

02 October 2015 | Sector Update

Alan Lim, CFA
alan.lim@midf.com.my | 03-21738464

PLANTATION

*Money does grow on trees***Upgrade to POSITIVE**

KEY HIGHLIGHTS

- Upgrade forecast of 2016 average CPO price by 9.5% to RM2300/MT from RM2100/MT.
- CPO price to benefit from weak Ringgit.
- Soybean oil price should have bottomed as inventory is expected to decline in 2015/16 season.
- El Nino is stronger than expected.
- Upgrade plantation sector to POSITIVE (from NEUTRAL).
- Upgrade TSH to BUY with new TP of RM2.33 (Previously NEUTRAL with TP of RM2.00).
- SIME (BUY; TP: RM9.10) is our top pick.
- Other BUYs are PPB (TP: RM18.00) and TAANN (TP: RM4.50).

Upgrade 2016 average CPO price to RM2300/MT from RM2100/MT. Reasons for the increase in CPO price assumption are: i) CPO price is expected to benefit from weak Ringgit, ii) soybean oil price should have bottomed and iii) El Nino has been stronger than expected. For 2015, we are maintaining our CPO price forecast at average RM2175/MT as YTD price of RM2172/MT is close to our forecast.

CPO price to benefit from weak Ringgit. We expect CPO price to benefit from the weak Ringgit trend. Although CPO price is not expected to increase significantly in USD due to the high US Dollar Index, we expect it to increase in Ringgit after the translation of the same USD price of CPO to weaker Ringgit. Note that we have now assumed average USD/MYR exchange rate of 1USD/RM4.40 for 2016 (previously 3.71). This is in line with our latest economist forecast of RM4.40 - 4.50 by end of 2015. Fundamentally, weaker Ringgit is expected to improve CPO competitiveness against other vegetable oil (especially soybean oil).

Inventory to decline by 12% to 2.20m MT by end-2015 due to low CPO production expected in 4Q2015 for Sabah. Oil World mentioned that "Production prospects have deteriorated and yields are likely to be down sizably in 4Q2015 and probably also in early 2016 as a result of the serious drought which was experienced in Feb to April with monthly rainfall well below the critical 100 mm level." We concur with this as we have highlighted previously in our sector report on 10-Aug-2015 that the dry season in Sabah from Feb to Apr this year should affect 4Q2015 CPO production. Note that palm oil tree usually produce less Fresh Fruit Bunches (FFB) 6 to 9 months after the dry spell. Overall, we expect this to reduce Malaysia palm oil inventory by 12% to 2.20m MT by end-2015 (from end-Aug level of 2.49m MT).

Change in production pattern prevented all time high inventory in September. We gather that the peak production month has shifted to August this year (instead of the usual September or October historically). Hence, we are reducing our inventory estimate for end-Sep by 6% to 2.58m MT after assuming September production to decline 5% MoM (from 2% increase MoM). Effectively, this means that the scenario of record high inventory exceeding previous record of 2.63m MT in Dec-2012 is unlikely to happen anytime soon. Looking ahead, we believe that seasonal production downtrend has started and this is supportive of CPO price in the near term.

Soybean oil price should have bottomed as inventory is expected to decline in 2015/16 season.

According to United States Department of Agriculture (USDA), global soybean oil inventory is expected to increase to 3.46m MT in 2015/2016 season (from 3.51m MT in 2014/2015 season). The decline in inventory is caused by the higher consumption growth expected at 5.2% against production growth of 4.8%. The higher consumption is driven by higher consumption expected from China (+7.4% to 15.24m MT) and India (+14.1% to 4.45m MT). Despite slower economic growth prospect in these countries, we wish to highlight that demand growth for soybean oil is likely to sustain as it is mainly used for food purposes.

Low Brent crude oil prices unlikely to affect CPO price as the correlation was already broken when Brent tumbled below USD80 per barrel.

Note that the correlation between CPO price and Brent crude oil has weakened to only 0.22 for the period of Nov-2014 to Sep-2015. This is significantly lower than the strong 0.85 correlation for the period of Jan-2000 to Oct-2014. Recall that Nov-2014 was the month when Brent crude oil price dropped below USD80 per barrel. We believe that the correlation has become insignificant as our estimate shows that discretionary demand for biodiesel is likely to have stopped completely when Brent crude oil price tumbled below USD80/barrel. This is caused by the negative margin experienced by biodiesel producer if they produce it independent of government subsidy. As a result of the weak correlation, we believe that persistently low Brent crude oil price will no longer affect CPO price. Fundamentally, this could be caused by the "new normal" in which the demand-supply dynamics of palm oil has get used to the absence of strong demand support from biodiesel consumption.

