

## Backward Integration Strategy Boosts Topline Performance

### Sugar Segment Hits a Home Run

In the just released financial scorecard for H1:2023 (*full year-end is March*), Flourmill of Nigeria Plc's (FLOURMILL) recorded a remarkable topline performance as it grew by 37.82%YoY to NGN720.58bn (vs NGN522.82bn in H1:2022). Increased revenue across all its business units propped total revenue significantly: Food (+32.07%), Sugar (+50.59%), Agro-allied (+52.29%) and Support (+10.34%) segments. The Sugar segment recorded impressive numbers due to increased volumes. **In our opinion, the introduction of Brown Sugar - locally produced sugar - which saw patronage from industrial customers in the North, aided in driving sales up in the segment. Given that recent floodings in the region are unlikely to affect the segment's performance, we expect this to persist in the long run.** While volume growth somewhat dulled in the food segment, it remained the major contributor to revenue (c.62%), expanding by 32.07% to NGN445.67bn due to higher product prices as the input process continued to rise. The firm continues to expand its distribution network, pushing its Amazing day cereal and repackaged products into newer regions. The agro-allied segment benefited from the commissioning of new fertilizer plants and feed milling plants in Kaduna which resulted in its impressive topline performance. The firm's effort to sustain distribution network expansion, developing its Business to Consumer (B2C) categories (Flour, Pasta, Noodles and Ball food) and establishing smaller Stock Keeping units (SKUs) for the fertilizer business also contributed to the impressive topline growth. **Given that the firm typically records its better performance in the second quarter of the year, we remain optimistic about prospects for price and volume growth, anchored mainly on expected gains from an expanded distribution network and product innovation. Thus, we project a 2023FY revenue of NGN1.64trn (from NGN1.16bn), implying a growth of 40.81%YoY topline expansion.**

### Business Acquisition Stifles Profitability Margins

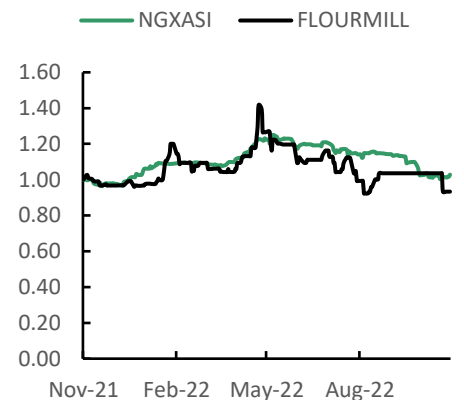
Production cost spiked by 39.14%YoY during the period to NGN651.79bn, outpacing the topline growth owing to higher raw material (+37.985) and power cost (+120.75%). Consequently, its cost to sales ratio increased to 90.45% (vs 89.59% in H1:2022). We see this as a resultant effect of the rising inflationary pressure and foreign exchange volatility in the domestic market.

Similarly, operating expenses ticked up by 13.95%YoY during the half-year period, influenced by higher personnel cost (+30.99%), depreciation (+25.39%) and legal expenses (+125.25%). Consequently, operating margins trended downwards to 4.21% (vs. 4.60% in H1:2022). **Given the management's commitment to increase CAPEX spending, we anticipate higher depreciation charges in the upcoming financial periods.** We note the significant uptick in debt obligations (+112.59%) owing to increased debt from the acquisition of Honeywell Flour Mills Plc. As a result, finance costs increased by 139.31%YoY to NGN22.32bn. Debt to EBIT and Debt to Asset ratios worsened to 10.43x and 0.34x (from 6.19x and 0.22x), respectively. Thus, Profit after tax declined significantly by 45.86% to NGN5.70bn (vs NGN10.53bn in H1:2022). Net margin also shrank to 0.79% from 2.01% in H1:2022. **Based on our expectation for production, operating and finance costs, we project an earnings performance of NGN23.68bn in 2023FY, implying a 7.93%YoY decline in the bottom line and a net margin of 1.44% (from 2.41%) in 2022FY.** We note that earnings quality also declined significantly as it recorded a positive net accrual of NGN11.04 and cashflow to net income ratio of -1.17x (vs. negative net accrual of NGN17.70bn and 2.68x in H1:2022).

