

11 July 2017 | Sector Update

PLANTATION**Maintain NEUTRAL*****June inventory is lower than expected*****KEY HIGHLIGHTS**

- **June inventory is lower than expected**
- **Production decline yoy in June should be temporary**
- **Export to China and India weaken in June**
- **Expect July-2017 inventory to increase 8% mom to 1.65m MT**
- **Maintain NEUTRAL with BUY on KLK (TP: RM29.25), TSH (TP: RM2.15) and TAANN (TP: RM4.30)**

June inventory is lower than expected. Malaysia palm oil inventory level of 1.53m MT as of end-June 2017 is lower than consensus estimate of 1.56m MT but is close to our estimate of 1.52m MT. Against last month, inventory level declined by 2% as production decline of 8.5% exceed export decline of 8.4%. Against same period last year, inventory remains lower yoy by 14 % against May's 5% decline yoy.

Production decline yoy in June should be temporary. CPO production declined by 8.5% mom and 1.2% yoy to 1.52m MT. Peninsular Malaysia palm production leads the decline by 12.1% mom to 760,050 MT and this is followed by Sabah (-7.1% to 428,835 MT) and Sarawak (-0.8% mom to 325,285 MT). June production decline by 1.2% yoy should be temporary and we maintain our view that the uptrend of strong production should continue from July onwards and throughout 3Q2017. The decline in June production yoy could be caused by slight difference in the timing of Hari Raya leave taken by FFB harvesters in 2017 against last year which has caused production to falls significantly in the last 10 days of June. Note that Hari Raya falls on 25 June this year against 6 July in 2016.

Export to China and India weaken in June. Export to China fell 39% mom to 273,699 MT. Besides China, export to India has also slipped 13% mom to 238,198 MT. We believe that lack of festival in June contributed to the weaker usage of palm oil in these countries.

Expect July-2017 inventory to increase 8% mom to 1.65m MT. Key assumptions are: i) production increase of 8% mom and ii) export decline of 2% mom. We believe that palm oil demand should remain lackluster in July in the absence of major festivals. Our export estimate is also close to cargo surveyors export performance of 1.9% decline for the first ten days of July. For production growth we are using seasonal factor to estimate the 8% increase.

Maintain NEUTRAL with BUY on KLK (TP: RM29.25), TSH (TP: RM2.15) and TAANN (TP: RM4.30). Our NEUTRAL view on the sector is maintained as we expect strong production in 2H2017 to cap CPO price upside. We like KLK for the Company earnings resiliency and its good FFB production growth estimated at 8% (highest among index-linked plantation stocks). We also like TSH due to: i) its strong 1QFY17 Core Net Profit which has grown 71% yoy, ii) attractive valuation at 17.8x PE which is close to its -0.5SD level of 18.1x and iii) its young age profile of ~7.3 years old which should allow them to register better FFB growth in the long run. Lastly, we have BUY call on TAANN as: i) its plantation division earnings growth should remain strong due to high FFB volume expected at 10% and ii) timber division is expected to remain profitable due to the support from high export logs price.

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

	Jun-17	May-17	Diff.	MoM %	Jun-16	YoY%
Opening Stocks	1,557	1,600	(43)	-2.7%	1,650	-5.6%
Production	1,514	1,654	(140)	-8.5%	1,533	-1.2%
Imports	46	47	(2)	-3.4%	20	133.5%
Total Supply	3,117	3,302	(185)	-5.6%	3,202	-2.7%
Exports	1,380	1,506	(126)	-8.4%	1,132	21.9%
Dom Disapp	210	239	(28)	-11.9%	294	-28.4%
Total Demand	1,590	1,745	(155)	-8.9%	1,426	11.5%
End Stocks	1,527	1,557	(30)	-1.9%	1,776	-14.0%
Stock/Usage Ratio	8.0%	7.4%			10.4%	

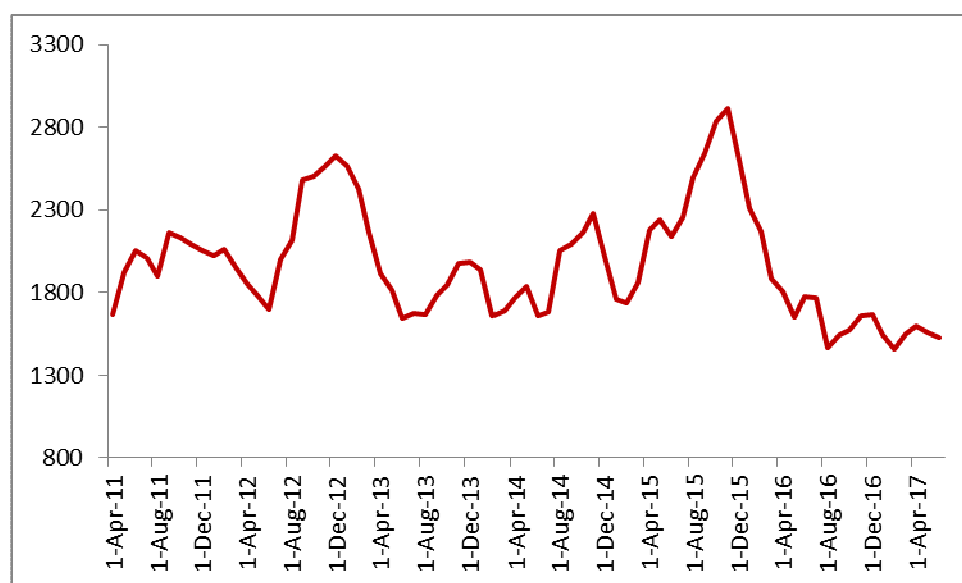
Source: MPOB, MIDF Research

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

Country	Jun-17	May-17	Jun-16	MoM%	YoY%	6M17	6M16	YoY%
China	69	113	101	-39%	-32%	693	601	15%
India	238	274	169	-13%	41%	1,117	1,428	-22%
EU	169	169	151	0%	12%	927	891	4%
Pakistan	124	108	88	14%	40%	438	368	19%
US	48	39	30	24%	59%	253	308	-18%
Others	733	803	602	-9%	22%	4,391	3,693	19%
Total	1,380	1,506	1,142	-8%	21%	7,819	7,289	7%

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	5.00	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	1.59	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	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.