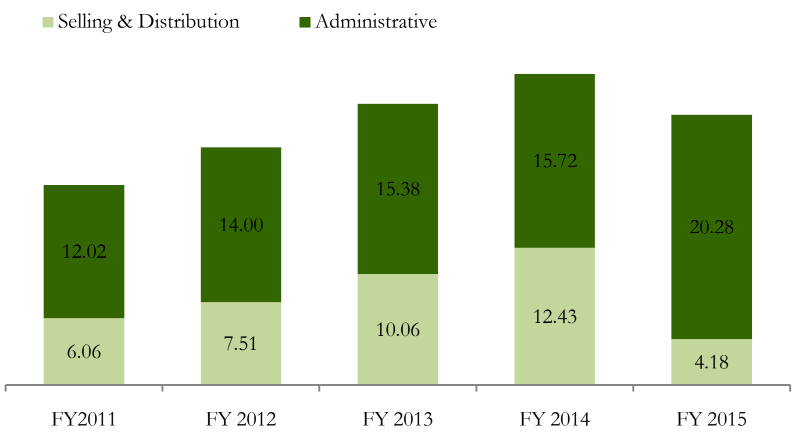
Gross Profit 5-year Trend (N'billion)



- Operating expenses declined 13.10% y/y to N24.46billion from N28.15billion in prior year, driven by a 66.35% decrease in selling & distribution expenses to N4.18billion from N12.43billion in the previous year. However, Administrative expensescame in higher by 29.01% to N20.28billion from N15.72billion in FY 2014.

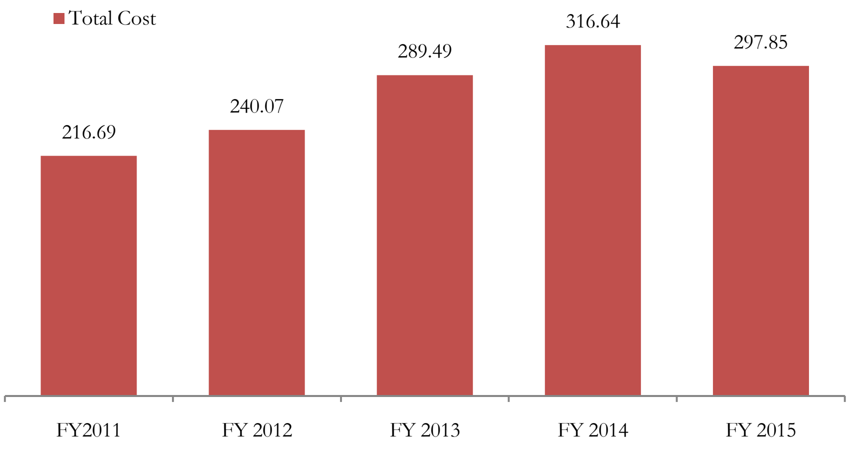
- The operating expense structure shows that a higher proportion of the firm's running costs are allocated to administrative expenses compared to selling & distribution expenses. In FY 2015, administrative expenses accountedfor 83% of opexwhile selling & distribution covered 17% of operating expenses. During the previous financial year, both expense heads accounted for 56% and 44% respectively.

Admin, Selling and distribution expenses (N'billion)



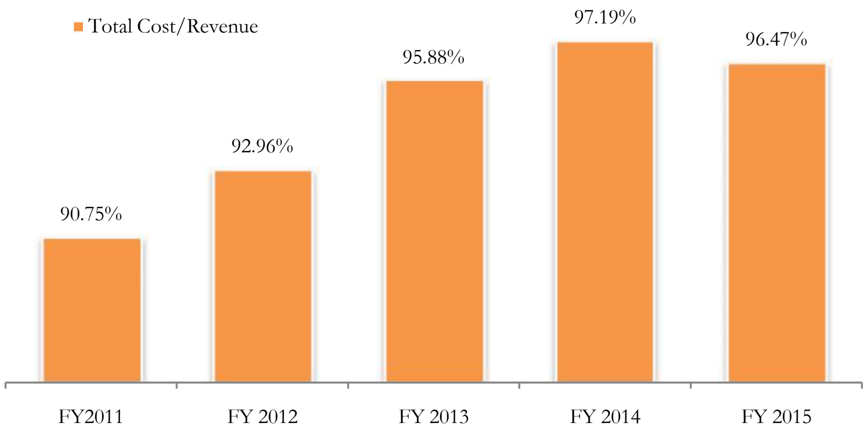
- We are of the opinion that the rise in admin.expenses is reflective of FMN's increasing personnel costs on the back of increased demand for labour, necessitated by the company's on-going expansion drive whereas declining selling and distribution expenses is reflective of the firm's improving supply chain/access to markets, and improvement in internal efficiencies

