PLANTATION

Maintain NEGATIVE

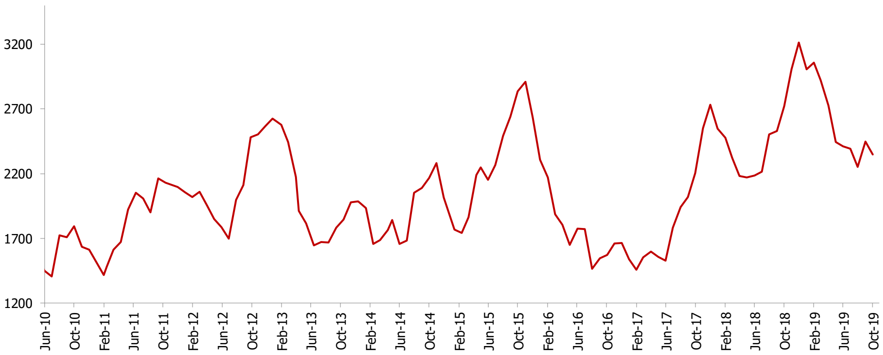
Sharp sequential decline in export to India

KEY INVESTMENT HIGHLIGHTS

- **October 2019 inventory declined by -14.4%yoy to 2.3m metric tonnes (mt) which was a slight reprieve but remained higher than in October 2017 and 2016 by +6.6% and +49.2% respectively.**
- **The export demand in October 2019 increased slightly by +4.0%yoy, mainly attributable to the steady demand growth from India (+121.4%yoy), China (+26.0%yoy) and the EU (+19.6%yoy)**
- **The CPO price continues to be on the recovery path amidst the lower-than-expected output and higher-than-expected export demand**
- **Maintain NEGATIVE stance on the sector with an unchanged 2019 CPO target price of RM2,090/mt**

Inventory level took a breather. Malaysian palm oil inventory in October 2019 fell by -14.4%yoy to 2.3m mt, the level last seen in July 2019. This was mainly attributable to the lower-than-anticipated output of 18.m which translates into a decline of -8.6%yoy amidst the typical seasonal higher production period and a steady export demand of +4.0%yoy to 1.6m mt. The stockpiles level also came in below Bloomberg and Reuters expectations by -7.6% and -6.7% respectively. We also observed that the larger year-over-year drop in inventory was largely due to high base effect seen in the 4Q18. Should the fall in production signals the end of the peak cycle, we are of the view that inventory may trend lower in coming months given the expectation of steady export demand growth.

Chart 1: Malaysia Palm Oil Inventory ('000 MT)



Source: Malaysia Palm Oil Board (MPOB), MIDFR

Higher-than-expected export demand. On a year-over-year basis, October 2019 export increased by +4.0%yoy to circa 1.6m mt. This came in above the expectation of Bloomberg and Reuters consensus by +3.9% and +3.0% respectively. We opine that the higher-than-expected export demand was primarily due to the purchases from India, China and EU. We are of the view that the increase in palm oil imports by China was primarily due to its low vegetable oil stocks in its country amidst the US-China trade war and African Swine Fever. The lower supply of soybean and weaker soy-based feed meal demand may have tilted the favour to palm oil imports as an alternative as both are close substitutes. As such, we have observed a rise in China's October 2019 import of palm oil by +26.0%yoy. We opine that the rose in EU market demand by +19.6%yoy to 200k mt in October 2019 continues to be used for larger biodiesel consumption.

COMPANY IN FOCUS

Sime Darby Plantation Bhd
Maintain **SELL |** Unchanged Target price: RM4.08
Price @ 11th November 2019: RM4.98

- Low CPO price continues to negatively impact the group's upstream operations
- Cost management efforts is insufficient to provide meaningful buffer
- We expect dividend payout to be unattractive leading to dividend yield of less than one percent

Share price chart

IOI Corporation Bhd
Maintain **SELL |** Unchanged Target price: RM3.48
Price @ 11th November 2019: RM4.40

- Low CPO price continues to negatively impact the group's normalised earnings
- Impact of lower CPO and PK prices were further aggravated by softer FFB production
- The higher effective tax rate also led to contraction in the group's profit margin

Share price chart

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However, there is a weakening demand growth from India as the Indian government raised additional tariff rate of 5.0% on Malaysian refined palm oil on 4th September 2019 to 50.0%. This is predicated on the fact that the purchases might be shifted towards Indonesian palm oil which has a cheaper pricing than Malaysian palm oil. The underperformance from the region could be also due to the halting of purchases by some Indian buyers in fear of a trade ban on Malaysian palm oil over Kashmir issue as the Mumbai-based Solvent Extractors' Association of India has called for a ban. This was manifested through a sharp decline of -29.2%mom of export to India. However, on a year-to-date basis, the 10MCY19 export demand growth remains robust at +14.1%yoy, underpinned mainly by India due to previous preferential tariff trade agreement and China's larger vegetable oil demand. Moving forward, we are of the view that export demand to largely remain stable in coming months. We expect the expected strengthening demand from China for restocking activities for the major Chinese New Year festival in January 2020 will help to partially offset the expected decline in export from India.

Table 1: October 2019 Export Performance ('000 MT)

Market	Oct-19	Sep-19	Oct-18	MoM%	YoY%	10M19	10M18	Ytd%
China	275.4	222.5	218.6	23.8	26.0	1,893.5	1,417.9	33.5
India	220.0	310.6	99.3	-29.2	121.4	4,128.2	1,987.6	107.7
EU	200.9	139.6	167.9	43.9	19.6	1,770.5	1,669.7	6.0
Pakistan	81.6	119.3	105.4	-31.6	-22.6	903.2	972.4	-7.1
US	28.1	31.0	47.0	-9.4	-40.2	494.4	446.6	10.7
Others	835.8	586.8	940.2	42.4	-11.1	6,477.0	6,312.7	2.6
Total	**1,641.7**	**1,409.9**	**1,578.5**	**16.4**	**4.0**	**15,666.8**	**13,728.6**	**14.1**

Source: MPOB, MIDFR

Lower-than-expected production. October 2019 production level came in lower than anticipated at 1.8m mt amidst the typical peak production cycle (i.e. August, September and October). We view that this was possibly due to the dry weather conditions in August and September 2019 and higher yields at the start of the year which may have slightly altered the regular output cycle. It was also worth noting that October 2019 represents the first month of decline on a sequential basis after three consecutive month of increase, This could potentially indicates that the palm's high output cycle likely ended in September 2019. The lower output was mainly attributable to lower contribution from the state of Kedah (-39.0%yoy), Perak (-24.3%yoy), Selangor (-20.9%yoy), Negeri Sembilan (-14.5%yoy) and Johor state (-12.0%yoy). This also came in lower than the Bloomberg and Reuters consensus by -4.5% and -4.4% respectively. However, on a year-to-date comparison, 10MCY19 CPO production still remained elevated (+7.1%ytd) due to higher output primarily from the state of Kelantan (+23.5%ytd), Terengganu (+20.9%ytd), Pahang (+19.2%ytd) and Negeri Sembilan (+12.1ytd). Moving forward, we view that the production growth to remain marginal throughout the rest of both CY19 and into CY20 given the dry conditions affecting the yields, low fertiliser application and replanting efforts.

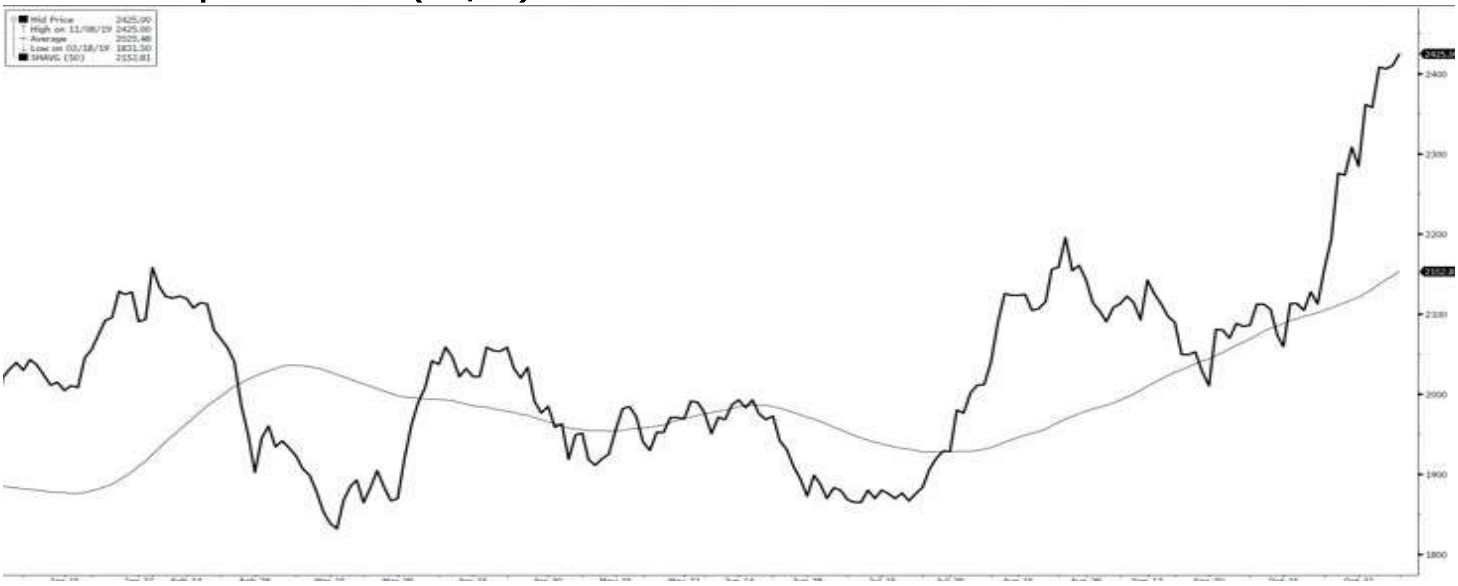
Table 2: Palm Oil Statistics for October 2019 ('000 MT)