### Recommendation

We maintain our target price of NGN40.68 for 2023FY on the back of a target P/E of 7.05x and an expected EPS of 5.77. This represents a 49.01% upside to its closing price of NGN27.30 on 18<sup>th</sup> November 2022. Thus, we rate the ticker a "BUY".

| Company                      | FLOURMILL      |
|------------------------------|----------------|
| <b>Valuation</b>             |                |
| Trailing EPS                 | 5.65           |
| BVPS                         | 47.82          |
| P/E                          | 5.36X          |
| P/BV                         | 0.63x          |
| Target PE                    | 7.05x          |
| Mar-2023 Exp. EPS            | 5.77           |
| Mar 2023 Target price        | <b>40.68</b>   |
| Current Price                | 27.30          |
| Up/Downside Potential        | <b>+49.73%</b> |
| <b>Ratings</b>               | <b>BUY</b>     |
| <b>Key metrics- Trailing</b> |                |
| ROE                          | 11.83%         |
| ROA                          | 2.90%          |
| Net margin                   | 0.79%          |
| Asset Turnover               | 1.71           |
| Leverage                     | 4.07           |
| Yr Hi                        | 32.30          |
| Yr Lo                        | 28.10          |
| YTD return                   | 13.93%         |
| Beta                         | 0.94           |
| Adjusted Beta                | 0.96           |
| Shares outstanding           | 4.10bn         |
| Market cap [NGN]             | 124.24bn       |
| Financial year end           | March          |
| Most Recent Period (MRP)     | H1:2023        |



Analyst  
Praise Ihansekhien

[praiseihansekhien@meristemng.com](mailto:praiseihansekhien@meristemng.com)  
(+234 817 007 1512)

Chart 1: Sensitivity Analysis

| Sensitivity Analysis of Dec-2022 Target Price to key model inputs |      |       |       |       |       | Min   | 34.98 |
|---|------|-------|-------|-------|-------|-------|-------|
|   |      |       |       |       |       | Max   | 46.94 |
|   |      |       |       |       |       | EPS   |       |
|   |      |       |       |       |       | 5.34  | 5.55  |
|   |      |       |       |       |       | 5.77  | 5.99  |
|   |      |       |       |       |       | 6.22  |       |
| Target PE   | 6.6x | 34.98 | 36.36 | 37.79 | 39.23 | 40.72 |       |
|   | 6.8x | 36.31 | 37.75 | 39.24 | 40.73 | 42.27 |       |
|   | 7.1x | 37.65 | 39.13 | 40.68 | 42.22 | 43.83 |       |
|   | 7.3x | 38.98 | 40.52 | 42.12 | 43.72 | 45.38 |       |
|   | 7.6x | 40.32 | 41.91 | 43.56 | 45.22 | 46.94 |       |

Financial Highlights and Forecasts (NGN billion)

| Profit & Loss Account | H1:2022 | H1:2023 | 2023F    | 2024F    | 2025F    | 2026F    | 2027F    |
|-----------------------|---------|---------|----------|----------|----------|----------|----------|
| Revenue               | 522.82  | 720.58  | 1,509.07 | 1,637.79 | 1,736.26 | 1,867.12 | 1,867.12 |
| Cost of sales         | 468.41  | 651.79  | 1,329.94 | 1,400.25 | 1,486.13 | 1,599.87 | 1,602.49 |
| Gross Profit          | 54.42   | 68.79   | 179.13   | 237.54   | 250.13   | 267.25   | 264.63   |
| Other income          | 0.41    | -0.46   | 0.84     | 1.56     | 0.92     | 1.72     | 2.00     |
| Operating expense     | 22.84   | 26.03   | 82.16    | 65.31    | 68.11    | 75.06    | 75.06    |
| Operating Profit      | 24.05   | 30.33   | 66.88    | 140.17   | 148.34   | 155.30   | 149.24   |
| Finance cost          | -9.33   | -22.32  | 39.21    | 74.61    | 168.05   | 441.12   | 1,372.08 |
| PBT                   | 15.48   | 8.38    | 33.17    | 70.50    | 14.89    | 280.63   | 1,217.31 |
| PBT                   | 10.53   | 5.70    | 22.56    | 47.94    | 10.13    | 190.83   | 827.77   |

