

12 November 2019

Plantation

NEUTRAL

Inventory Continues Decline After Sept Pause



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October 2019 inventory fell (-4.1% MoM) to 2.35m MT, below both consensus/our estimates of 2.52m/2.78m MT (+2.8%/13.4% MoM), respectively, due to: (i) lower-than-expected production (-2.5% MoM) vs. consensus/our estimates (+2.0%/+3.7% MoM) on dry weather impact in June-October, and (ii) higher-than-expected exports (+16.4% MoM) vs. consensus/our forecasts (+13.0%/-5.1% MoM) which stemmed from China (+24% MoM) as demand for palm oil as a substitute to soybean oil remained strong, EU (+44% MoM), and other countries (+42% MoM) such as Turkey, Nigeria, and Netherlands as they stock up on inventory. For November, we estimate: (i) production decline (-2.2% MoM) on continued impact from dry weather, (ii) slightly lower exports (-0.8% MoM) as India remains weak. Nevertheless, we expect demand (1.95m MT) to outstrip supply (1.83m MT) leading to lower ending stocks of 2.23m MT (-5.1% MoM) in November. We **maintain NEUTRAL on the plantation sector** with an unchanged **CY19-20 CPO price forecast of RM2,100-RM2,400/MT**. All-in, after weighing the potential positives and negatives, we believe 2020 should spell out a better year for planters. **Our preferred picks for the sector are KLK (OP; TP: RM24.60) and HSPLANT (OP; TP: RM1.70).**



October 2019 CPO inventory declined 4.1% MoM to 2.35m metric tons (MT), below both consensus and our estimates of 2.52m MT (+2.8% MoM) and 2.78m MT (+13.4% MoM), respectively. This is attributed to: (i) lower-than-expected production of 1.80m MT (-2.5% MoM) vs. consensus/our estimate of 1.88m/1.91m MT (+2.0%/+3.7% MoM) respectively, and (i) higher-than-expected exports of 1.64m MT (+16.4% MoM) vs. consensus/our forecast of 1.59m/1.34m MT (+13.0%/-5.1% MoM), respectively. Deviation in production largely stemmed from the impact of the dry weather in June-October. On the other hand, exports surprised positively due to stronger-than-expected demand from: (i)

China (+24% MoM) as demand for palm oil as a substitute to soybean oil remained strong, (ii) EU (+44% MoM), and (iii) other countries (+42% MoM) such as Turkey, Nigeria, and Netherlands as they stock up on inventory.

November 2019 production to decline further by 2.2% MoM to 1.76m MT. The impact from the dry weather in June-early October is expected to continue on for the next 2-3 months. Alongside cost managing maneuvers such as lower new planting activities and lower fertiliser application in the past 1-2 years, we believe production should continue to decline. We forecast November output to fall by 2.2% MoM to 1.76m MT.

Exports to decline slightly to 1.63m MT (-0.8% MoM) in November 2019. Moving forward, we expect to see a 0.8% MoM decline in export volume to 1.63m MT, as exports to India continue to remain weak due to the impact of India's import tariff increase. Based on cargo surveyors' (AmSpec & Intertek) data for 1st – 10th November, exports have seen an increase of 56k MT (+16% MoM). However, we believe this should moderate throughout November as demand from other countries also normalise post-festive season.

November 2019 inventory to further decline to 2.23m MT (-5.1% MoM). We expect demand of 1.95m MT to outstrip supply of 1.83m MT, leading to lower ending stocks of 2.23m MT (-5.1% MoM) in November. Meanwhile, we expect CPO prices to remain range-bound (RM2,300-2,500/MT) for the remaining 4QCY19, supported by (i) healthy soybean oil-crude palm oil (SBO-CPO) premium of USD106/MT (close to 3-year average of USD111/MT), (ii) strong demand amidst slowing production, and (iii) weaker ringgit (CY19E USD/MYR of 4.20 vs. current USD/MYR of 4.14).

