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Wednesday, March 11, 2015

Market Access

"Inventory, Production and Export Level in Focus"

Table 1: Plantation Sector Operational Metrics Projection

	2014	2015F
CPO Price (RM/MT)	2,408	2,300
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 Sector Statistics

	Feb'15	Jan'15	Feb'14	m-o-m	y-o-y	YTD'15	YTD'14	Change
Average CPO Price (RM/MT)	2,265	2,294	2,632	-1%	-14%	2,279	2,580	-12%
CPO Production (Million Tonnes)	1.12	1.16	1.28	-3%	-12%	2.28	2.73	-17%
Palm Oil Export (Million Tonnes)	0.97	1.19	1.35	-18%	-28%	2.16	2.72	-20%
Ending Stocks (Million Tonnes)	1.74	1.77	1.66	-2%	5%	nm	nm	nm

Source: MPOB, M&A Securities

February production remains low. As predicted, the latest data from MPOB shows that palm oil production for the month of February 2015 had dropped at a slower pace of 3.37% m-o-m to 1.12 million tonnes vs. 1.16 million tonnes in January 2015 (y-o-y: -12.09%), 6th straight months of decline as production hit its low production cycle coupled with the lag impact from the dry weather in 2014. FFB yield for Malaysia fell to 1.09 tonnes/ha in February 2015 against 1.16 tonnes/ha in January 2015 and 1.21 tonnes/ha in February 2014 with yield in Sabah and Sarawak falling by a bigger margin (-17.2% QoQ, -17.2% YoY) compared with Peninsular Malaysia (+8.7% MoM, -1.8% YoY).

Stocks pile eased to 1.74 million tonnes. Palm oil stocks decreased by 1.5% m-o-m to 1.74 million tonnes at end February 2015 (+5.2%: y-o-y) in tandem with lower palm oil production and lower palm oil import of 63.5k tonnes from 89.9k tonnes the month before (+669%: y-o-y). Lower stocks and production failed to lift CPO price higher as demand were poor coupled with weaker soy oil prices that consistently put pressure on the CPO price competitiveness. This however should benefit the CPO price in the short term, in our view.

Palm Oil exports falling 18% m-o-m to 971 thousand tonnes. Palm oil export volume in February 2015 tumbled by 18.4% m-o-m to 971 thousand tonnes (-28.1% y-o-y) compared to the previous month of 1.19 million tonnes, the lowest in 8 years for the month of February (Feb'07: 811 thousand tonnes). This was mainly due to lower demand from major importing countries like China

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

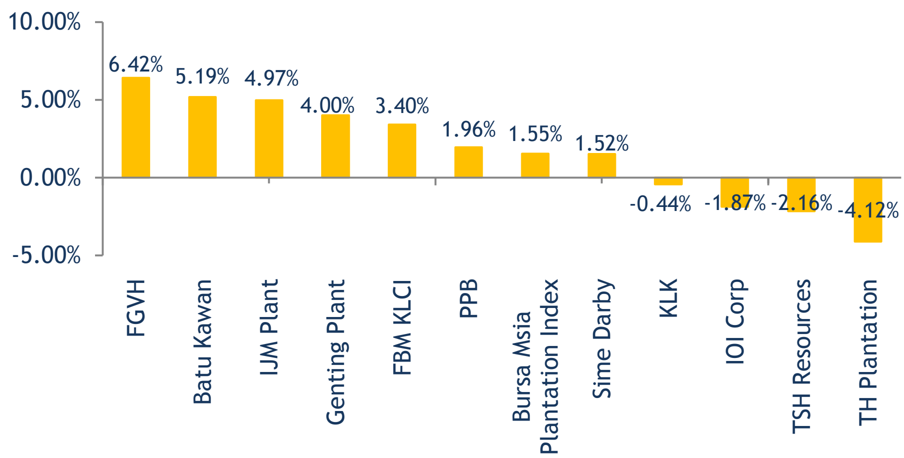
(the most alarming), Pakistan, EU, Vietnam and South Korea coupled with seasonally lower demand for the month of January and February. Demand growth from China had already slowed down considerably in 2014 and the momentum has continued in 2015 as shown in China import data that fell by 19.9% y-o-y in January 2015 due to economic uncertainty (GDP growth 2014: 7.4%; 2015F 7.0%). China import of palm oil has declined by an alarming 70% on m-o-m basis (75% y-o-y), followed by Pakistan that slipped by 40%, EU dropped by 21% and South Korea tanked by 48%. However, many thanks to India which saw an increase in demand or clocking a commendable 38.7% m-o-m growth (20% y-o-y) as we believe they have been done their restocking activities due to deficit in domestic vegetable oil stockpiles. The shortfall has also been negated by burgeoning demand from other countries namely South Africa, Philippines, UAE, Benin and Japan.