Cost profile (N'billion)



- Overall, total costs decreased 5.93% to N297.85billion from N316.64billion in FY2014. Consequently, the ratio of total cost to revenue stood at 96.47% in FY2015 down from 97.19% in FY2014. This implies that 96.47% and 3.53% of sales revenue translates to cost and profitability respectively.

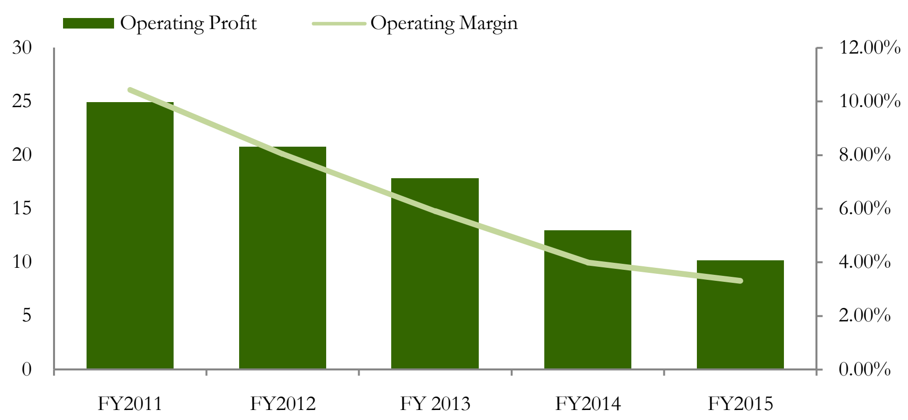
Total Cost/Revenue ratio



- FMN plans to commence a scheme of mergers with its listed subsidiaries; Golden Noodles Nigeria Ltd, Golden Transport Company Ltd, New Horizon Flour Mills Ltd and Quilvest properties Ltd (a real estate and property mgt). The enlarged FMN, upon completion of the restructuring would be able to streamline operations, reduce administrative costs, improve operating efficiency and derive the full benefits of synergy in line with the company's long term strategic objectives.

- Operating profit declined by 21.55% y/y to N10.21billion in FY 2015 from N13.02billion in FY 2014, shrinking operating margin to 3.31% from 4.00% in FY2014. Income realized from non-core business activities (other income) declined 117.68% to (N685.05million) from N3.87billion in prior year whileinvestment income declined 54.18% y/y to N2.30billion for FY2015 from N5.02billion in the previous year.

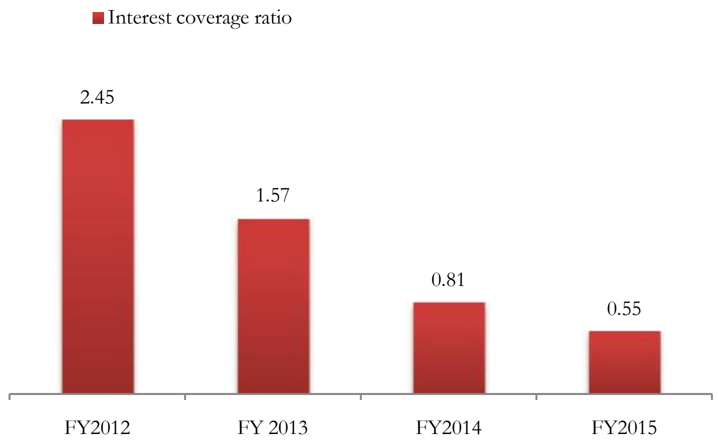
Operating Profit and Margin



- Finance cost increased 16.16% y/y to N18.7billion from N16.10billion, while interest coverage ratio dropped to 0.55x from 0.81x in FY2014. Borrowing costs are of particular concern and have remained relatively high with the average premium lending rate inching a little to 16.9% at the end of Q1,2015 (16.7% in March, 2014).

