

11 July 2019 | Sector Update

# PLANTATION

**Maintain NEGATIVE**

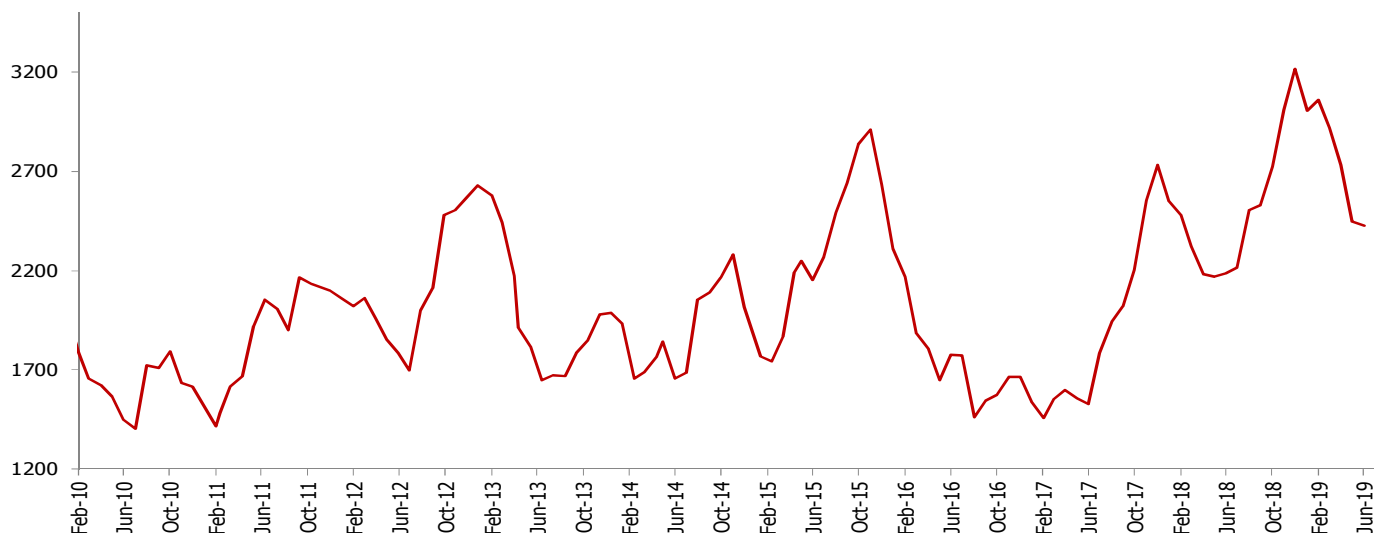
*Stockpiles stay above market expectations*

## KEY HIGHLIGHTS

- **June 2019 inventory level came in higher by +13.9%yoy to 2.4m metric tonnes (mt), representing the 24<sup>th</sup> month of year-over-year increase since July 2017**
- **June 2019 CPO of 1.5m mt (+13.9%yoy) outpace export demand of 1.4m mt (+22.4%yoy)**
- **We opine that CPO price to remain subdued as a result of oversupply in both palm oil and soybean stocks, competitive pricing from Indonesia, and expected higher production in 2H2019**
- **Maintain NEGATIVE stance on the sector with an unchanged CPO target price of RM2,090/mt**

**Inventory level remains elevated.** Malaysia's June 2019 palm oil stockpiles rose by +13.9%yoy to 2.4mt, which came in higher than both Bloomberg and Reuters consensus by +2.3%yoy and +3.1%yoy respectively. The monthly inventory level has been on the rise on a year-over-year basis for the past 24 months since July 2017. This was primarily attributable to the higher production level (despite in historical low production period) and weaker-than-expected export. Meanwhile, on a month-over-month basis, there was a marginal decline in June 2019 inventory level (-1.0%mom). Nonetheless, we are of the view that the slight reprieve in inventory which was at 11-month low was insufficient to lift the CPO price.

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



Source: Malaysia Palm Oil Board (MPOB), MIDFR

**Export demand came in slightly below market expectation.** On a year-over-year basis, June 2019 export rose by +22.4%yoy to circa 1.4m mt. This was mainly attributable to the higher demand from key importers such as India (+165.2%yoy), Iran (+196.4%yoy), Spain (+166.6%yoy) and Italy (+123.6%yoy). However, it was below the Bloomberg and Reuters consensus by -0.5% and -0.3% respectively. We opine this was primarily due to the normalization of export demand post the Ramadan season and Hari Raya Aidilfitri where large purchases of palm oil were made prior and during these festivities. This was evident from the month-over-month datasets whereby the export demand declined by -19.2%mom, mainly from India (-20.0%mom), US (-57.0%mom), and Iran (-49.7%mom) and Netherlands (-37.3%mom).

