

10 June 2024

Plantation

1QCY24 Results Review: A Patience Game

NEUTRAL



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1QCY24 plantation sector earnings were muted. Downstream continued to disappoint which dampened earnings of all three big integrated players, SDG (formerly SIMEPLT), IOI, and KLK. Upstream earnings held better on easier costs and firm CPO prices: thus, smaller, more upstream-centric players fared better. Meanwhile, SDG's solar farming plans highlight a lucrative alternative land use for the sector but limited sector-wide impact is expected as many planters are likely to stay oil palm-centric. Maintain NEUTRAL. PBV of 1.1x is not demanding but there is no strong upside catalyst. Higher CPO would be such a catalyst but supply-demand scenario suggests firm rather than bullish CPO prices ahead. We continue to prefer players with the ability and/or flexibility to grow such as PPB (OP; TP: RM17.50), TSH (OP; TP: RM1.30), and UMCCA (OP; RM6.00).

A mix first quarter. After an optimistic start of the year, with Bursa Plantation Index almost touching a 2-year high of 7,500.86 on 8 May 2024, the plantation sector's 1QCY24 results ended weak. The larger integrated players continued to disappoint due to their greater downstream exposure. Despite flattish-to-modest upstream recovery, downstream margins continued to be a drag. Smaller to mid-size players with more upstream-centric operations fared better in 1QCY24.

Quarterly Results Performance

	1QCY24						4QCY23					
	KENANGA			CONSENSUS			KENANGA			CONSENSUS		
	Above	Within	Below	Above	Within	Below	Above	Within	Below	Above	Within	Below
GENP		1			1			1				1
HSPLANT		1				1	1					1
IOI			1			1			1			1
KLK			1			1			1			1
PPB			1			1		1				1
SDG*			1			1			1			1
TAH		1				1	1					1
TSH		1				1		1				1
UMCCA	1			1					1		1	
Total	1	4	4	1	1	7	2	3	4	-	5	4
Total (%)	11	44	44	11	11	78	22	33	44	-	56	44

Source: Kenanga Research, Bloomberg

* New name for Sime Darby Plantation

Downstream continued to face headwind. All three large integrated players, IOI (MP; TP: RM3.80), KLK (MP; TP: RM21.00) and SDG (MP; TP: RM4.00), failed to meet expectations for their Jan-Mar 2024 quarterly results. Offtake for downstream food such as refining fared better than non-food oleo-chemicals but margins continued to stay tight. Nonetheless, downstream revenue improved QoQ on restocking and, potentially, bottoming out but overall market was still not strong.

Upstream fared better, thanks to firm CPO prices as well as slightly lower costs. MPOB reported firm 1QCY24 CPO price of RM3,983/MT, which came in seasonally higher QoQ (+9%) but flattish YoY (-0.3%). Meanwhile, fuel and fertiliser prices have dropped by 15%-35% YoY, respectively, during 1QCY24m, and coupled with recovering FFB output in Malaysia, upstream cost pressures have eased. Moving ahead, some wage inflation can be expected but palm kernel prices (PK) have also improved after having declined since mid-CY22. A byproduct when milling CPO, PK sales is used to offset CPO milling cost.

Smaller, more upstream centric players are set to do better. Compared to the larger integrated groups, smaller plantation players performed better in 1QCY24, essentially coming in within Kenanga's expectations though many still disappointed consensus expectations. In this regard, the plantation sector as a whole, emerged worse off in 1QCY24 compared to 4QCY23 as only 33% of plantation companies met consensus expectation in 1QCY24 compared to 56% in the previous quarter.

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Can large scale solar (LSS) trigger a sector re-rating? Malaysia has about 26GW of power generation capacity, 10% of which is solar with the intentions to add another 2 GW of solar under LSS5. LSS5 request-for-proposal is closing next month with projects due to commence by 2026. As 2GW of solar would need about 3,000 Ha of surface area, some estates will likely be home to solar installations. SDG is already planning several solar projects, not just those under LSS5 but a 267-Ha solar installation at its own Kerian Integrated Green Industrial Park (KIGIP) development. In general, land owners such as planters can get involved economically in solar opportunities via two main routes:

- (a) **Rental model.** Leasing out suitably located or unproductive sites to solar farms is straight forward. A 1GW solar farm will require about 1,500 Ha, potentially giving rise to RM15-20m of annual after-tax rental income. A similar sized oil palm estate would have generated only half the return in the past five years though better planters did earn RM10m-15m a year.
- (b) **Developer and owner.** A more lucrative option is for planters to develop and operate their own solar farms. After tax returns can reach RM100m a year for a 1GW of solar capacity. As many listed planters are well capitalised, this will probably be their choice option though perhaps not as large as 1GW which needs RM2b-3b in upfront capital to set up.

