

## Consumer Staples

# Flour Mills Nigeria Plc: Showcasing unprecedented progress in the growth of organic sales and profitability

With the Nigerian government's ongoing focus on promoting agricultural development through its policies and budgetary plans, Flour Mills Nigeria Plc can leverage this support to build a strong agribusiness that can meet domestic food demand, generate export revenue, and create jobs. How effectively is the company taking advantage of this opportunity?

This report was prepared by Adebowale Atere.



This report is the exclusive property of Gifted Analysts and may not be reproduced in any form without the express written consent of our management. While we have taken great care to ensure the accuracy and completeness of the information contained in this publication, which has been obtained from publicly available sources, we cannot guarantee its accuracy or completeness. Users should make their own investment decisions without relying solely on the information provided herein. This report and the opinions expressed within it should not be considered as an offer to sell or a solicitation to buy any securities or other investments. Gifted Analysts is not licensed by the Securities and Exchange Commission and does not solicit investments from the general public. Gifted Analysts, its directors, and employees may invest in securities of companies using information contained in this document. Gifted Analysts and its members accept no responsibility or liability for any actions taken as a result of the information provided in this publication.

Copyright © Gifted Analysts 2023.  
All rights reserved.

## Company Overview

Flour Mills of Nigeria Plc (FMN) is a leading Food and Agro-allied group in Nigeria. Established in 1960 as a limited liability company and a pioneer in wheat milling in Nigeria, FMN has grown to become one of Africa's largest brands in the food and agro-allied industry.

In 2022, FMN reported total revenue of ₦1.16 trillion, representing a compound annual growth rate of 16.48% since 2018.

FMN's operations are divided into four main sectors: Food, Sugar, Agro-allied, and Support services. The Food and Agro-allied sectors are the largest contributors to the company's revenue, accounting for 64% and 18% respectively in 2022. FMN's entry into the agricultural sector began in 1978 with the acquisition of a 10,000-hectare farm in Kaboji, Niger state.

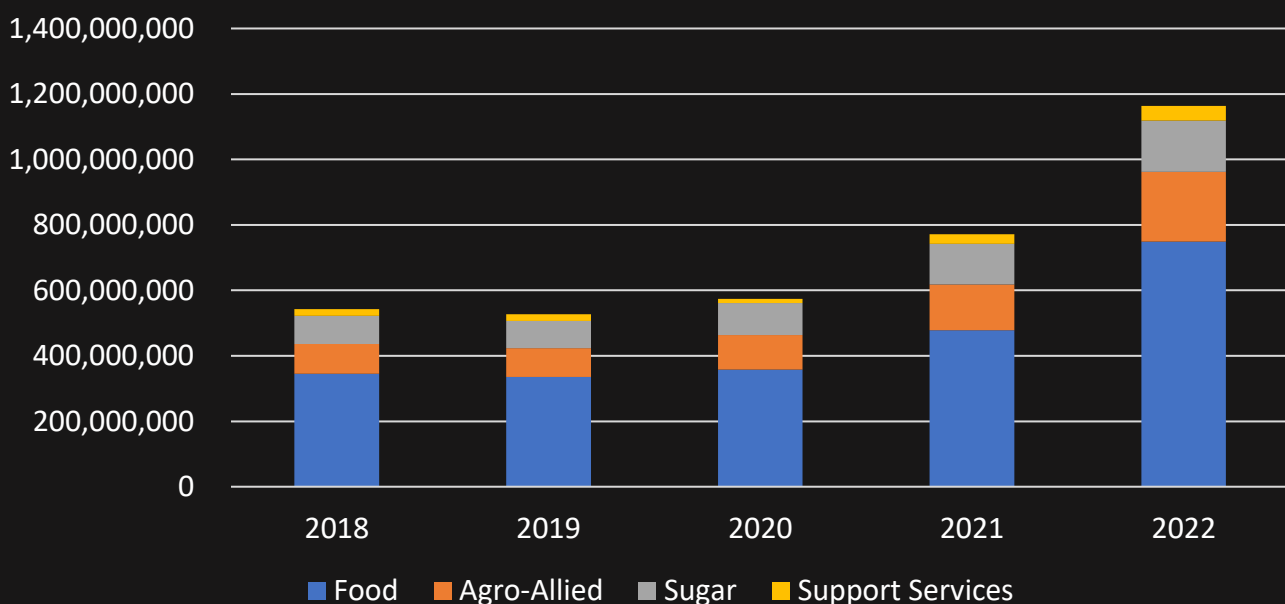
Since its entry into the agricultural sector, FMN has invested significantly in the primary processing of locally grown crops such as soybean, palm fruit, cassava, maize, sugar cane, and sorghum. The company has also focused on the storage, aggregation, and distribution of locally sourced grains.