| Balance Sheet                 | 2022FY | H1:2023 | 2023F  | 2024F    | 2025F    | 2026F    | 2027F     |
|-------------------------------|--------|---------|--------|----------|----------|----------|-----------|
| Property, Plant and Equipment | 226.84 | 336.77  | 242.44 | 260.71   | 282.65   | 302.35   | 319.86    |
| Total Debt                    | 148.83 | 316.39  | 374.94 | 604.27   | 1,389.76 | 3,713.35 | 11,556.48 |
| Total Assets                  | 667.01 | 929.72  | 904.99 | 1,186.76 | 1,969.64 | 4,106.29 | 11,081.24 |
| Total Equity                  | 195.90 | 196.10  | 189.81 | 228.85   | 206.67   | (4.45)   | (879.94)  |
| Total Current Liabilities     | 293.59 | 453.87  | 358.31 | 419.54   | 607.78   | 1,139.11 | 2,856.76  |
| Non-Current Liabilities       | 177.52 | 279.75  | 356.87 | 538.36   | 1,155.19 | 2,971.63 | 9,104.42  |
| Total Liabilities             | 471.11 | 733.62  | 715.18 | 957.91   | 1,762.97 | 4,110.74 | 11,961.18 |

| Financial Ratios    | 2022FY | H1:2023 | 2023F  | 2024F  | 2025F  | 2026F    | 2027F    |
|---------------------|--------|---------|--------|--------|--------|----------|----------|
| Gross Margin        | 10.41% | 9.55%   | 11.87% | 14.50% | 14.41% | 14.31%   | 14.17%   |
| Operating Margin    | 4.60%  | 4.21%   | 4.43%  | 8.56%  | 8.54%  | 8.32%    | 7.99%    |
| Net Margin          | 2.01%  | 0.79%   | 1.49%  | 2.93%  | -0.58% | -10.22%  | -44.33%  |
| Return on Asset     | 4.69%  | 2.90%   | 2.49%  | 4.58%  | -0.64% | -6.28%   | -10.90%  |
| Return on Equity    | 16.88% | 11.83%  | 11.88% | 22.90% | -4.65% | -188.73% | 187.19%  |
| Earnings per share  | 2.57   | 1.39    | 5.50   | 11.69  | (2.47) | (46.54)  | (201.88) |
| Asset Turnover      | 1.55   | 1.71    | 1.67   | 1.57   | 1.10   | 0.61     | 0.25     |
| Financial Leverage  | 3.27   | 4.07    | 4.77   | 5.00   | 7.25   | 30.05    | (17.17)  |
| Debt to Asset Ratio | 0.22   | 0.34    | 0.41   | 0.47   | 0.63   | 0.84     | 1.01     |
| Debt to EBIT Ratio  | 10.43  | 6.10    | 5.61   | 4.73   | 6.91   | 16.81    | 50.14    |
| Current Ratio       | 1.40   | 1.24    | 1.76   | 2.13   | 2.72   | 3.31     | 3.75     |
| Quick Ratio         | 0.43   | 0.50    | 0.86   | 1.34   | 2.14   | 2.98     | 3.62     |

## Contact Information

### Brokerage and Retail Services

topeoludimu@meristemng.com (+234 905 569 0627)  
 contact@meristemng.com

### Investment Banking/Corporate Finance

rasakisalawu@meristemng.com (+234 806 022 9889)  
 seunlijofi@meristemng.com (+234 808 536 5766)

### Wealth Management

funmilolaadekola-daramola@meristemng.com (+234 805 498 4522)  
 crmwealth@meristemng.com  
 Tel : +234 01 738 9948

### Meristem Finance Limited

[olasokomubo@meristemfinance.com](mailto:olasokomubo@meristemfinance.com) (+234 803 324 7996)  
[matthewawotundun@meristemfinance.com](mailto:matthewawotundun@meristemfinance.com) (+234 802 390 6249)

### Registrars

[oluseyiowoturo@meristemregistrars.com](mailto:oluseyiowoturo@meristemregistrars.com) (+234 802 321 0561)  
[martinaosague@meristemregistrars.com](mailto:martinaosague@meristemregistrars.com) (+234 802 303 1783)  
[www.meristemregistrars.com](http://www.meristemregistrars.com)  
 Tel: +23401-280 9250