Bursa Malaysia Plantation Index Analysis. The plantation sector bellwether index continued to show good performance in 2015. It surged by 1.55% YTD against FBMKLCI that inched up by 3.40%. It ended January 2015 at 8,009.67, 8.6% lower y-o-y. YTD, FGVH share price has again led its peers, surging by 6.4% followed by Batu Kawan at 5.2% and IJM Plant at 5.0%. The worst performer YTD was TH Plant after its share price dipped by 4.1% followed by TSH Resources at 2.2%, IOIC at 1.9% and KLK 0.4%.

Table 3: YTD Share Price Performance (Plantation Sector)

Stock (RM)	Share Price (Feb 2015)	Share Price (Dec 2014)	YTD Gain (%)
SIME Darby	9.33	9.19	1.52%
FGVH	2.32	2.18	6.42%
IOI Corp	4.71	4.80	-1.87%
Genting Plant	10.40	10.00	4.00%
IJM Plant	3.80	3.62	4.97%
KLK	22.70	22.80	-0.44%
PPB	14.58	14.30	1.96%
Batu Kawan	18.24	17.34	5.19%
TSH Resources	2.26	2.31	-2.16%
TH Plantation	1.63	1.70	-4.12%
Bursa M'sia Plantation Index	8,010	7,887	1.55%
FBM KLCI	1,821	1,761	3.40%

Plantation Sector Players YTD Share Price Performance (2015)



Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

4Q2014 Company's result mixed. The 4Q2014 results for companies under our coverage were mixed. Only half registered higher top-line and bottom-line growth (q-o-q) while net earnings for some were lower (y-o-y) affected by margin erosion, injured by low CPO average selling prices and production growth coupled with unrealised fair value loss in foreign currency forward exchange contracts arising from weaker Ringgit during the quarter. On the other hand, those companies that registered positive YTD top-line growth were supported by higher FFB and CPO production growth as more younger plantation areas came into maturity together with more new matured area coming to harvest especially in Sarawak and Indonesia.

Company	Earnings	Remarks
IOI Corporation (IOIC)	Below	Below-than-expected earnings result due to 1) lower contribution from resource-based manufacturing segment – lower margins from oleo-chemicals and refinery sub-segments, and unrealised fair value loss in foreign currency forward contract due to weaker Ringgit; 2) lower average CPO price realised; 3) higher net foreign currency translation loss on foreign currency denominated borrowings; and 4) higher effective tax rate. During the 1H15, FFB and CPO production grew by 4% and 8% y-o-y respectively.
Kuala Lumpur Kepong (KLK)	Below	Disappointing net profit mainly was caused by weaker-than-expected EBIT contribution from both the plantation and manufacturing division, impacted by 1) weaker CPO and rubber selling prices; 2) lower FFB and rubber production; 3) higher production cost of CPO; and 4) negative margins from the downstream business. During the 1Q15, FFB and rubber production shrunk by 6% and 26% q-o-q respectively.
Genting Plantations (GENP)	Above	Higher top-line and bottom-line numbers were driven by 1) better-than-expected contribution from property division mainly due to one-off industrial land sales in Indrapura, Pulai Johor; 2) higher FFB production especially in Indonesia plantation estates; 3) higher biodiesel sales; and 4) lower unrealised exchange losses in USD denominated borrowings of RM8 million as opposed to RM69 million in FY13. In FY14, FFB production grew 9% y-o-y.
IJM Plantations (IJMP)	Within	9M15 results came in within our expectation. Top-line and bottom-line numbers were higher mainly due to 1) higher sales volume especially from the Indonesian operations as a result of increased in FFB and CPO production as more areas turned into maturity; 2) higher sales volumes from the Malaysian operations; and 3) lower unrealised exchange loss due to a lesser adverse impact from the exchange rate movement of Rupiah against the US Dollar. During the 9M15, total FFB and CPO production grew by 30% and 17% y-o-y respectively.

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

TH Plantations (THP)	Below	Despite of the modest increase in revenue in FY14 and marginal increase in CPO average selling price realised, the group registered lower bottom-line figures as margins got squeezed with production cost increased (young estates and younger age profile). In FY14, FFB and CPO production grew by 1% and 3% y-o-y respectively.
TSH Resources (TSH)	Below	Below than expected earnings result were due to 1) lower average CPO price realised in 2H14; 2) operational loss in wood product manufacturing; and 3) higher effective tax rate. Higher revenue and core operating profit in FY14 were due to strong FFB and CPO production supported by higher palm product prices. The better EBIT margin was also attributed to the improvement in unit production cost and operational efficiency. In FY14, FFB and CPO production grew by 18% and 10% y-o-y respectively.

