

13 March 2017 | Sector Update

## PLANTATION

**Maintain NEUTRAL**

**February inventory came in within expectation**

### KEY HIGHLIGHTS

- **February inventory came in within expectation**
- **Production has increased yoy consecutively for the third months**
- **Weak export due to low demand from China**
- **Expect March-2017 inventory to increase 11% mom to 1.62m MT**
- **Maintain NEUTRAL view with BUY call on KLK**

**February inventory came in within expectation.** Malaysia palm oil inventory level of 1.46m MT as of end-February 2017 is close to consensus estimate of 1.48m MT. It is also close to our estimate of 1.47m MT. Against last month, inventory level declined by 5% despite 14% slip in export due to strong local consumption and low production (down 1% mom). Against same period last year, inventory remains significantly lower yoy as it has tumbled 33%yoy.

**Production has increased yoy consecutively for the third months.** The monthly decline in production driven by lower production in Sabah (down 7% mom to 323,244 MT). This is followed by Sarawak in which production slipped 7% mom to 274,848 MT. Surprisingly, Peninsular Malaysia production increased 4% mom to 660,446 MT despite the shorter calendar months. On a yearly basis, production has increased by 21% and this suggests that the palm trees have started to recover from the impact of severe El Nino.

**Weak export due to low demand from China.** Export to China declined 38% mom to 103,169 MT and we think this is caused by the coldest weather there during February. Note that palm oil usage tends to be lower in cold weather as it will solidify. Meanwhile, export to India declined 4% mom to 133,488 MT possibly due to higher use of domestically produced vegetable oils there.

**Expect March-2017 inventory to increase 11% mom to 1.62m MT.** Key assumptions are: i) production increase of 13% mom and ii) export decline of 3% mom. We are expecting lower export of palm oil in the absence of any major festivals in March. Although cargo surveyors data shows much higher decline in export by 25%mom in the first ten days of March, we believe that the drop is not representative of the full month impact due to the short number of days covered. For production growth we are using seasonal factor to estimate the 13% increase.

**Stay NEUTRAL; Our only BUY call is KLK (TP: RM29.25).** We reiterate our NEUTRAL view on the sector with 2017 average CPO price of RM2725 per MT unchanged. The best earnings quarter in the recent years has been registered in 4QCY2016. In the coming quarter of 1QCY17, planters earnings is expected to be lower qoq as the expected 6% rise in CPO price is not enough to offset the 25% decline in FFB volume. Our Top Pick for the sector is KLK (BUY with TP of RM29.25) as the Company's 1QCY17 result should fare better against other planters as it has locked in forward sales when the CPO price is high. The Company's earnings are also resilient and matched consensus expectation most of the time.

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

|                          | Feb-17       | Jan-17       | Diff.        | MoM %        | Feb-16       | YoY%          |
|--------------------------|--------------|--------------|--------------|--------------|--------------|---------------|
| <b>Opening Stocks</b>    | <b>1,541</b> | <b>1,667</b> | <b>(126)</b> | <b>-7.5%</b> | <b>2,309</b> | <b>-33.2%</b> |
| <b>Production</b>        | <b>1,259</b> | <b>1,277</b> | <b>(18)</b>  | <b>-1.4%</b> | <b>1,043</b> | <b>20.7%</b>  |
| Imports                  | 40           | 72           | (31)         | -43.7%       | 68           | -40.3%        |
| <b>Total Supply</b>      | <b>2,840</b> | <b>3,015</b> | <b>(175)</b> | <b>-5.8%</b> | <b>3,419</b> | <b>-16.9%</b> |
| Exports                  | 1,107        | 1,287        | (180)        | -14.0%       | 1,085        | 2.0%          |
| Dom Disapp               | 274          | 187          | 87           | 46.3%        | 165          | 66.1%         |
| <b>Total Demand</b>      | <b>1,381</b> | <b>1,474</b> | <b>(93)</b>  | <b>-6.3%</b> | <b>1,250</b> | <b>10.5%</b>  |
| <b>End Stocks</b>        | <b>1,459</b> | <b>1,541</b> | <b>(82)</b>  | <b>-5.3%</b> | <b>2,169</b> | <b>-32.7%</b> |
| <b>Stock/Usage Ratio</b> | <b>8.8%</b>  | <b>8.7%</b>  |              |              | <b>14.5%</b> |               |