### Trust Services

damilolahassan@meristemng.com (+234 803 613 9123)  
 trustees@meristemng.com

### Group Business Development

saheedbashir@mersitemng.com (+234 802 454 6575)  
 ifeomaogalue@meristemng.com (+234 802 3942967)  
 info@meristemng.com

### Client Services

adefemtaiwo@meristemng.com (+234 803 694 3034)  
 car@meristemng.com

### Investment Research

[damilarejojo@meristemng.com](mailto:damilarejojo@meristemng.com) (+234 816 890 2771)  
[praiseihansekhien@meristemng.com](mailto:praiseihansekhien@meristemng.com) (+234 817 007 1512)  
[research@meristemng.com](mailto:research@meristemng.com)

**Corporate websites:** [www.meristemng.com](http://www.meristemng.com) [www.meristemwealth.com](http://www.meristemwealth.com) [www.meristemregistrars.com](http://www.meristemregistrars.com)

**Meristem Research can also be accessed on the following platforms:**

**Meristem Research portal:** [meristem.com.ng/rhub](http://meristem.com.ng/rhub)

**Bloomberg:** MERI <GO>

**Capital IQ:** [www.capitaliq.com](http://www.capitaliq.com)

**Reuters:** [www.thomsonreuters.com](http://www.thomsonreuters.com)

**ISI Emerging Markets:** [www.securities.com/ch.html?pc=NG](http://www.securities.com/ch.html?pc=NG)

**FactSet:** [www.factset.com](http://www.factset.com)

---

## Analyst's Certification and Disclaimer

---

This research report has been prepared by the research analyst(s), whose name(s) appear(s) on the cover of this report. Each research analyst hereby certifies, with respect to each security or issuer covers in this research that:

- (1) all of the views expressed in this report accurately reflect his or her personal views about any and all of the subject securities or issuers (the Issuer); and
- (2) no part of any of the research analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this report. Research analysts' compensation is determined based upon activities and services intended to benefit the investor clients of Meristem Securities Limited (the firm). Like all of the firm's employees, research analysts receive compensation that is impacted by overall Firm profitability, which includes revenues from other business units within the firm.
- (3) each research analyst and/or persons connected with any research analyst may have interacted with sales and trading personnel, or similar, for the purpose of gathering, synthesizing and interpreting non-material non-public or material public market information.

As at the date of this report, any ratings, forecasts, estimates, opinions or views herein constitute a judgment, and are not connected to research analysts' compensations. In the case of non-currency of the date of this report, the views and contents may not reflect the research analysts' current thinking. This document has been produced independently of the Issuer. While all reasonable care has been taken to ensure that the facts stated herein are accurate and that the ratings, forecasts, estimates, opinions and views contained herein are fair and reasonable, neither the research analysts, the Issuer, nor any of its directors, officers or employees, shall be in any way responsible for the contents hereof, and no reliance should be placed on the accuracy, fairness or completeness of the information contained in this document. No person accepts any liability whatsoever for any loss howsoever arising from any use of this document or its contents or otherwise arising in connection therewith.

**Analysts' Compensation:** The equity research analysts responsible for the preparation of this report receive compensation based upon various factors, including the quality and accuracy of research, client feedback, competitive factors, and overall firm revenues, which include revenues from, among other business units, Investment Banking.

---

## Investment Ratings

---

### Fair Value Estimate

We estimate stock's fair value by computing a weighted average of projected prices derived from discounted cash flow and relative valuation methodologies. The choice of relative valuation methodology (ies) usually depends on the firm's peculiar business model and what in the opinion of our analyst is considered as a key driver of the stock's value from a firm specific as well as an industry perspective. However, we attach the most weight to discounted cash flow valuation methodology.

### Target Price Estimate

While we believe that the fair value is underpinned by the future benefits stream and growth outlooks, which are primary drivers of value, the market might not align to the fair value estimate within the estimated investment horizon. Thus, we do not derive our target price from the fair value but from a trading perspective using the year projected earnings or book value and the respective target multiples. Notwithstanding, we are of the opinion that the variance between the two should not be too significant.