CPO price movement. The 3-month CPO futures price rallied in February 2015 which saw the CPO futures to hit its highest level of RM2,357/MT in 9th February, before it ended the month at RM2,305/MT. Aligned with the derivatives market, MPOB's CPO price for February 2015 shrunk by 1.3% m-o-m to an average of RM2,264.50/MT (-13.9% y-o-y), while MPOB average CPO price YTD was RM2,279.25/MT, slipping by RM301/MT or 11.7% lower against RM2,580.25/MT recorded in the same period last year.

Our view. We maintain our **Neutral** call on the sector despite unconvincing recent earnings results season. Most of the company are facing the same dilemma of lower CPO average selling price realised, slower production, poor downstream margins or higher unrealised forex translation loss arising from weaker Ringgit. To add to the wound, narrower premium of soybean oil price against palm oil price has put pressure on the CPO price competitiveness. Meanwhile, soft crude oil prices may tamper the prospects demand for biodiesel as weaker crude oil prices will make palm oil less attractive and not economically viable particularly as an option for biodiesel feedstock.

Although production are expected to be soft until it enters its seasonally peak seasons in the 2H15 due to seasonal factor as well as lag impact of dry weather in 2014, downside risk of palm product prices are seen to be elevated. Export of palm products are expected to moderate in 2015 as import from major trading partner are likely to be slower judging by the 19.9% drop in China's import figure in January 2015. According to MPOB report, India has overtaken China position as the largest palm oil export market for Malaysia in 2014 with intake of 3.23 million tonnes as against China of 2.84 million tonnes. We maintain our assumption on CPO prices in the range of RM2,100/MT – RM2,500/MT throughout the year and averaging at RM2,300/MT in 2015 for now. We call a HOLD call on Genting Plant (TP: RM10.63), KLK (TP: RM21.50), TSH Resources (TP: RM2.08), and TH Plant (TP: RM1.45) but a SELL call on IJM Plant (TP: RM3.20) and IOI Corp (TP: RM4.04). TSH (Hold: RM2.08) and Genting Plant (Hold: RM10.63) emerge as our top pick benefiting from 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

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

which provides visible revenue and earnings growth catalyst; and 3) operational efficiencies and promising long-term earnings growth potential.

Table 4: Export by Selected Destinations

	Feb'14 ('000 tonnes)	Jan'15 ('000 tonnes)	Feb'15 ('000 tonnes)	Changes (%) YoY	MoM
Total	***1,351.44***	***1,191.26***	***971.64***	***-28.10%***	***-18.44%***
China	257.43	216.25	64.77	-74.84%	-70.05%
India	185.06	160.17	222.16	20.05%	38.70%
Pakistan	98.88	55.51	33.31	-66.32%	-40.01%
Netherlands	87.77	131.42	96.60	10.06%	-26.49%
USA	42.60	64.66	51.28	20.37%	-20.70%
Singapore	32.14	33.28	31.09	-3.27%	-6.60%
Vietnam	34.55	52.72	41.23	19.35%	-21.78%
Iran	11.70	25.67	21.14	80.59%	-17.66%
South Korea	43.27	41.47	21.53	-50.23%	-48.08%
South Africa	10.37	12.38	14.16	36.58%	14.41%
Philippines	31.12	40.46	64.62	107.66%	59.70%
Japan	36.83	41.97	43.70	18.64%	4.11%
UAE	11.25	5.22	6.66	-40.84%	27.56%
EU	151.84	172.27	136.51	-10.10%	-20.76%
Benin	47.85	17.72	23.13	-51.67%	30.47%

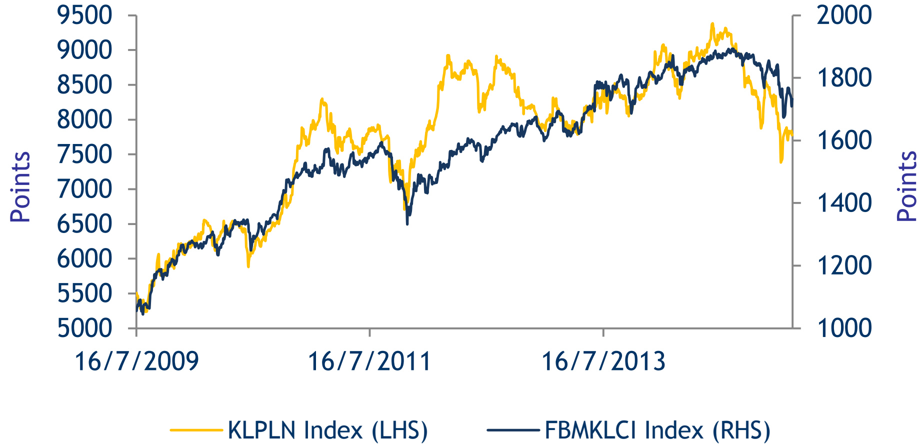
Source: MPOB, M&A Securities

Table 5: YTD Major Export Destinations (Major Customers)

	YTD'14 ('000 tonnes)	YTD'15 ('000 tonnes)	Changes ('000 tonnes)	%
Total	***2,719.40***	***2,162.90***	***-556.5***	***-20.46%***
China	563.32	281.02	-282.31	-50.11%
India	366.98	382.33	15.36	4.18%
EU	353.39	308.78	-44.61	-12.62%

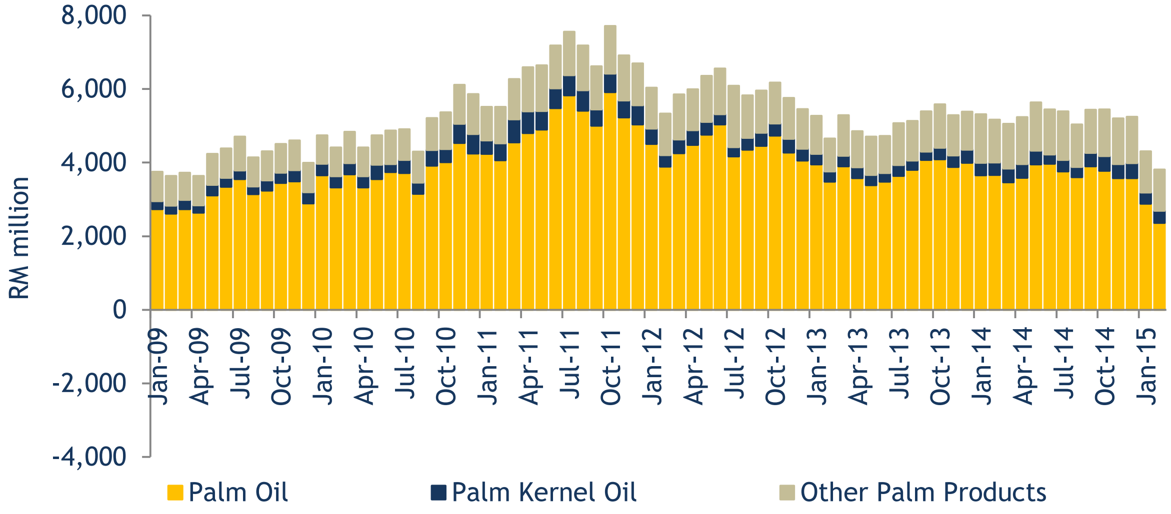
Source: MPOB, M&A Securities

FBM KLCI vs. Bursa Malaysia Plantation Index (June 2009- February 2015)



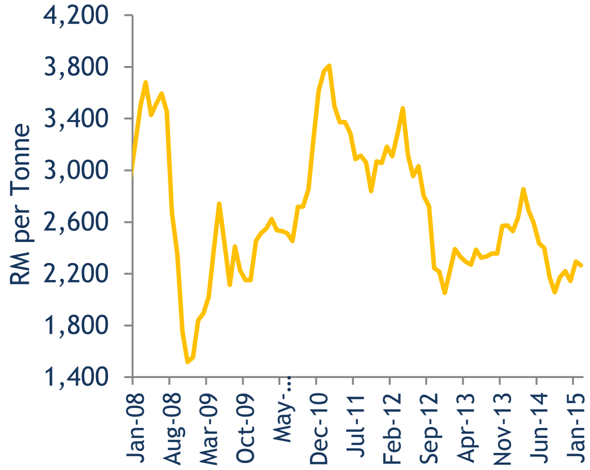
Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

Palm Oil Export Since 2009
(January 2009- February 2015)

