

12 September 2017 | Sector Update

PLANTATION

Maintain NEUTRAL

August inventory is within expectation

KEY HIGHLIGHTS

- **August inventory is within expectation**
- **Export to India and China improved**
- **Production declined in August after one off surge in July**
- **The data is neutral to CPO price**
- **Expect September-2017 inventory to increase 7%mom to 2.08m MT**
- **Maintain NEUTRAL with BUY on KLK (TP: RM29.25), GENP (TP: RM12.06), TSH (TP: RM2.15) and TAANN (TP: RM4.30)**

August inventory is within expectation. Malaysia palm oil inventory level of 1.94m MT as of end-August 2017 is within market expectation of between 1.90m to 2.00m MT. However, it is lower than our estimate of 2.10m MT as export came in stronger than expected. Against last month, inventory level increased by 9% as production volume of 1.81m MT exceeded export volume of 1.49m MT. Against same period last year, inventory is higher by 33% (against July's increase of 1%yoy).

Export to India and China improved. Export to India surged 14%mom to 183,286 MT as pre stocking activity for Deepavali may have started. For China, export remains strong with 3%mom growth to 194,251 MT due to pre stocking activity of Mid-Autumn Festivals.

Production declined in August after one off surge in July. Palm oil production declined 1%mom but increased 6%yoy to 1.81m MT in August. The decline in August production was caused by the high base effect in July as more fruits are available for harvesting after harvesters took leave to go back to Indonesia for Hari Raya in June. Hence, we believe that the seasonal uptrend in production should continue in September.

The data is neutral to CPO price. Overall, we are neutral on the latest MPOB stats as it falls within market expectation. Having said that, we believe that the market should monitor the dry weather condition in the US as it could drive soybean oil price higher (and hence CPO as well).

Expect September-2017 inventory to rise 7%mom to 2.08m MT. Key assumptions are: i) production increase of 3%mom, and ii) export increase of 5%mom. We believe that palm oil demand should be supported by good export growth to India as the pre stocking activity should continue. Our export assumption is deemed conservative as cargo surveyors' data shows growth of 7% to 9% in export for the first ten days of September. For production growth we are using seasonal factor to estimate the 3% increase.

Maintain NEUTRAL view on the sector. Our NEUTRAL view on the sector is maintained with average CPO price of RM2725 per MT for both 2017 and 2018. We believe that there is little downside risk to our estimate as YTD CPO price is RM2865 per MT and we expect CPO price to be well supported at above RM2700 per MT throughout 4Q2017. Top Pick for the sector is KLK (BUY with TP of RM29.25) for the Company earnings resiliency and its good FFB production growth estimated at 10% (highest among index-linked plantation stocks). We also like GENP (TP: RM12.06) due to strong 1HFY17 earnings surge of 157%yoy to RM150.9m and robust FY17 FFB growth expected at 13%.


For mid cap planters, we like TSH (TP: RM2.15) due to: i) its strong 1HFY17 CNI which has grown 30%yoy, ii) attractive valuation at close to its -0.5SD level, and iii) solid FY17 FFB growth expected at 16%. Lastly, we have a BUY call on TAANN (TP:RM4.30) as i) its plantation division earnings growth should remain strong due to high FFB growth expected at 10%, and ii) timber division outlook remains profitable albeit challenging. 

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

| | Aug-17 | Jul-17 | Diff. | MoM % | Aug-16 | YoY% |
|--------------------------|--------------|--------------|-------------|--------------|--------------|---------------|
| Opening Stocks | 1,785 | 1,527 | 258 | 16.9% | 1,771 | 0.8% |
| Production | 1,811 | 1,827 | (17) | -0.9% | 1,702 | 6.4% |
| Imports | 42 | 53 | (11) | -21.3% | 8 | 433.6% |
| Total Supply | 3,637 | 3,407 | 230 | 6.8% | 3,480 | 4.5% |
| Exports | 1,488 | 1,398 | 90 | 6.4% | 1,824 | -18.4% |
| Dom Disapp | 208 | 225 | (18) | -7.8% | 193 | 7.8% |
| Total Demand | 1,695 | 1,623 | 72 | 4.5% | 2,016 | -15.9% |
| End Stocks | 1,942 | 1,785 | 157 | 8.8% | 1,464 | 32.6% |
| Stock/Usage Ratio | 9.5% | 9.2% | | | 6.1% | |

Source: MPOB, MIDF Research

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

| Country | Aug-17 | Jul-17 | Aug-16 | MoM% | YoY% | 8M17 | 8M16 | YoY% |
|--------------|--------------|--------------|--------------|-----------|-------------|---------------|---------------|-----------|
| China | 194 | 189 | 299 | 3% | -35% | 1,076 | 1,111 | -3% |
| India | 183 | 157 | 440 | 16% | -58% | 1,462 | 2,057 | -29% |
| EU | 177 | 213 | 236 | -17% | -25% | 1,317 | 1,317 | 0% |
| Pakistan | 69 | 78 | 84 | -12% | -18% | 584 | 513 | 14% |
| US | 44 | 51 | 53 | -13% | -17% | 348 | 437 | -20% |
| Others | 821 | 710 | 713 | 16% | 15% | 5,917 | 5,062 | 17% |
| Total | 1,488 | 1,398 | 1,824 | 6% | -18% | 10,704 | 10,497 | 2% |

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 | 9.05 | NEUTRAL | SOP with plantation sector @ 26.8x FY18E PE. 26.8x is the higher of IOICORP and KLK Target PE. |
| IOICORP | 4.95 | NEUTRAL | 24.7x Fwd. PE on FY18F 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 | 1.59 | NEUTRAL | 1.0x Price to Book Value |
| GENP | 12.06 | BUY | SOP with plantation sector @ 24.7x FY17E PE. 24.7x is the lower valuation between IOICORP and KLK. |
| IJMP | 3.00 | NEUTRAL | 18.6x Fwd. PE on FY18F earnings reflecting mean valuation. |
| TSH | 2.15 | BUY | 22.3x Fwd. PE on FY17F earnings reflecting mean valuation. |
| TAANN | 4.30 | BUY | 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. |