Altogether, the plantation sector is set to gain from a more vibrant solar sector thanks to demand for surface area. However, the impact of solar installation on the plantation sector is expected to be limited as many planters will remain focus on oil palm.

For a perspective, even if Malaysia were to install solely solar to double its present-day power generation capacity of 26GW to 52GW, only 40k Ha (0.04m Ha) of surface area will be required. In contrast, planted Malaysian oil palm area was 5.65m Ha in CY23. Malaysia's SEDA (or Sustainable Energy Development Authority) target for solar capacity to be just slightly above 7GW come 2035. Nevertheless, solar farming can prove lucrative use for selected pieces of land for planters. SDG is already pursuing solar driven growth and its earnings should enjoy 5%-10% uplift in the coming 3-5 years from its solar initiatives.

Maintain NEUTRAL. Trading at PBV of 1.1x, the plantation sector downside is likely limited. However, there is no strong upside catalyst. Easing upstream cost is positive for margins but unlikely to sufficiently compelling to trigger an upward re-rating. Higher CPO prices would be a stronger upside catalyst but current supply-demand scenario of the global edible oil trade suggests firm but flattish CPO prices ahead. Hence, our NEUTRAL stance for the sector with preference for planters with the ability and/or capability to grow their business such as (a) **PPB** and its mass consumer food and cinema businesses, (b) **TSH** which is developing 8k-10k Ha of new oil palm area or an expansion of 25%-30%, and (c) **UMCCA** which should see stronger contribution moving forward from its maturing Indonesian estates.

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RMm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net Div. (sen)	Net Div Yld
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
PLANTATION																	
GENTING PLANTATIONS BHD	MP	5.93	6.00	1.2%	5,320.2	Y	12/2024	33.9	36.1	21.0%	6.4%	17.5	16.4	1.0	5.6%	21.0	3.5%
HAP SENG PLANTATIONS HOLDINGS	MP	1.79	2.00	11.7%	1,431.4	Y	12/2024	12.8	13.1	13.0%	2.8%	14.0	13.6	0.7	5.2%	8.0	4.5%
IOI CORP BHD	MP	3.90	4.10	5.1%	24,194.4	Y	06/2024	18.9	21.2	-22.3%	12.0%	20.6	18.4	2.2	11.6%	11.0	2.8%
KUALA LUMPUR KEPONG BHD	MP	21.16	21.00	-0.8%	23,199.9	Y	09/2024	90.0	125.7	8.7%	39.7%	23.5	16.8	1.5	6.7%	50.0	2.4%
PPB GROUP BHD	OP	14.82	17.50	18.1%	21,082.9	Y	12/2024	111.1	132.5	38.1%	19.3%	13.3	11.2	0.7	5.6%	45.0	3.0%
SIME DARBY PLANTATION BHD	MP	4.34	4.00	-7.8%	30,014.2	Y	12/2024	16.1	18.9	25.9%	17.7%	27.0	23.0	1.7	6.2%	15.0	3.5%
TA ANN HOLDINGS BHD	MP	4.08	4.00	-2.0%	1,797.1	Y	12/2024	40.9	43.5	3.5%	6.2%	10.0	9.4	1.0	10.0%	25.0	6.1%
TSH RESOURCES BHD	OP	1.11	1.30	17.1%	1,532.0	Y	12/2024	6.9	7.4	-1.8%	6.3%	16.0	15.1	0.7	9.2%	2.0	1.8%
UNITED MALACCA BHD	OP	5.04	6.00	19.0%	1,057.2	Y	04/2024	24.6	32.8	-25.4%	33.3%	20.5	15.3	0.7	3.2%	12.0	2.4%
Simple Average					109,629.4					8.9%	19.5%	19.7	16.5	1.1	7.0%		3.3%

Source: Bloomberg, Kenanga Research

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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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