- The major expansion programmes and strategic acquisition FMN embarked on in the last five years were debt financed. The latter stage of the expansion coincided with the sudden slump in global crude oil prices which resulted in major devaluation of the Naira leading to increase in financial charges.

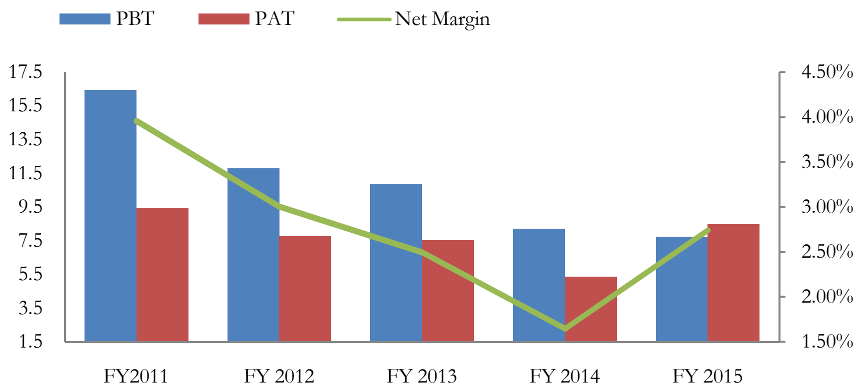
Interest Coverage



- To reduce the company's debt burden, lower interest charges and augment working capital, FMN plans to raise tier 1 capital via a right issue of N30billion. Inflow from the second phase of UNICEM disposal worth N26billion will also be used to pay off existing debts and lower interest charges which will boost earnings numbers going forward. Notwithstanding, we did not considerthis in our forecast for FY 2016 as this is an exceptional line item.

- Profit before tax declined 6.12% to N7.72billion from N8.22billion reported in FY2014. However, Profit after Tax increased 57.66% to N8.46billion from N5.67billion in FY2014; the gain of N14.28billion from partial disposal of UNICEM rescued the company from a loss position of N5.5billion to profitability. As a result, net margins increased by 1.09% to 2.74% from 1.65% in FY 2014.

PAT, PBT and Net Margin

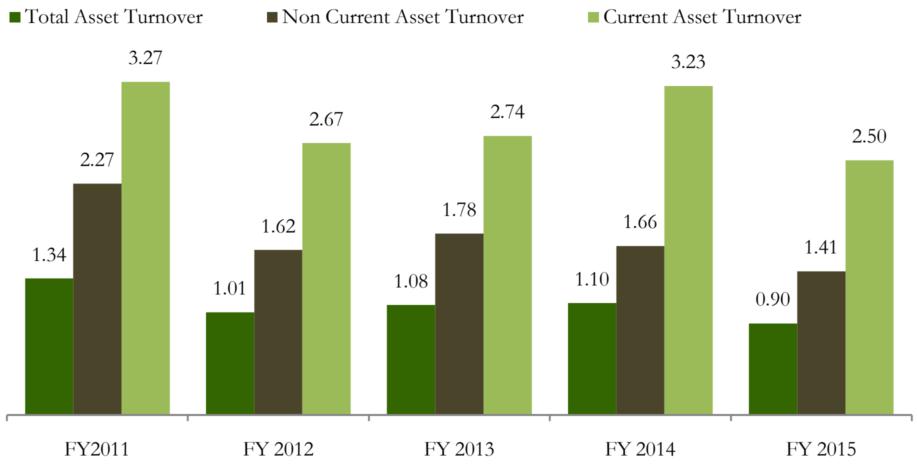


- The recent devaluation of the naira following the sharp drop of crude oil prices negatively impacted on the group's financial performance with an exchange loss of N5.1billion. We are of the opinion that when finance cost is significantly reduced, the profitability performance of FMN will also improve.

