

13 July 2016 | Sector Update

PLANTATION

Maintain POSITIVE***June inventory level is within expectation***

KEY HIGHLIGHTS

- **June 2016 inventory level of 1.78m MT is within expectation**
- **Exports declined -12%mom due to weaker demand from India**
- **Production increased 12%mom to 1.53m MT**
- **Strong Brent crude oil price has improved biodiesel consumption in Malaysia and Indonesia**
- **Expect July inventory to increase 11%mom to 1.96m MT**
- **USDA is expecting global soybean oil inventory to decline**
- **Maintain POSITIVE view on the sector. Top pick is KLK (TP: RM27.38)**

June 2016 inventory level of 1.78m MT is within expectation as it is only 3% above consensus estimate of 1.72m MT but 3% below our estimate of 1.83m MT. Moreover, the inventory figure increased 8%mom, the first increase in seven months, but nonetheless it declined -17%yoy. Separately, exports for the first 10 days have improved between 5% and 9% based on cargo surveyors' data.

Exports declined -12%mom due to weaker demand from India. Note that export to India slipped -49%mom to 159k MT after the end of stocking activity for Ramadhan month. Demand from China is also weak (-5% to 101k MT). However, we believe that demand from China should pick up due to stocking activity ahead of the Mid-Autumn Festival which will fall on 15-Sep this year.

Production increased 12%mom to 1.53m MT and this is within the seasonal pattern seen historically. Sarawak production growth is the highest at 17%mom to 311,060 MT followed by Sabah (15%mom to 461,788 MT) and Peninsular Malaysia (9%mom to 759,765 MT). Having said that, the tree stress impact continues in Jun-2016 as production is lower by -13%yoy.

Strong Brent crude oil price has improved biodiesel consumption in Malaysia and Indonesia. Average Brent crude oil price has increased 5%mom to USD49.93/barrel in June and we believe that this has improved local palm oil consumption in Malaysia (via higher biodiesel consumption). Note that local consumption of 293,587 MT in Malaysia is a new record high. The significantly low imports of palm oil from Indonesia (-2%mom and -81%yoy) should be caused by the high usage of biodiesel in Indonesia hence limiting supply from there.

Expect July inventory to increase 11%mom to 1.96m MT. Our key assumptions are: i) 8%mom increase in production in line with historical production pattern, and ii) 5% increase in export due stocking up activity ahead of Mid-Autumn festival in China.

USDA is expecting global soybean oil inventory to decline. The latest World Agriculture Supply and Demand Estimate (WASDE) by United States Department of Agriculture (USDA) shows that soybean oil inventory is expected to decline by -5% or 200,000 MT to 3.67m MT in 2016/2017 season. We gather that the ending stocks estimate has been reduced to 3.67m MT (against last month estimate of 3.72m MT).


Maintain POSITIVE view on the sector. We maintain our average CPO price assumption of RM2,450/MT (YTD: RM2,506/MT) for the year 2016 which is 14% higher than 2015 average of RM2,153.50/MT. We believe that China is likely to stock up palm oil in the near term as the inventory has fall down to below average level in major ports. Our top pick is KLK due to: i) its earnings is expected to benefit from high CPO price due to its high exposure to palm oil business, ii) good earnings growth of +41%yoy to RM536m in 1HFY16, and iii) it is one of the rare big cap index-linked planters which is Shariah compliant and also an RSPO member. 

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

	Jun-16	May-16	Diff.	MoM %	Jun-15	YoY%
Opening Stocks	1,650	1,804	(154)	-8.5%	2,249	-26.6%
Production	1,533	1,365	168	12.3%	1,764	-13.1%
Imports	20	20	(0)	-1.9%	103	-81.0%
Total Supply	3,202	3,189	14	0.4%	4,116	-22.2%
Exports	1,132	1,282	(150)	-11.7%	1,697	-33.3%
Dom Disapp	294	256	37	14.6%	267	9.8%
Total Demand	1,426	1,539	(113)	-7.3%	1,965	-27.4%
End Stocks	1,776	1,650	126	7.7%	2,151	-17.4%
Stock/Usage Ratio	10.4%	8.9%			9.1%	