El Nino is stronger than expected. The recent Southern Oscillation Index data has shown reading as low as negative 22 which is way below negative 8 level which is indicative of El Nino weather condition. This is significantly below the range of negative 10 to negative 15 zone observed three months ago. Hence, we have now assumed strong El Nino (previously weak El Nino) and expect Malaysia palm oil production to decline 1%yoy in 2016 to 19.1m MT (previously +2%yoy to 19.7m MT). As a result, our 2016 inventory assumption has been reduced by 20% to 1.58m MT. In the latest information by Australia Bureau Of Meteorology, it was mentioned that "a strong El Niño that is likely to persist into early 2016. Tropical Pacific sea surface temperatures are at levels not seen since the 1997–98 event". Lower inventory is expected to be positive to CPO price.

Upgrade plantation sector to POSITIVE. Upgrade TSH to BUY with New TP of RM2.33 (Previously NEUTRAL with TP of RM2.00). FGV upgraded to NEUTRAL with unchanged TP of RM1.30.

In line with higher CPO price assumption, we have increased our earnings assumption for FY16 for all planters under our coverage. Accordingly, our Target Price has been increased for all planters except FGV which is maintained as we are using 1.0x Price to Net Tangible Assets method. FGV has been upgraded to NEUTRAL as their outlook should improve in line with better CPO price prospect. We have upgraded TSH to BUY as its FFB growth is expected at 12% in FY16 which means that the Company is poised to enjoy superior earnings growth against other mid-cap peers. Its young age profile estimated at 7.3 years old means that its FFB production is more resilient to El Nino.

SIME (BUY; TP: RM9.10) is our top pick.

Our contrarian BUY call on SIME has been accurate so far. Note that SIME share price has surged 8.0% to RM8.05 as of yesterday since our upgrade on 27-Aug-2015 when the share price was RM7.45. This has clearly outperformed FBMKLCI performance of 3.4% within the same period. Having said that, we believe there is still upside to SIME as its FY16 FFB growth expected at 10%yoy is the highest among big cap peers (average: 2% FFB growth). Most of the FFB growth is expected to come from New Britain Palm Oil Limited (NBPOL) which will start its first full year contribution in FY16. Our new TP for SIME is RM9.10 (previously RM8.80) after assuming higher CPO price of RM2300/MT for FY16.

Other BUYs are PPB (TP: RM18.00) and TAANN (TP: RM4.50). We like PPB due to its strong 1HFY15 earnings growth of 34%yoy as it rides the earnings recovery from Wilmar. PPB is also poised to benefit from higher USDMYR rate as Wilmar earnings is reported in USD. For TAANN, we expect its timber division to benefit from higher USDMYR as the division's product (Export Log and Plywood) prices are quoted in USD. Hence, TAANN is poised to enjoy earnings growth from both plantation and timber divisions.



Table 1: Change in calls and target prices

Company	Last Price (RM) @ 1-Oct-15	Upside/(Downside)	Net Dvd Yield (%)	Expected Total Return (%)	New TP (RM)	New Call	Previous TP (RM)	Previous Call
SIME	8.05	13.0%	3.3%	16.3%	9.10	BUY	8.80	BUY
IOICORP	4.40	-2.3%	3.6%	1.3%	4.30	NEUTRAL	4.00	NEUTRAL
KLK	22.28	5.0%	2.6%	7.6%	23.40	NEUTRAL	21.00	NEUTRAL
PPB	15.36	17.2%	1.3%	18.5%	18.00	BUY	17.80	BUY
FGV	1.51	-13.9%	3.7%	-10.2%	1.30	NEUTRAL	1.30	SELL
GENP	10.14	0.6%	1.0%	1.6%	10.20	NEUTRAL	9.00	NEUTRAL
IJMP	3.29	10.9%	2.7%	13.6%	3.65	NEUTRAL	3.50	NEUTRAL
TSH	1.96	18.9%	1.3%	20.2%	2.33	BUY	2.00	NEUTRAL
TAANN	3.76	19.7%	1.3%	21.0%	4.50	BUY	4.30	BUY