FMN's product portfolio includes popular brands such as Golden Penny Pasta and Golden Penny Noodles, as well as other well-known products like Couscous, Mai Kwabo Macaroni and Spaghetti, and Auntie B Spaghetti Slim..

## Industry Overview

In 2022, Flour Mills Nigeria Plc generated approximately 64% of its revenue from its Food division. The company plays a significant role in promoting food security in Nigeria through its various operations in the food industry. Flour Mills has focused on increasing operational and capital efficiency by prioritizing local content in

**FMN Revenue (₦'000) by sector from 2018 - 2022**



its supply chains and supporting backward integration programs across its five key value chains: Grains, Oils & Fats, Sugar, Feeds & Proteins, and Cassava Starches.

The food industry is a significant contributor to Nigeria's economy, accounting for approximately 30% of the country's manufacturing sector and employing over 4 million people. In the first quarter of 2021, agriculture contributed 22.35% to Nigeria's Gross Domestic Product. With 70.8 million hectares of agricultural land and major crops including maize, cassava, guinea corn, yam beans, millet, and rice, Nigeria is the world's largest producer of cassava, yam, and cowpea.

Despite its importance to the economy, Nigeria's agricultural sector faces challenges such as poor land tenure systems, low levels of irrigation farming, climate change, and land degradation. The government has implemented various initiatives and programs to address these challenges.

FMN competes with other companies in the food industry such as Honeywell Flour Mills Ltd (in which FMN holds a 76.8% stake), Dangote Flour Mills Plc, and Olam.

## SWOT Analysis

### Strengths

- Robust ability relative to rivals to increase market presence and capture a significant portion of market opportunity
- Solid technical know-how accumulated over the years
- Strong brand recognition and reputation, with a wide range of products and an established distribution network for these products

### Weaknesses

- Narrow profit margins

### Opportunities

- Enhanced government backing to promote domestic agricultural output and guarantee self-reliance in food production
- An Increasing population, with tendencies to consume more wheat products
- Solid synergies with the acquisition of a 76.8% stake in Honeywell Flour Mills Ltd

### Threats

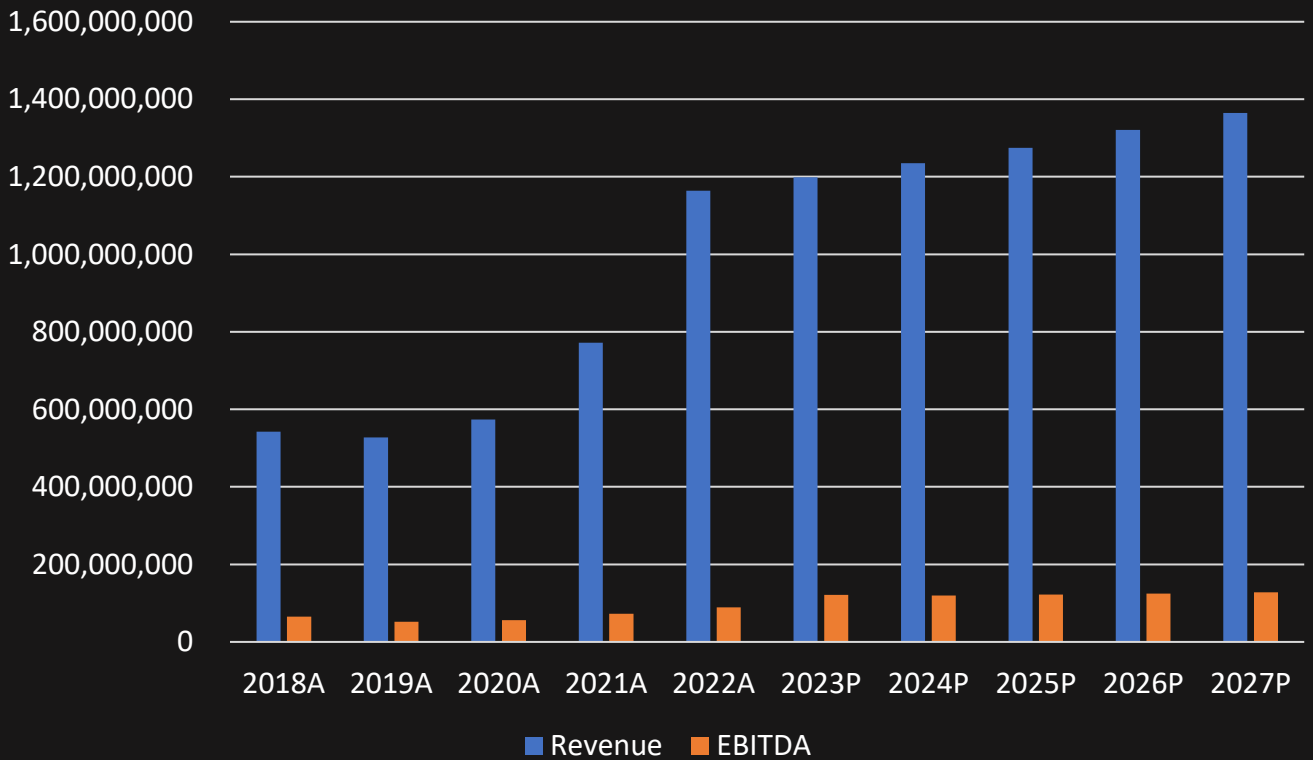
- Regulatory obligations and change in government policies
- Key macroeconomic indicators including exchange rate instability, inflationary pressures, and recessionary conditions
- Price volatility of commodities
- Health-conscious trend with a negative bias towards wheat products (Gluten)

