

21 June 2016 | Sector Update

**PLANTATION***Slight delay in B10 implementation***Maintain POSITIVE****KEY HIGHLIGHTS**

- **Slight delay in B10 implementation to July.**
- **Neutral on the news.**
- **Biodiesel consumption has improved in Malaysia.**
- **We believe that CPO is currently undervalued as its discount against soybean oil has widened to USD110/MT despite the tight inventory at 5-year low.**
- **Maintain POSITIVE view on the sector. Top pick is KLK (TP: RM27.38).**

**Slight delay in B10 implementation to July.** According to Reuters, "Malaysia is in talks with oil companies about moving the start of its B10 biodiesel mandate to July, a month later from an earlier plan to begin the program in June, aiming to complete full implementation of the new standard by August". We gather that the rationale is for oil companies to reset their blending ratios and procure palm methyl ester (PME).

**Neutral on the news.** The delay is not expected to affect Malaysia palm oil inventory level significantly as it is already at its 5-year low level of 1.65m MT as of end-May 2016. In the long run, we believe that the B10 implementation will be made 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 the manageable level of below 2.5m MT especially during the peak production months between September and November.

**Biodiesel consumption has improved in Malaysia.** We believe that the increase in local palm oil consumption in Malaysia for May is likely to be caused by higher biodiesel consumption. As it is, May palm oil consumption locally has increased by 3.4%mom and 8.9%yoy to 260,522 MT.

**We believe that CPO is currently undervalued as its discount against soybean oil has widened to USD110/MT despite the tight inventory at 5-year low.** From the recent low discount of USD54/MT, CPO-Soybean Oil discount has doubled to USD110/MT currently. The current discount is higher than the one-year average of USD98/MT and is now at +0.5 Standard Deviation above the mean.

**Maintain POSITIVE view on the sector. Top pick is KLK (TP: RM27.38).** We maintain our bullish view on CPO price with near term target range of RM2,500 to RM2,800 per MT. 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. 

**Chart 1: CPO discount against soybean oil (USD/MT)**



Source: Malaysia Palm Oil Board (MPOB)

**Table 1: 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

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.