Source: MIDF Research Estimate

Table 2: Summary of change in earnings forecast

Company	FY15/16 Core Net Profit (New)	FY16/17 Core Net Profit (New)	FY15/16 Core Net Profit (Old)	FY16/17 Core Net Profit (Old)	FY15/16 Core Net Profit Change (%)	FY16/17 Core Net Profit Change (%)	Basis of change
SIME	2521.7	2761.3	2503.0	2734.1	0.8%	1.0%	CY2016 CPO price increased to RM2300/MT. Earnings for Industrial division is trimmed due to weaker demand expected for its product as miners reduce their capex due to low coal price.
IOICORP	1181.0	1203.6	1099.5	1122.2	7.4%	7.3%	CY2016 CPO price increased to RM2300/MT.
KLK	853.5	1060.5	853.5	951.8	0.0%	11.4%	CY2016 CPO price increased to RM2300/MT.
PPB	963.7	987.9	962.7	977.1	0.1%	1.1%	CY2016 CPO price increased to RM2300/MT. PPB earnings is less sensitive to CPO price due to its diversified business via Wilmar.
FGV	79.1	154.6	79.1	109.9	0.0%	40.7%	CY2016 CPO price increased to RM2300/MT.
GENP	283.9	316.1	283.9	276.8	0.0%	14.2%	CY2016 CPO price increased to RM2300/MT.
IJMP	165.4	183.5	158.4	151.8	4.4%	20.8%	CY2016 CPO price increased to RM2300/MT.
TSH	106.7	140.4	106.7	120.5	0.0%	16.5%	CY2016 CPO price increased to RM2300/MT.
TAANN	95.0	100.4	95.0	96.1	0.0%	4.5%	CY2016 CPO price increased to RM2300/MT.

Source: MIDF Research Estimate

Table 3: Global soybean oil demand and supply forecast

In metric tonne (mt)	2013/14*	2014/15F	2015/16F
Inventory (Begin)	3.75	3.35	3.51
Production	44.98	48.38	50.70
Import	9.35	10.03	10.25
TOTAL SUPPLY	58.08	61.76	64.46
Export	9.39	10.74	11.02
Domestic	45.34	47.52	49.98
TOTAL DEMAND	54.73	58.26	61.00
Inventory (End)	3.35	3.51	3.46

Source: United States Department Of Agriculture (USDA)

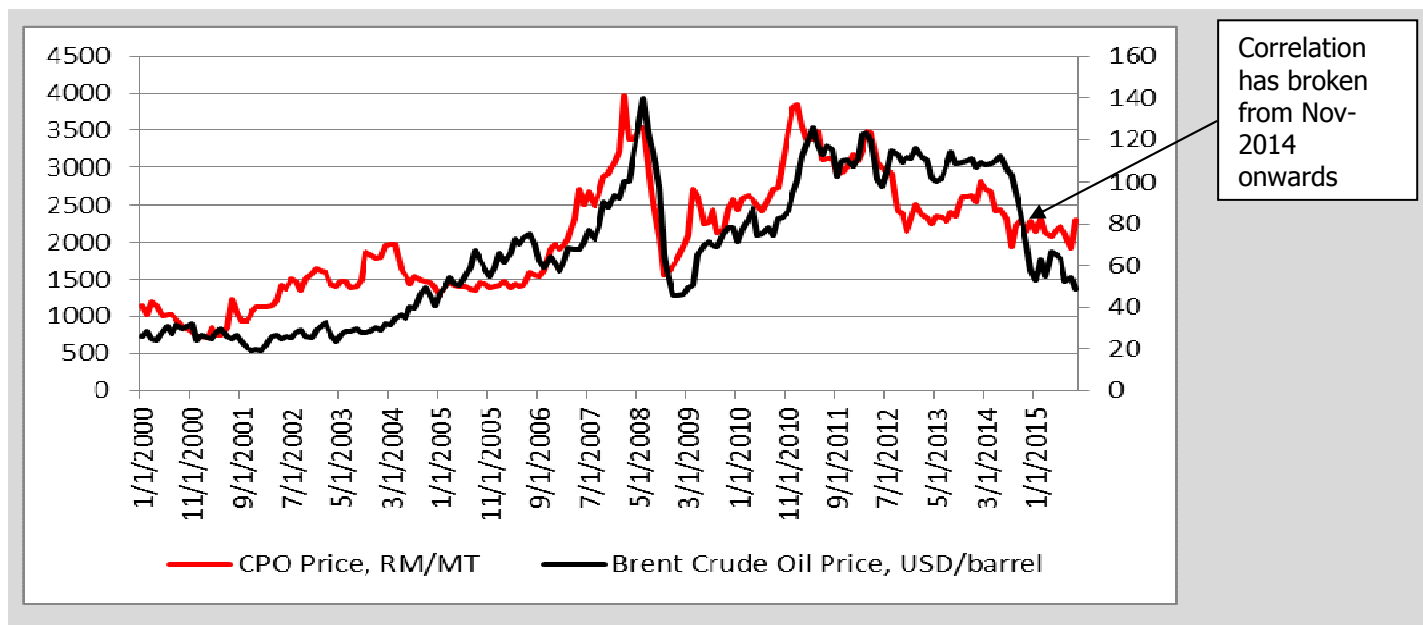
*Marketing year for soybean begins on 1-Oct and ends on 30-Sep