## Financial Analysis

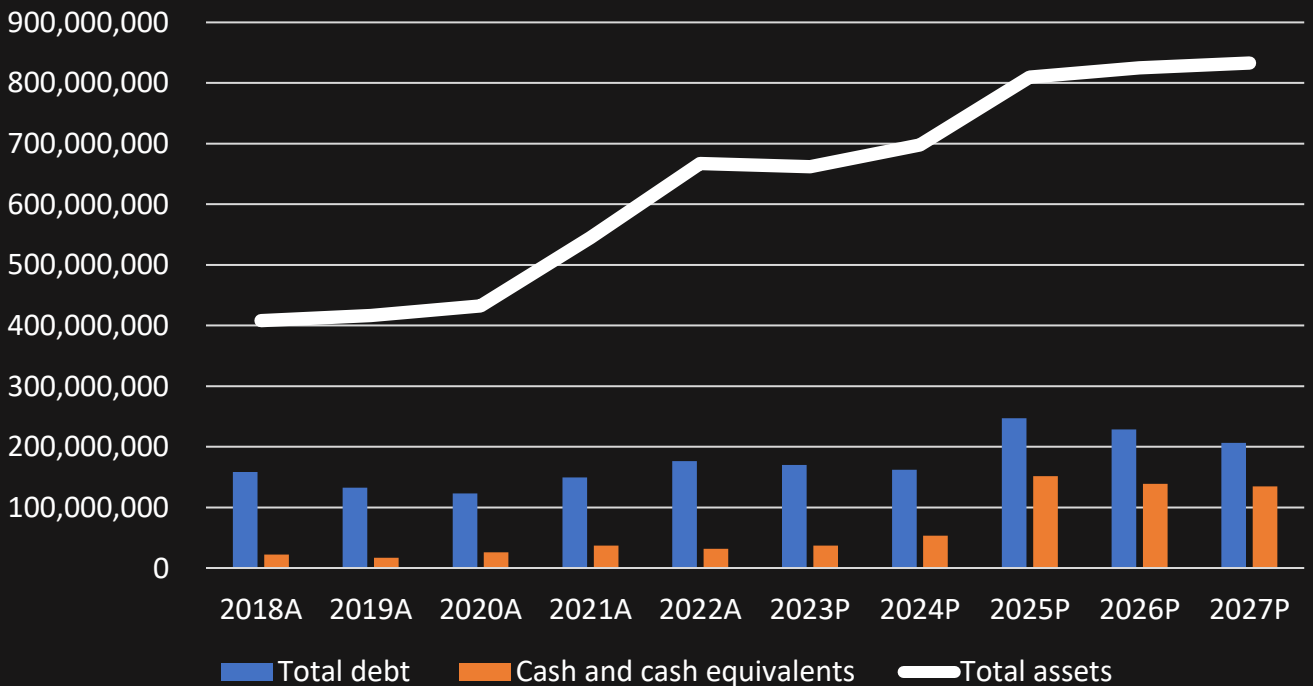
According to the income statement data, Flour Mills Nigeria Plc has achieved significant revenue growth over the past five years, increasing from ₦542.7 billion in 2018 to ₦1.16 trillion in 2022. While the company's cost of sales has also increased during this period, it has done so at a slower rate than revenue growth, resulting in an increase in gross profit from ₦68.8 billion in 2018 to ₦108.1 billion in 2022.

