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FDC MONTHLY ECONOMIC UPDATE

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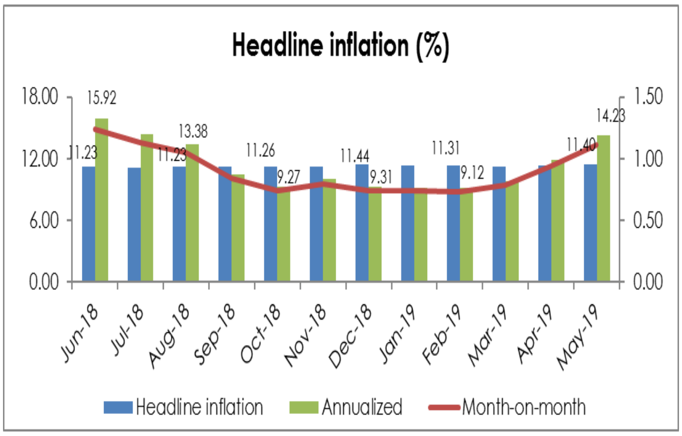
In This Issue ...

Headline inflation up marginally by 0.03% to 11.4% in the month of May

As widely expected, Nigeria's headline inflation in the month of May rose for the second month in a row, albeit marginally, by 0.03% to 11.40%. The uptick in the general price level was seasonally driven as the core sub-index (which is inflation less seasonality) continued its moderating trend. The planting season coupled with elevated security threats in the food producing states resulted in a decline in food supply. This coupled with increased seasonal demand, especially during the Eid-Fitri celebrations, pushed up commodity prices.



[1]

Month-on-month inflation recorded its sharpest rise in 2019

The month-on-month inflation (a better reflection of current prices and inflation expectations) was up 17bps to 1.11% (14.23% annualized) in the month of May. This is the third consecutive monthly increase and the sharpest rise in 2019, due to higher monthly food and core inflation. Rising monthly general price level suggests that inflationary pressures loom especially with the minimum wage implementation.

Data Breakdown

Food inflation advanced to 13.79%

The year-on-year and month-on-month food price indices increased by 0.09% and 0.27% to 13.79% and 1.41% respectively in the month of May. This is a reflection of the planting season effects. The commodities that recorded the highest increase in prices were: bread and cereals, meat, fish, milk, cheese and egg, potatoes, yam and other tubers, oils and fats, vegetables.

[1]NBS, FDC Think Tank

Core inflation down to 9.0%

The annual and monthly core sub-indices (inflation less seasonalities) moved in varied directions in the month of May. While the annual core sub-index fell by 0.3% to 9.0%, the monthly core sub-index was up 0.05% to 0.75%. Even though the rise in the monthly core inflation is marginal, it suggests that inflationary pressures in the near term would not only be driven by seasonal factors. The items that recorded the highest price increases were: tobacco, repair of household appliances, cleaning, repair and hire of clothing, domestic and household services among others.

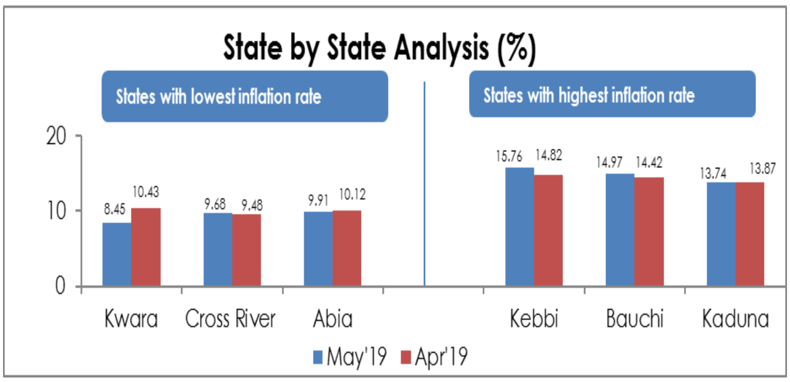
Core inflation is 2.34% below the 364-day primary market T/bills rate of 12.34%p.a. This is a positive real rate of return on investment.

Rural &Urban Indices

On an annual basis, urban inflation increased by 0.06% to 11.76% while rural inflation fell slightly by 0.01% to 11.07% in the month of May. However, on a monthly basis, both indices increased by 15bps and 17bps to 1.15% and 1.07% respectively. This suggests that the harvest season is likely to commence earlier in 2019 compared to the previous year.

State by State Analysis

Kwara state recorded the lowest inflation rate (8.45%), followed by Cross River (9.68%) and Abia (9.91%). The states with the highest inflation rates were Kebbi (15.76%), Bauchi (14.97%) and Kaduna (13.74%). Analysis showed that inflation rates were highest mainly in the Northern belt, in states with insecurity threats and disruption. In addition, the average diesel price in these three states was N231.84/liter, 0.51% above the average national diesel price of N230.67/liter.



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[2]NBS, FDC Think Tank

Sub-Saharan Africa (SSA) – Inflation trend down

With the exception of Nigeria, all the Sub-Saharan African (SSA) countries under our review recorded declines in inflation. At the last MPC meeting, most of these SSA countries left their monetary policy rate unchanged.

Country	May Inflation (%)	May Policy rate (%)	GDP Growth rate Q1'19 (%)
Nigeria	11.4 ↑	13.5 ↔	2.01 ↓
Angola	17.14 ↓	15.5 ↓	2.2* ↑
Kenya	5.49 ↓	9.0 ↔	5.9* ↓
South Africa	4.4* ↓	6.75 ↔	1.4* ↓
Ghana	9.4 ↓	16.0 ↔	6.8* ↓
Uganda	3.3 ↓	10.0 ↔	6.6* ↑

[3]

Outlook

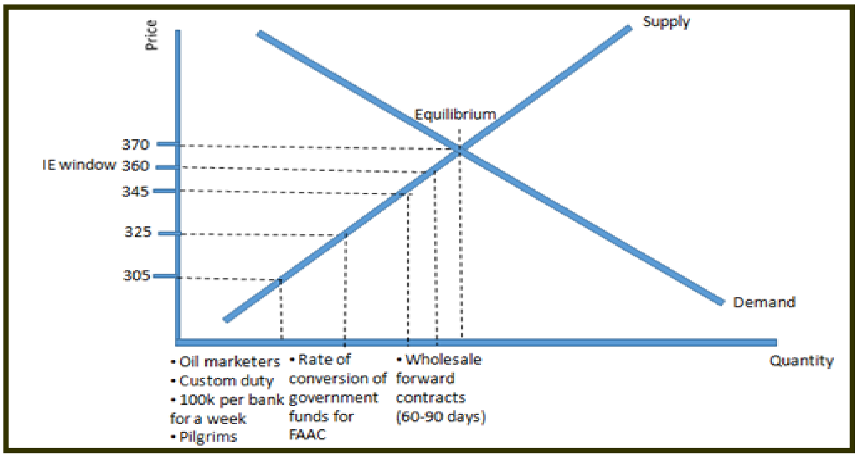
Even though the rise in the headline inflation was marginal, the sharp increase in the monthly general price level suggests that inflationary pressures are intensifying. Hence, we expect the rising inflation trend to be sustained in coming months. This would be driven by factors including the planting season and minimum wage implementation. This would be one of the major considerations at the next MPC meeting in July. The committee is likely to be more aggressive in its policy response.

[3]Trading Economics, FDC Think Tank, *April figure, **March figure

CBN's Exchange Rate Policy: Possibility of Unification?

The exchange rate has been a subject of political and market acrimony in Nigeria. For an oil-dependent economy with a high marginal propensity to import (approximately 70%) and where smuggling is still paramount, exchange rate management remains a sensitive issue. Nigeria's excessive dependence on oil revenue as a major source of foreign exchange has made the country vulnerable to external shocks. The exchange rate is determined by both subjective and objective factors including – the level of external reserves, balance of trade, terms of trade among others.

The structure of the Nigerian forex market is that of a price discriminating monopoly, wherein there are different prices for the same product (currency) and the CBN is the main supplier. This has created room for speculative trading, arbitrage and abuse, resulting in either transaction gains or losses for companies that are dollar dependent. Currently, there are approximately seven different exchange rates in Nigeria.



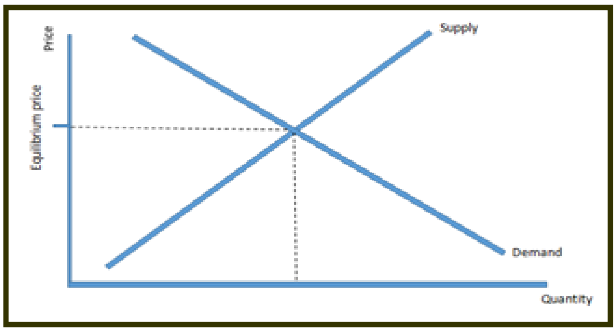
Recently, the CBN revised the official rate on its website to 'market determined' and adjusted the customs duty rate to N326/$ from N306/$. This led to speculations by some analysts that the CBN is making a move towards achieving a unified exchange rate. Contrary to this, the official rate was reversed to its original value (N306/$) and the apex bank reaffirmed that there are no changes to the country's exchange rate structure. Nonetheless, the initial revision of the rate coupled with the adjustment in the custom duty rate, is a pointer to a possible unification in the near term. The CBN is probably testing the markets for a reaction.

The optimal solution

The exchange rate is the price that brings about equilibrium between aggregate demand and supply for the currency. Typically, the pricing of a product is determined by its market structure. For instance, in a perfectly competitive market, the price of a commodity is determined by the intersection of the demand and supply curve. In the exchange rate market, there is the fixed or flexible exchange rate system. The flexible exchange rate is a dynamic equilibrium rate which allows for adjustments based on market fundamentals. Currently, Nigeria's exchange rate mechanism is a managed fixed system with multiple rates- this is rigid with limited volatility.

