

05 June 2018 | Sector Update

PLANTATION

Expect Earnings to Improve in 2HCY2018

Maintain POSITIVE

KEY HIGHLIGHTS

- An unexciting quarter in 1QCY18
- Underperformers are mostly caused by non-plantation divisions
- Expect earnings to improve in 2HCY2018
- Maintain our POSITIVE view on the sector
- Top picks are KLK and GENP

An unexciting quarter in 1QCY18. Out of the 10 plantation companies under our coverage, there are 2 outperformers, 4 underperformers and 4 within expectations. SIMEPLT and IJMLNT earnings are above expectation due to better than expected cost controls. As for the 4 underperformers, it is mostly due to non-plantation divisions except for TSH which was affected by higher than expected cost. The four companies with earnings matching expectations are IOICORP, KLK, PPB and GENP.

Table 1: Summary of Plantation Company Earnings In 1QCY2018

Company	Quarter	Cumulative CNP (RM m)		Comment On Result
		RM 'm	% YoY	
SIMEPLT	3QFY18/9MFY18	1006	18%	Above ours but within consensus expectations. Operating expenses came in lower than expected in 3QFY18 (declined 11% yoy).
IOICORP	3QFY18/9MFY18	925	12%	Within ours but above consensus. Consensus may have underestimated the FFB growth for IOICORP.
KLK	2QFY18/6MFY18	540	-19%	Within both ours and consensus expectations.
PPB	1QFY18/3MFY18	190	-44%	Within ours but below consensus. Consensus may have overestimated the earnings from PPB businesses in Malaysia.
FGV	1QFY18/3MFY18	20	NA	Below both ours and consensus expectation. Earnings contribution from associate came in weaker than expected.
GENP	1QFY18/3MFY18	73	-2%	Within both ours and consensus expectations.
IJMLNT	4QFY18/12MFY18	70	-41%	Above ours but below consensus expectations. Operating expenses came in lower than expected in 4QFY18 (declined 19% yoy).
TSH	1QFY18/3MFY18	5	-86%	Below both ours and consensus expectation. Cost came in higher than expected.
TAANN	1QFY18/3MFY18	5	-86%	Below both ours and consensus expectation. Lower than expected production of export logs.
FIMACOR	4QFY18/12MFY18	32	-55%	Below expectation due to weaker than expected earnings in the "production of security and confidential documents" division.

Source: Company, MIDF Research Compilation

Underperformers are mostly caused by non-plantation divisions. For FGV, its earnings contribution from associate came in weaker than expected. Meanwhile, TAANN has been affected by lower than expected production of export logs. Lastly, FIMACOR earnings are affected by weaker than expected earnings in the “production of security and confidential documents” division. Post 1QCY18 result, we have downgraded two stocks. These include FIMACORP (from BUY to NEUTRAL; TP from RM2.30 to RM1.95) and TAANN (from NEUTRAL to SELL; TP from RM3.20 to RM2.35).

Expect earnings to improve in 2HCY2018. We expect CPO price to improve in 2HCY2018 as we believe that the uptrend in production is now getting close to the end. Recall that palm oil production declined 1% mom in April-2018 but increased 0.7% yoy to 1.56m tonnes. The production decline mom from March to April is rare and this is the first time it occurs in 8 years. The increase of 0.7% yoy is a significant slowdown from March-2018 increase of 7.5% yoy and this could be an indicator that the strong uptrend in production may be over soon. Hence, we expect better CPO price in 2H2018 to translate into better earnings.

Maintain POSITIVE on the sector. We maintain our positive view on the sector as we expect CPO price to increase to USD650 per tonne in the next 3 months. The good global economy growth should lead to higher consumption per capita. Additionally, strong support on CPO demand came from the news that Indonesia plans to expand its biodiesel program to B25 (from B20 currently) in early 2019. On the supply side, consensus estimate of huge supply growth may not be fully realized as the upcycle in production is getting closer to its end.

Top picks are KLK and GENP. We like KLK for its earnings resiliency and decent dividend yield of 2.5%. We like GENP as we expect its FFB growth at 13% yoy to be the strongest among planters under our coverage. This is due to new contribution from recently acquired estate of 12,893 ha and 5000 ha coming to maturity in Indonesia.

Table 1: Target Price and Recommendations

Company	TP	Call	Valuation Basis
SIMEPLT	5.55	NEUTRAL	Blended 26.5x Target PE and 3.0x PB method.
IOICORP	4.50	NEUTRAL	23.0x Fwd. PE on FY18F earnings reflecting mean valuation.
KLK	28.50	BUY	26.8x Fwd. PE on FY18F earnings reflecting +1.0SD valuation.
PPB	19.40	NEUTRAL	1.1x Price To Book Value.
FGV	1.75	NEUTRAL	1.1x Price To Book Value reflecting mean valuation.
GENP	12.00	BUY	SOP with plantation sector @ 23.7x FY18F PE. 23.7x is at 10% discount to big cap planters Target PE.
IJMP	2.30	NEUTRAL	19.5x Fwd. PE on FY19F earnings reflecting mean valuation.
TSH	1.30	NEUTRAL	22.3x Fwd. PE on FY18F earnings reflecting mean valuation.
TAANN	2.35	SELL	12.5x Fwd. PE on FY18F earnings reflecting -0.5SD valuation.
FIMACOR	1.95	NEUTRAL	SOP with plantation sector @ 11.5x FY19F, PE. 11.5x is based on 40% discount to average Target PE for mid cap planters.

Source: MIDF Research Estimate

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.