Table 4: Basis of valuation

Company	Valuation Basis
SIME	SOP with plantation sector @ 23.2x FY16E PE. 23.2x is the avg of IOICORP and KLK Target PE.
IOICORP	23.1x Fwd. PE on FY16F earnings reflecting mean valuation.
KLK	23.5x Fwd. PE on FY16F earnings reflecting mean valuation.
PPB	21.6x Fwd. PE on FY16F earnings reflecting +0.5SD valuation.
FGVH	1.0x Price to Net Tangible Asset (P/NTA).
GENP	SOP with plantation sector @ 23.1x FY16E PE. 23.1x is the lower valuation between IOICORP and KLK.
IJMP	18.6x Fwd. PE on FY16F earnings reflecting mean valuation.
TSH	22.3x Fwd. PE on FY16F earnings reflecting mean valuation.
TAANN	16.6x Fwd. PE on FY16F earnings reflecting mean valuation.

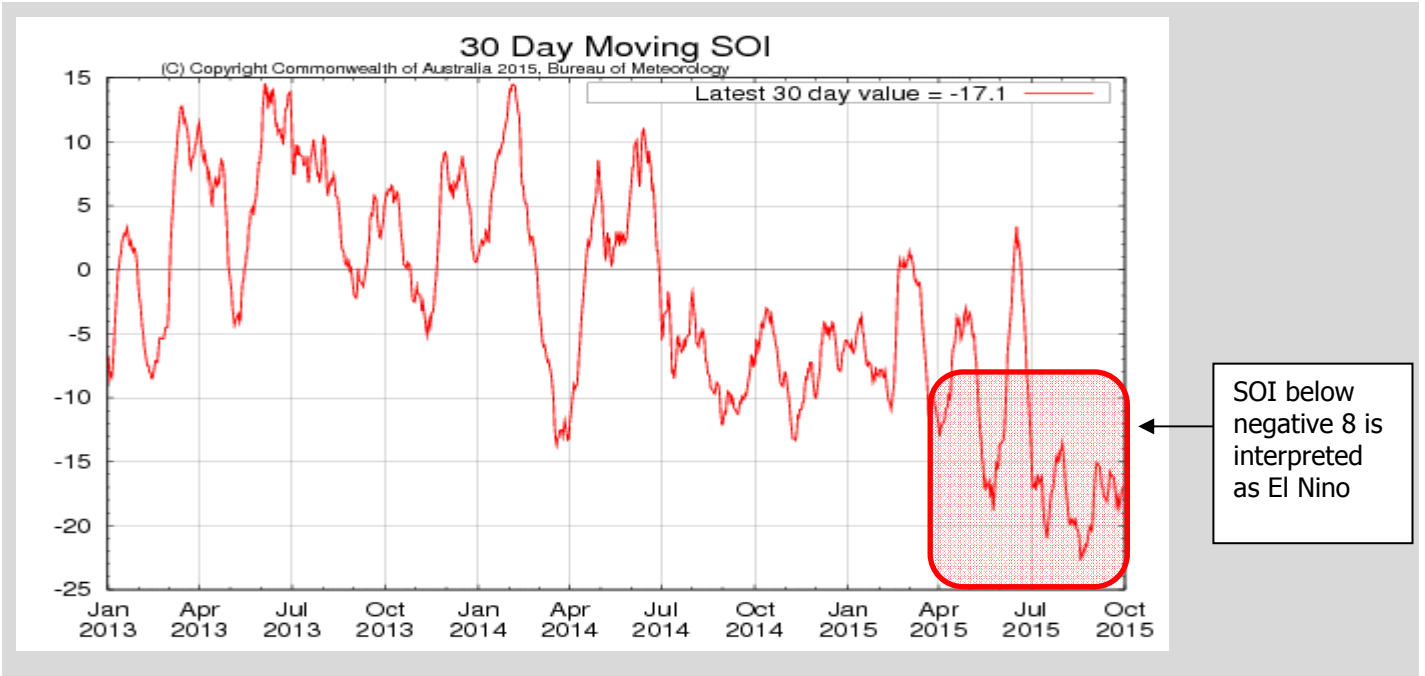
Source: MIDF Research Estimate

Chart 1: The correlation between Brent crude oil and CPO