	Oct-19	Sep-19	Oct-18	YoY %	MoM %	10MCY19	10MCY18	Ytd %
Opening Stocks	**2,448.3**	**2,251.8**	**2,541.2**	**-3.7**	**8.7**	**3,215.1**	**2,732.1**	**17.7**
Production	**1,795.9**	**1,842.4**	**1,965.0**	**-8.6**	**-2.5**	**16,986.4**	**15,862.9**	**7.1**
Imports	85.0	71.1	117.3	-27.5	19.6	779.4	598.5	30.2
Total Supply	**4,329.2**	**4,165.4**	**4,623.4**	**-6.4**	**3.9**	**20,980.9**	**19,193.5**	**9.3**
Exports	1,641.7	1,409.9	1,578.5	4.0	16.4	15,666.8	13,728.6	14.1
Dom Disapp	339.4	307.2	310.9	9.1	10.5	2,966.1	2,720.4	9.0
Total Demand	**1,981.1**	**1,717.1**	**1,878.9**	**5.4**	**15.4**	**18,632.9**	**16,449.0**	**13.3**
End Stocks	**2,348.1**	**2,448.3**	**2,744.5**	**-14.4**	**-4.1**	**2,348.1**	**2,744.5**	**-14.4**
Stock/Usage Ratio (%)	**9.9%**	**11.9%**	**12.2%**			**1.1%**	**1.4%**	

Source: MPOB, MIDFR

Year-to-date average CPO price still hovering slightly above RM2,000/mt level. In October 2019, the average CPO price recovered to above RM2,200/mt level, representing an increase of +13.1%yoy, coming from a low base effect due to low CPO prices experiencing in 4QCY18. This is premised on the expectation that inventory will continue to trend downwards amidst weaker production level in a peak cycle and a continued stable export demand. Thus, this could possibly be a tailwind to the recovery of the CPO price in coming months. Nonetheless, the 10MCY19 average CPO price of about RM2,005/mt remains a discount of -12%yoy as compared to prior corresponding period due to the sustained low CPO prices in 1HCY19. Nonetheless, this is still within our 2019 average CPO price assumption of RM2,090/mt, bearing a variance of -4.2%. Furthermore, we opine that the CPO price will continue to recover predominantly due to the expectancy of further decline in inventory level in view of the lower CPO production. However, we view that the sentiment might be partially moderated by the lower-than-anticipated export demand from India.

Chart 2: CPO Spot Price Trend (RM/mt)



Source: Bloomberg, MIDFR

Maintain NEGATIVE. Despite the year-over-year decline in October 2019 production level, the year-to-date output remains high at 17.0m mt due to a robust fresh fruit bunch (FFB) yield in 1HCY19. Note that the 1HCY19's FFB yield was 8.44mt/ha as compared to 7.93mt/ha during same period in review. Assuming the peak output period has ended early in September 2019, coupled with a steady export demand growth rate, we are likely to see a continued gradual downward trend in the inventory level. This will continue to lend support to the recovery of CPO price. Meanwhile, the weakening export demand from india might partially dampen the price which could be mainly predicated on factors such as: (1) India's 5.0% tariff hike resulting in removal of Malaysian palm oil preferential treatment across ASEAN region, (2) Chinese buyers resume loading up soybean and, (3) Winter season (i.e. November to February) where palm oil might not be the most suitable oil to be consumed as it tends to turn semi-solid or thick. All in, we are maintaining our **NEGATIVE** stance on the sector with an unchanged 2019 CPO price target of **RM2,090/mt**.

PEER COMPARISON TABLE

Stock	FYE	Rec.	Price @	Tgt Price (RM)	Core EPS (sen)		CORE PE (x)		Net DPS (sen)		Net Dvd Yield (%)	
			11-Nov-19		CY19F	CY20F	CY19F	CY20F	CY19F	CY20F	CY19F	CY20F
Genting Plantation	Dec	SELL	10.14	8.40	20.6	30.1	49.2	33.7	10.9	12.1	1.1	1.2
IOI Corporation	Jun	SELL	4.40	3.48	12.6	14.0	35.0	31.5	9.3	11.0	2.1	2.5
IJM Plantation	Mar	SELL	1.61	1.16	3.9	4.5	41.3	35.5	2.0	3.0	1.2	1.9
Kuala Lumpur Kepong	Sep	SELL	22.20	18.78	67.3	75.6	33.0	29.4	45.0	45.0	2.0	2.0
Sime Darby Plantation	Dec	SELL	4.98	4.08	2.1	6.3	237.1	79.0	1.1	3.8	0.2	0.8
PPB Group	Dec	NEUTRAL	18.10	17.43	64.6	72.1	28.0	25.1	19.4	21.6	1.1	1.2
Ta Ann Holdings	Dec	NEUTRAL	2.55	2.18	8.5	18.2	30.0	14.0	10.0	10.0	3.9	3.9
TSH Resources	Dec	NEUTRAL	0.95	0.89	3.6	4.6	26.2	20.6	1.0	1.2	1.1	1.3
FGV Holdings	Dec	NEUTRAL	1.23	0.96	-3.0	-2.1	-40.6	-59.7	N/A	N/A	N/A	N/A

Source: Company, MIDFR

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% 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.