Additionally, the company's operating profit (EBIT) has grown from ₦48.4 billion in 2018 to ₦65.5 billion in 2022, indicating that Flour Mills Nigeria Plc has effectively managed its operating expenses and improved its profitability over this period.

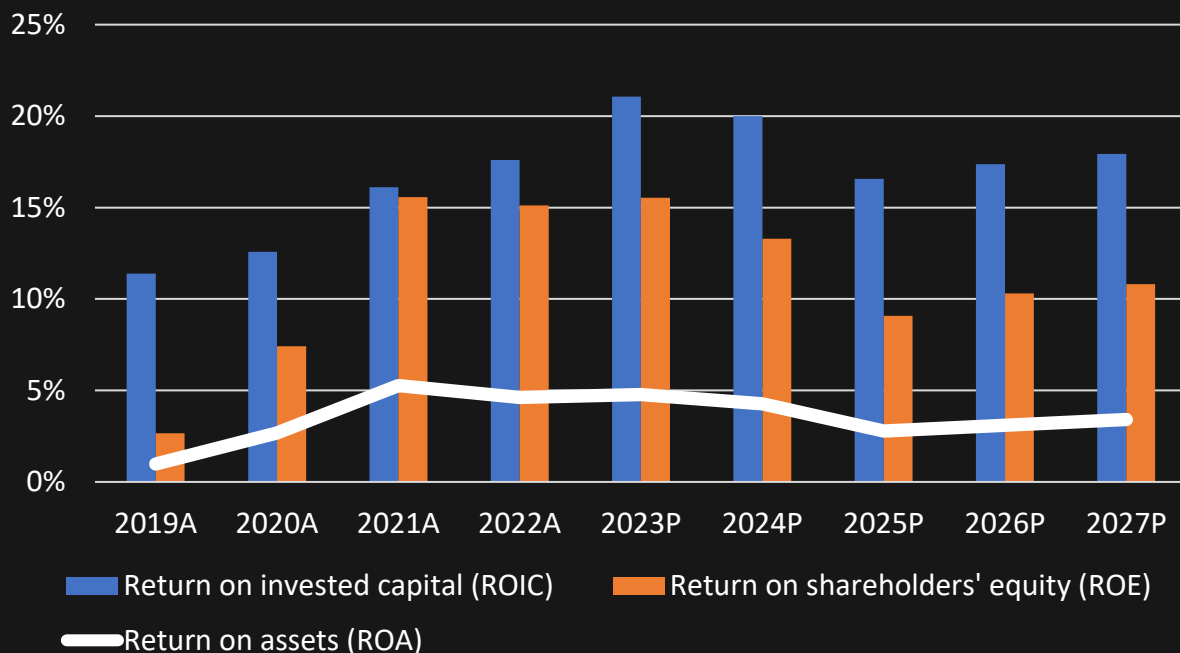
### Revenue and EBITDA (₦'000)