Maintain NEUTRAL on the plantation sector with an unchanged CY19-20 CPO price forecast of RM2,100-RM2,400/MT. All-in, after weighing the potential positives and negatives, we believe 2020 should spell out a better year for planters. **Our preferred picks for the sector are KLK (OP; TP: RM24.60) and HSPLANT (OP; TP: RM1.70).**

- (i) **KLK (OP; TP: RM24.60).** At current price, KLK is trading at Fwd. PBV of only 2.2x (implying -2.0SD from mean) which we believe is unjustified given its: (i) above-average FFB growth (for big caps) of 4.3%, (ii) above-sector average FY20 ROE of c.8% (vs. sector's average of c.5%), and (ii) decent dividend yield of 2.2%.
- (ii) **HSPLANT (OP; TP: RM1.70).** We like HSPLANT as a pure upstream planter allowing it to capitalize on the recovery in CPO price to a greater extent. Its zero exposure to Indonesia also allows it to mitigate the impact of the dry weather. At current price, HSPLANT is trading at Fwd. PBV of only 0.74x (implying -1.5SD from mean) which we think is unwarranted given its: (i) above-average FFB growth prospect of 4.5%, (ii) net cash position of c.RM52m, and (iii) low EV/planted Ha of RM33k, implying 20% discount to small cap planters' average EV/planted Ha of RM41k.

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Exhibit 1: Palm Oil Statistics for Oct-2019 ('000 tonnes)

	Oct-19	Sep-19	Diff.	MoM %	Oct-18	YoY%
Opening Stks	2,449	2,241	208	9.3%	2,529	-3.2%
Production	1,796	1,842	(47)	-2.5%	1,965	-8.6%
Imports	85	71	14	19.6%	117	-27.5%
Total Supply	4,329	4,154	175	4.2%	4,612	-6.1%
Exports	1,642	1,410	232	16.4%	1,578	4.0%
Dom Disapp	340	296	44	14.9%	311	9.2%
Total Demand	1,981	1,706	276	16.2%	1,889	4.9%
End Stks	2,348	2,449	(100)	-4.1%	2,722	-13.8%
Stock/Usage Ratio	9.9%	12.0%			12.0%	

Source: MPOB, Kenanga Research

Exhibit 2: Monthly Exports and YTD exports for Oct-2019 ('000 tonnes)

	Oct-19	Sep-19	Oct-18	MoM%	YoY%	10M19	10M18	YoY%
China	275	223	214	23.8%	28.9%	1,905	1,413	34.8%
India	220	311	99	-29.2%	121.5%	4,144	1,987	108.5%
EU	201	140	166	43.9%	20.8%	1,751	1,668	5.0%
Pakistan	82	119	105	-31.6%	-22.5%	901	972	-7.3%
US	28	31	47	-9.4%	-40.2%	494	447	10.7%
Others	836	587	940	42.4%	-11.1%	6,461	7,241	-10.8%
Total	1,642	1,410	1,571	16.4%	4.5%	15,657	13,727	14.1%

Source: MPOB, Kenanga Research

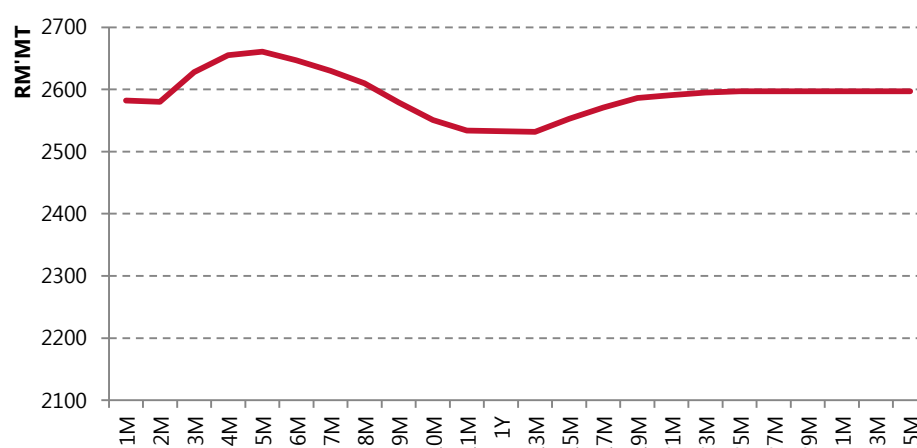
Exhibit 3: CPO Prices - Current & Forecast