In addressing Nigeria's forex market challenges, it is important to concentrate on changing the structure of the market rather than focusing on the rates. This is because rates are determined by the market structure. More importantly, the exchange rate needs to be aligned with economic fundamentals. Thus, the optimal solution to Nigeria's exchange rate conundrum is a dynamic equilibrium (unified) exchange rate. Here, there will be a unified rate that would change in line with market realities.

Equilibrium Exchange Rate with no Gaps



The unification of the exchange rate would play a crucial role in eliminating arbitrages and increasing efficiencies in the forex market. However, we cannot ignore policy making concern of its pass through effect on prices, especially with the adjustments in the custom duty rate. A higher exchange rate makes imports more expensive, thus increasing import bill of manufacturers. They could pass on the costs to the consumers, share the pass through effect or bear the brunt of it all. On a positive note, government revenue will increase and imports could be discouraged.

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Nollywood & On-line Distribution: An End to Piracy?

'Old Nollywood' or 'New Nollywood', the Nigerian film industry remains an essential part of the economy. In terms of annual film productions, the industry currently ranks as the second largest movie industry in the world, following Bollywood (India, producing over 1,000 movies per year). Nollywood produces over 900 films on an annual basis while Hollywood boasts of over 600 movies per year.

In 2016, Nigeria's arts, entertainment and recreation sector was worth approximately N239billion ($664million). However, this pales in comparison to successes of Western movies such as Walt Disney's Black Panther, which grossed a total of $1.3billion globally. Without addressing challenges such as copyright infringements and piracy, financing and distribution, the FGN's estimated export revenue of $1billion from the industry by 2020 would not be feasible.

The disruptive innovation of video-on-demand services

In any business or industry, a disruptive innovation is one that creates a new market and value network, eventually displacing established market leading firms, products and alliances. Take for instance, the introduction of transportation networks like Uber, Bolt, which reduced the demand for the regular 'yellow cabs' in Nigeria or the introduction of e-mobile top up which made many recharge card sellers redundant.

Within the Nigerian movie industry, distribution channels have evolved from the days of Idumota market to cinema halls to online streaming. Movie enthusiasts are now willing to subscribe on a monthly or annual basis to video-on-demand platforms such as Irokotv, Netflix, Hulu amongst others.

Netflix has recognized the growing demand for online streaming and ramped up its investment in African productions. Netflix now boasts of original Nollywood movies including Lionheart, Chief Daddy and its African animated series, Mama K's team 4. In addition, Irokotv (dubbed the 'Netflix' of Africa) has a wide array of over 5,000 African movies and attracts more than 10 million views per month. This has allowed Africans living in diaspora, who live beyond the reach of pirated DVDs, the opportunity to enjoy organic entertainment. The monetization of movies has also become easier for filmmakers and producers.

Over the years, piracy in Nollywood has eaten deep in the industry and narrowed the profit margin of filmmakers and investors. Investors are wary of taking up the distribution burden for fear of seeing their movies being hawked in Ajah traffic.

The recent disruption in the distribution of Nollywood films has the potential to reduce the level of piracy in the coming years. As more video-on-demand sites enter the market and the competition within the telecommunication industry makes data cheaper, pirated movies would soon become a thing of the past.

Nollywood Is Ready to Go Global Thanks to Netflix

Global Perspective: Culled from Bloomberg

Streaming will help Nigeria's film industry, Africa's most vibrant, reach a much wider audience.

In December 2018, EbonyLife Films, a studio in Lagos, Nigeria, premiered Chief Daddy, a feature-length drama about an eccentric billionaire who dies suddenly, touching off a madcap scramble among his relatives over his estate. The movie was an immediate hit with audiences in Nigeria. By the end of the month it had emerged as the country's most popular theatrical release of the year.

Not long ago the economic life cycle of Chief Daddy might have ended there. Nollywood, the nickname for Nigeria's robust film industry, has long been hamstrung by piracy. For years filmmakers have watched with frustration as swarms of illegitimate DVDs quickly overwhelmed their promising cinematic efforts, slashing potential profits and making it difficult to raise money to produce future films.

But in the spring of 2019 the makers of Chief Daddy managed to cash in on a new window of opportunity, this time online. EbonyLife sold the movie's global streaming rights to Netflix Inc., for an undisclosed sum. In March the streaming service made the movie available to 149 million customers in 190 countries, most of whom live well beyond the reach of those pirated DVDs.

"As a continent, Africa has remained creatively silent for centuries, our stories are seldom told outside of our families and villages and often from the perspective of someone looking in," says Mo Abudu, chief executive officer of EbonyLife. The arrival of streaming technology has the potential to upend that dynamic and introduce Nigerian films to a much broader market on both sides of the Atlantic, she says: "Now is a good opportunity for more capital to be pumped into Nollywood."

Netflix first launched its service in Africa in 2016. Since then the streaming giant has been ramping up its investment in African productions. Last September, Netflix acquired its first original film from Nollywood, Lionheart, a drama about a woman who steps into the male-dominated transportation industry when her father falls ill. This April, Netflix announced its first African animated series, Mama K's Team 4, a futuristic tale about four teenage girls in Zambia who are recruited by a former secret agent to save the world. It's being produced by Triggerfish Animation, a studio in South Africa. While declining to say how many subscribers Netflix has in Africa, a spokesman for the service pointed to several other African movies and series that it has in development.

That's welcome news to the Nollywood community, which since its inception in the 1990s has emerged as a promising source of growth within the Nigerian economy. According to a 2017 report by PricewaterhouseCoopers LLP, Nollywood is the second-largest producer of films in the world, trailing only India's Bollywood. Nigeria's arts, entertainment, and recreation sector, of which Nollywood is a significant part, generated 239 billion naira ($664 million) in 2016 and is projected to continue growing. Nigeria's National Film and Video Censors Board estimates that the number of West African films released annually between 2015 and 2017 more than doubled, to 87.

In the past, Nollywood movies have been heavily consumed across Africa and rarely seen outside the continent. But the industry's boosters point to the recent success of several Western movies—including Walt Disney Co.'s Black Panther (which grossed $1.3 billion globally and was the top-selling movie ever in West Africa, according to Nigeria's film board) and Beasts of No Nation, the critically acclaimed film distributed by Netflix about a boy soldier fighting in a civil war in West Africa—as evidence of growing demand among U.S. and European audiences for stories rooted in African culture, traditions, and mythology.

While Nollywood films typically lack the kind of big-budget production values that U.S. and European moviegoers are accustomed to, creators in the region say the industry has gradually been shifting from mostly low-quality DVD releases toward slicker productions for both home video and cinematic release. To make more big-budget films, the industry will need to attract deeper, more reliable pools of financing.

This year, the Cannes Film Festival hosted its first Pavillon Afriques, highlighting filmmaking from across the continent.

In May top Nollywood producers, filmmakers, and executives traveled to France for the Cannes Film Festival's first "Pavillon Afriques," a series of sessions and screenings highlighting the opportunities and challenges facing filmmakers from across the continent.

Their goal: raising visibility for Nollywood and participating in discussions about financing, dealmaking, and the expansion of distribution. Inya Lawal, founder of Nigerian production house Ascend Studios, hopes the focus on African filmmaking at Cannes will show that programming can be done on a global scale. “It’s been a process to get here,” she says.

Nollywood creators continue to grapple with less than ideal conditions at home. Kunle Afolayan, a Nigerian director and producer, says that while the arrival of streaming and video-on-demand services has made monetizing Nollywood movies easier, piracy is still “eating deep into the industry.” He has four films slated for DVD release but is having trouble “because nobody is willing to take the distribution responsibility” given the likelihood that pirated copies could hit the streets the very next day.

Still, Nollywood veterans are hopeful the industry is poised to prosper in the emerging era of globally connected home entertainment. “We have an enabling environment,” says Afolayan. “The content makers are hungry for work. Anybody who comes in now is coming in at the right time.” —With Tope Alake and Karen Toulon

BOTTOM LINE - Nollywood, the most vibrant segment of Africa’s film industry, has long sought richer sources of financing. Netflix, on the continent since 2016, could be one very deep pocket.

Economic Diversification Through Reviving Nigeria's Cocoa Industry

In the 1950s through the 1960s, Nigeria was the world's second largest cocoa exporter behind only Ghana. However, since the discovery and commercial exploration of crude oil in the 1970s, cocoa production has been neglected. Nigeria is now the fourth largest producer of cocoa, behind Ivory Coast, Ghana and Indonesia.[4] The increasing dominance of Ivory Coast in global cocoa production is manifested in its harvested area. At 4.15 million hectares, it is 248.74% larger than Nigeria's harvested area of 1.19 million hectares.[5]

Perhaps more concerning is Nigeria's focus on cocoa exports rather than its vertical integration.[6] Consequently, Nigeria imports processed cocoa products, such as cocoa butter, cake, powder and chocolate, from Europe to augment inadequate local processing.