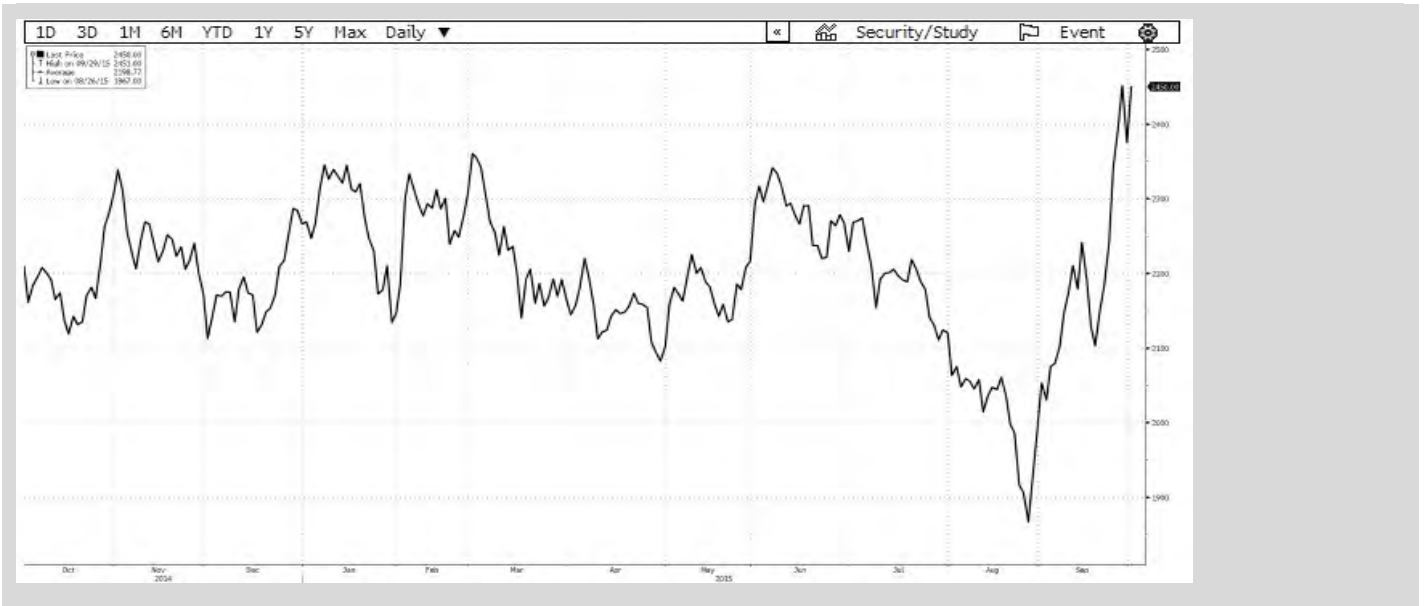
Source: Bloomberg, MIDF Research

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



Source: Australia Bureau of Meteorology, MIDF Research

Chart 3: CPO price movement



Source: Bloomberg, MIDF Research

Table 5: SIME Earnings Forecast

FYE Jun	FY13A	FY14A	FY15A	FY16F	FY17F
Revenue	46,109	43,908	43,729	47,057	49,784
EBIT	4,493	4,219	3,277	3,908	4,290
PBT	4,314	3,965	3,003	3,457	3,813
Net Income	3,701	3,353	2,313	2,522	2,761
Core Net Income	2,995	3,270	2,071	2,522	2,761
EPS (sen)	61.58	55.50	37.68	41.08	44.98
Core EPS (sen)	49.83	54.13	33.74	41.08	44.98
Net DPS (sen)	34.0	36.0	25.0	26.7	29.2
Net Dvd Yield	4.2%	4.5%	3.1%	3.3%	3.6%
Core PER	16.2	14.9	23.9	19.6	17.9
NTA/share (RM)	4.36	4.53	4.29	4.29	4.45
P/NTA	1.85	1.78	1.87	1.88	1.81
ROE	13.7%	11.7%	7.6%	8.3%	8.8%
ROA	7.6%	6.6%	3.8%	4.5%	4.8%

