

15 January 2018 | Sector Update

# PLANTATION

**Maintain POSITIVE**

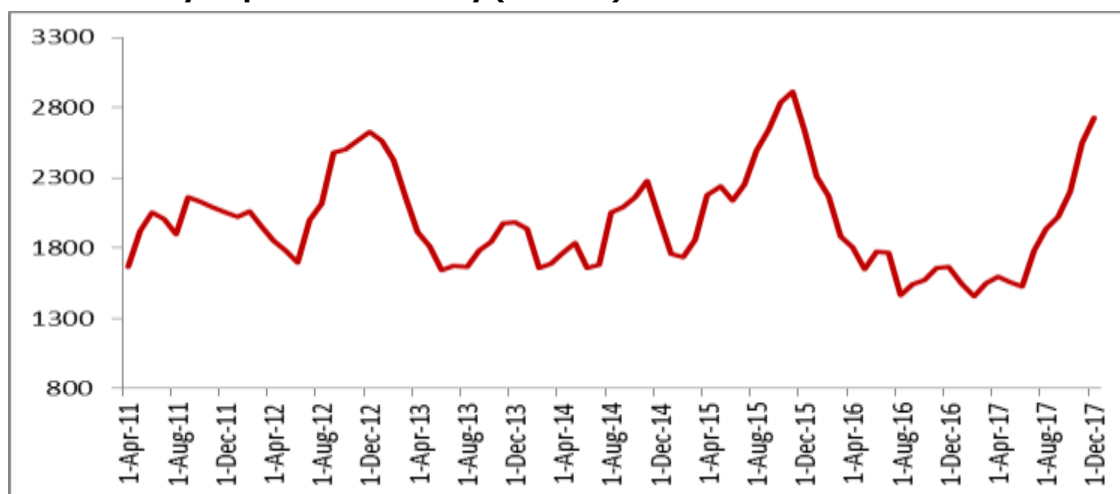
*Export to strengthen from January onwards*

## KEY HIGHLIGHTS

- **December inventory is higher than expected**
- **Export improved 5% mom**
- **Production declined in December**
- **The data is slightly negative to CPO price but export should strengthen from January onwards**
- **Expect December inventory to be flat at 2.73m MT**
- **Maintain POSITIVE view on the sector with IOICORP as top pick**

**December inventory is higher than expected.** Malaysia palm oil inventory level of 2.73m MT as of end-December 2017 is higher than market expectation of 2.69m MT. It is also higher than our estimate of 2.59m MT as export came in weaker than expected. Note that December export growth of 5% mom is lower than market expectation of 9% increase mom. Against last month, inventory level increased by 7% as total production and imports at 1.85m MT exceeded total export and local disappearance amount of 1.67m MT. Against same period last year, inventory is higher by 64% yoy (against November's increase of 54% yoy).

**Chart 1: Malaysia palm oil inventory ('000 MT)**



Source: Malaysia Palm Oil Board (MPOB)

**Export improved 5% mom.** Export increased 5% mom to 1.42m MT in December 2017. We gather that the export to European Union jumped 35% mom to 209,500 MT. This could be caused by the widening discount of palm oil against rapeseed oil and soybean oil in December which has improved palm oil competitiveness against competing vegetable oils. Despite the increase in export, the growth is limited at 5% as strong Ringgit factor capped the upside. Note that Ringgit has strengthened by 1.1% mom to 4.0465 by end-December.

**Table 1: Palm Oil Statistics for December-2017 ('000 MT)**

|                          | Dec-17       | Nov-17       | Diff.        | MoM %        | Dec-16       | YoY%         |
|--------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| <b>Opening Stocks</b>    | <b>2,554</b> | <b>2,204</b> | <b>350</b>   | <b>15.9%</b> | <b>1,663</b> | <b>53.6%</b> |
| <b>Production</b>        | <b>1,834</b> | <b>1,943</b> | <b>(109)</b> | <b>-5.6%</b> | <b>1,474</b> | <b>24.5%</b> |
| Imports                  | 15           | 30           | (15)         | -50.3%       | 45           | -66.5%       |
| <b>Total Supply</b>      | <b>4,403</b> | <b>4,177</b> | <b>226</b>   | <b>5.4%</b>  | <b>3,181</b> | <b>38.4%</b> |
| Exports                  | 1,423        | 1,356        | 67           | 4.9%         | 1,268        | 12.2%        |
| Dom Disapp               | 248          | 267          | (18)         | -6.9%        | 247          | 0.7%         |
| <b>Total Demand</b>      | <b>1,671</b> | <b>1,623</b> | <b>48</b>    | <b>3.0%</b>  | <b>1,515</b> | <b>10.3%</b> |
| <b>End Stocks</b>        | <b>2,732</b> | <b>2,554</b> | <b>178</b>   | <b>7.0%</b>  | <b>1,667</b> | <b>63.9%</b> |
| <b>Stock/Usage Ratio</b> | <b>13.6%</b> | <b>13.1%</b> |              |              | <b>9.2%</b>  |              |