Major World's Cocoa Producing Countries in 2016/2017

Country	2016 (metric tons)	2017 (Metric tons)
Ivory Coast	1,634,000	2,034,000
Ghana	858,720	883,652
Indonesia	656,817	659,776
Nigeria	298,029	328,263
Cameroon	289,312	295,028
Brazil	213,843	235,809

[7]

[4]Food and Agricultural Organization (2019). "Crops". United Nations. http://www.fao.org/faostat/en/#data/QC
[5]Area harvested in Ivory Coast rose astronomically from 260,000 hectares in 1961 to 4.15 million hectares in 2017. Nigeria on the other hand had a 70% increase in its harvested area to 1.19 million hectares in 2017 from 700,000 hectares in 1961 (FAOSTAT).
[6]The share of Nigeria's cocoa exports in total cocoa produced fell from 94.85% in 1961 to 76.33% in 2016. This compares with its major rival, Ivory Coast, whose export share in total production declined sharply from 104.1% to 57.69% over the same period (FAOSTAT).
[7]Food and Agricultural Organization (2019). "Crops". United Nations. http://www.fao.org/faostat/en/#data/QC

Reviving the ailing cocoa industry by encouraging youth participation in production, improving training and financing, and focusing on vertical integration along the cocoa value chain, would expand the government's revenue base, offer economic diversification, and also conserve hard-earned foreign exchange earnings.

Challenges facing the cocoa industry in Nigeria

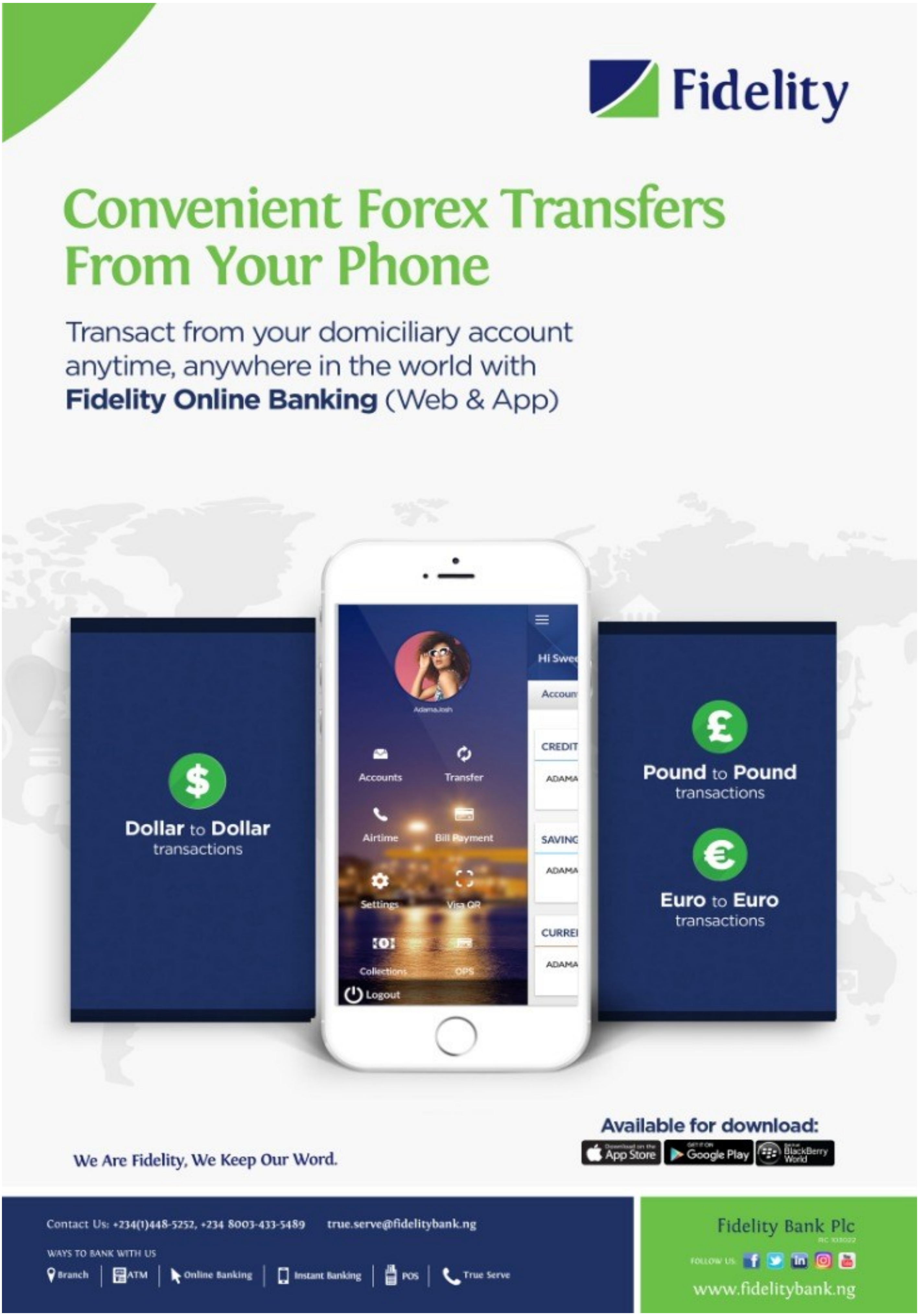
Dwindling labor invested in the industry

Most of the national yield is cultivated by small holder farmers, dependent on inherited farmland, leaving little room for expansion and new entrants to the industry. With weak prospects for a stable future in the cocoa industry, the next generation is not staying in the rural areas to continue the cycle of inheritance. This has left the burden of cocoa production on aged farmers.

Low yields – both in quality and quantity.

The lack of adequate inputs and proper training of farmers in modern farming practices has resulted in the production of poor yields, both in quality and quantity. Low and declining yields have been attributed to inconsistent production patterns, disease incidence, pest attack and little agricultural mechanization.[8] These factors, coupled with the predominance of ageing trees, have contributed to poor quality yields in Nigeria. Extension service agents were established to educate farmers on new farming methods and correct chemical applications. However, the rural areas, where the target cocoa farmers reside, remain inaccessible to these agents due to poor road and communication networks. This has left a number of farmers grappling with poor farm management. The large expanse of land devoted to cocoa production in Ivory Coast is also reflected in the increasing yields over time. At 4.90 tons per hectare, Ivory Coast's cocoa yield was 78% higher than Nigeria's yield of 2.75 tons per hectare in 2017.[9] Improvement in yields in Ivory Coast can be partly attributed to a series of training programs taken by farmers on modern measures to control pests and diseases. A case in point is the ***"cocoa life"*** training program. Amadou Ouattara, one of its beneficiaries, testified that having spent over two years on the program, his farm yield rose by 71.43% to 600 kilogram (0.6 tons) per hectare from 350 kg (0.35 tons) per hectare.

[8]Cadoni, P. (2013). "Analysis of incentives and disincentives for cocoa in Nigeria". Technical notes series, MAFAP (Monitoring African Food and Agricultural Policies project), FAO. www.fao.org/mafap .
[9]The yield gap between Ivory Coast and Nigeria rose sharply from 16.17% in 1961 to 78.07% in 2017 (FAOSTAT).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Limited access to finance

Difficulty in accessing funds at affordable rates has impeded production expansion. There has been various intervention programs in the agricultural sector. A case in point is the CBN's Anchor Borrowers' Scheme. The program, which was launched on November 17, 2015 by the Nigerian President, aims to link anchor companies (mainly food processors) to small holder farmers (SHFs) of key agricultural products. The scheme offers loans targeted at SHFs involved in the production of cereals, cotton, roots and tubers, tree crops (including cocoa), legumes, tomatoes and livestock. Farmers' access to the loan, at a 9% interest rate, is through their membership in a cooperative society of 5 to 20 people. When harvested, the SHF supplies the produce to the agro-processor who pays the cash equivalent into the farmer's account. The major challenge with the program is that the CBN's disbursements are delayed causing a delay in harvesting the crops.

Less developed cocoa value

Cocoa processing firms in Nigeria operate well below their full capacity, utilizing only 40% when an ideal target is 85%. FTN Cocoa Processors Plc, for example, which has a 20,000 metric ton capacity, only processes 600 metric tons, while Oluji Limited, the oldest cocoa processing company, processes 2,000 metric tons out of its 30,000 metric ton capacity. Ede Cocoa Processing Factory is Nigeria's most attractive cocoa processing firm with production capacity of over 70,000 metric tons.[10] Even if Nigeria's processing firms were operating at optimum capacity that would only be 102,000 metric tons a year, well below that of Ivory Coast and Ghana whose 2017/18 grindings reached 580,000 metric tons and 280,000 metric ton respectively.[11]

Addressing the challenges

First and foremost, there is a need to encourage youth participation in cocoa production. Possible measures to adopt include creating widespread awareness on the profitability of the industry, organizing training workshops to enable prospective young farmers to acquire the needed skills, setting aside a special intervention fund to empower the able-bodied participating youths, and regular monitoring of the performance of beneficiaries, which will form the basis on which new funds are disbursed. Successful young cocoa farmers could serve as role models to other unemployed youths.

[10]Inwalomhe Donald (2018). "Ede Cocoa Processing Factory: Nigeria's only surviving cocoa processing factory". Osun Defender. http://www.osundefender.com/ede-cocoa-processing-factory-nigerias-only-surviving-cocoa-processing-factory-by-inwalomhe-donald/
[11]www.fitchsolutions.com

Secondly, farmers should have adequate access to high-quality and subsidized inputs and be trained on effective methods of applying chemicals so as to increase yields and improve the quality of cocoa produce. Farmers should also be trained on modern farming practices. Ivory Coast offers a strong example, where a private company, Cargill, trained over 39,060 cocoa farmers in the correct application of fertilizer under the program called "Cocoa promise" in 2012. This program increased yields by 49%. By extension, there was a 22% increase in cocoa farmers' net household income.[12]

Similarly, the Nigerian government should ensure that cocoa farmers have adequate access to finance at the lowest possible cost. Government intervention in the agricultural sector should be targeted at ensuring food sufficiency. One of the positive outcomes of the Anchor Borrowers' Scheme was the boost to local rice production, which rose by 5.45% to 5.8 million tons in 2017 from 5.5 million tons in 2015 (the inception of the program). A similar focus on other agricultural products, such as cocoa, is needed to drive increased production for local consumption and exports.

