

01 June 2016 | Sector Update

## PLANTATION

**Maintain POSITIVE*****Progressive implementation of B10 from June onwards***

### KEY HIGHLIGHTS

- **B10 effective today**
- **Annual domestic consumption of 709,000 MT**
- **Positive on the news**
- **Biodiesel consumption has improved in Malaysia**
- **Separately, we expect Malaysia palm oil inventory to decline 7%mom to 1.70m MT in May**
- **Maintain POSITIVE view on the sector and our top pick is KLK (TP: RM27.38)**

**B10 effective today.** The Plantation Industries and Commodities Ministry of Malaysia has announced the increase of biodiesel blend for the transport sector to B10. As for industrial sector (which cover commercial and power generation sector), the B7 Programme will be implemented for the first time. We gather that both programmes are to be implemented progressively from June.

**Annual domestic consumption of 709,000 MT.** Both programmes are expected to contribute to annual domestic consumption of crude palm oil of 709,000 MT. Additionally, there will be savings of 820m litres of diesel and 2.16m MT of carbon dioxide annually. According to the Ministry, "This is expected to contribute towards meeting Malaysia's commitment in the Conference of Parties (COP 21) under the United Nations Framework Convention on Climate Change (UNFCCC) to reduce greenhouse gas (GHG) emission by 45% by 2030 based on 2005 emission intensity".

**Positive on the news.** The news is positive to CPO price as higher biodiesel consumption locally should reduce the inventory of palm oil in Malaysia. In the long run, we expect the biodiesel program to keep the total inventory at manageable level of below 2.5m MT especially during the peak production month between September to November.

**Biodiesel consumption has improved in Malaysia.** We believe that the increase in local palm oil consumption in Malaysia for April is likely to be caused by higher biodiesel consumption. As it is, April palm oil consumption locally has increased by 8.7%mom and 1.6%yoy to 263,771 MT.

**Separately, we expect Malaysia palm oil inventory to decline 7%mom to 1.70m MT in May.** Our key assumptions are: i) 7%MoM increase in production in line with historical production pattern, and ii) 11% improvement in export due to stocking up activity ahead of Ramadhan. Note that the usage of palm oil usually picks up during Ramadan month (which should begin around 6-June) as Muslims break day-long fasts with communal meals.

**Maintain POSITIVE view on the sector. Top pick is KLK (TP: RM27.38).** We maintain our bullish view on CPO price. However, our RM3000/MT target has been shifted to end-August due to slower than expected demand from China recently. Our top pick is KLK due to: i) 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) one of the rare big cap index-linked planters which is Shariah compliant and also an RSPO member.



**Table 1: Basis of valuation**

<b>Company</b>	<b>TP</b>	<b>Call</b>	<b>Valuation Basis</b>
SIME	7.85	NEUTRAL	SOP with plantation sector @ 25.1x FY17E PE. 25.1x is the avg of IOICORP and KLK Target PE.
IOICORP	4.25	NEUTRAL	20.4x 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	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	4.20	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.