Source: MPOB, MIDF Research

**Table 2: Monthly Exports and YTD Exports ('000 MT)**

| Country      | Dec-17       | Nov-17       | Dec-16       | MoM%      | YoY%       | 12M17         | 12M16         | YoY%      |
|--------------|--------------|--------------|--------------|-----------|------------|---------------|---------------|-----------|
| China        | 175          | 204          | 159          | -14%      | 10%        | 1,917         | 1,872         | 2%        |
| India        | 107          | 100          | 165          | 7%        | -35%       | 2,025         | 2,820         | -28%      |
| EU           | 209          | 155          | 173          | 35%       | 21%        | 1,989         | 2,049         | -3%       |
| Pakistan     | 84           | 94           | 96           | -11%      | -12%       | 1,017         | 880           | 15%       |
| US           | 66           | 53           | 35           | 25%       | 87%        | 555           | 590           | -6%       |
| Others       | 781          | 750          | 640          | 4%        | 22%        | 9,032         | 7,806         | 16%       |
| <b>Total</b> | <b>1,423</b> | <b>1,356</b> | <b>1,268</b> | <b>5%</b> | <b>12%</b> | <b>16,535</b> | <b>16,017</b> | <b>3%</b> |

Source: MPOB, MIDF Research

**Production declined 6% in December.** Palm oil production declined 6% mom but was up 24% yoy to 1.83m MT in December. This confirmed our belief that production has peaked in October and the trend of seasonal production decline has resumed in December. Going forward, we expect January production to decline by 9% to 1.67m MT.

**The data is slightly negative to CPO price but export should strengthen from January onwards.** Overall, we are slightly negative on CPO price as the latest inventory data came in higher than market expectation. However, we remain positive on the sector as the latest move by Malaysia government to temporary suspend CPO export tax price should encourage demand from major consumers such as China and India.

**Expect December inventory to be flat at 2.73m MT.** We expect export to improve 1% mom as the temporary suspension of palm oil export tax for three months should bode well for demand. As mentioned previously, we expect production to decline 9% to 1.67m MT in January due to seasonal factor.

**Maintain our POSITIVE view on the sector.** We maintain our palm oil price forecast of RM2900 per MT for 2018. Reiterate positive view on the sector due to improved demand outlook for palm oil in 2018. We also think that the supply growth may not be fully realized due to ongoing labour shortage and the high replanting activity planned by major plantation companies.

**Top pick is IOICORP (BUY; TP: RM5.50).** Top Pick for the sector is IOICORP due to: i) overall margin improvement at the Group level after sale of 70% stake in Lodders Crokiaan (Lodders), ii) special dividend of 13.0 sen and iii) net gearing is expected to decline significantly to 0.25x (from 0.78x). We also have BUY calls on KLK, GENP, TSH, TAANN and FIMACORP.

**Chart 2: Discount between palm oil and soybean oil**



Source: Bloomberg

**Table 1: Target Price and Recommendations**

| Company | TP    | Call    | Valuation Basis  |
|---------|-------|---------|--|
| SIMEPLT | 5.60  | NEUTRAL | Blended 26.5x Target PE and 3.0x PB method.  |
| IOICORP | 5.50  | BUY     | 26.3x Fwd. PE on FY18F earnings reflecting +1.0SD valuation.   |
| KLK     | 29.00 | BUY     | 26.8x Fwd. PE on FY18F earnings reflecting +1.0SD valuation.   |
| PPB     | 17.69 | NEUTRAL | 1.0x Price to Book Value   |
| FGV     | 1.96  | NEUTRAL | 1.23x Price to Book Value reflecting +0.5SD valuation  |
| GENP    | 12.60 | BUY     | SOP with plantation sector @ 24.7x FY17F PE. 24.7x is the lower valuation between IOICORP and KLK.                     |
| IJMP    | 2.85  | NEUTRAL | 19.5x Fwd. PE on FY18F earnings reflecting mean valuation.   |
| TSH     | 1.90  | BUY     | 22.3x Fwd. PE on FY17F earnings reflecting mean valuation.   |
| TAANN   | 4.50  | BUY     | 16.6x Fwd. PE on FY17F earnings reflecting mean valuation.   |
| FIMACOR | 2.60  | BUY     | SOP with plantation sector @ 11.5x FY18F 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 >15% over the next 12 months.   |
| TRADING BUY  | Stock price is expected to <i>rise</i> by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.  |
| NEUTRAL      | Total return is expected to be between -15% and +15% over the next 12 months.  |
| SELL         | Total return is expected to be <-15% over the next 12 months.  |
| TRADING SELL | Stock price is expected to <i>fall</i> by >15% 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. |