In addition, in order to boost revenue, the Nigerian government could encourage and empower cocoa farmers in grinding cocoa beans and packaging them to meet up with international standards rather than relying solely on cocoa bean exports. Nigeria can draw useful lessons from Ivory Coast and Ghana which have visions of becoming major cocoa processing countries just as they dominate the world's cocoa production space. Ivory Coast aims to process at least half of its raw cocoa locally, up from a third currently. In order to achieve this, the country has attracted private investments in the cocoa industry. For instance, in 2015, Olam International, the world's third largest grinder, opened a $75 million factory with a production capacity of 75,000 metric tons.

Conclusion and outlook

Nigeria has the potential to restore its position as a top cocoa producer in the world if it can address its current challenges. The Cocoa Association of Nigeria is already optimistic, projecting an increase in output from the current 230,000 metric tons to 714,000 metric tons by 2029. Similarly, Nigeria could save a large chunk of foreign exchange earnings by improving its cocoa processing capacity. Promoting forward and backward linkages would ensure the participation of processed food companies such as Cadbury and Nestle in complementing government's efforts towards reviving the ailing cocoa industry in Nigeria.

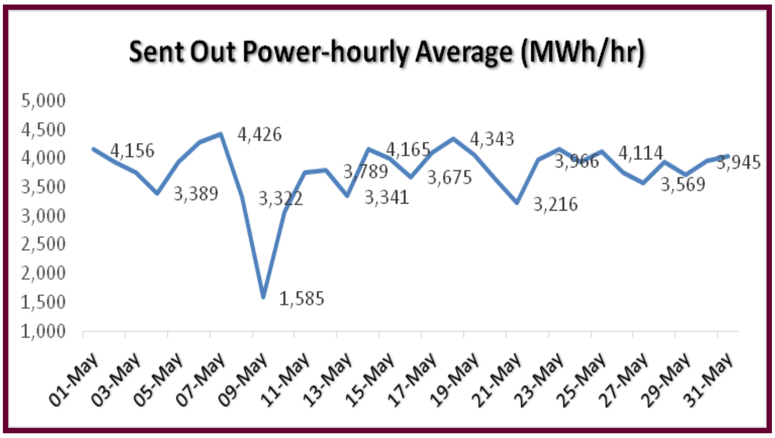
[12]Cargill (2017). "The 2016/2017 Cargill Cocoa Promise Global Summary Report". https://www.cargill.com/doc/1432129192723/cargill-cocoachocolate-promise-report-en.pdf

Macroeconomic Indicators

Power Sector

The average on-grid power output declined by 5.83% to 3,774MWh/h in May compared to the average of 4,008MWh/h in April. On May 9th, the national power output fell 1,585MWh/h due to total system collapse. This makes it the sixth time the country's power grid has collapsed in 2019.

Gas remains the major constraint to power output. The gas constraint during the period was 56.68% (52,299.83MWh/h) of total constraints (92,272.83MWh/h). Revenue loss in May amounted to N45.25bn (N543bn annualized).



[13]

Outlook

We expect the average power output to maintain its current level and remain heavily reliant on gas. The possibility of a shortfall in power output would be moderated by an increase in the hydro-power output as the rainy season reaches its peak. In addition, the borrowed fund of $350 million from World Bank to aid Nigeria's rural electrification would boost power output.

Impact

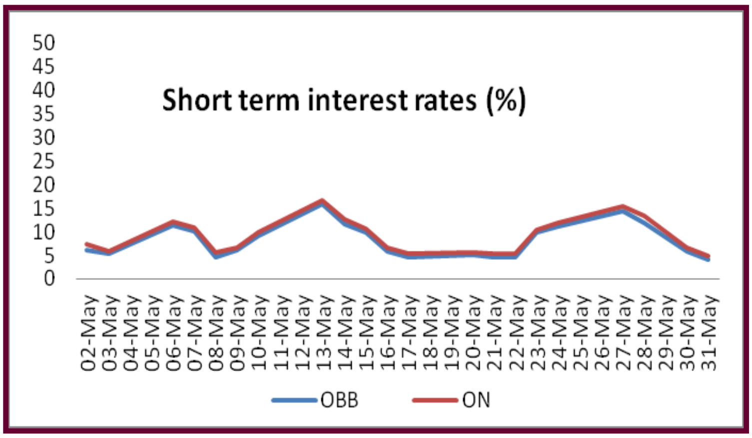
A stable power supply would have a positive impact on the social and economic wellbeing of the people. In addition, it would limit logistics costs and reduce the firms demand for alternative energy sources, such as, diesel. The retail price of diesel has remained high at N230-240/litre.

[13] FG, FDC Think Tank

Money Market

The average opening position within the banking system rose by 107.20% to N289.48bn in May from N139.71bn in April. The rise in liquidity could be attributed to the cut in the MPR. On the other hand, the CBN heightened its tightening strategy by increasing its issuance of OMO bills. The total OMO bills issued in May was 113.21% higher at N1.13trn relative to the prior month. The net outflow also increased to N640.59bn from N443.82bn. Open Buy Back (OBB) and Over-night (ON) rates decreased by 200bps and 236bps to close at 4.14% and 4.93% respectively.

On May 30th, there was a primary market auction worth N67.37bn. The 182-day and 364-day tenors declined by an average of 55.5 basis points (bps) to close at 11.95%p.a and 12.20%p.a. while the 91-day tenor was flat at 10%pa.The CBN wants to restrict the amount of Treasury Bills held in banks' balance sheets and redirect their lending focus to the private sector in order to boost growth and create employment. At the secondary market, the 91-day T/Bill yield increased by 16bps while the 182-day and 364-day tenors declined by an average of 117bps.



[14]

T/bills Tenor	Secondary market rates as at May 2nd (%pa)	Secondary market rates as at May 31st (%pa)	Direction	Primary market rates as at May 2nd (%)	Primary market rates as at May 30th (%)	Direction
91	10.35	10.51	↑	10.00	10.00	↔
182	12.60	11.45	↓	12.49	11.95	↓
364	12.74	11.55	↓	12.77	12.20	↓

[14] FMDQ, CBN

The Nigerian Inter-Bank Treasury bill True Yield (NITTY) declined by an average of 94bps across the three tenors in May.

NITTY Tenor	Rates on May 2nd (%pa)	Rates on May 31st (%pa)	Direction
30	10.86	9.61	↓
90	10.88	10.59	↓
180	13.39	12.11	↓

[15]

Outlook

We expect the CBN to continue with its management of excess liquidity using measures such as the sale of OMO and Treasury Bills.

Impact

A fall in liquidity within the banking system would result in lower interbank cost of borrowing (NIBOR rates).

Forex Market

The Nigerian forex market is segmented with multiple exchange rates. The most important rate being the Investors and Exporters window (IEFX). No less than 55%-60% of Nigerian forex transactions are traded at this window. The CBN and most exporters and investors use this window. It serves not only as a source of price discovery but also a barometer for measuring potential and actual CBN intervention in the market. Some of the exchange rate determinants are balance of payments, capital inflows and trade balance.

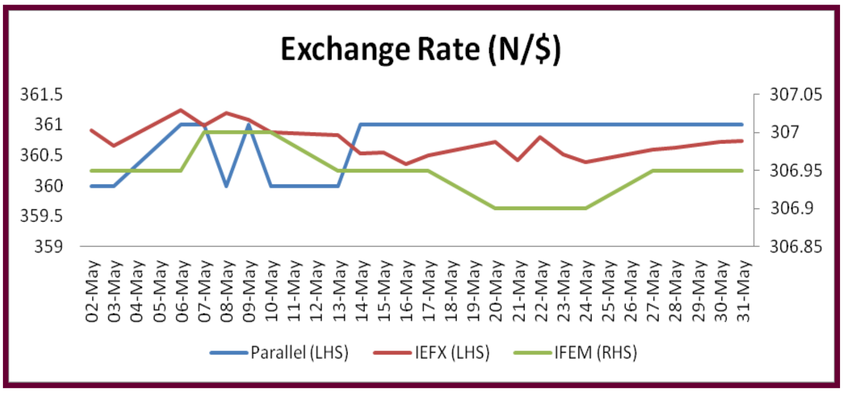
Exchange Rate

During the review period, the naira depreciated to N361/$ at the parallel market. This could be mainly attributed to forex demand pressure, arising from high naira liquidity and a decline in CBN's forex intervention which stood at $950.43 million, 16.08% lower than $1.13 billion in April. Whilst the naira appreciated by 1.06% against the pound sterling to close the period at N465/£, it depreciated against the euro to close at N402/€.

At the I& E window, the naira depreciated to close at N360.74/$. The window recorded a total turnover of $4.11 billion, 21.56% lower than a total turnover of $5.24 billion recorded in April.

On the other hand, the currency appreciated at the Interbank Foreign Exchange Market to N306.90/$ before retreating to close at N306.95/$ on May 31st.