Balance Sheet Analysis

- FMN's statement of financial position as at March, 2015 revealed an increase of 11.45% in non-current assets to N219.24billion from N195.71billion in FY2014. It was driven by a 23.42% increase in Property, Plant and Equipment (PPE) to N208.94billion from N169.28billion in FY2014. Investment in associates declined 100% to N0.00 from N7.79billion while current assets increased 22.57% y/y to N123.60billion from N100.84billion in FY2014. Hence, total asset rose by 15.56% y/y to N342.84billion from N296.67billion in FY 2014.
- Fixed asset turnover reduced to 1.41x from 1.66x in FY2014; current asset turnover declined to 2.50x in FY2015 from 3.23x in FY 2014. Overall, total asset turnover declinedto 0.90x from 1.10x in FY2014. Deteriorating asset turnover implies that asset utilisation is less efficient compared to the prior year.

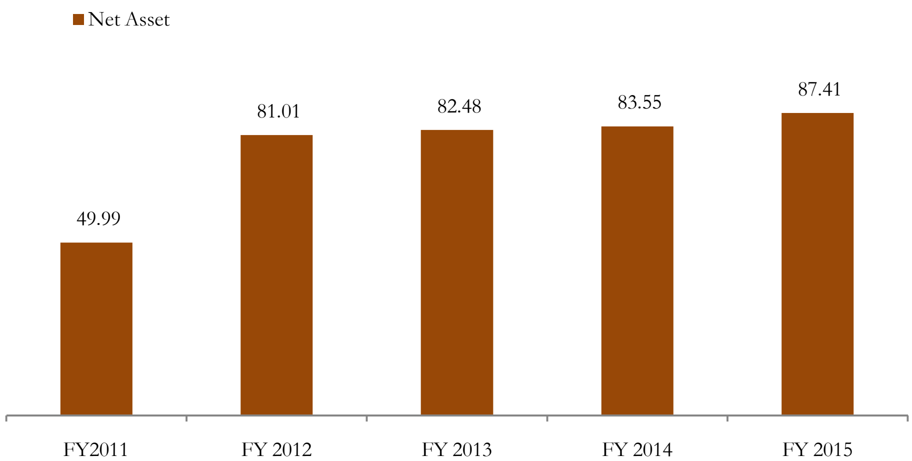
Asset Turnover; Non-current, current and Total Assets



- Cash and Cash equivalents grew 85. 03% to N31.13billion in FY 2015 from N 16.82billion in FY2014. However, trade and other receivables came in lower by 10. 99% while inventories increased 7.45% in FY2015 to N68.42billion in prior year.

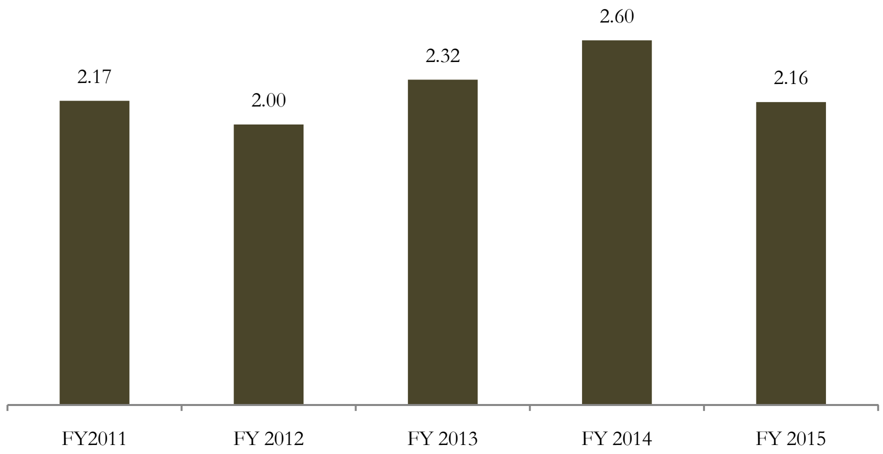
- Total liabilities declined 8.38% y/y to N255.43billion from N278.78billion in FY2014. Non-current liabilities fell by 49.23% y/y to N76.22billion from N150.12billion in FY 2014 while current liabilities increased 39.29% y/y to N179.21billion from N128.65billion in the previous year. Consequently, net assets increased marginally by 4.61% to N87.41billion from N83.55billion in FY 2014.