	RM/MT
Last Price (08-November-19)	2,425
Year-to-date Average	2,026
2018 Average	2,235

	CY19 RM/MT
CPO Price Forecast	2,100
Revisions	+0%

Source: Bloomberg, Kenanga Research

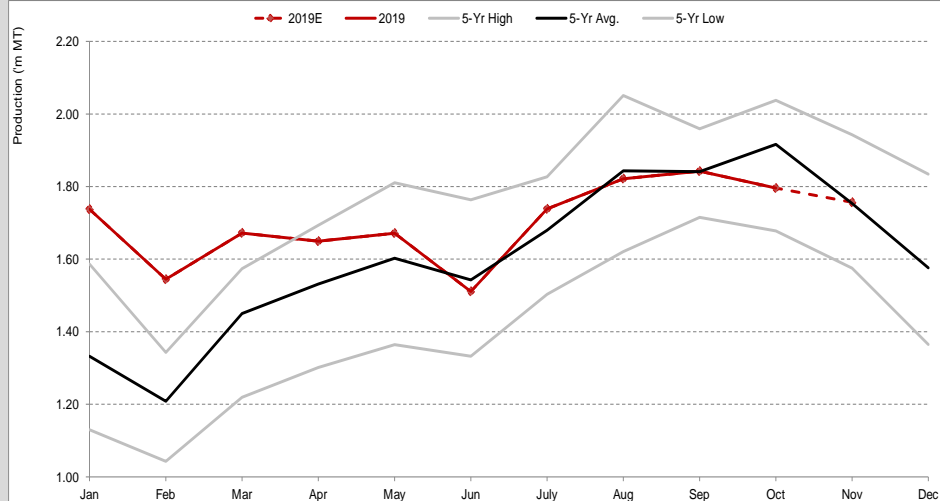
Exhibit 4: CPO Forward Curve as of 11-November-19



Source: Bloomberg, Kenanga Research

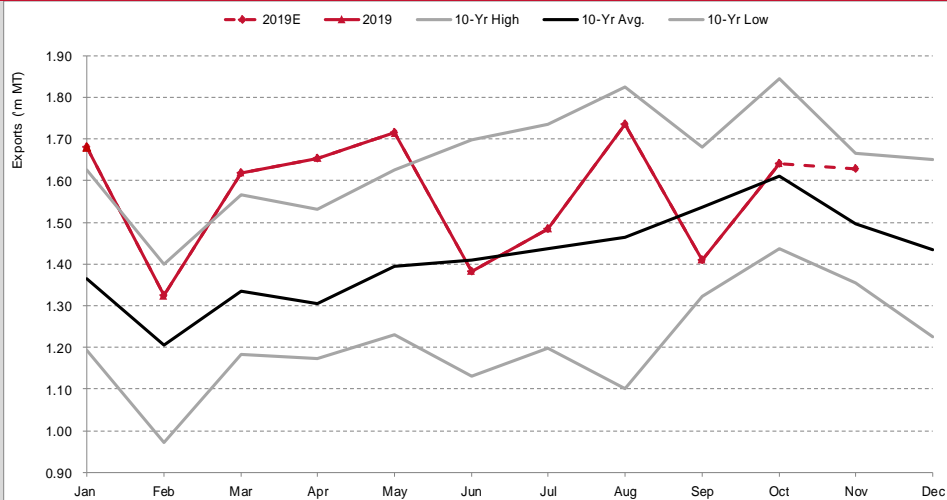
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Exhibit 5: Malaysia 2019E CPO Production vs. 5-year Trends