[15]FMDQ



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Outlook

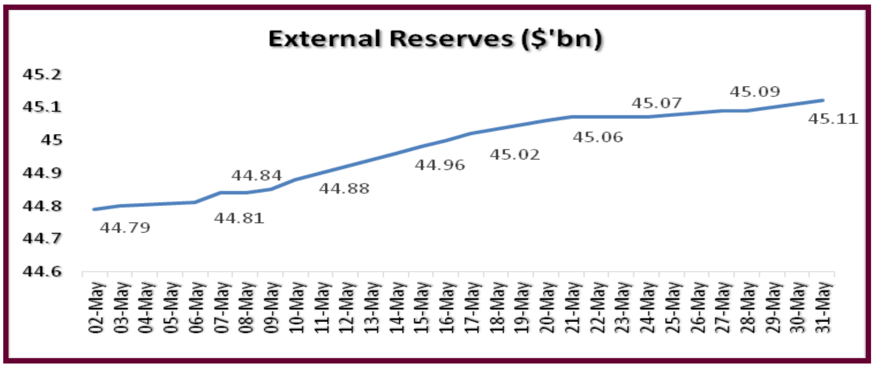
Increased demand for dollar from travelers (Hajj) could mount pressures on the exchange rate. However, we expect the naira to remain stable within the band of N361-362/$ at the parallel market in the coming weeks due to continuous CBN forex intervention and OMO intervention strategy.

Impact

A stable exchange rate is positive for import-dependent manufacturers.

External Reserves

Nigeria's gross external reserves increased by 0.74% to $45.12bnon May 31st from $44.79bn on May 2nd. This could be largely attributed to a decline in the CBN's forex intervention which was 16.08% lower than in the preceding month. Subsequently, Nigeria's import cover increased to 11.23 months from 11.15 months on May 2nd.



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Outlook

Brent accounts for about 80% of Nigeria's dollar revenue. Oil prices have plunged 18.23% in two weeks. A continuous decline in oil prices could weigh negatively on the level of external reserves.

Impact

A decrease in the level of external reserves would limit the CBN's forex intervention when needed and reduce the country's buffers against negative external shocks.

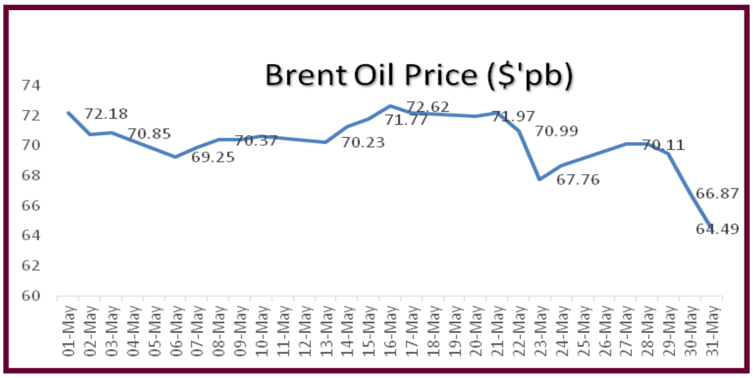
[16]FMDQ, CBN, FDC Think Tank
[17]CBN

Commodities Market- Exports

Nigeria is an export dependent economy. It derives over 80%-90% of its export revenue from crude petroleum and LNG.

Oil Prices

Brent price averaged $70.22pb in May, 1.95% lower than the average of $71.62pb in April. This was largely driven by escalated trade tensions between the two largest economies (US/China) globally and an increase in the US shale stockpile.



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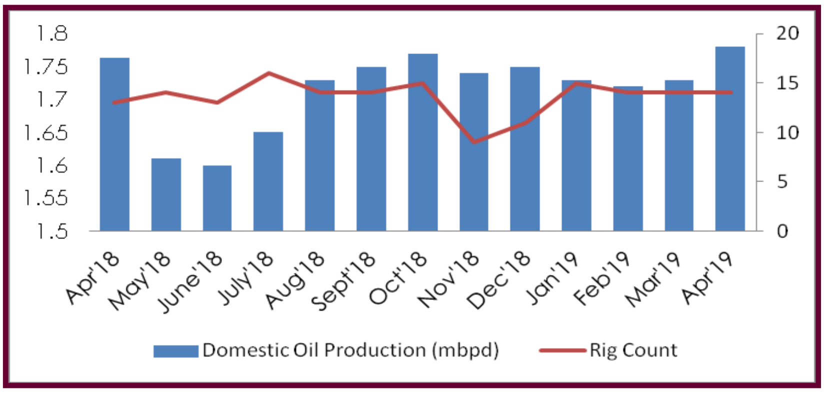
Outlook

We expect oil prices to continue the downward trend in the near term as US threatens to impose tariffs on imports from Mexico. Nevertheless, the group's extension of production cut would be known after its bi-annual meeting on June 25th and 26th.

Oil Production

According to OPEC's latest monthly report, Nigeria's oil production increased by 5.20% to a 14-month high of 1.82mbpd in April. This was despite a flat rig count of 14 in April. Meanwhile, OPEC crude oil production averaged 30.03mbpd, marginally unchanged from the previous month of 30.02mbpd.



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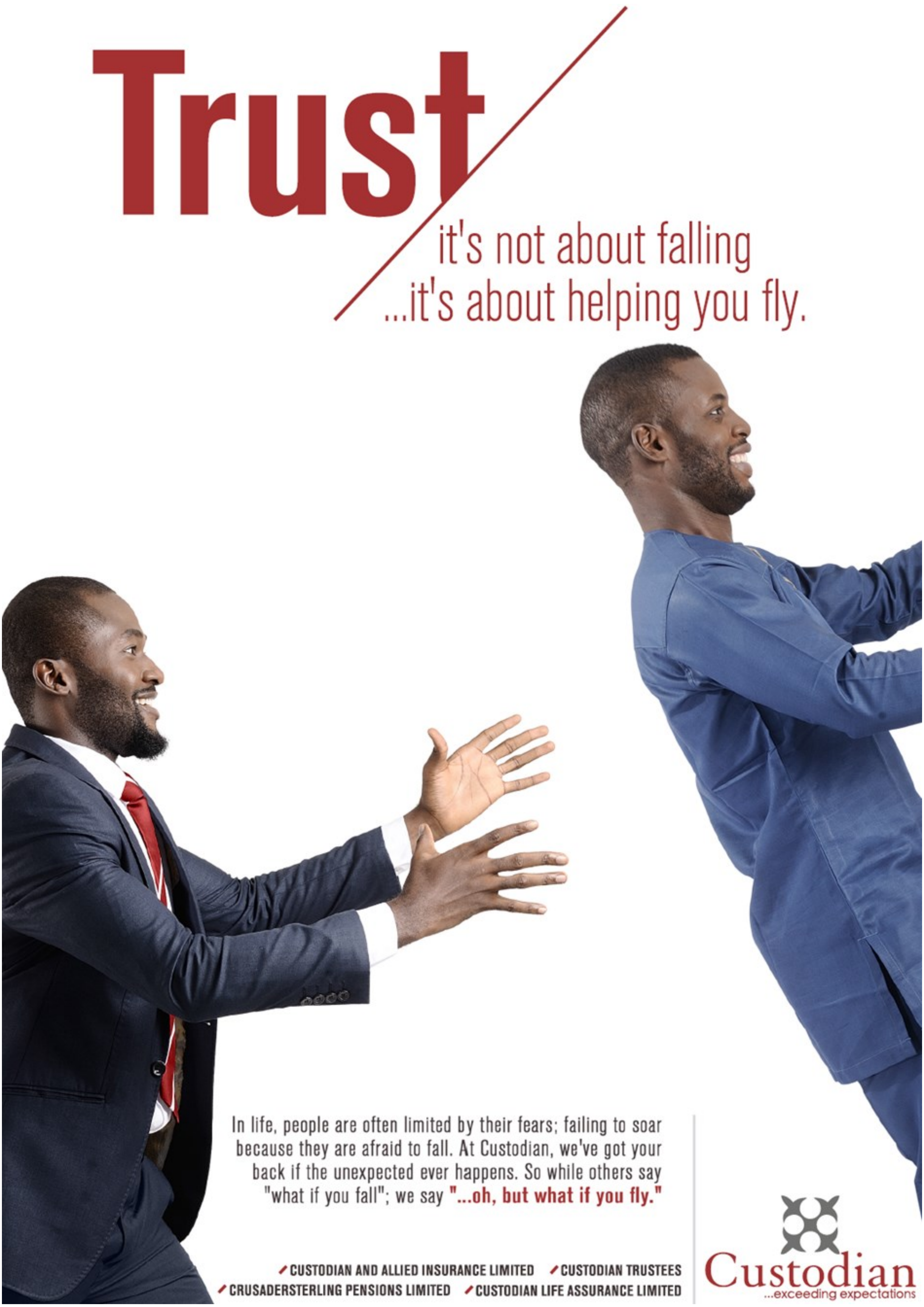
[18]Bloomberg
[19]OPEC and Baker Hughes


Trust
it's not about falling
...it's about helping you fly.
In life, people are often limited by their fears; failing to soar because they are afraid to fall. At Custodian, we've got your back if the unexpected ever happens. So while others say "what if you fall"; we say "...oh, but what if you fly."
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CUSTODIAN TRUSTEES
CRUSADERSTERLING PENSIONS LIMITED
CUSTODIAN LIFE ASSURANCE LIMITED
Custodian
...exceeding expectations

Outlook

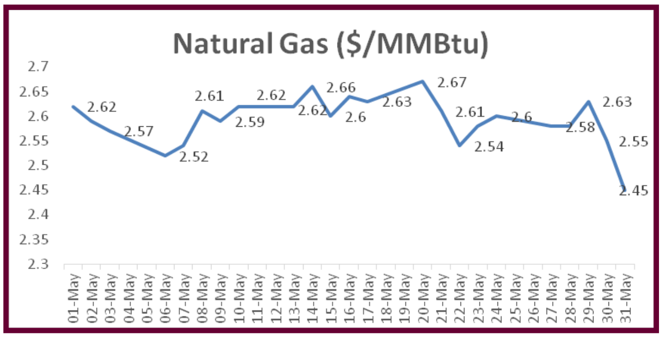
We expect lower crude oil production in the coming months. This would be supported by improved compliance by Nigeria to its production quota of 1.685mbpd.