### Ratings Specification

- BUY:** Target Price of the stock is above the current market price by at least **10 percent**
- HOLD:** Target Price of the stock ranges between **-10 percent and 10 percent** from the current market price.
- SELL:** Target Price of the stock is more than **10 percent** below the current market price.

## Definitions

**Price Targets:** Price targets 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 market and may not occur if the company's earnings fall short of estimates.

**Asset allocation:** The recommended weighting for equities, cash and fixed income instrument is based on a number of metrics and does not relate to a particular size change in one variable.

## Movements in Price Target

**Company Name:** Flour Mills Of Nigeria Plc

| Date      | Price (N) | Previous Target Price(N) | New Target Price (N) | Previous Recommendation | New Recommendation |
|-----------|-----------|--------------------------|----------------------|-------------------------|--------------------|
| 11-Feb-22 | 32.30     | 40.65                    | 40.65                | BUY                     | BUY                |
| 01-Jul-22 | 32.00     | 40.65                    | 45.79                | BUY                     | BUY                |
| 21-Nov-22 | 27.30     | 45.79                    | 40.68                | BUY                     | BUY                |

## Company disclosures

Meristem or the analyst(s) responsible for the coverage may have financial or beneficial interest in securities or related investments discussed in this report, which could, unintentionally, affect the objectivity of this report. Material interests, which Meristem or the analyst(s) have with companies or in securities discussed in this report, are disclosed below:

| Company                    | Disclosure |
|----------------------------|------------|
| Flour Mills of Nigeria Plc |            |
|                            |            |

- a. The analyst(s) hold(s) personal positions (directly or indirectly) in a class of the common equity securities of the company.
- b. The analyst responsible for this report, as indicated on the front page, is a board member, officer or director of the company
- c. Meristem beneficially owns 1% or more of the equity securities of the company
- d. Meristem has been the lead manager or co-lead manager of any publicly disclosed offer of securities of the company over the past 12 months.
- e. Meristem beneficially holds a major interest in the debt of the company
- f. Meristem has received compensation for investment banking activities from the company within the last 12 months
- g. Meristem intends to seek, or anticipates receipt of compensation for investment banking services from the company in the next 3 months
- h. The content of this research report has been communicated with the company, following which this research has been materially amended before its distribution
- i. The company is a client of the stock broking division of the Meristem group.
- j. The company is a client of the investment banking division of the Meristem group.
- k. Meristem is the registrar to the company.
- l. The company owns more than 5% of the issued share capital of Meristem
- m. Meristem has other financial or other material interest in the company.

---

## Conflict of Interest

---

It is the policy of Meristem Securities Limited and its subsidiaries and affiliates (Individually and collectively referred to as "Meristem") that research analysts may not be involved in activities that suggest that they are representing the interests of Meristem in a way likely to appear to be inconsistent with providing independent investment research. In addition, research analysts' reporting lines are structured so as to avoid any conflict of interests.

For example, research analysts are not subject to the supervision or control of anyone in Meristem's Investment Banking or Sales and trading departments. However, such sales and trading departments may trade, as principal, on the basis of the research analysts' published research. Therefore, the proprietary interests of those Sales and Trading departments may conflict with your interests.

---

## Important Disclosure

---

**For U.S. persons only:** This research report is a product of Meristem Securities, which is the employer of the research analysts who has prepared the research report. The research analysts preparing the research report are resident outside the United States (U.S.) and are not associated persons of any U.S. regulated broker-dealer and therefore the analysts are not subject to supervision by a U.S. broker-dealer, and are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

This report is intended for distribution by Meristem Securities only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the U.S. Securities and Exchange Act, 1934 (the Exchange Act) and interpretations thereof by U.S. Securities and Exchange Commission (SEC) in reliance on Rule 15a 6(a)(2). If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not the Major Institutional Investor.

---

## Legal entity disclosures

---

Meristem Securities Limited is a member of The Nigerian Stock Exchange and is authorized and regulated by the Securities and Exchange Commission to conduct investment banking and financial advisory business in Nigeria. However, the company through its subsidiaries carries out stock broking, wealth management, trustees and registrars businesses which are regulated by the SEC and ICMR.

Copyright 2022 Meristem Securities Limited. All rights reserved. This report or any portion hereof may not be reprinted, sold or redistributed without the written consent of Meristem Securities Limited.