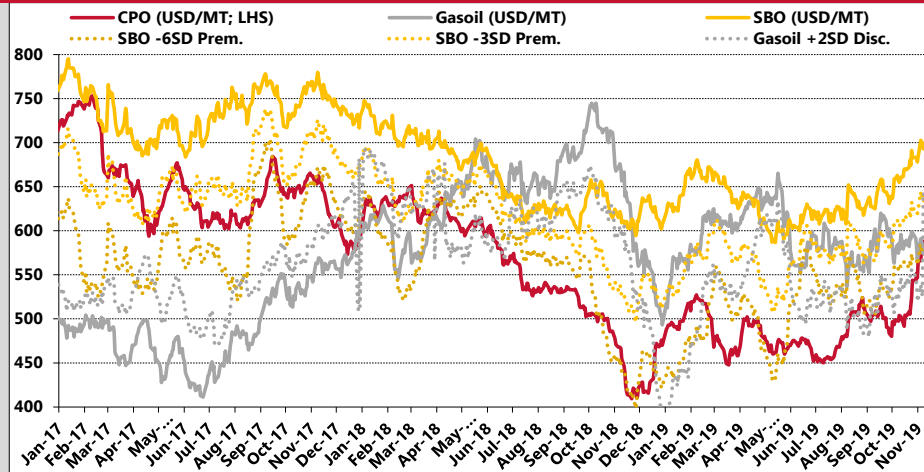
Source: MPOB, Kenanga Research

Exhibit 6: Malaysia 2019E CPO Exports vs. 10-year Trends



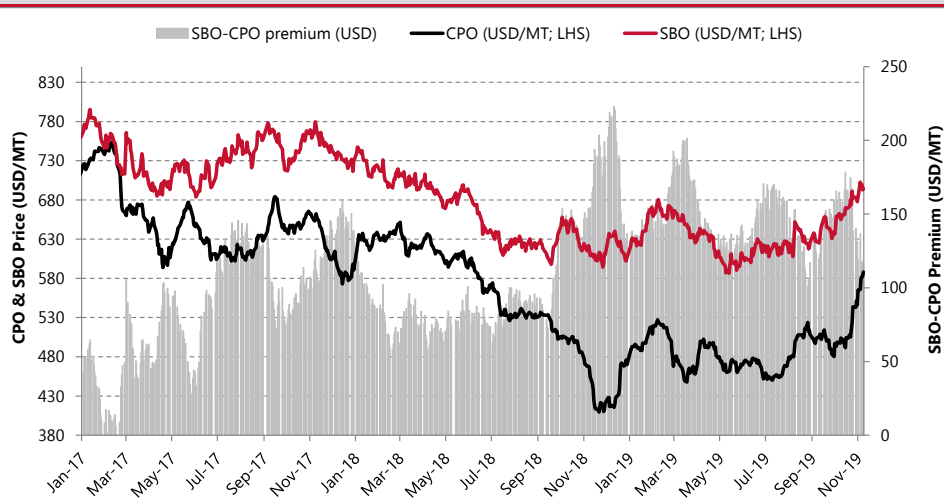
Source: MPOB, Kenanga Research

Exhibit 7: CPO vs. SBO Price and Gasoil Premium/Discount



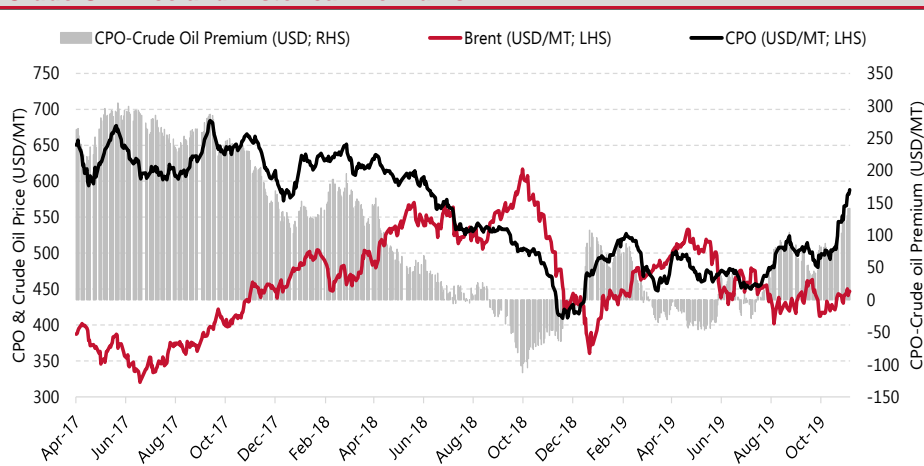
Source: Bloomberg, Kenanga Research

Exhibit 8: CPO vs. SBO Price and Historical Premiums



Source: Bloomberg, Kenanga Research

Exhibit 9: CPO vs. Crude Oil Price and Historical Premiums



Source: Bloomberg, Kenanga Research

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Peer Comparison

Name	Last Price	Market Cap	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price (RM)	Rating
	(RM)	(RM'm)			1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE																	
CB INDUSTRIAL PRODUCT HLDG	0.850	430.0	Y	12/2019	-23.4%	14.5%	-34.9%	43.6%	8.5	13.1	9.1	0.6	0.6	4.5%	4.7%	0.860	MP
FGV HOLDINGS BHD	1.23	4,487.2	Y	12/2019	3.8%	3.8%	-332.3%	70.8%	N.A.	N.A.	52.5	1.0	1.0	-1.2%	0.0%	1.15	MP
GENTING PLANTATIONS BHD	10.14	9,097.6	Y	12/2019	4.9%	10.8%	28.2%	52.2%	57.1	48.6	34.6	2.0	2.1	4.4%	1.1%	9.80	MP
HAP SENG PLANTATIONS HLDGS	1.54	1,231.5	Y	12/2019	4.5%	14.3%	-61.0%	253.3%	42.4	108.5	30.7	0.7	0.7	0.7%	0.6%	1.70	OP