Impact

Crude oil accounts for approximately 90% of Nigeria's export revenue. A reduction in production coupled with bearish prices is negative for Nigeria's terms of trade, balance of trade and fiscal position.

Natural Gas

The average price of Natural gas declined by 0.38% to $2.59/mmbtu from $2.60/mmbtu in April, due to a surge in US natural gas supply.



[20]

Outlook

We expect softer prices in subsequent weeks on the back of higher global supply.

Impact

Nigeria is the fourth largest producer of natural gas globally, with an output of 20.7 metric tonnes in 2018.[21] A decline in prices would be negative for non-oil export revenue and filter through to lower FAAC disbursements. LNG accounts for about 12.6% of Nigeria's total export revenue.[22]

Cocoa

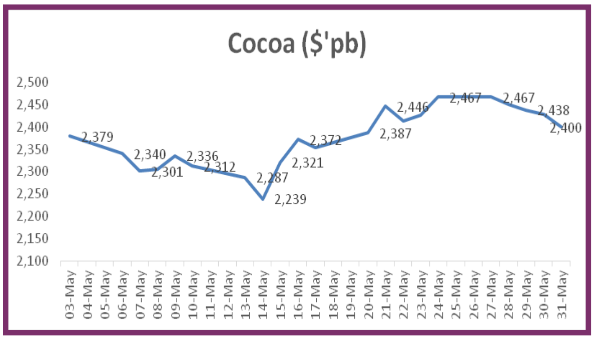
Cocoa prices averaged $2,365/mt in May, 0.30% lower than $2,372/mt in April despite a robust global demand.

Outlook

We anticipate an increase in the level of Ghana's cocoa production and this could likely result in higher global supply. Therefore, we expect prices to maintain the downward trend and trade within the range of $2,200/mt-$2,400/mt in the near term.

Impact

Nigeria is among the top six producers of cocoa globally. A decline in cocoa prices would have a negative impact on non-oil export earnings and fiscal buffers.



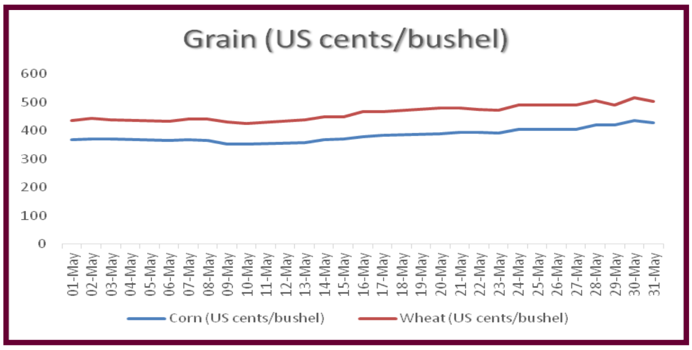
[23]

[20]Bloomberg
[21]EIU
[22]EIU
[23]Bloomberg

Commodities Market- Imports

Wheat

The average price of wheat increased by 1.84% to $462.62/bushel in May, from $454.28/bushel in April due to weak supplies amid late planting in the US.



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Corn

The price of corn averaged $384.57/bushel in May, 5.71% higher than the average of $363.81/bushel recorded in April amid trade tensions between the US and Mexico.

Grains- Outlook

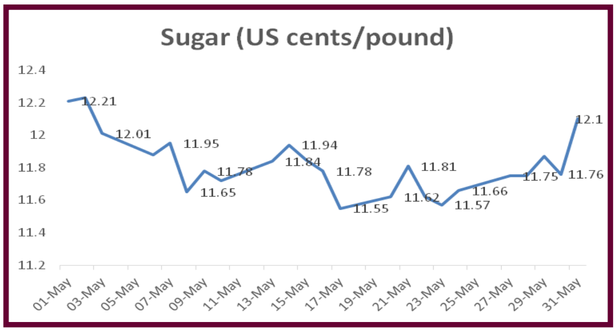
The US threat to impose tariffs on Mexico imports could weigh negatively on grain prices as Mexico is the leading buyer of US corn and wheat.

Impact

Nigeria's manufacturing firms depend largely on imported grains to augment lower domestic production. A decrease in global grain prices would translate to lower production costs of grain-dependent companies.

Sugar

Sugar prices averaged $11.82/pound in May, 7.08%lower than the average of $12.72/pound recorded in the previous month. This was partly driven by a weak demand from Pakistan.



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Outlook

We expect prices of sugar to reverse its bearish trend in the coming weeks due to lower output from Asian markets such as Thailand and China.

Impact

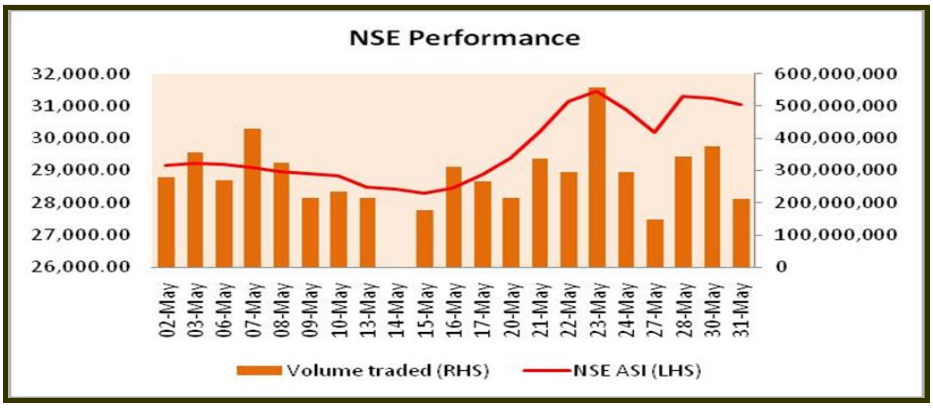
Sugar is an important ingredient in most consumable goods. Nigeria imports 1.87mn metric tonnes of this commodity annually, emerging as the world's 9th largest importer. An increase in the global price of sugar signals a possible increase in the country's import bill.

[24] Bloomberg
[25] Bloomberg

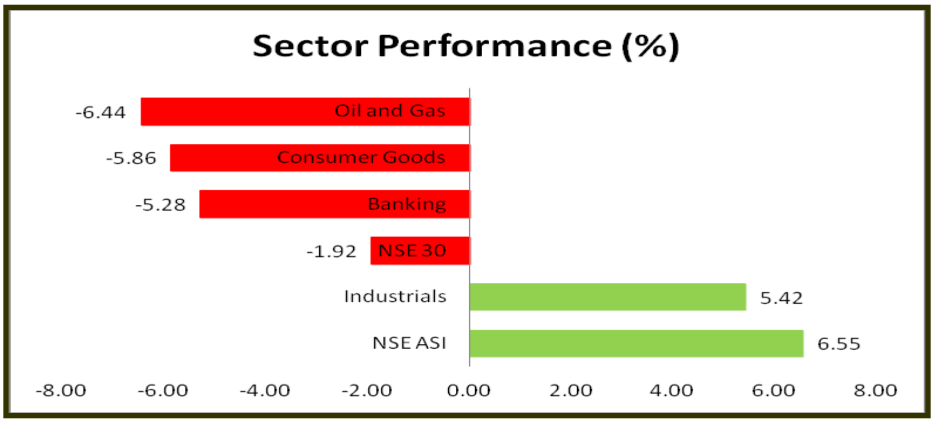
Stock Market Update

The listing of MTN Nigeria Communications on May 16 helped buck the 8-day losing streak of the Exchange. The NSE ASI gained 6.55% in the month of May to close at 31,069.37 points despite trading mostly negative. Similarly, the market capitalization jumped 24.82% to N13.68 trillion from N10.96 trillion at the start of the month. Market breadth was negative at 0.24x relative to0.39x in April as 71 stocks lost, 78 remained unchanged and 19 stocks gained.

The NSE traded at a price to earnings (P/E) ratio of 7.69xasat May 31st, 3.78% higher than April's close (7.41x).



The average value of traded spiked 44.48% to N5.23billion, while the average volume traded declined by 32.59% to 288.81 million units.



All the sub-indices except Industrials lost in May.

Thomas Wyatt Nigeria Plc topped the gainers' list with a 60% increase in its share price; followed by Beta Glass Corporation Plc (33.93%), Fidson Healthcare Plc (20.24%), Courteville Business Solutions Plc (20%) and A.G. Leventis Nigeria Plc (15.38%).

TOP 5 GAINERS (N)				
Company	**April 30'19**	**May 31'19**	**Absolute Change**	**% Change**
Thomas Wyatt Nigeria Plc	0.25	0.4	0.15	60
Beta Glass Corporation Plc	56	75	19	33.93
Fidson Healthcare Plc	4.2	5.05	0.85	20.24
Courteville Business Solutions Plc	0.2	0.24	0.04	20
A.G. Leventis Nigeria Plc	0.26	0.3	0.04	15.38

On the other hand, Goldlink Insurance Plc was the top loser falling by 50%, followed by Champion Breweries Plc (-29.37%), Academy Press Plc (-24.24%), Chams Plc (-24%) and Forte Oil Plc (-22.1%).

TOP 5 LOSERS (N)				
Company	**April 30'19**	**May 31'19**	**Absolute Change**	**% Change**
Goldlink Insurance Plc	0.40	0.20	-0.20	-50.00
Champion Breweries Plc	1.43	1.01	-0.42	-29.37
Academy Press Plc	0.33	0.25	-0.08	-24.24
Chams Plc	0.50	0.38	-0.12	-24.00
Forte Oil Plc	35.30	27.50	-7.80	-22.10

Corporate Disclosures

The under listed companies released Q1'19 financial statements in the month of May.

