Market Access

Plantation Sector

(Neutral)

"A Glance - What an immature and young mature plants could promise"

Table 1: Plantation Sector Operational Metrics Projection

	2014	2015F
CPO Price (RM/MT)	2,408	2,150
CPO Production (Million Tonnes)	19.7	20.5
Palm Oil Export (Million Tonnes)	17.3	18.5
Ending Stocks (Million Tonnes)	2.0	2.05

Source: M&A Securities

Table 2: Plantation Statistics

Companies	Age profile (hectares)				Young Matured (ha)		Total Planted Area(ha)	Average Age (years)
	Immature		Matured		Hectares	%		
IOI Corporation	29,019	16.2%	149,749	83.8%	19,632	11.0%	178,768	13
Kuala Lumpur Kepong	32,354	16.1%	168,243	83.9%	55,576	27.7%	200,597	12
Genting Plantations	40,694	31.8%	87,184	68.2%	23,388	18.3%	127,878	7
IJM Plantations	18,370	31.2%	40,530	68.8%	17,545	29.8%	58,900	8
TH Plantations	22,001	36.4%	38,415	63.6%	19,597	32.4%	60,416	9
TSH Resources	25,019	47.5%	27,669	52.5%	14,922	28.3%	52,688	7

Source: Companies, M&A Securities

CPO prices have weakened in the past months as rising production and stocks levels coupled with falling exports have spooked investors. However, growing concern about the impact of recent dry weather and haze from the burning forest in Indonesia as well as the weakening of Ringgit has somehow brought back the bull. As mentioned in our report "Betting on El-Nino for Palm Oil Price Up-Cycle" last year, we postulated that weather would play an important role in the supply equation of production and yield, and inextricably one of the key catalysts to CPO price movement. Although planted area and/or harvested area also play an important factor that would affect palm oil production, yield is more important in determining the production as its variability is associated with weather factors. Dry and hot weather causes moisture stress in palms, hinders growth of leaves and fruit and hence, potentially curbing yield. That said, we posit that palm oil production is expected to be effected in the next 6 to 12 months due to the spill-over effect of bad weather from the drought that took place in the 2nd half of February and 1st half of April 2015 in Sabah, 2nd half of July 2015 till now in East and Central Kalimantan, and July 2015 in Sumatera. No doubt that the weakening of

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Ringgit has also impacted our export competitiveness and hence, supporting the demand of palm oil and lifting its prices.

CPO price rallied. The 3-month CPO futures price has rallied in the last week of September with the affirmative movement carried over to 6 October 2015, which saw the CPO futures at its highest intra-day level of RM2,460/MT (6-years intra-day low of RM1,863/MT in 25 Aug 2015) in 29 September 2015 before closing at RM2,276/MT in 8 October 2015. The reversal could be due to the firmer Ringgit (8 Oct 15: USDMYR4.2358; 29 Sept 15: USDMYR4.4565) that has probably caused demand to shift to Indonesia. This is along with bearish outlook on higher palm oil production and stockpile levels in September figure (will be publish by MPOB on 12 Oct 2015) could weigh further palm prices, causing sentiment to turn dry. Aligned with the derivatives market, MPOB price has also rallied in the last week of September and carried over until 5 October 2015, which saw its highest level of RM2,307.50/MT in 5 October 2015 before declining back to RM2,182/MT in 8 October 2015.

Subsequent to the CPO price rally, the plantation sector bellwether index for 10 days period in 29 Sept to 8 Oct 2015 had registered encouraging performance, surging 5.9% against FBMKLCI which only increased by 5.5%. Share price of the plantation players also rode the positive sentiment where in the 10-day period, SIME share price has led its peers performance after surging by 17% followed by TSH at 11.8%, IOIC (11.0%), FGV (9.1%), TH Plant (5.3%), KLK (4.8%), IJM Plant (3.5%), Genting Plant (3.0%) and Batu Kawan (2.1%).

