

12 January 2016 | Sector Update

## PLANTATION

**Maintain POSITIVE*****Bullish data from Dec-2015 palm inventory statistics***

### KEY HIGHLIGHTS

- **December 2015 inventory level was lower than expected at 2.63m MT.**
- **Tree stress impact continues as production plunged 15%mom.**
- **Steady export volume at 1.48m MT.**
- **Expect Jan inventory to decline 9%mom to 2.40m MT.**
- **Maintain POSITIVE view on the sector.**
- **Top picks are IOICORP (TP: RM4.95) and TAANN (RM6.50).**
- **Other BUYs are PPB (TP: RM18.00) and TSH (TP: RM2.33).**


**December 2015 inventory level of 2.63m MT was below expectation** at 4% lower than consensus forecast of 2.73m MT. It was also 7% below our estimate of 2.83m MT. In comparison to November level of 2.91m MT, inventory was depleted significantly by 10%mom as production decline rate of 15%mom was way higher than export decline rate of 1%mom. Accordingly, Stock/Usage ratio was also lower at 12.5% (against Nov-2015's 14.2%). Overall, the data is positive to CPO price as strong depletion in stocks suggests that demand has outpaced supply significantly in Dec-2015.

**Tree stress impact continues as production plunged 15%mom.** Peninsular Malaysia production declined the most (-17%mom to 673k MT) followed by Sabah (-16%mom to 432k MT) and Sarawak (-9%mom to 294k MT). The November to December 2015 decline rate of 15%mom was higher than the past 5-year (from 2010 to 2014) corresponding monthly period average decline of 12%mom. Hence, we believe that the tree stress impact has started to kick in as a result of lagged effect from El Nino. Recall that Australia Bureau of Meteorology has officially announced an El Nino condition on 12-May-2015.

**Steady export volume at 1.48m MT.** Total Malaysia export for palm oil declined by only 1%mom to 1.48m MT due to lower export to China (-41% to 95k MT), India (-15% to 333k MT) and Pakistan (-15% to 48k MT). However, this was neutralised by stronger export to United States (+72% to 72k MT) and European Union (+24% to 266k MT). Lower demand for palm oil from China may be caused by lower consumption of palm oil during winter season. As for India and Pakistan, the lower export may be caused by normalization of demand after the stock up activity ahead of Deepavali celebration on 10-Nov.

**Expect Jan inventory to decline 9%mom to 2.40m MT.** Our key assumptions for January inventory estimate are: (i) 9%mom decline in production in line with historical production pattern, and (ii) 8% drop in export as demand are usually lower during winter in the Northern Hemisphere. As palm oil tends to solidify in cold weather, it is used less during winter season.

**Maintain POSITIVE view on the sector. Top picks are IOICORP (TP: RM4.95) and TAANN (RM6.50).** We expect CPO price to improve and range between RM2400/MT to RM2600/MT with an average of RM2500/MT in 1Q2016. Our top pick is IOICORP due to: (i) its stock price is due for rerating after it regained Shariah status on 30-Nov, (ii) strong earnings growth of +41%yoy to RM338m in 1QFY16, and (iii) its earnings profile has the most pure (100%) exposure to palm oil among the big cap index-linked planters. We also like TAANN due to: (i) strong earnings growth of +38%yoy to RM115m in 9MFY15, and (ii) its timber division should benefit from higher USD/MYR as the division's product (Export Log and Plywood) prices are quoted in US Dollar.

**Other BUYs are PPB (TP: RM18.00) and TSH (TP: RM2.33).** We like PPB due to: (i) good 9MFY15 earnings growth of +12%yoy to RM710m, and (ii) it is expected to benefit from higher USD/MYR rate as Wilmar earnings is reported in US Dollar. As for TSH, we like the stock due to: (i) its FFB growth expected at 12% in FY16 is higher than other mid-cap peers' average of 7%, (ii) its young age profile estimated at 7.3 years old means that its FFB production is more resilient to El Nino. 