Source: MPOB, MIDF Research

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

Country	Jun-16	May-16	Jun-15	MoM%	YoY%	6M16	6M15	YoY%
China	101	106	244	-5%	-59%	601	1,280	-53%
India	159	310	436	-49%	-63%	1,418	1,546	-8%
EU	151	117	217	29%	-30%	892	1,018	-12%
Pakistan	88	77	72	16%	24%	368	344	7%
US	30	59	44	-49%	-32%	308	326	-5%
Others	602	613	685	-2%	-12%	3,693	3,334	11%
Total	1,132	1,282	1,697	-12%	-33%	7,279	7,847	-7%

Source: MPOB, MIDF Research

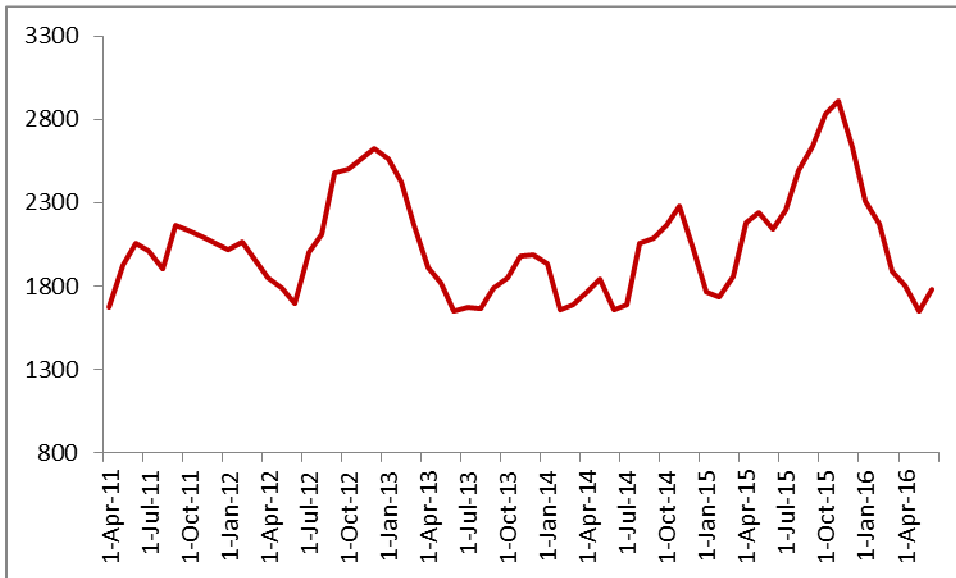
Table 3: Global Soybean Oil Statistics ('000 000 MT)

	2014/15*	2015/16F	2016/17F
Inventory (Begin)	3.63	3.62	3.87
Production	49.06	52.19	53.82
Import	10.08	11.72	11.01
TOTAL SUPPLY	62.77	67.53	68.70
Export	11.1	12.47	11.96
Domestic	48.04	51.20	53.07
TOTAL DEMAND	59.14	63.67	65.03
Inventory (End)	3.62	3.87	3.67

*Marketing year which begin in October and ends in September

Source: US Department of Agriculture

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



Source: Malaysia Palm Oil Board (MPOB)

Table 4: Basis of valuation

Company	TP	Call	Valuation Basis
SIME	7.85	NEUTRAL	SOP with plantation sector @ 25.1x FY17E PE. 25.1x is the avg of IOICORP and KLK Target PE.
IOICORP	4.82	BUY	23.1x Fwd. PE on FY16F earnings reflecting mean valuation.
KLK	27.38	BUY	26.8x Fwd. PE on FY16F earnings reflecting +1.0SD valuation.
PPB	18.60	BUY	21.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
FGV	1.33	NEUTRAL	1.0x Price to Net Tangible Asset (P/NTA).
GENP	9.85	NEUTRAL	SOP with plantation sector @ 23.5x FY16E PE. 23.5x is the lower valuation between IOICORP and KLK.
IJMP	3.13	NEUTRAL	18.6x Fwd. PE on FY16F 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.