What an immature and young mature plants could promise - at glance. Looking at the scenario, we assume there would be rising interest in plantation stock with higher growth potential and/or with downstream involvement and has economic of scale. As such, we suggest long-term investor to look out for plantation's company with the above-mentioned criteria provided that the company has solid fundamentals; lean balance-sheet, strong cash-flow position and efficient estate management practise, as we deem this will be the perfect recipe that will push pull investors to accumulate their holdings.

Placing other factors being equal, ceteris paribus, TSH Resources has emerge to be the biggest potential candidate for exponential growth in the next few year measured by the biggest percentage of immature area, where 48% of its planted oil palm estates can be deemed as immature age (read: age between 0 – 3 years), followed by TH Plant (36%), Genting Plant (32%), IJM Plant (31%), KLK (16%) and IOI Corp (16%). Mirroring from these immature area, the youngest average age profile of estate would be Genting Plantation and TSH Resources (7-years), followed by IJM Plant (8-years), TH Plant (9-years), KLK (12-years) and IOI Corp (13-years). This solid metrics will be a key earnings driver moving forward of at least for another 5 to 10 years especially when the trees gets mature. On the other hand, KLK and IOI Corp are among the company with highest percentage of area under production as more area can be harvested to benefit of the turn-around of the palm oil prices. KLK led its peers with 83.9% of it planted oil palm estates area under production, followed by IOI Corp (83.8%), IJM Plant (68.8%), Genting Plant (68.2%), TH Plant (63.6%) and TSH Resources (52.5%). Though TSH recorded the lowest percentage of mature area planted, TSH has the highest plantable reserves measuring approximately 53,430 hectares or 59% of its total land bank – which we believe a

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good candidate for the company's long-term growth sustainability. We are of the views that, once CPO price on a roll, these fundamentally and attractive operating matrix companies will accelerate first.

Conclusion. Although the lowly hanging fruits, as in brightly lit operational metrics of the above companies may take time to realise, but we firmly believe that investors should turn their radar on them and start accumulating their stocks despite the tepid stock market and CPO price movement. We believe the above selected companies will be the first to ride on the wave once the local market enters its bull market and patiently placing trust in these stocks will pay off handsome reward. We believe the CPO up-cycle will emerge in the next few years and hence, worth accumulating these stocks especially when there are currently trading at the bottom at the moment.

Our view. At this stage we maintain our **NEUTRAL** call on plantation sector, but if the landscapes change, we may review our call on the sector. At this junction, our average CPO price target of RM2,150/MT for 2015 and RM2,300/MT for 2016 stays. We remain positive on the long-term outlook of the oil palm plantation sector as we believe the key CPO price drivers are still in place. However, we are cautiously optimistic that CPO price rally may not sustain as supply is expected to remain elevated while demand will take time to catch up and hence, leading to high stock levels. We still believe that macro issue cause by uncertainty of the world economy such as the slowing growth in China, the US interest rates uncertainties coupled with a drop in oil prices, have made a lot of volatility in the commodity market and hence, going to dampen demand especially from China, US and EU.

At this stage, we maintain **HOLD** call on KLK (TP: RM21.21), Genting Plant (TP: RM9.66) and TSH Resources (TP: RM1.95). However, due to the recent rally in plantation stocks, we have SELL call on TH Plant (TP: RM1.21), IJM Plant (TP: RM2.93) and IOI Corp (TP: RM3.60). We continue to favor TSH (Hold: RM1.95) and Genting Plant (Hold: RM9.66) given their bright outlook underpinned by 1) better FFB yield moving forwards as more young trees will reach its prime age; 2) high percentage of immature to young matured land over planted area which provides visible revenue and earnings growth catalyst; and 3) operational efficiencies and promising long-term earnings growth potential.