Company	Sector	Top line (N'billion)	Profit After Tax (N'billion)
Computer Warehouse Group Plc	ICT	1.91 54.03% ↑	0.05 1150% ↑
Jaiz Bank Plc	Financial Services	2.32 29.74% ↑	0.43 258.33% ↑
MRS Oil Nigeria Plc	Oil and Gas	13.51 59.73% ↓	-0.73 297.23% ↓
Forte Oil Plc	Oil and Gas	42.56 59.53% ↑	0.65 506.25% ↑
Japaul Oil & Maritime Services Plc	Oil and Gas	0.14 27.27% ↑	-0.56 82.5% ↑
May & Baker Nigeria Plc	Healthcare	1.87 16.58% ↓	0.13 18.75% ↓
Union Diagnostic & Clinical Services Plc	Healthcare	0.32 28.89% ↓	0.03 70% ↓
Tantalizers Plc	Services	0.31 22.5% ↓	0.08 33.34% ↑
Chams Plc	ICT	1.26 70.27% ↑	0.18 50% ↑
Law Union and Rock Insurance Plc	Financial Services	2.24 24.45% ↑	0.07 36.37% ↓
Union Home Real Estate Investment Trust	Real Estate/ Construction	0.12 20% ↓	0.08 20% ↓
Omoluabi Mortgage Bank Plc	Financial Services	0.13 8.34% ↑	0.03 25% ↓
C & I Leasing Plc	Services	7.81 20.52% ↑	0.40 8.11% ↑

Regulatory Actions

The National Broadcasting Commission suspends the operating license of DAAR

The National Broadcasting Commission has suspended indefinitely the operating license of DAAR Communications Plc, the parent company of Africa Independent Television (AIT) and Ray Power 100.6 FM (Abuja and Lagos). The suspension was as a result of the company's inability to pay the license renewal fees as well as complaints about the broadcast contents of the company. The immediate impact of this decision on the company's share price was neutral, as the share price was flat at N0.40 as at June 7th.

Securities and Exchange Commission concludes investigation of Oando Plc

The Securities and Exchange Commission concluded its investigation of Oando Plc following petitions that accused the company of certain infractions of securities and other relevant laws in 2017. The Commission engaged Deloitte & Touche to conduct a forensic audit of the company's activities. The findings of the report revealed infractions such as false disclosures, market abuses, misstatements in financial statements, internal control failures and corporate governance lapses. The Group Chief Executive Officer of the company, Mr. Wale Tinubu, and other affected board members were ordered to resign. SEC also barred Mr. Tinubu and the Deputy Group Chief Executive Officer of the company, Mr. Omamofe Boyo, from being directors of public companies for a period of five years. SEC has constituted an interim management team headed by Mr. Mutiu Sunmonu, a former MD of Shell SPDC. The team is expected to convene an Extra Ordinary General Meeting on or before July 1, 2019 to appoint a new Board of Directors for the company.

Oando reported total liabilities of N794.18 billion in Q1'19. A default on its loan repayments could raise the non-performing loan ratios of its creditors and ultimately weigh on their profitability in 2019. Oando's share price plunged 9.52% to N3.52 on June 7th.

Outlook

We expect the NSE to be bullish in the near term as investors take advantage of low stock prices on the market. However, a prolonged depressed oil prices could hamper the gains expected.

Equity Report: Flour Mills of Nigeria Plc

Analyst Recommendation: Buy

Market Capitalization: N54.74bn

Recommendation Period: 365 days

Current Price: N13.75

Industry: Food, Beverage and Tobacco

Target Price: N18.50

Analyst Note

Demand in the Food and Beverage industry remains tepid due to the sluggish economy. Weak income levels have necessitated adjustments that resulted in negative consequences on the volume of sales. Higher prices have constrained consumer spending power and discretionary incomes have shrunk while tax rates remain the same. These factors have worsened economic conditions leading to increased unemployment. Although the GDP grew, it is still fragile, tepid and non-inclusive. GDP growth rate stood at 1.9% in 2018, 0.7% lower than the population growth rate of 2.6%.

Investment in the food, beverage and tobacco sector is in line with an enormous potential for growth as Nigeria is the largest consumer market in sub-Saharan Africa.

We expect revenues to remain stable for key players in the industry as bread and other wheat derivative meals are still major staple foods in Nigeria. However, volume may contract as consumer income levels continue to struggle amid weak economic prospects.

High competitive environment weighs on topline

Flour Mills Nigeria (FMN) reported a contraction in its top-line and bottom-line for the nine-month period ending December 31, 2018 (9M'19).[26] The company's revenue declined toN400.64 billion, 6.29% lower than N427.51 billion recorded in 9M'18.Although all reporting segments recorded a decline in 9M 2019, the strongest headwinds came from FMN's sugar, posting a sales decline of -14% year over year, and agro-allied businesses, which saw sales declining by -10%year over year. These two revenue streams account for 32% of FMN total revenue. The dampened performance is largely attributed to the cost of raw material input, intense competition and logistics. Price competition, particularly in the animal feeds and sugar businesses, high input costs in the edible oil business and constraints emanating from the perennial gridlock in Apapa contributed to the decline in revenue.

Low finance cost – A switch to non-interest bearing instruments

Profit before tax declined by 42% to N11.28 million in 9M 2019. This was as a result of a 72% decline in other income, 47% increase in selling and distribution expenses and 12% increase in administrative expenses. The finance cost fell sharply to N16.55 million, a decline of 34%, when compared to N25.16 million in the same period in 2017. This resulted from the switch to non-interest bearing instruments, such as increasing the payable days and reducing receivable days. FMN's trade payables increased substantially by 210% to N30.95 billion from a negative of N28.15 billion. The profit after tax declined sharply by 41% to N7.88 million in Q3'18 from N13.27 million in Q3'17, despite lower tax expenses for the period. Tax expenses fell by 46% to N3.38 million from N6.26 million in the same period in 2017.

[26]Fiscal year ends March 31, 2019 (FY 2019)

Direct cost burden remains a major constraint and a common factor in the flour milling industry. Although the industry is still heavily reliant on importation of raw materials, efforts are made towards backward integration. The industry is optimal especially due to weak demand, which is a result of high prices generally. Nevertheless, investments in cost efficiency remain essential to maximizing profitability.

The flour milling industry is dominated by Flour Mills of Nigeria as it controls more than 40% of the market. Other leading players in the industry include Honeywell Flour Mills and Olam International (acquired Dangote Flour Mills). Despite the weak economic conditions, FMN recorded a remarkable profit compared to its competitors. This is evident in its earnings per share (EPS) of N1.89, which is 5% higher than that of Honeywell Flour Mills (N1.80), its listed rival on the Nigerian Stock Exchange (NSE).

FMN was incorporated on September 29, 1960 as a private limited liability company and was converted to a public limited company in November 1978. While the company's major business activity is flour milling, it has diversified into various business ventures over the years. The company pioneered flour milling in Nigeria through its first mill in Apapa in 1962 with a capacity of 500 metric tons/day. Now, its Apapa milling complex is the largest single site mill in the world with over 8,000 metric tons capacity. The food segment comprises approximately 79% of the company's revenue base. The company's food basket consists of semovita, pasta, noodles, snacks, margarine, vegetable oils, refined sugar, masavita and cereals.

Flour Mills diversified into woven polypropylene sack manufacturing in 1978 through its investment in BAGCO. With two plants in Kano and Lagos, the company engages in the packaging of flour, grains, salt, fertilizers, detergent and farm harvests. It also exports polymer bags to other African countries and the US. FMN further diversified into its agro-allied business in 1978 through its investment in the10,000 hectare Kaboji farm close to Niger state. There, it processes locally grown soybean, palm fruit, cassava, maize and sugarcane and stores and distributes agro-inputs (fertilizers).

Flour Mills invested greatly in support services, which deal with the manufacturing and marketing of packaging materials, power generation, transport logistics and port operations. The company diversified into cement through a large cement terminal in Apapa under Burham Cement and invested in United Cement Manufacturing Company Ltd (UNICEM) in 2012. However, the investment into cement was disposed of in 2015 to enable the company focus on its food and agro allied businesses.

In the management's quest to position the company for further growth and ensure optimal financial structures, the fertilizer business will be removed from FMN and registered as an independent company. However, this is subject to the approval of the Securities and Exchange Commission

Below is a snapshot of Flour Mill's latest annual financials.