**Table 1: Palm Oil Statistics for Dec-2015 ('000 MT)**

	Dec-15	Nov-15	Diff.	MoM %	Dec-14	YoY%
<b>Opening Stocks</b>	<b>2,909</b>	<b>2,836</b>	<b>73</b>	<b>2.6%</b>	<b>2,281</b>	<b>27.6%</b>
<b>Production</b>	<b>1,399</b>	<b>1,654</b>	<b>(255)</b>	<b>-15.4%</b>	<b>1,365</b>	<b>2.5%</b>
Imports	82	122	(39)	-32.3%	90	-8.7%
<b>Total Supply</b>	<b>4,391</b>	<b>4,611</b>	<b>(221)</b>	<b>-4.8%</b>	<b>3,736</b>	<b>17.5%</b>
Exports	1,483	1,500	(16)	-1.1%	1,520	-2.4%
Dom Disapp	276	203	73	36.0%	200	37.7%
<b>Total Demand</b>	<b>1,759</b>	<b>1,702</b>	<b>57</b>	<b>3.3%</b>	<b>1,720</b>	<b>2.3%</b>
<b>End Stocks</b>	<b>2,631</b>	<b>2,909</b>	<b>(278)</b>	<b>-9.5%</b>	<b>2,016</b>	<b>30.5%</b>
<b>Stock/Usage Ratio</b>	<b>12.5%</b>	<b>14.2%</b>			<b>9.8%</b>	

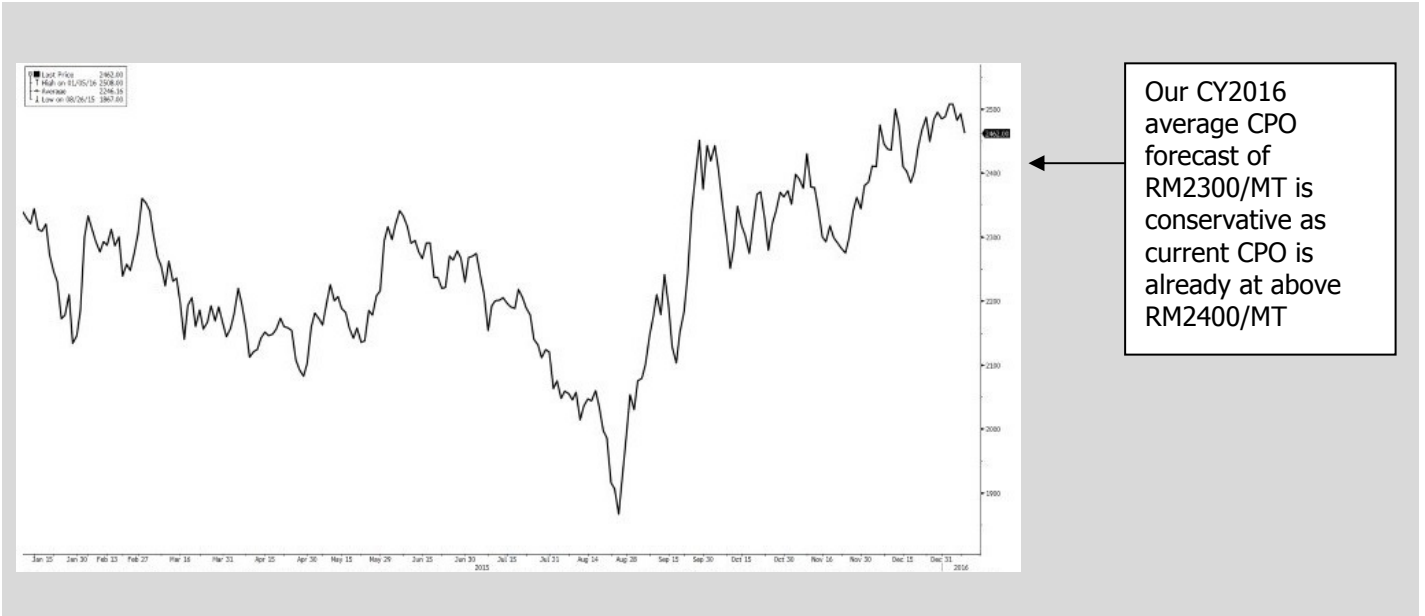
Source: MPOB, MIDF Research

**Table 2: Monthly Exports and YTD Exports ('000 MT)**

Country	Dec-15	Nov-15	Dec-14	MoM%	YoY%	12M15	12M14	YoY%
China	95	160	257	-41%	-63%	2,380	2,839	-16%
India	333	390	364	-15%	-8%	3,683	3,229	14%
EU	266	215	242	24%	10%	2,414	2,412	0%
Pakistan	48	57	64	-15%	-25%	706	812	-13%
US	72	42	76	72%	-5%	696	783	-11%
Others	670	635	516	5%	30%	7,561	7,227	5%
<b>Total</b>	<b>1,483</b>	<b>1,500</b>	<b>1,520</b>	<b>-1%</b>	<b>-2%</b>	<b>17,440</b>	<b>17,303</b>	<b>1%</b>