- **Net Assets (N'billion)**



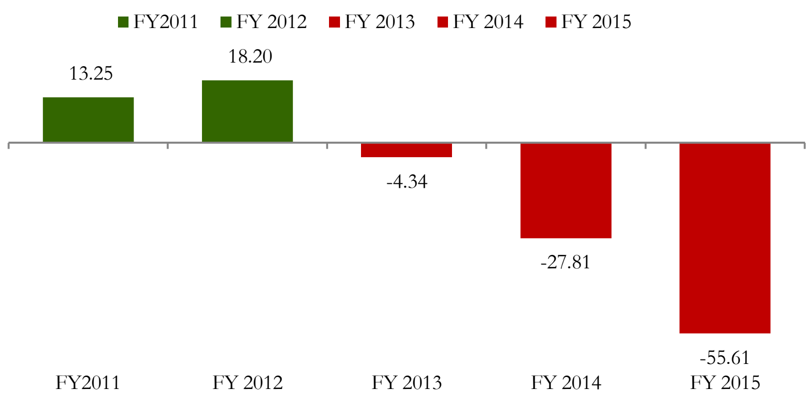
- The company's debt to equity ratio increased to 2.16x in FY2015 from 1.82x in the prior year and still remains below peer average of 3.26x. Total debt rose 24.01% y/y to N188.49billion from N151.96billion in FY2014. However, long-term debt declined 15.11% y/y to N55.26billion from N65.09billion in FY'14; total debt to asset ratio increased to 0.55x from 0.51x in FY 2014 compared to industry average of 0.39x.

Debt/Equity Ratio



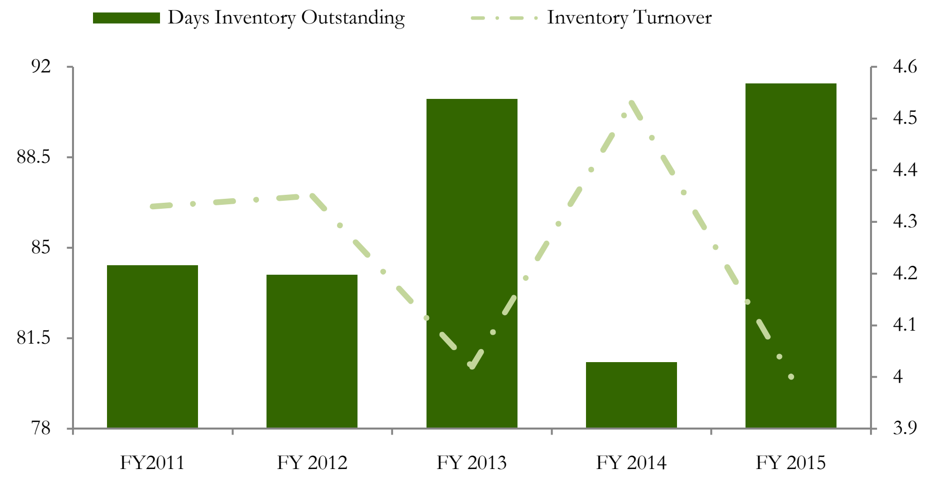
- FMN Nig Plc had reported negative working capital for 3 consecutive financial years (2013 – 2015). Working capital declined further to a (N55.61billion) from (N27.81billion) in FY2014. The increase of 49.05% y/y and 84.65% y/y in current borrowings and short term unsecured bond respectively was responsible for the increased negative value of working capital in FY2015. A negative working capital shows that the company current liability is higher than its current asset implying that operating activities are carried out via short term borrowed funds.