Income Statement for Flour Mills of Nigeria					
N'000	**2014**	**2015**	**2016**	**2017**	**2018**
Revenue	325,790,187	308,756,526	342,586,459	524,464,448	542,670,409
Cost of Sales	(288,485,692)	(273,389,567)	(304,961,737)	(457,775,380)	(473,895,352)
Gross Profit	**37,304,495**	**35,366,959**	**37,624,722**	**66,689,068**	**68,775,057**
Other Gains and Losses (Other Income)	3,873,953	(685,050)	(7,720,517)	(1,488,216)	5,943,332
Selling and Distribution Expenses	(6,081,666)	(4,184,382)	(5,003,801)	(5,341,148)	(6,180,092)
Administration Expenses	(15,721,482)	(20,281,760)	(15,848,261)	(18,419,807)	(20,115,372)
Operating Profit	**19,375,300**	**10,215,767**	**9,052,143**	**41,439,897**	**48,422,925**
Investment Income	5,027,713	2,303,588	1,103,475	1,562,304	816,319
Finance Costs	(16,101,379)	(18,703,526)	(22,397,762)	(32,529,354)	(32,697,477)
Share of Loss in Associate Company	(73,651)	(381,012)	-	-	-
Gain on Disposal of Investment in Asso	-	14,289,953	23,731,422	-	-
Profit Before Tax	**8,227,983**	**7,724,770**	**11,489,278**	**10,472,847**	**16,541,767**
Income Tax Credit/(Expense)	(2,860,108)	738,292	2,931,006	(1,636,395)	(2,925,993)
Profit After Tax	**5,367,875**	**8,463,062**	**14,420,284**	**8,836,452**	**13,615,774**
Profit from Discontinued Operations		11,280	-		-
Profit for the Year	5,367,875	8,474,342	14,420,284	8,836,452	13,615,774

Balance Sheet for Flour Mills of Nigeria Plc					
N'000	**2014**	**2015**	**2016**	**2017**	**2018**
Property, plant and equipment	169,287,517	208,940,475	211,588,076	216,866,184	217,901,400
Intangible assets	554,905	496,248	735,330	208,370	1,095,317
Goodwill	4,148,022	4,148,022	4,148,022	4,148,022	4,148,022
Investment properties	-	-	2,023,379	1,929,196	1,841,977
Investment in subsidiaries	-	-	-	-	-
Investment in associates	7,790,094	-	-	-	-
Other financial assets/investments	135,456	114,716	45,696	24,140	62,900
Deferred charges/Deferred tax assets	-	411,431	66,022	1,846,674	6,459,761
Long-term loans receivable	11,457,561	3,904,188	-	989,022	944,472
Biological assets	609,112	58,509	352,020	29,131	37,710
Deposit for shares	-	-	-		-
Other long term assets	1,734,837	1,583,075	1,703,939	1,679,252	1,610,730
Prepayments					
Non-current assets	**195,717,504**	**219,656,664**	**220,662,484**	**227,719,991**	**234,102,289**
Inventories	63,683,942	68,426,003	58,698,768	117,296,162	111,373,409
Biological assets	144,885	399,081	182,613	558,480	179,653
Trade and other receivables	15,478,510	15,373,448	18,966,168	21,403,132	19,083,085
Prepayments	4,004,007	3,060,090	13,625,250	69,851,473	21,364,109
Non-current assets held for sale	-	3,514,035	-	755,516	-
Due from related companies	3,331,669	1,699,790	-	-	-
Cash and bank balances	16,825,163	31,131,719	33,213,043	45,018,503	22,245,372
Current assets	**103,468,176**	**123,604,166**	**124,685,842**	**254,883,266**	**174,245,628**
Total Assets	**299,185,680**	**343,260,830**	**345,348,326**	**482,603,257**	**408,347,917**
Share capital	1,192,842	1,312,126	1,312,126	1,312,126	2,050,197
Share premium	36,812,540	36,812,540	36,812,540	36,812,540	75,377,444
Fixed assets revaluation exercise	-	-	(89,760)	(111,316)	(72,556)
Capital reserve	281,201	281,201	-	-	-
Retained earnings	41,636,076	45,946,617	54,900,934	60,450,685	67,903,735
Equity attributable to owners of the compan	**79,922,659**	**84,352,484**	**92,935,840**	**98,464,035**	**145,258,820**
Non-controlling interest	3,636,773	3,057,910	2,829,934	4,080,309	5,357,888
Total Equity	**83,559,432**	**87,410,394**	**95,765,774**	**102,544,344**	**150,616,708**
Borrowings	48,614,076	55,260,645	48,009,715	50,879,043	29,376,221
Unsecured fixed rate bond	16,484,216	-	-	-	-
Deferred revenue	3,136,133	7,182,184	7,093,966	8,618,213	9,117,232
Deferred tax liabilities	11,117,827	9,607,954	5,768,040	7,819,480	12,307,605
Retirement benefit obligation	3,673,114	3,245,308	4,077,811	3,676,418	5,193,788
Long service award	1,317,571	1,340,140	1,593,819	1,568,859	1,948,287
Non-current liabilites	**84,342,937**	**76,636,231**	**66,543,351**	**72,562,013**	**57,943,133**
Borrowings	76,443,426	113,940,442	100,830,460	141,702,267	103,922,863
Unsecured fixed rate bond	10,424,384	19,248,115	-	-	-
Deferred revenue	865,738	1,472,527	1,076,024	2,089,158	2,578,896
Trade and other payables	38,116,032	42,560,787	50,416,914	94,567,170	56,993,533
Due to related companies	34,381	22,290	-	-	-
Provisions	16,109	47,126	-	-	-
Current tax liabilities	2,666,511	1,802,610	1,336,015	2,136,490	3,151,317
Customer Deposits	-	-	11,029,933	12,453,166	11,201,608
Dividend payable	92,297	120,307	1,936,869	2,032,098	2,005,814
Bank Overdraft			16,412,986	49,023,812	19,934,045
Derivative Liabiities	-	-	-	3,492,739	-
Current liabilites	**128,658,878**	**179,214,205**	**183,039,201**	**307,496,900**	**199,788,076**
Total liabilites	**213,001,815**	**255,850,436**	**249,582,552**	**380,058,913**	**257,731,209**
Total equity and liabilites	**296,561,247**	**343,260,830**	**345,348,326**	**482,603,257**	**408,347,917**

Management

Capable of capitalizing on potential growth opportunities in the food industry

Although FMN recorded a decline in revenue growth in its 9M financials, the earnings before interest, tax, depreciation and amortization (EBITDA), which is a true reflection of the company's earnings, increased by 15.19%.This shows that the management continues to make a significant effort to sustain returns, drive growth and remain a major player in Nigeria's food industry. Its ability to generate returns is evident in its series of capacity enhancement projects and launch of new flour brand varieties.

The successful N39.9 billion rights issue will provide the management with the much needed funds to pay down outstanding short term debt. This was evidenced in the reduction of finance costs by 34.22% for 9M financials. This reduction in finance costs will strengthen the balance sheet and management's drive to expand business.

Mr. Paul Gbededo is the Group Managing Director and Chief Executive Officer (CEO) of Flour Mills Nigeria Plc. He is a graduate of the Plastic and Rubber Institute (London) as well as an Associate of the National College of Rubber Technology from the Polytechnic of North London UK in 1980. He holds an MSc Degree in Polymer Technology from Loughborough University of Technology, UK. He joined Flour Mills in 1998 as the General Manager in charge of Golden Fertilizer and has since gained over 30 years of extensive experience in the Flour Milling industry.

Mr. John George Coumantaros is the Non-Executive Chairman of the Board of Directors. He has a BA in History from Yale University. He has over 30 years' experience in international trade, logistics and manufacturing industry. He joined Flour Mills in 1984 and was appointed to the board as a Non-Executive Director in 1990. Mr. Coumantaros is an experienced and successful entrepreneur and sits on the board of several international companies such as Oxbow Carbon LLC (an international energy company) and ELBISCO (a fast moving consumer food business in Greece). He replaced Mr. George Coumantaros, the founder of the company. George Coumantaros led the company through its inception in 1962 when it produced 600 metric tons per day to its current milling capacity of over 8,000 metric tons per day.

MD/CEO

Mr. Paul Gbededo

Chairman

Mr. John G Coumantaros

The Bulls Say and the Bears Say

Bulls say:

* Maintains market leadership in the Nigerian flour milling industry

* Rich product portfolio which ensures sustainability of revenue

* Renowned brand value

* Upward review of minimum wage to bolster consumer spending

* Talented and experienced management team proficient in technical and marketing skills

* Synergies from its investments in backward integration program

* Favorable government policies towards firms invested across Nigeria's agricultural value chains

* Innovative initiatives to improve customer's satisfaction

Bears say:

* Intense competition from other leading players such as Honeywell Flour Mills Plc and Olam International

* Poor infrastructure increases pressure on operating margins

* Shift of market preference to low-priced products

Risks and Outlook

The key risks that could prevent FMN from achieving its strategic goals and meeting shareholder expectations include currency risk, interest rate risk as well as credit and liquidity risk.

The management hedges against currency exposure using derivatives. In addition, FMN has invested extensively in its input commodities value chain through its involvement in the backward integration programme of agro-allied products. This would reduce the company's exposure to exchange rate risk.

To mitigate against interest rate risk, the company maintains a centralized treasury department, carrying out group borrowing to obtain lower interest rates. The group also negotiates long term credit facilities and obtains subsidized loans from the government in order to reduce the risk associated with high cost of borrowing.

Flour Mills addresses credit risk by setting credit limits and dealing primarily with credit worthy counterparts. The company transacts with corporate entities that are rated the equivalent of an investment grade or above. The company manages its liquidity risks by maintaining adequate reserves, banking facilities and reserve borrowing facilities.

Despite the severity of the risks facing Flour Mills, as olid risk management is in place. It includes its backward integration of agricultural projects, corporate growth and its productive use of debt to fund expansion. These strategies demonstrate that the company has a viable investment plan. As such, it is a company with prospects to enhance shareholder value.

Our Valuation

We derived our valuation for FMN by using the Discounted Cash Flow (DCF) methodology. Our fair value estimate for Flour Mills stood at **N18.50**, which is a 34.54% upside on its current share price of N13.75 as at May 28, 2019. The discount rate [weighted average cost of capital (WACC)] of 11.8% is derived using a 14.55% risk free rate [the yield for a 10-year Federal Government of Nigeria (FGN) bond maturing in April 2029], a beta of 1.06 an after-tax cost of debt of 7.8%, and a market risk premium of 6.4%. The calculated long-term cash flow growth rate to perpetuity is 5.0%.

Based on our analysis above, we place a BUY rating on the stock