Source: Company, MIDF Research

Table 6: IOICORP Earnings Forecast

FYE Jun	FY13A	FY14A	FY15A	FY16F	FY17F
Revenue	12,199	11,911	11,621	11,684	11,688
EBIT	1,719	1,800	1,347	1,602	1,624
PBT	1,604	1,671	457	1,507	1,535
Net Income	1,280	1,255	168	1,181	1,204
Core Net Income	1,233	1,391	1,054	1,181	1,204
EPS (sen)	20.03	19.69	2.65	18.60	18.96
Core EPS (sen)	19.29	21.83	16.60	18.60	18.96
Net DPS (sen)	15.50	20.00	9.00	15.81	16.11
Net Dvd Yield	3.5%	4.5%	2.0%	3.6%	3.7%
Core PER	22.8	20.2	26.5	23.7	23.2
NTA/share (RM)	2.07	0.88	0.72	1.08	1.11
P/NTA	2.13	5.03	6.07	4.07	3.96
ROE	9.4%	20.8%	3.3%	16.0%	15.9%
ROA	5.4%	8.2%	1.3%	7.1%	7.4%

Source: Company, MIDF Research

Table 7: KLK Earnings Forecast

FYE Sep	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	10,570	9,147	11,130	12,945	13,640
EBIT	1,471	1,241	1,395	1,205	1,485
PBT	1,560	1,200	1,318	1,189	1,460
Net Income	1,211	918	992	853	1,060
Core Net Income	1,127	912	1,032	853	1,060
EPS (sen)	113.7	86.2	93.1	80.1	99.6
Core EPS (sen)	105.8	85.6	96.9	80.1	99.6
Net DPS (sen)	65.0	50.0	55.0	47.4	58.9
Net Dvd Yield	2.9%	2.2%	2.5%	2.1%	2.6%
Core PER	21.1	21.5	19.0	21.8	21.5
NTA/share (RM)	6.66	2.07	0.88	1.07	1.10
P/NTA	3.34	2.00	4.73	3.85	3.75
ROE	17.0%	12.2%	12.8%	10.3%	12.2%
ROA	10.6%	7.8%	7.7%	6.5%	7.7%

Source: Company, MIDF Research

Table 8: PPB Earnings Forecast

FYE Dec	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	3,018	3,313	3,701	3,742	3,933
EBIT	198	278	313	337	337
PBT	917	1,063	1,028	1,072	1,098
Net Income	842	983	917	964	988
Core Net Income	842	953	917	964	988
EPS (sen)	71.0	82.9	77.3	81.3	83.3
Core EPS (sen)	71.0	80.3	77.3	81.3	83.3
Net DPS (sen)	20.0	25.0	23.0	24.4	25.0
Net Dvd Yield	1.3%	1.6%	1.5%	1.6%	1.6%
Core PER	21.6	19.1	19.9	18.9	18.4
NTA/share (RM)	11.97	13.14	14.12	14.25	14.83
P/NTA	1.28	1.17	1.09	1.08	1.04
ROE	5.9%	6.3%	5.5%	5.7%	5.6%
ROA	5.4%	5.8%	4.9%	5.3%	5.3%

Source: Company, MIDF Research

Table 9: FGV Earnings Forecast

FYE Dec	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	12,886	12,568	16,369	17,527	18,226
EBIT	957	1,478	885	507	678
PBT	1,094	1,536	859	461	560
Net Income	806	982	325	166	155
Core Net Income	766	42	176	79	155
EPS (sen)	22.09	26.92	8.92	4.54	4.24
Core EPS (sen)	20.99	1.16	4.84	2.17	4.24
Net DPS (sen)	14.0	16.0	10.0	4.5	4.2
Net Dvd Yield	11.5%	13.1%	8.2%	3.7%	3.5%
Core PER	5.8	105.3	25.2	56.3	28.8
NTA/share (RM)	1.48	1.53	1.33	1.37	1.37
P/NTA	0.82	0.80	0.92	0.89	0.89
ROE	13.2%	14.9%	5.1%	2.5%	2.4%
ROA	4.9%	4.7%	1.6%	0.7%	0.7%

