

## PLANTATION

**Maintain POSITIVE**

### *Less Soybean Planting in the United States*

#### KEY HIGHLIGHTS

- **Less soybean planting in 2016 in US.**
- **The news is positive to CPO price.**
- **The impact of improved soybean oil price is more significant than the impact of strong Ringgit.**
- **Expect severe stockpile depletion in 2QCY2016 to boost CPO price to RM3000/MT.**
- **Maintain POSITIVE view on the sector.**
- **KLK (TP: RM27.38) is our top pick.**

**Less soybean planting in 2016 in US.** The latest Prospective Plantings report by United States Department of Agriculture (USDA) shows that United States (US) farmer intends to plant less soybean this year. Note that soybean planting area is estimated to decline by 1% to 82.2m acres. In 23 of the 31 estimating states in US, farmers are expecting either flat or lower soybean acreage against last year.

**The news is positive to CPO price.** Lower soybean acreage in US should lead to lower supply of soybean and eventually soybean oil in the market. As a result, soybean oil price is expected to appreciate and hence lead to higher CPO price as well. Note that the correlation between soybean oil and CPO is very strong historically at more than 0.85 as both commodities are used as substitute for each other in the food and industrial use.

**The impact of improved soybean oil price is more significant than the impact of strong Ringgit.** We expect the recent strong Ringgit rally to be slightly negative to CPO price as it makes palm oil to be more expensive in Dollar and hence less competitive globally. Having said that, the negative impact from strong Ringgit is smaller to CPO price as the magnitude of appreciation in soybean oil is more than the appreciation of Ringgit. In March, soybean oil has gained 11.6% as compared to Ringgit 8.4% gain.

**Expect severe stockpile depletion in 2QCY2016 to boost CPO price to RM3000/MT.** Malaysia palm oil stockpile is expected to drop to the critical level of 1.50m MT towards the end of 2QCY2016. The impact of El Nino on oil palm tree production is only at the beginning stage. Hence, CPO production will be significantly lower than what it used to be in 1HCY2016. We think that there is a chance that the CPO discount against soybean oil (SBO) should narrow even to zero level due to severe supply shock in the market. Such rare phenomenon occurs before in Feb-2011 in which CPO price surge to RM3800/MT as inventory drop to 1.48m MT. Our key assumptions are SBO price to stay at around USD725/MT and USD/MYR rate of 4.15.

**Maintain positive view on the sector. Top pick is now KLK (New TP: RM27.38; Old TP: RM24.00).** We have upgraded KLK to BUY with new Target Price of RM27.38 (from NEUTRAL; TP: RM24.00). Our Forward PE valuation has been increased to 26.8x based on +1.0 Standard Deviation valuation (from 23.5x on Mean valuation). The increase in valuation is to reflect the scarcity of Shariah and RSPO member plantation companies among the big cap index-linked planters. KLK earnings exposure to palm oil business is also high at 88%.

**Table 1: Basis of valuation**

Company	TP	Call	Valuation Basis
SIME	8.05	NEUTRAL	SOP with plantation sector @ 25.1x FY17E PE. 25.1x is the avg of IOICORP and KLK Target PE.
IOICORP	4.82	NEUTRAL	23.1x Fwd. PE on FY16F earnings reflecting mean valuation.
KLK	27.38	BUY	26.8x Fwd. PE on FY16F earnings reflecting mean valuation.
PPB	18.60	NEUTRAL	21.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
FGV	1.33	SELL	1.0x Price to Net Tangible Asset (P/NTA).
GENP	10.66	NEUTRAL	SOP with plantation sector @ 23.5x FY16E PE. 23.5x is the lower valuation between IOICORP and KLK.
IJMP	3.57	NEUTRAL	18.6x Fwd. PE on FY16F earnings reflecting mean valuation.
TSH	2.28	NEUTRAL	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	6.80	BUY	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.