

11 November 2016 | Sector Update

PLANTATION

Maintain POSITIVE

Inventory numbers came in below consensus estimate

KEY HIGHLIGHTS

- **October inventory came in below consensus estimate**
- **Slight slowdown in demand from India and China**
- **Production unexpectedly decline mom and may have peaked in September**
- **Expect Nov-2016 inventory to increase by only 3% to 1.63m MT.**
- **Maintain POSITIVE view on. BUY KLK (TP: RM27.38) and IOICORP (TP: RM5.05)**

October inventory came in below consensus estimate. Malaysia palm oil inventory level of 1.57m MT as of end-October 2016 is spot on as per our estimate but came in below consensus estimate of 1.67m-1.68m MT. We believe that consensus have underestimated the impact of lagged El Nino impact which has caused October production to decline 2%mom (against historical pattern of increasing). Against last month, inventory level has inched up by only 2%mom as production remains very limited. Against same period last year, inventory remains significantly lower yoy as it has tumbled 44%yoy.

Slight slowdown in demand from India and China. Export to India dropped 22% mom to 203,898 MT while export to China slipped 5% mom to 187,204 MT. Usage of palm oil may have temporary declined in China in the absence of stocking activity ahead of major festival. As for India, the end of stocking activity for Deepavali festival have caused lower demand for palm oil.

Production unexpectedly decline mom and may have peaked in September. Sarawak production declined the most by 4% mom to 350,773 MT. This is followed by Peninsular Malaysia in which production slipped 2% mom to 855,692 MT. Lastly, Sabah production fell 1% mom to 471,408 MT. On a yearly basis, production tumbled 18% and this suggests that the impact of El Nino is still there.

Expect Nov-2016 inventory to increase by only 3% to 1.63m MT. Key assumptions are: i) export decline of 6%mom and ii) production decline of 2%. We are expecting export decline as colder temperature in Northern Hemisphere should lead to lower usage of palm oil in China and European Union. However, the inventory is expected to remain tight as it is only expected to increase by 3% mom as production is also expected to decline 2% mom. Cargo surveyors' data shows export decline of 16%mom in the first ten days of November. For production growth we are using seasonal factor to estimate the 2% decline.

Maintain POSITIVE view on the sector. BUY KLK (TP: RM27.38) and IOICORP (TP: RM5.05). We expect CPO price to remain high at the range of RM2500 to RM3000 per MT in the next three months. We like KLK (BUY; TP RM27.38) due to its high exposure to palm oil business and good earnings growth of +18%yoy to RM747m in 9MFY16. We also like IOICORP (BUY; TP RM5.05) due to its pure exposure to palm oil business both in the upstream and downstream divisions. The Company's profit is also expected to recover in FY17 after the uplift of RSPO suspension.

Table 1: Palm Oil Statistics for October-2016 ('000 MT)

	Oct-16	Sep-16	Diff.	MoM %	Oct-15	YoY%
Opening Stocks	1,546	1,464	82	5.6%	2,642	-41.5%
Production	1,678	1,715	(37)	-2.2%	2,037	-17.6%
Imports	27	2	25	1398.7%	73	-63.4%
Total Supply	3,251	3,181	70	2.2%	4,752	-31.6%
Exports	1,431	1,451	(20)	-1.4%	1,712	-16.4%
Dom Disapp	246	183	63	34.2%	207	19.1%
Total Demand	1,677	1,635	42	2.6%	1,918	-12.6%
End Stocks	1,574	1,546	28	1.8%	2,834	-44.5%
Stock/Usage Ratio	7.8%	7.9%			12.3%	

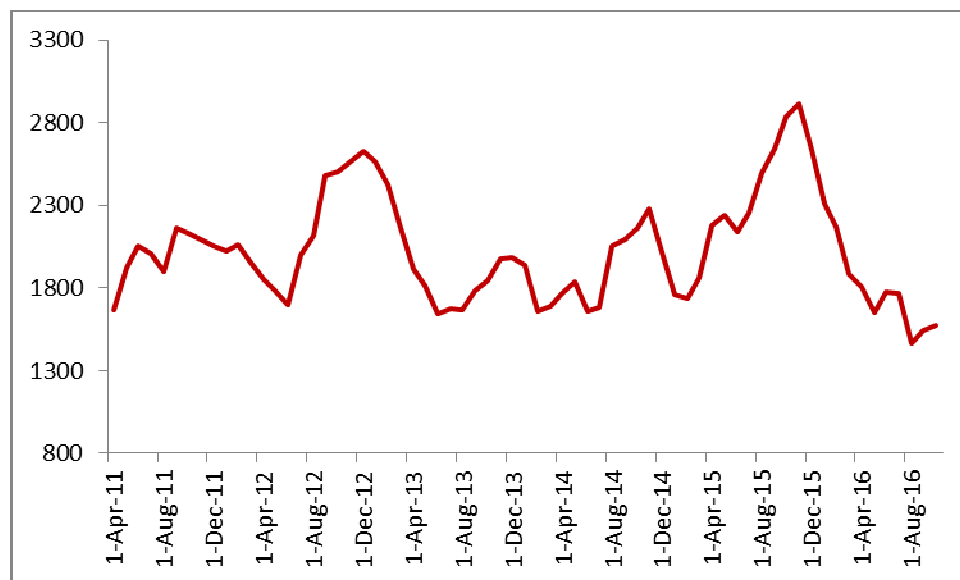
Source: MPOB, MIDF Research

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

Country	Oct-16	Sep-16	Oct-15	MoM%	YoY%	10M16	10M15	YoY%
China	187	198	167	-5%	12%	1,495	2,125	-30%
India	204	262	441	-22%	-54%	2,523	2,960	-15%
EU	226	172	222	31%	2%	1,714	1,934	-11%
Pakistan	88	92	58	-4%	53%	694	602	15%
US	36	40	75	-10%	-52%	513	581	-12%
Others	690	687	749	0%	-8%	6,439	6,256	3%
Total	1,431	1,451	1,712	-1%	-16%	13,379	14,457	-7%

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	7.75	NEUTRAL	SOP with plantation sector @ 25.1x FY17E PE. 25.1x is the avg of IOICORP and KLK Target PE.
IOICORP	5.05	BUY	24.7x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
KLK	27.38	BUY	26.8x Fwd. PE on FY16F earnings reflecting +1.0SD valuation.
PPB	14.70	NEUTRAL	19.5x Fwd. PE on FY17F earnings reflecting mean valuation.
FGV	1.77	NEUTRAL	1.0x Price to Book Value.
GENP	9.72	NEUTRAL	SOP with plantation sector @ 24.7x FY17E PE. 24.7x is the lower valuation between IOICORP and KLK.
IJMP	3.13	NEUTRAL	18.6x Fwd. PE on FY17F earnings reflecting mean valuation.
TSH	2.10	NEUTRAL	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	3.50	NEUTRAL	16.6x Fwd. PE on FY16F earnings reflecting mean valuation.

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.