Source: Company, MIDF Research

Table 10: GEPN Earnings Forecast

FYE Dec	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	1,233	1,384	1,643	1,420	1,589
EBIT	395	287	513	350	391
PBT	404	300	520	391	432
Net Income	327	228	377	284	316
Core Net Income	329	330	382	284	316
EPS (sen)	43.1	30.0	49.3	37.1	41.3
Core EPS (sen)	43.4	43.5	50.0	37.1	41.3
Net DPS (sen)	9.4	35.8	10.0	9.3	10.3
Net Dvd Yield	0.9%	3.5%	1.0%	0.9%	1.0%
Core PER	23.4	23.3	20.3	27.3	24.5
NTA/share (RM)	4.28	4.30	4.89	4.92	5.23
P/NTA	2.37	2.36	2.07	2.06	1.94
ROE	9.6%	6.6%	9.7%	7.2%	7.6%
ROA	6.9%	4.7%	6.7%	5.4%	5.7%

Source: Company, MIDF Research

Table 11: IJMP Earnings Forecast

FYE Mar	FY13A	FY14A	FY15A	FY16F	FY17F
Revenue	486	647	668	582	624
EBIT	159	153	141	217	239
PBT	157	109	89	209	231
Net Income	120	89	90	165	183
Core Net Income	129	109	142	165	183
EPS (sen)	14.9	11.1	10.7	19.6	21.8
Core EPS (sen)	16.0	13.7	16.8	19.6	21.8
Net DPS (sen)	7.0	7.0	6.0	8.8	9.8
Net Dvd Yield	2.1%	2.1%	1.8%	2.7%	3.0%
Core PER	16.0	13.7	16.8	19.6	21.8
NTA/share (RM)	1.74	1.73	1.91	1.80	1.92
P/NTA	1.89	1.91	1.72	1.83	1.71
ROE	8.6%	6.4%	5.6%	10.9%	11.3%
ROA	5.6%	4.0%	3.5%	7.7%	8.1%

Source: Company, MIDF Research

Table 12: TSH Earnings Forecast

FYE Dec	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	984	1,016	1,071	960	1,042
EBIT	111	156	174	191	236
PBT	100	164	168	156	203
Net Income	77	151	124	107	140
Core Net Income	89	140	151	107	140
EPS (sen)	5.73	11.54	9.20	7.93	10.44
Core EPS (sen)	6.64	10.73	11.24	7.93	10.44
Net DPS (sen)	2.50	3.50	2.50	1.98	2.61
Net Dvd Yield	1.3%	1.8%	1.3%	1.0%	1.3%
Core PER	29.5	18.3	17.4	24.7	18.8
NTA/share (RM)	0.69	0.84	0.92	0.99	1.08
P/NTA	2.82	2.33	2.12	1.99	1.82
ROE	8.7%	14.3%	10.5%	8.4%	10.2%
ROA	3.5%	6.4%	4.8%	4.2%	5.4%

Source: Company, MIDF Research

Table 13: TAANN Earnings Forecast

FYE Dec	FY12A	FY13A	FY14A	FY15F	FY16F
Revenue	790	770	1,012	1,035	1,051
EBIT	93	64	166	139	146
PBT	78	113	168	129	136
Net Income	57	93	124	95	100
Core Net Income	80	70	126	95	100
EPS (sen)	15.51	25.09	33.37	25.63	27.10
Core EPS (sen)	21.69	18.84	34.06	25.63	27.10
Net DPS (sen)	5.00	5.00	20.00	10.25	10.84
Net Dvd Yield	1.3%	1.3%	5.3%	2.7%	2.9%
Core PER	17.3	20.0	11.0	14.7	13.9
NTA/share (RM)	2.42	2.57	2.91	3.07	3.23
P/NTA	1.55	1.46	1.29	1.23	1.16
ROE	6.0%	9.2%	11.0%	8.0%	8.1%
ROA	3.4%	5.2%	6.6%	5.0%	5.1%

Source: Company, MIDF Research

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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.