Working Capital (N'billion)



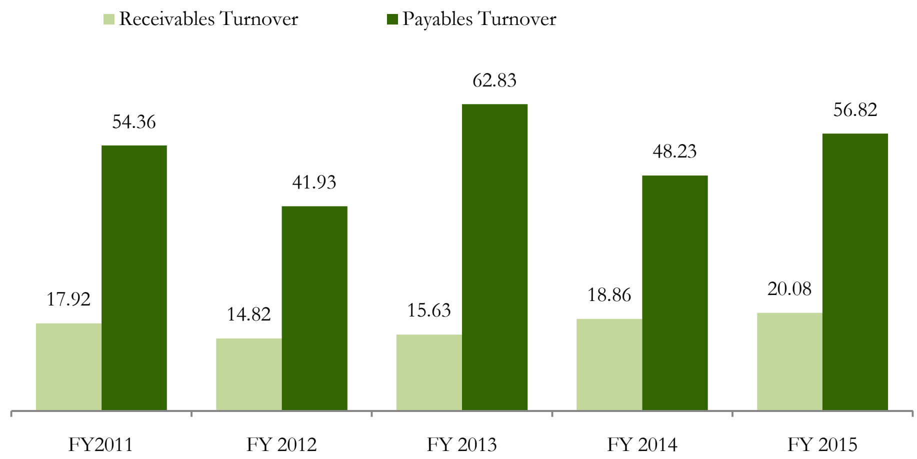
- Inventory turnover declined to 4.00x from 4.53x in the prior financial year, indicating an increase in inventory build-up as result of dwindling sales in FY2015 while Days inventory outstanding increased to 91. 35 days from 80.57days in FY2014.

Inventory Turnover and Days Inventory Outstanding



- Receivables turnover ratio increased to 20.08x from 18.86x in FY2014, implying that the FMN's extension of credit and collection of account receivable improved in FY2015. However, trade payable turnover declined to 6.42x from 7.57x in FY 2014. Days receivables outstanding (DRO) declined to 18.17days from 19.35 days in FY2014 while days payable outstanding increased to 56.82 days from 48.23 days in FY2014.

Receivables and Payables Turnover



Valuation

- We highlighted several pressure points unsupportive of the firm's profitability; operating activities are carried out using short term borrowed funds which is a concern for liquidity. Profit margins are not sustainable due to high financial charge and dwindling sales.

- In calculating the fair value for the company, we used three valuation methods: the Discounted Dividend Model (DDM), Free Cash Flow to Equity (FCFE) and Price Multiples. Gordon sustainable growth rate was calculated to be 3.82% using ROE of 9.68% and earnings retention rate of 39.48%.

- Applying an equal weight to DDM, FCFE and Price Multiples, we arrived at a target price of N30.93 per share. At the current price of N24.15, this gives an upside potential of 28.07%. We therefore place a BUY recommendation at this point in anticipation that the company will see an improvement in it's debt profile based on management's current strategies, if future earnings numbers are to improve. YtD, FMN shares have returned (38.39%) compared to market return of (14.35%).

Profit & Loss (N'Mn)

