

12 May 2017 | Sector Update

PLANTATION

Maintain NEUTRAL***April inventory came in within expectation***

KEY HIGHLIGHTS

- **April inventory came in within expectation**
- **Production uptrend continues for the fifth month**
- **Good export growth due to strong demand from Northern Hemisphere**
- **Expect May-2017 inventory to increase 6% mom to 1.70m MT**
- **Maintain NEUTRAL view with BUY call on KLK**

April inventory came in within expectation. Malaysia palm oil inventory level of 1.60m MT as of end-April 2017 is close to our estimate of 1.59m MT and consensus estimate of 1.63m MT possibly. Against last month, inventory level increased by 3% as production growth of 6% exceeded export growth of 1%. Against same period last year, inventory remains lower yoy by 11% but the decline rate has is lower against March's 18% decline yoy.

Production uptrend continues for the fifth month. CPO production has shown a strong recovery with 6% increase mom and 19% yoy to 1.55m MT. Sabah CPO production leads the recovery (+11% mom to 428,152 MT) and this is followed by Peninsular Malaysia (+6% to 820,077 MT) and Sarawak (-1% mom to 299,824 MT). April production increase of 19% yoy suggests that the palm trees have fully recovered from the impact of severe El Nino and the uptrend of strong production have started.

Good export growth due to strong demand from Northern Hemisphere. Export to China increased 33% mom to 137,334 MT. Besides China, export has also improved in European Union (+11% to 149,679 MT) and United States (+19% to 51,434 MT). We believe that the better demand is caused by the warmer weather in the spring season as palm oil usage tend to increase in the warm weather as it will remain in the liquid form.

Expect May-2017 inventory to increase 6% mom to 1.70m MT. Key assumptions are: i) production increase of 7% mom and ii) export growth of 7% mom. We are expecting better export of palm oil due to restocking activity ahead of Ramadhan in key consumers such as India and Pakistan. Our estimate is deemed conservative as cargo surveyors reported 13% increase in the first ten days of May. For production growth we are using seasonal factor to estimate the 7% increase.

Stay NEUTRAL; Our only BUY call is KLK (TP: RM29.25). We reiterate our NEUTRAL view on the sector with 2017 average CPO price of RM2725 per MT unchanged. The best earnings quarter in the recent years has been registered in 4QCY2016. In the coming quarter of 1QCY17, planters earnings is expected to be lower qoq as the 7% rise in CPO price to RM3152/MT is not enough to offset the 15% decline in production. Our Top Pick for the sector is KLK (BUY with TP of RM29.25) as the Company's 1QCY17 result should fare better against other planters as it has locked in forward sales when the CPO price is high. The Company's earnings are also resilient and matched consensus expectation most of the time.

Table 1: Palm Oil Statistics for April-2017 ('000 MT)

| | Apr-17 | Mar-17 | Diff. | MoM % | Apr-16 | YoY% |
|--------------------------|--------------|--------------|------------|-------------|--------------|---------------|
| Opening Stocks | 1,553 | 1,459 | 94 | 6.4% | 1,886 | -17.6% |
| Production | 1,548 | 1,464 | 84 | 5.7% | 1,301 | 19.0% |
| Imports | 54 | 102 | (47) | -46.6% | 42 | 30.3% |
| Total Supply | 3,156 | 3,025 | 130 | 4.3% | 3,229 | -2.3% |
| Exports | 1,283 | 1,266 | 18 | 1.4% | 1,165 | 10.2% |
| Dom Disapp | 272 | 206 | 66 | 31.9% | 264 | 3.2% |
| Total Demand | 1,556 | 1,472 | 83 | 5.7% | 1,428 | 8.9% |
| End Stocks | 1,600 | 1,553 | 47 | 3.0% | 1,800 | -11.1% |
| Stock/Usage Ratio | 8.6% | 8.8% | | | 10.5% | |

