

10 August 2015 | Sector Update

PLANTATION**Maintain NEUTRAL*****CPO price should bottom at RM2000/MT*****KEY HIGHLIGHTS**

- **Dorab Mistry opined that CPO may slump to RM1900/MT by end-Sep**
- **We disagree and think that RM2000/MT is already the bottom**
- **El Nino has no impact to CPO price since it was announced in May-2015 hence it is expected to be immaterial to CPO price in the near term**
- **Soybean oil price may have bottomed as USDA is estimating 30.5 to 33.5 US cents per pound**
- **Maintain NEUTRAL with 2015 and 2016 average CPO price of RM2,175 and RM2,100 respectively**
- **PPB (BUY; TP: RM17.80) is our top pick**

CPO at RM1900/MT by end-Sep? Dorab Mistry predicted that CPO price will decline to RM1900/MT by end-Sep due to higher than expected increase in CPO output and weaker effects from El Nino as compared to the past. Dorab Mistry is revising higher his estimate for Malaysia CPO production to 20.0m MT (from 19.7m MT) while Indonesia production is expected at 32.0m MT (from 31.5m MT). Yesterday, CPO price increased slightly by RM9/MT to RM2,046/MT. However, it has declined by RM220/MT or 9.7% Year-To-Date (YTD).

We disagree with Dorab Mistry and think that RM2,000/MT is already the bottom. On the high production mentioned by Dorab Mistry, we believe that Malaysia CPO production should remain flat year-on-year in 2015 at 19.7m MT. This is due to the dry season in Sabah from Feb to Apr this year. As a result, 4Q2015 CPO production should be affected and this should keep production growth limited. Note that palm oil trees usually produce less Fresh Fruit Bunches (FFB) between 6 to 9 months after a dry spell.

El Nino has no impact to CPO price since it was announced in May-2015 hence it is expected to be immaterial to CPO price in the near term. We also believe that the market did not factor in the El Nino impact since May due to many false signals in the past. Recall that Australia Bureau of Meteorology confirmed the El Nino event on 12-May-2015 at the time in which CPO price was at RM2,225/MT. Since then, we notice that CPO price did not appreciate significantly and has actually declined in the first one week after the news. As a result, we believe that the "weaker El Nino" effect as mentioned by Dorab Mistry is unlikely to cause downward reaction to CPO price.

Soybean oil price may have bottomed as USDA is estimating 30.5 to 33.5 US cents per pound. The latest soybean oil price at less than 30.5 US cents per pound is already below USDA estimate of 30.5 to 33.5 US cents per pound. Additionally, it has declined 10% YTD possibly due to higher soybean oil inventory globally. As global soybean oil inventory is only expected to inch up by 4%yoy to 3.66m MT in the 2015/2016 marketing year, we believe that most of the negative news should have been priced in.

Maintain NEUTRAL with 2015 and 2016 average CPO price of RM2,175 and RM2,100 respectively; PPB (BUY; TP: RM17.80) is our top pick. Our average CPO price for both 2015 and 2016 are unchanged as we think that CPO price is likely to have found its bottom at RM2000/MT. For the rest of the year, we expect CPO price to range between RM2,000/MT to RM2,250/MT. Despite our positive view on CPO price, we maintain our NEUTRAL call as we expect the upcoming quarterly result to be lower year-on-year for most planters in line with lower CPO price in 2QCY15 against 2QCY14. Our top pick is PPB as we expect the upcoming result by end-August to register strong growth of at least 20%yoy in view of recent good set of result from Wilmar (1HFY15 Core Net Profit increased 21%yoy). We also expect PPB's 1HFY15 earnings growth to outperform all other index-linked planters (SIME, IOICORP and KLK). Lastly, PPB is poised to benefit from higher USD/MYR rate as Wilmar earnings is reported in US Dollar.

Table 1: Global soybean oil demand and supply forecast

In metric tonne (mt)	2013/14*	2014/15F	2015/16F
Inventory (Begin)	3.74	3.36	3.52
Production	45.01	47.95	50.01
Import	9.35	9.79	10.36
TOTAL SUPPLY	58.10	61.10	63.89
Export	9.39	10.08	10.86
Domestic	45.36	47.50	49.38
TOTAL DEMAND	54.75	57.58	60.24
Inventory (End)	3.36	3.52	3.66

Source: United States Department Of Agriculture (USDA)

*Marketing year for soybean begins on 1-Oct and ends on 30-Sep

Table 2: Basis of valuation

Company	TP	Call	Valuation Basis
SIME	8.80	NEUTRAL	SOP with plantation sector @ 23.2x FY16E PE. 23.2x is the avg of IOICORP and KLK Target PE.
IOICORP	4.45	NEUTRAL	23.1x Fwd. PE on FY16F earnings reflecting mean valuation. Target price is higher despite lower CPO price as we have rollover to FY16F.
KLK	21.00	NEUTRAL	23.5x Fwd. PE on FY16F earnings reflecting mean valuation. Target price is higher despite lower CPO price as we have rollover to FY16F.
PPB	17.80	BUY	21.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
FGVH	1.60	NEUTRAL	20.8x Fwd. PE on FY16F earnings reflecting -2.0SD valuation.
GENP	9.06	NEUTRAL	SOP with plantation sector @ 23.1x FY16E PE. 23.1x is the lower valuation between IOICORP and KLK.
IJMP	3.50	NEUTRAL	18.6x Fwd. PE on FY16F earnings reflecting mean valuation.
TSH	2.33	NEUTRAL	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	4.00	NEUTRAL	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.