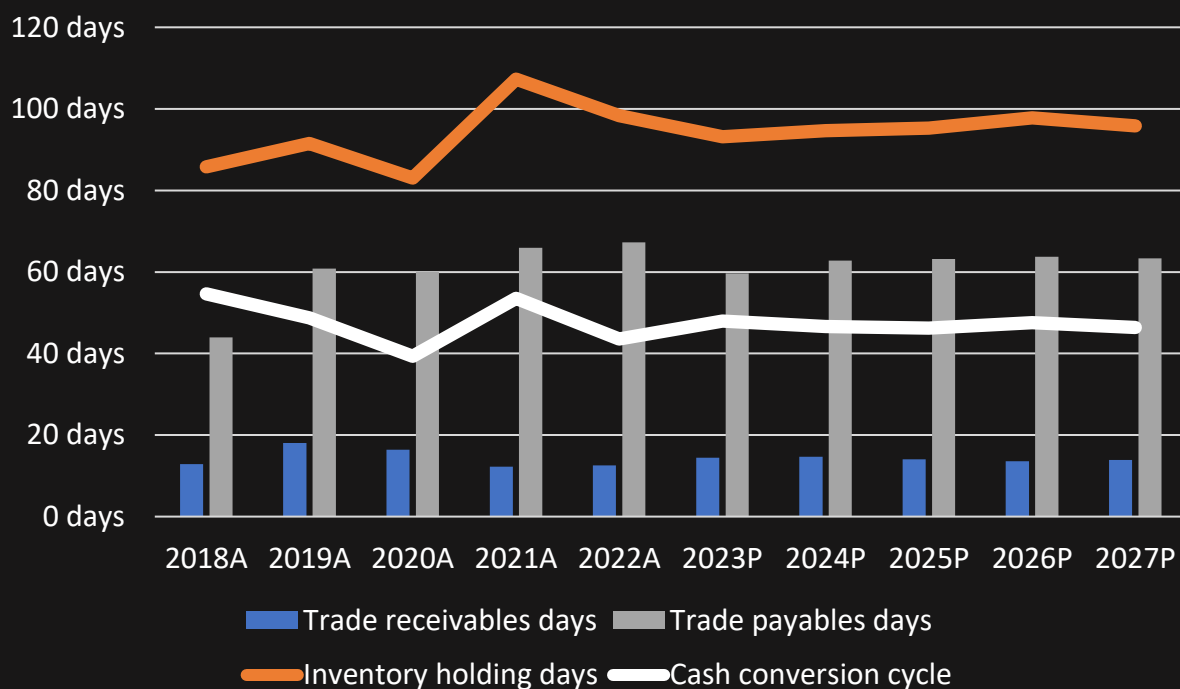
### Total debt, Cash and Total assets (₦'000)



## Profitability Ratios – ROIC, ROE and ROA



## Activity and Cash Conversion Cycle



Flour Mills Nigeria Plc has also experienced growth in its net income over the past five years, increasing from ₦13.6 billion in 2018 to ₦28.0 billion in 2022.

This indicates that the company has effectively managed its tax expenses and improved its bottom line.

However, the company's gross profit margin has decreased from 12.7% in 2018 to 9.3% in 2022, suggesting that its cost of sales has grown at a faster rate than its revenue.

Similarly, the company's operating profit margin has decreased from 8.9% in 2018 to 5.6% in 2022, indicating that its operating expenses have grown at a faster rate than its revenue.

The company's net profit margin has also decreased slightly from 2.5% in 2018 to 2.4% in 2022. These ratios suggest that while Flour Mills Nigeria Plc has achieved strong revenue and profitability growth over the past five years, its profit margins have decreased, indicating a need for improved cost management and operational efficiency going forward.

The company's total assets have grown significantly over this period, from ₦408.3 billion in 2018 to ₦667.0 billion in 2022, driven by increases in both non-current and current assets.

Its total equity has also increased, from ₦150.6 billion in 2018 to ₦195.9 billion in 2022, indicating that the company has generated profits and retained earnings to increase its equity. Flour Mills Nigeria Plc's total liabilities have also increased over the past five years, growing from ₦257.7 billion in 2018 to ₦471.1 billion in 2022.

This growth has been driven by increases in both non-current and current liabilities. The company's current ratio has improved over this period, increasing from 0.87 in 2018 to 1.40 in 2022, indicating an improvement in its ability to meet short-term obligations.

Additionally, the company's debt-to-equity ratio has decreased from 1.05 in 2018 to 0.90 in 2022, suggesting that it has relied slightly less on debt financing relative to equity financing to fund its growth over this period.

## **Financial Modelling and Valuation Methodology**

Flour Mills Nigeria Plc generates revenue from four primary sectors: Food, Sugar, Agro-allied, and Support services. Most of the company's revenue is derived from the Food and Agro-allied sectors.

The projected real GDP growth rate for each of these sectors can provide valuable insights into the company's future performance. However, it is important to note that wheat is the major commodity associated with Flour Mills Nigeria Plc.

Expert Market Research reports that the global wheat market reached a consumption value of around USD 153.2 billion in 2022 and is expected to grow at a CAGR of 5.3% during the forecast period of 2023-2028.

Data from Macrotrends indicates that the price of wheat as of June 01, 2023, is \$6.5139 per bushel. This represents an increase of approximately 31% from the average closing price of \$4.9757 per bushel in 2018.