**Table 1: June 2019 export performance ('000 MT)**

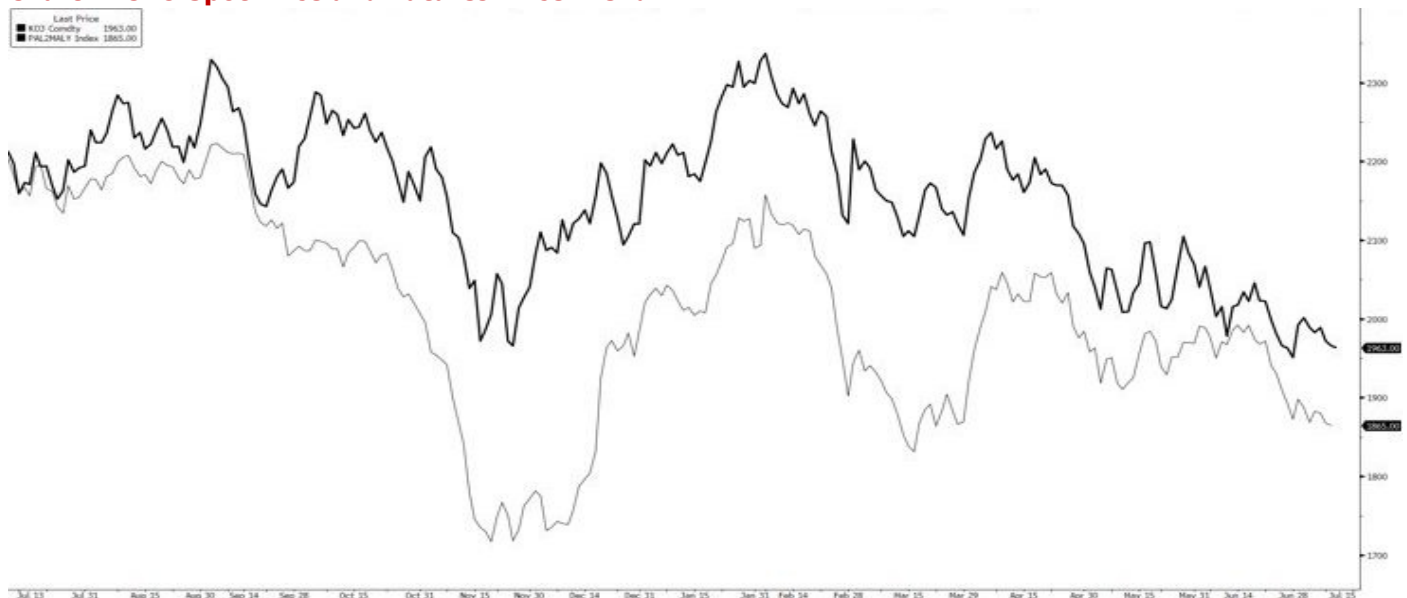
	June-19	May-19	June-18	MoM (%)	YoY (%)	6M19	6M18	YoY (%)
China	107.6	127.1	155.6	-15.3	-30.8	1,007.1	865.7	16.3
India	423.6	528.6	159.7	-19.9	165.2	2,585.2	1,389.2	86.1
EU	182.0	200.8	135.3	-9.3	34.6	1,123.3	1,036.1	8.4
Pakistan	76.7	69.7	98.7	10.0	-22.3	512.3	627.8	-18.4
US	52.1	121.1	46.6	-57.0	11.8	347.4	270.1	28.6
Others	540.7	664.7	533.665	-18.7	1.3	3,801.4	4,045.2	-6.0
<b>Total</b>	<b>1,382.8</b>	<b>1,711.9</b>	<b>1,129.5</b>	<b>-19.2</b>	<b>22.4</b>	<b>9,376.7</b>	<b>8,234.0</b>	<b>13.9</b>

Source: MPOB, MIDFR


**Output level remains in overdrive mode.** June 2019 production level recorded at 1.5m mt, representing an increase of +13.9%yoy. The higher output was mainly attributable to higher production from the state of Kelantan (+58.1%yoy), Terengganu (+58.0%yoy), Pahang (+44.2%yoy) and Negeri Sembilan (+24.8%yoy). The higher output also represented the sixth month of year-over-year increase. Nonetheless, it came in lower than the Bloomberg and Reuters consensus by -2.0% and -1.3% respectively. On a year-to-date comparison, 6MCY19 CPO production remained elevated (+9.8%ytd) due to higher output primarily from the state of Kelantan (+28.9%ytd), Terengganu (+24.7%ytd), Pahang (+19.2%ytd), Kedah (+17.2%ytd) and Perak (+15.1%ytd).