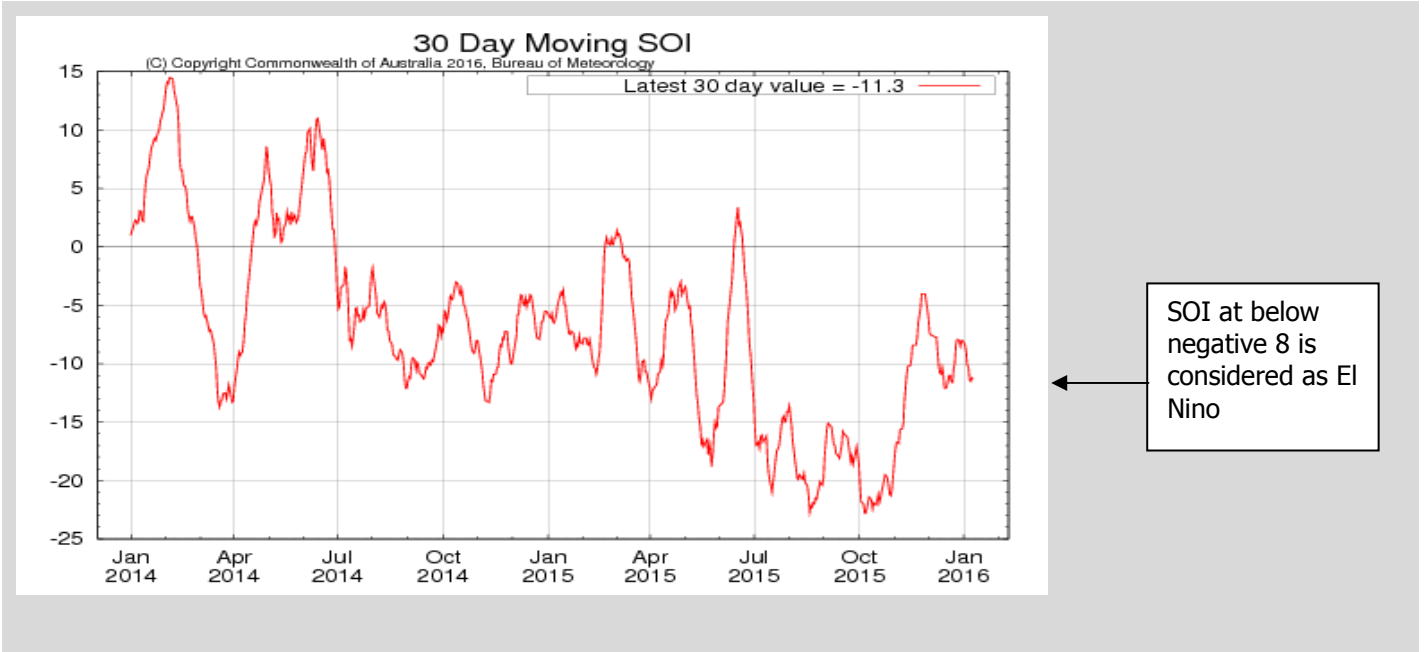
Source: MPOB, MIDF Research

**Chart 1: CPO price movement**



Source: Bloomberg, MIDF Research

**Chart 2: SOI Index has stayed in the El Nino zone persistently**



Source: Bloomberg, MIDF Research

**Table 3: Basis of valuation**

<b>Company</b>	<b>TP</b>	<b>Call</b>	<b>Valuation Basis</b>
SIME	8.20	NEUTRAL	SOP with plantation sector @ 23.2x FY16E PE. 23.2x is the avg of IOICORP and KLK Target PE.
IOICORP	4.95	BUY	26.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
KLK	22.50	NEUTRAL	23.5x Fwd. PE on FY16F earnings reflecting mean valuation.
PPB	18.00	BUY	21.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
FGV	1.30	SELL	1.0x Price to Net Tangible Asset (P/NTA).
GENP	9.53	NEUTRAL	SOP with plantation sector @ 23.1x FY16E PE. 23.1x is the lower valuation between IOICORP and KLK.
IJMP	3.65	NEUTRAL	18.6x Fwd. PE on FY16F earnings reflecting mean valuation.
TSH	2.33	BUY	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	6.50	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.