	2012	2013	2014	2015	2016(E)
Revenue	258,268.25	301,941.32	325,790.18	308,756.52	326,560.52
Changes (%)	8.15	16.91	7.90	(5.23)	5.77
Cost of Sales	218,559.73	264,042.48	288,485.69	273,389.56	284,107.97
Changes (%)	10.04	20.81	9.26	(5.23)	3.92
Gross Profit	39,708.52	37,898.84	37,304.49	35,366.95	42,452.91
Changes (%)	(1.19)	(4.56)	(1.57)	(5.19)	20.04
Operating Expense	21,514.36	25,448.73	28,155.64	24,466.14	25,457.97
Changes (%)	18.95	18.29	10.64	(13.10)	4.05
Investment Income	2,372.93	5,363.68	5,027.71	2,303.58	1,732.44
Changes (%)	(8.65)	130.29	(8.00)	(54.18)	(24.79)
Other income	2,596.50	5,407.30	3,873.95	-685.05	1,753.81
Changes (%)	(8.06)	(108.25)	(28.36)	(117.68)	356.01
Operating Profit	20,790.66	17,857.42	13,022.80	10,215.76	13,702.22
Changes (%)	(16.58)	(14.11)	(27.07)	(21.55)	34.13
Finance Cost	8,493.21	11407.26	16,101.37	18,703.52	19,368.18
Changes (%)	36.16	34.31	41.15	16.16	3.55
PBT	11,803.16	10,876.84	8,227.98	7,724.76	1,113.02
Changes (%)	(28.23)	(7.85)	(24.35)	(6.12)	(85.59)
Tax	(4,041.53)	(3,337.03)	(2,860.10)	738.29	232.39
PAT	7,761.62	7,539.81	5,367.87	8,463.06	1,345.42
Changes (%)	(17.87)	(2.86)	(28.81)	57.66	(84.10)
EPS	3.08	2.83	1.93	3.47	0.51

Statement of Financial Position

	2012	2013	2014	2015	2016(E)
Assets (N'mn)					
Cash and Cash Equivalent	26,239.13	21,837.48	16,825.16	31,131.71	28,821.66
Inventories	50,277.45	65,650.49	63,683.94	68,426.00	68,115.03
Account Receivables	17,425.46	19,314.18	17,271.62	15,373.44	13,657.63
Total CA	96,700.42	110,173.47	100,843.7	123,604.16	120,976.93
Total NCA	159,560.85	169,964.51	195,831.50	219,245.23	220,282.68
Total Assets	256,261.27	280,137.99	296,675.24	342,849.39	341,259.62

Liabilities & Equity

	2012	2013	2014	2015	2016(E)
Account Payable	25,109.25	45,454.10	38,116.03	42,560.78	40,300.34
Borrowings	39,703.05	53,877.81	76,443.42	113,940.44	116,751.39
Total Current Liabilities	78,495.81	114,509.97	128,658.87	179,214.20	174,952.90
Total NCL	130,152.75	146,217.90	150,129.42	76,224.80	52,410.33
Total Equity	81,015.53	82,485.25	83,559.43	87,410.39	83,709.28
Total Lia. & Equity	289,664.10	343,213.13	362,347.73	342,849.39	316,119.05

Activity Ratios

	2012	2013	2014	2015	2016(E)
Inventory turnover (x)	4.35	4.02	4.53	4.00	4.17
Receivables turnover(x)	14.82	15.63	18.86	20.08	23.91
Payables turnover(x)	8.70	5.81	7.57	6.42	7.05
Days inventory outstanding	83.96	90.75	80.57	91.35	87.51
Days Sales Outstanding	24.63	23.35	19.35	18.17	15.27
Days Payables Outstanding	41.93	62.83	48.23	56.82	51.77

Leverage and Solvency Ratios

	2012	2013	2014	2015	2016(E)
Equity Multiplier(x)	3.16	3.40	3.55	3.92	3.84
Debt -to-equity	2.00	2.32	2.60	2.16	1.84
Total debt-to-assets(x)	0.63	0.68	0.73	0.55	0.48
Total asset-to-Liability(x)	1.23	1.07	1.06	1.34	1.50
Interest coverage (x)	2.45	1.57	0.81	0.55	0.97

Efficiency Ratios

	2012	2013	2014	2015	2016(E)
Fixed assets turnover(x)	1.62	1.78	1.66	1.41	1.48
Current assets turnover(x)	2.67	2.74	3.23	2.50	2.70
Total assets turnover(x)	1.01	1.08	1.10	0.90	0.96
Equity turnover(x)	3.19	3.66	3.90	3.53	3.68

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