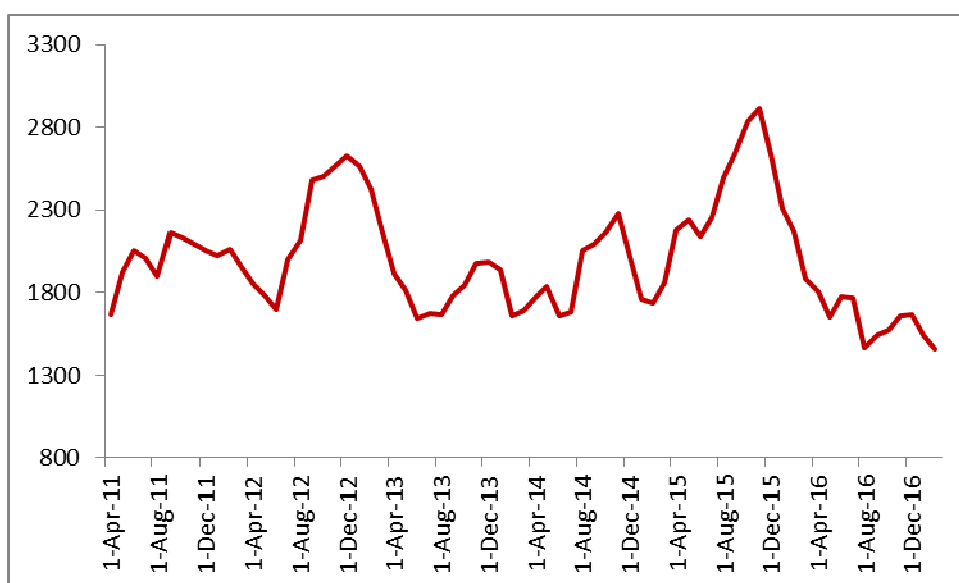
Source: MPOB, MIDF Research

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

| Country      | Feb-17       | Jan-17       | Feb-16       | MoM%       | YoY%       | 2M17         | 2M16         | YoY%      |
|--------------|--------------|--------------|--------------|------------|------------|--------------|--------------|-----------|
| China        | 103          | 167          | 53           | -38%       | 94%        | 271          | 158          | 72%       |
| India        | 133          | 139          | 178          | -4%        | -25%       | 273          | 441          | -38%      |
| EU           | 153          | 137          | 209          | 12%        | -27%       | 290          | 394          | -26%      |
| Pakistan     | 49           | 48           | 21           | 3%         | 130%       | 97           | 86           | 12%       |
| US           | 36           | 36           | 50           | 1%         | -27%       | 72           | 108          | -33%      |
| Others       | 783          | 750          | 574          | 4%         | 36%        | 1,533        | 1,178        | 30%       |
| <b>Total</b> | <b>1,259</b> | <b>1,277</b> | <b>1,085</b> | <b>-1%</b> | <b>16%</b> | <b>2,535</b> | <b>2,365</b> | <b>7%</b> |

Source: MPOB, MIDF Research

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



Source: Malaysia Palm Oil Board (MPOB)

**Table 3: Basis of valuation**

| Company | TP    | Call    | Valuation Basis  |
|---------|-------|---------|--|
| SIME    | 9.00  | NEUTRAL | SOP with plantation sector @ 26.8x FY17E PE. 26.8x is the higher of IOICORP and KLK Target PE.     |
| IOICORP | 5.30  | NEUTRAL | 24.7x Fwd. PE on FY17F earnings reflecting +0.5SD valuation.                                       |
| KLK     | 29.25 | BUY     | 26.8x Fwd. PE on FY17F earnings reflecting +1.0SD valuation.                                       |
| PPB     | 17.69 | NEUTRAL | 1.0x Price to Book Value   |
| FGV     | 1.77  | NEUTRAL | 1.0x Price to Book Value   |
| GENP    | 11.55 | NEUTRAL | SOP with plantation sector @ 24.7x FY17E PE. 24.7x is the lower valuation between IOICORP and KLK. |
| IJMP    | 3.53  | NEUTRAL | 18.6x Fwd. PE on FY17F earnings reflecting mean valuation.   |
| TSH     | 2.15  | NEUTRAL | 22.3x Fwd. PE on FY17F earnings reflecting mean valuation.   |
| TAANN   | 4.25  | NEUTRAL | 16.6x Fwd. PE on FY17F earnings reflecting mean valuation.   |

Source: MIDF Research Estimate

Alan Lim, CFA  
[alan.lim@midf.com.my](mailto:alan.lim@midf.com.my)  
03-21738464

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).  
 (Bank Pelaburan)  
 (A Participating Organisation of Bursa Malaysia Securities Berhad)

## DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein. This document may not be reproduced, distributed or published in any form or for any purpose.

### 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. |