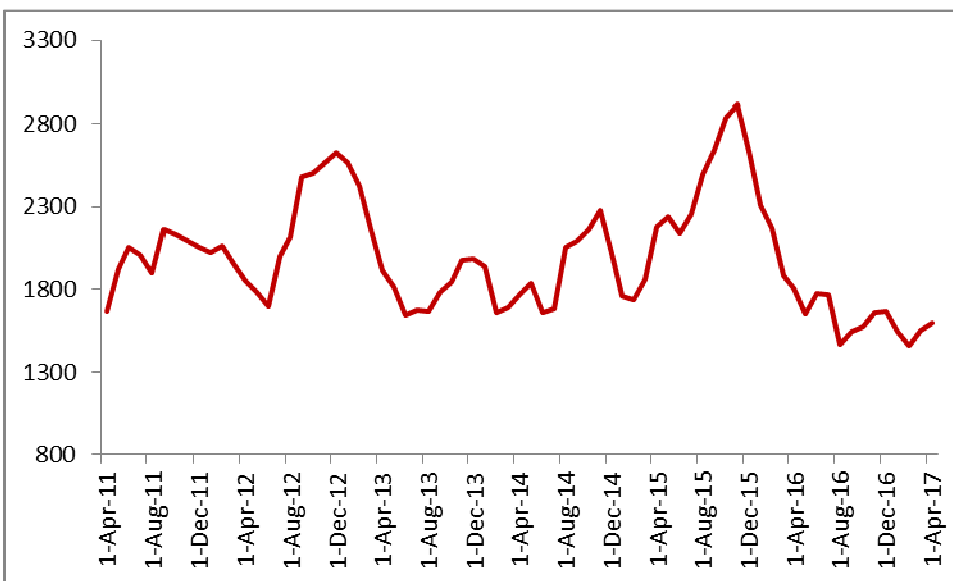
Source: MPOB, MIDF Research

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

| Country | Apr-17 | Mar-17 | Apr-16 | MoM% | YoY% | 4M17 | 4M16 | YoY% |
|--------------|--------------|--------------|--------------|-----------|------------|--------------|--------------|-----------|
| China | 137 | 104 | 95 | 33% | 45% | 511 | 395 | 30% |
| India | 161 | 171 | 180 | -6% | -10% | 605 | 948 | -36% |
| EU | 150 | 135 | 101 | 11% | 49% | 574 | 623 | -8% |
| Pakistan | 55 | 55 | 72 | 0% | -24% | 206 | 203 | 1% |
| US | 51 | 43 | 50 | 19% | 2% | 167 | 218 | -24% |
| Others | 729 | 758 | 667 | -4% | 9% | 2,869 | 2,477 | 16% |
| Total | 1,283 | 1,266 | 1,165 | 1% | 10% | 4,933 | 4,865 | 1% |

Source: MPOB, MIDF Research

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



Source: Malaysia Palm Oil Board (MPOB)

Table 3: Basis of valuation

| Company | TP | Call | Valuation Basis |
|---------|-------|---------|--|
| SIME | 9.00 | NEUTRAL | SOP with plantation sector @ 26.8x FY17E PE. 26.8x is the higher of IOICORP and KLK Target PE. |
| IOICORP | 5.30 | NEUTRAL | 24.7x Fwd. PE on FY17F earnings reflecting +0.5SD valuation. |
| KLK | 29.25 | BUY | 26.8x Fwd. PE on FY17F earnings reflecting +1.0SD valuation. |
| PPB | 17.69 | NEUTRAL | 1.0x Price to Book Value |
| FGV | 1.77 | NEUTRAL | 1.0x Price to Book Value |
| GENP | 11.55 | NEUTRAL | SOP with plantation sector @ 24.7x FY17E PE. 24.7x is the lower valuation between IOICORP and KLK. |
| IJMP | 3.53 | NEUTRAL | 18.6x Fwd. PE on FY17F earnings reflecting mean valuation. |
| TSH | 2.15 | NEUTRAL | 22.3x Fwd. PE on FY17F earnings reflecting mean valuation. |
| TAANN | 4.25 | NEUTRAL | 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. |