IJM PLANTATIONS BHD	1.61	1,417.7	Y	03/2020	0.6%	14.7%	37.4%	93.1%	N.A.	50.2	26.0	0.8	0.8	1.6%	1.2%	1.65	MP
IOI CORP BHD	4.40	27,652.4	Y	06/2020	-2.0%	5.9%	37.1%	11.8%	36.4	26.5	23.7	3.0	2.8	11.0%	2.3%	4.60	MP
KUALA LUMPUR KEPONG BHD	22.20	23,642.2	Y	09/2019	-14.8%	15.1%	-27.5%	40.7%	26.5	36.6	26.0	2.3	2.3	5.6%	1.8%	24.60	OP
PPB GROUP BERHAD	18.10	25,749.1	Y	12/2019	5.4%	5.6%	19.0%	6.3%	27.3	22.9	21.6	1.2	1.2	5.4%	1.8%	16.50	UP
SIME DARBY PLANTATION BHD	4.98	34,285.2	Y	12/2019	87.7%	12.0%	63.2%	184.5%	153.3	93.9	33.0	2.6	2.6	2.7%	0.6%	5.10	MP
SOUTHERN ACIDS MALAYSIA BHD	3.79	519.0	Y	03/2020	12.4%	6.9%	49.8%	20.0%	29.9	20.0	16.7	0.9	0.8	4.3%	1.6%	3.65	MP
TA ANN HOLDINGS BERHAD	2.55	1,123.2	Y	12/2019	-5.8%	15.9%	-50.1%	85.9%	13.7	27.5	14.8	0.8	0.8	3.1%	2.0%	2.85	OP
TSH RESOURCES BHD	0.950	1,311.2	Y	12/2019	1.0%	13.3%	-1.1%	36.9%	26.5	26.7	19.5	0.9	0.9	3.4%	0.9%	1.00	MP
UNITED MALACCA BHD	5.22	1,094.6	Y	04/2020	8.1%	13.5%	-377.0%	73.1%	N.A.	N.A.	89.2	0.6	0.7	-0.5%	1.1%	5.30	MP
Simple Average					6.3%	11.3%	-49.9%	74.8%	42.2	43.1	30.6	1.3	1.3	3.5%	1.5%		

Source: Bloomberg, Kenanga Research

Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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