

Plantation Sector


Maintain NEUTRAL

Windfall Tax Outlook

DEVELOPMENT

- According to media reports yesterday, the Government will be reviewing windfall tax on palm oil industry.
- YAB Deputy Prime Minister Fadillah Yusof said Putrajaya hopes to complete its review on the existing windfall tax by next year.

OUR VIEW

- If we were to take KLK as a case study, for FY21-22; the breakdown of Cess & Taxes paid by KLK for FY21-22 showed a contribution of 2%-3% for MPOB, 49-60% for Malaysia Export Tax, 12%-29% for Windfall Profit Levy, and 26%-20% for Sabah Sales Tax. KLK was taxed at a higher rate of 15% (CY21: 7.5%) in FY22, totalling RM110m (+578%yoy). This was in line with higher average CPO realized at RM4,774/Mt (CY21: RM3,485/Mt), which unfavourably affected core profits but still came in higher at RM2.17b. We anticipate KLK's windfall profit tax to be significantly lower at RM40m (-64%yoy), given the lower average CPO realized at RM3,800 for FY23F, bringing decent earnings of RM1.52b for the full financial year.
- Based on its 2QFY23 performance, we observed 1 of the input (fertilizers) of production cost had eased. In fact, fertilizers price index had fallen to 167.9 pts (-45%yoy), and notably, feedstock for fertiliser including urea, phosphate, and potassium have stabilized, to the average of USD310/Mt (-60%yoy), USD344/Mt (+31%yoy), and USD369/Mt (-68%yoy) respectively. Meanwhile natural gas prices in Europe dropped to average of USD31.6/mmbtu (-33%qoq, -64%yoy). Therefore, we expect most of the planters will incur lower operational expenses in 2HCY23, at least, due the typical industry practices that fertilizers stocks to be locked in 6-12 months in advance.
- The cost of production for 1HCY23 was still high due to higher locked-in fertilizer prices in 2HCY22 (the weighted average cost of production for fertilizers increased from 15% to 30% last year) and high labor costs. All in all, this would consequently result in ceteris paribus of production cost in CY23. Since there is not much change in costs of production for planters in this year, we're seeing the revision for windfall profit levy remain status quo now, however, it can be tweak higher for CY24 following;
 - 1) lower locked-in fertilisers price in 2HCY23 (which will result in lower fertilisers cost in 1HCY24) – down in production cost.
 - 2) in anticipation of higher average realized CPO price (our forecast RM4,200/Mt for CY24).
- As planters appear to have more room to absorb windfall profit tax, this will allow the government to adjust a larger windfall profit levy in CY24-25.
- Maintain **NEUTRAL**. While we acknowledge the El-Nino events (which would constrict the supply side) could be a potential catalyst for the CPO prices to remain elevated for the remaining of the months c. CY24 RM3,800-4,200/Mt, we are also concern on its fragile demand outlook on the back inflationary pressure coupled with tight household spending on high base interest rate locally and globally. All factors considered, we maintain our **NEUTRAL** stance on the sector with CPO target price of **RM3,800 Mt** for CY23. Our top pick for plantation company is **KLK** with a **TP** of **RM24.60**. 

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MIDF AMANAH INVESTMENT BANK: GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% 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.

ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell

☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology