

25 November 2016 | Sector Update

PLANTATION

Maintain POSITIVE***US lifts biofuel mandate to new record***

KEY HIGHLIGHTS

- **US lifts biofuel mandate to new record.**
- **The news is positive to CPO price.**
- **Maintain our Nov-2016 inventory forecast of 1.63m MT.**
- **Maintain POSITIVE view on the sector**
- **BUY call on KLK (TP: RM29.05), IOICORP (TP: RM5.05) and TAANN (TP: RM4.50)**

US lifts biofuel mandate to new record. United States has increased its biofuel mandate by 6% to 19.28b gallons in 2017 which is a new record. The news has caused soybean oil price to surge by 6.8% to US cents 37.14 per pound in Chicago Board of Trade (CBOT) market. Note that soybean oil is the main input used to produce biofuel in the US. In August-2016, 54% of the total input used to produce biofuel in US came from soybean oil.

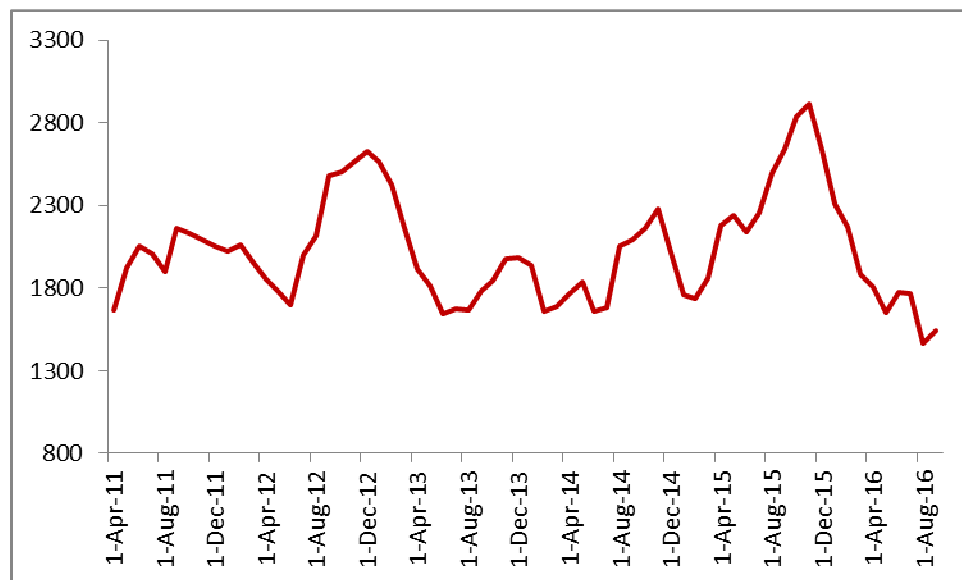
The news is positive to CPO price. As palm oil is commonly used as a substitute to soybean oil for food and industry purpose, CPO price is expected to increase. As it is, CPO price has surged by 1.5% (more than RM50 per MT) to around RM3000/MT as of time of writing. Coupled with tight inventory situation (Oct-2016 inventory of 1.57m MT has tumbled 45% yoy against Oct-2015's 2.83m MT), we reiterate our view that CPO price should stay at the high range of RM2500 to RM3000 per MT.

Maintain our Nov-2016 inventory forecast of 1.63m MT. Key assumptions are: i) export decline of 6% mom and ii) production decline of 2%. However, the inventory is expected to remain tight as it is only expected to increase by 3% mom. While cargo surveyors' data shows export decline of between 8% to 9% mom in the first twenty days of November, we expect export to pick up as high soybean oil price should encourage demand for palm oil. For production growth we are using seasonal factor to estimate the 2% decline.

Maintain POSITIVE view on the sector. BUY KLK (TP: RM29.05) and IOICORP (TP: RM5.05). Our top pick is KLK (BUY; TP RM29.05) due to its high exposure to palm oil business and good earnings growth of +33%yoy to RM1.05b in FY16. We also like IOICORP (BUY; TP RM5.05) due to its pure exposure to palm oil business both in the upstream and downstream divisions. The Company's profit is also expected to recover in FY17 after the uplift of RSPO suspension.

Small to mid-cap pick is TAANN (TP: RM4.50). We have recently upgraded TAANN after its good set of earnings in 9MFY16 due to better than expected FFB production. We like the Company due to: i) its FFB production growth is the strongest among peers (+8%yoy in 9MFY16), ii) better outlook for timber division due to recent strengthening of USD and Sarawak State Government's effort to promote timber products in Japan.

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



Source: Malaysia Palm Oil Board (MPOB)

Table 1: Basis of valuation

Company	TP	Call	Valuation Basis
SIME	7.75	NEUTRAL	SOP with plantation sector @ 25.1x FY17E PE. 25.1x is the avg of IOICORP and KLK Target PE.
IOICORP	5.05	BUY	24.7x Fwd. PE on FY17F earnings reflecting +0.5SD valuation.
KLK	29.05	BUY	26.8x Fwd. PE on FY17F earnings reflecting +1.0SD valuation.
PPB	14.70	NEUTRAL	19.5x Fwd. PE on FY17F earnings reflecting mean valuation.
FGV	1.77	NEUTRAL	1.0x Price to Book Value.
GENP	9.72	NEUTRAL	SOP with plantation sector @ 24.7x FY17E PE. 24.7x is the lower valuation between IOICORP and KLK.
IJMP	3.13	NEUTRAL	18.6x Fwd. PE on FY17F earnings reflecting mean valuation.
TSH	2.10	NEUTRAL	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	4.50	BUY	16.6x Fwd. PE on FY17F 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.