Data from the Food and Agriculture Organization of the United Nations (FAO) indicates that global cereal trade is expected to remain near the 2022/23 level.

A predicted decline in global wheat trade is anticipated to offset increases in the world trade of coarse grains and rice. In Nigeria, wheat is the third most widely consumed grain after maize and rice.

Despite high consumption levels, it is estimated that Nigeria produces only about 1% (63,000 metric tons) of the 5-6 million metric tons of wheat consumed annually within the country.

The country's population growth is driving this trend, with wheat consumption projected to increase by 3.5% in 2023.

In response to its dependence on imported wheat, driven by growth in the bakery sector and strong local demand for bread, the Nigerian government is taking steps to increase domestic production.

According to an annual attaché report on the grains sector dated April 7, Nigeria's wheat production is projected to reach 160,000 tonnes in 2022-23, up from 90,000 in 2021-22.

Considering potential price increases in the cost of wheat, population growth and rising demand for wheat products both globally and in Nigeria, real GDP growth has been projected for the sectors that generate revenue for Flour Mills Nigeria Plc.

Based on these projections, continuous revenue growth with a conservative CAGR of 2.7% from 2022 to 2027 is expected.

Cost of goods sold is also expected to grow continuously but at a slower rate than revenue, with a CAGR of 2.4%. This is due to an expectation that management cost savings will improve efficiently at higher amounts of income generated.

The firm has debt instruments maturing in 2023, 2025 and 2027. An assumption has been made on funding via debt in 2025 since interest rates are currently high and it is expected that by then conditions will have improved for the firm to take advantage and ramp up production, to increase working capital and liquidity.

To calculate the company's weighted average cost of capital (WACC), a target capital structure of 54% equity and 46% debt was used.

The risk-free rate was based on the yield of an FGN bond maturing in 2032, while the gross cost of debt was derived from the yield of a Flour Mills bond maturing in 2027.

The perpetuity growth rate was calculated using the average real GDP growth rate from 2018 to 2022.

Three valuation methods were used: the Discounted Free Cash Flow method, the Dividend Discount Model method, and the Comparable method.

For the Comparable method, the P/E ratios of companies in the same industry were averaged over a five-year period from 2018 to 2022.



## Valuation Metrics

Perpetuity Growth Rate	1.85%
Weight Average Cost of Capital (WACC)	12.13%

Valuation Methodology	Weight	Price
Discounted Free Cash Flow Method	40%	₦69.91
Dividend Discount Model Method	30%	₦27.52
Comparable Method	30%	₦122.84
<b>Target Price</b>	<b>100%</b>	<b>₦73.07</b>

## Upside/Downside

Share Price as at Close of Business 2 <sup>nd</sup> of June 2023	₦34.90
<b>Potential Gain/Loss</b>	<b>109.37%</b>

## Risk and opportunity

Flour Mills Nigeria Plc aims to achieve continued organic growth across the group by focusing on its philosophy of putting consumers at the heart of its business.

Despite the challenges posed by the COVID-19 pandemic, the group achieved impressive year-on-year revenue growth of 34% between 2021 and 2020 and 51% between 2022 and 2021.

To sustain this growth trajectory, Flour Mills plans to invest in production capacity and increase aggregation and sourcing while also improving operational efficiency through cost optimization initiatives.

The company's management maintains reserves to fund investments in key business areas such as local content creation and its B2C route-to-market strategy.

The group's food division is focused on doubling its operating profit within five years. Flour Mills' strategy includes expanding its consumer business by driving growth in existing categories and entering new ones through enhanced innovation capabilities, investing in a winning route-to-consumer approach, and maximizing value creation in its B2B and B2C businesses.

Projections suggest that the company has the potential to achieve increased growth in free cash flow to the firm over the foreseeable future.

Investors in Flour Mills Nigeria Plc may face several risks and threats to the business. One such risk is market volatility in the food and agro-allied industry in Nigeria, which can be

subject to fluctuations in demand and supply that affect the prices of agricultural commodities.

For example, Nigeria's agricultural trade deficit increased from ₦549.3 billion in 2018 to ₦689.7 billion in 2019.

Operational risks, such as crop failure due to weather conditions or pest infestations, as well as risks associated with the supply chain, including transportation and storage, may also impact the company's performance.

Additionally, regulatory risk is a factor to consider, as the food and agro-allied industry in Nigeria is subject to government regulations and policies that can change over time and affect the profitability of investments in the industry.