Table 3: Peers Comparison - Stocks under Coverage

Company	Mkt. Cap (RM m)	Price (RM)	EPS (sen)		P/E (X)		P/B (X)		ROE	Div. Yield	TP	Call
			FY1	FY2	FY1	FY2	FY1	FY2				
IOI CORP	27,716.1	4.40	15.3	19.0	28.8	23.2	3.3	3.1	3.0	2.1	3.60	SELL
KLK	24,153.4	22.68	93.5	101.3	24.3	22.4	2.8	2.7	10.3	2.5	21.21	HOLD
GENPLANTS	8,039.9	10.34	36.1	47.6	28.6	21.7	1.9	1.8	7.9	0.7	9.66	HOLD
IJM PLANTS	3,073.2	3.49	11.8	14.5	29.6	24.1	1.9	1.8	6.0	1.7	2.93	SELL
TH PLANTS	1,157.8	1.31	2.7	6.0	48.5	21.8	0.9	0.9	2.9	0.5	1.21	SELL
TSH RESOURCES	2,833.5	2.09	4.9	9.8	42.7	21.3	2.3	2.1	4.5	0.6	1.95	HOLD
Average					**33.7**	**22.4**	**2.2**	**2.1**	**5.8**	**1.4**		

Notes: FY1 is the current FY estimate

Source: Bloomberg, M&A Securities

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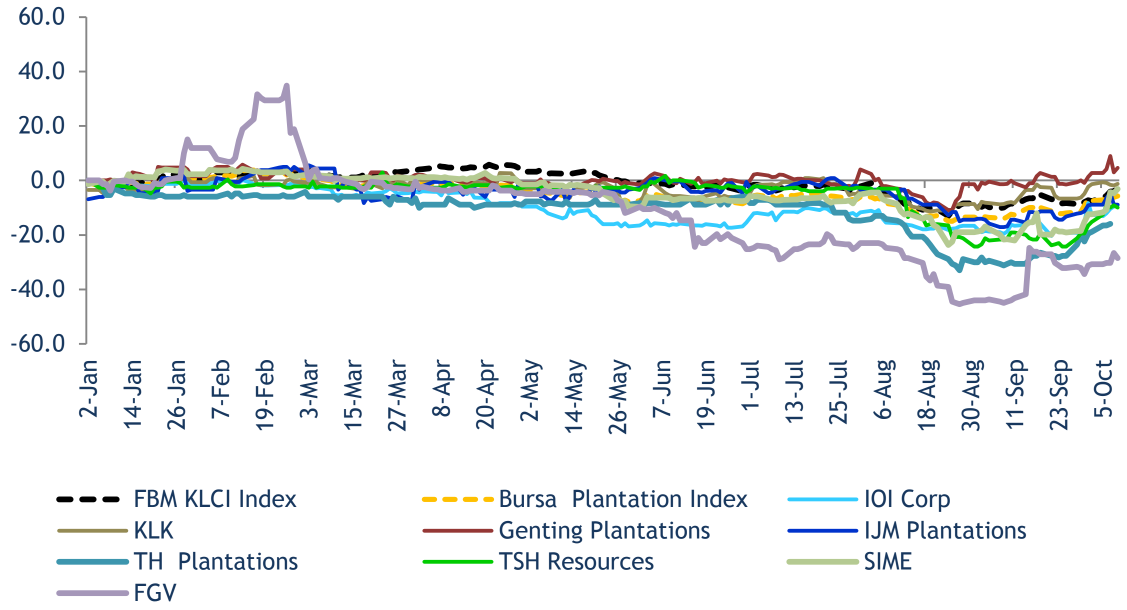
YTD Performance - Plantation Players vs. Bursa Plantation and FBMKLCI Index



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STOCK RECOMMENDATIONS

BUY	*Share price is expected to be ≥+10% over the next 12 months.*
TRADING BUY	*Share price is expected to be ≥+10% within 3-months due to positive news flow.*
HOLD	*Share price is expected to be between -10% and +10% over the next 12 months.*
SELL	*Share price is expected to be ≥-10% over the next 12 months.*

SECTOR RECOMMENDATIONS

OVERWEIGHT	*The sector is expected to outperform the FBM KLCI over the next 12 months.*
NEUTRAL	*The sector is expected to perform in line with the FBM KLCI over the next 12 months.*
UNDERWEIGHT	*The sector is expected to underperform the FBM KLCI over the next 12 months.*

DISCLOSURES AND DISCLAIMER

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