**Price remains depressed.** Since the beginning of the year, the Malaysian CPO spot price has declined by -10.4% to RM1,872/mt as at June 2019. Such level was last seen in March 2019 where CPO spot price was averaging around RM1,893/mt. Similarly, the average third-month benchmark palm oil futures dropped by -13.4%yoy to RM2,106/mt. In comparison, the price spread between futures and spot is getting narrower, signaling the market's negative sentiments on the CPO price going forward. Note that, the spread has narrowed to RM78/mt in June 2019 as compared to RM209/mt in January 2019. Thus, we do not expect any significant recovery in the CPO price in the near-to-medium term.

**Chart 2: CPO Spot Price and Futures Price Trend**



Source: Bloomberg

**Maintain NEGATIVE.** The outlook on the CPO price remains bearish in view of the protracted global palm oil glut arising mainly from overproduction in both Malaysia and Indonesia. Moreover, the palm oil industry is about to enter into its historical high production season (i.e. August to October) which coincides with the weaker export demand prospects in second half of the year. Furthermore, the likelihood of a production disruption caused by El-Nino in the near term has turned minimal as the ENSO outlook turns 'INACTIVE' from 'WATCH' previously, according to the Australia Bureau of Meteorology. Consequently, we are of the view that stockpiles level might potentially reverse into an uptrend if export demand couldn't keep pace, inhibiting any potential recovery in the CPO price. We also opine that the CPO price war between Indonesia and Malaysia might deepen due to the increased supplies of cheaper Indonesian palm oil flooding the market, causing further downward pressure on the Malaysian CPO price. On the export front, the global soybean glut and India's imposition of 7.5% (*previously zero percent*) import duty on palm stearin are additional dampening factors to the CPO inventory level. All in, we are maintaining our **NEGATIVE** stance on the sector with an unchanged 2019 CPO price target of **RM2,090/mt.** 

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

	June-19	May-19	Difference	MoM (%)	June-18	YoY (%)
<b>Opening Stocks</b>	2,447.4	2,729.4	(281.9)	-10.3	2,170.6	12.8
<b>Production</b>	1,518.2	1,671.5	(153.2)	-9.2	1,332.7	13.9
Imports	101.3	61.8	39.5	63.9	85.9	17.9
<b>Total Supply</b>	<b>4,066.9</b>	<b>4,462.6</b>	<b>(395.7)</b>	<b>-8.9</b>	<b>3,589.2</b>	<b>13.3</b>
Exports	1,382.8	1,711.9	(329.1)	-19.2	1,129.5	22.4
Dom Disapp	260.4	303.3	(43.0)	-14.2	272.7	-4.5
<b>Total Demand</b>	<b>1,643.1</b>	<b>2,015.2</b>	<b>(372.1)</b>	<b>-18.5</b>	<b>1,402.2</b>	<b>17.2</b>
<b>End Stocks</b>	<b>2,423.8</b>	<b>2,447.4</b>	<b>(23.6)</b>	<b>-1.0</b>	<b>2,187.0</b>	<b>10.8</b>
<b>Stock/Usage Ratio (%)</b>	<b>12.3</b>	<b>10.1</b>			<b>13.0</b>	

Source: MPOB, MIDF

**Table 3: Peer comparison**

Stock	FYE	Rec.	Price @	Tgt Price	Core EPS (sen)		CORE PE (x)		Net DPS (sen)		Net Dvd Yield (%)	
			10-Jul-19	(RM)	FY19F	FY20F	FY19F	FY20F	FY19F	FY20F	FY19F	FY20F
Genting Plantation	Dec	SELL	10.04	8.90	25.0	31.8	40.2	31.6	13.3	15.9	1.3	1.6
IOI Corporation	Jun	SELL	4.27	3.48	11.6	13.9	36.8	30.7	9.0	10.5	2.1	2.5
IJM Plantation	Mar	SELL	1.52	1.13	-1.3	5.2	-116.9	29.2	2.0	3.0	1.3	2.0
Kuala Lumpur Kepong	Sep	SELL	24.56	18.77	62.7	78.2	39.2	31.4	45.0	45.0	1.8	1.8
PPB Group	Dec	NEUTRAL	18.72	17.48	70.8	72.4	26.4	25.9	21.2	21.7	1.1	1.2
Ta Ann Holdings	Dec	NEUTRAL	2.28	2.22	15.4	18.6	14.8	12.3	10.0	10.0	4.4	4.4
Sime Darby Plantation	Dec	NEUTRAL	4.88	4.50	8.8	13.6	55.5	35.9	4.9	8.2	1.0	1.7
TSH Resources	Dec	NEUTRAL	0.90	0.89	3.6	4.6	24.8	19.5	1.0	1.2	1.1	1.3
FGV Holdings	Dec	NEUTRAL	1.12	1.26	1.5	2.4	74.7	46.7	N/A	N/A	N/A	N/A

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### STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> 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 <i>fall</i> 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.