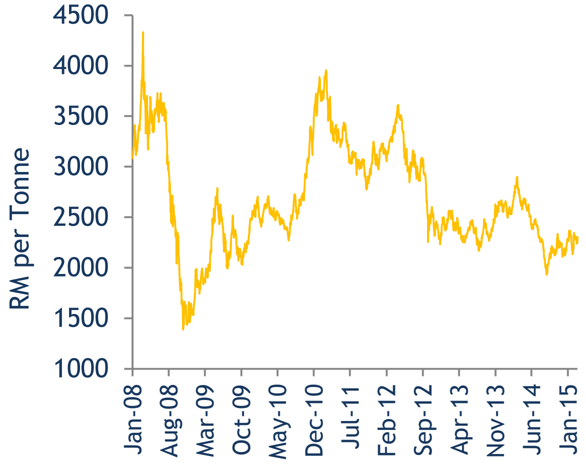


Source: MPOB, M&A Securities

MPOB Monthly Average CPO Price
(January 2008- February 2015)

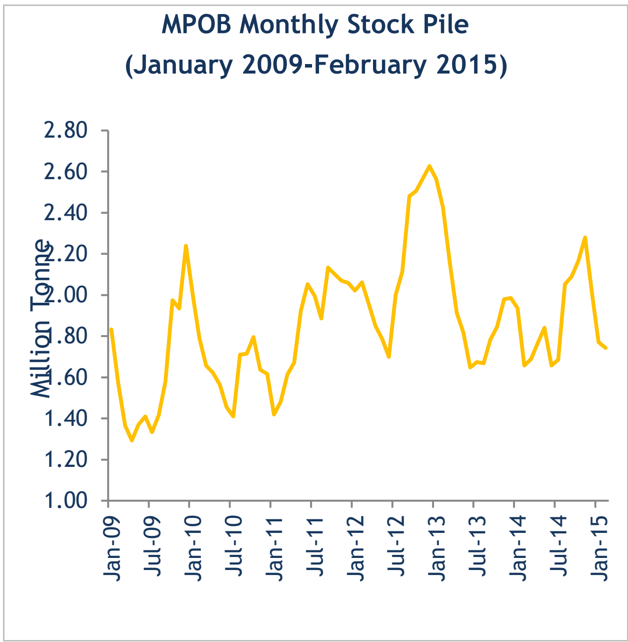


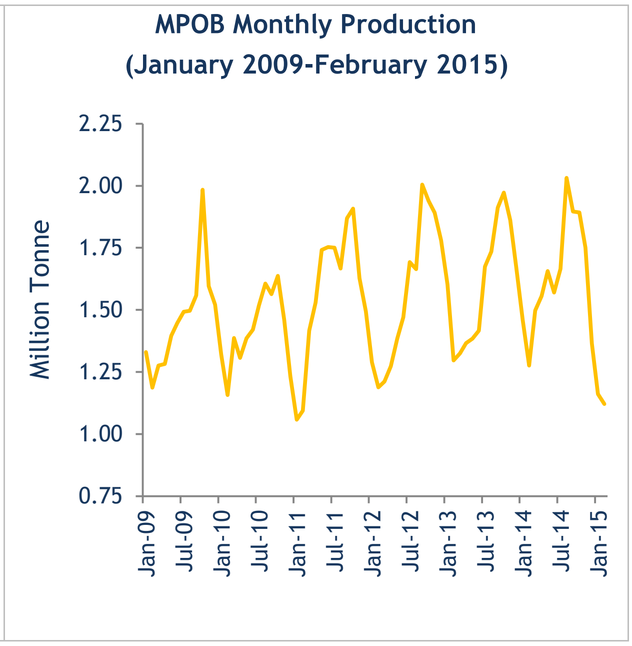
3-mth CPO Futures CPO Price
(January 2008-February 2015)



Source: MPOB, Bloomberg

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277





Source: MPOB, Bloomberg

Table 6: 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	29,201.6	4.59	15.6	22.9	29.4	20.0	3.5	3.4	24.7	0.6	4.04	SELL
KLK	23,663.5	22.22	99.5	110.9	22.3	20.0	2.7	2.6	13.5	2.7	21.50	HOLD
GENPLANTS	7,831.3	10.16	52.3	58.9	19.4	17.2	1.9	1.8	9.7	1.3	10.63	HOLD
IJM PLANTS	3,328.6	3.78	12.5	17.1	30.2	22.1	2.2	2.1	6.4	1.3	3.20	SELL
TH PLANTS	1,414.2	1.60	7.3	9.5	21.9	16.8	1.2	1.1	5.6	1.7	1.45	HOLD
TSH RESOURCES	3,036.9	2.24	10.4	11.6	21.5	19.3	2.9	2.6	7.0	1.2	2.08	HOLD
Average					**24.1**	**19.3**	**2.4**	**2.3**	**11.2**	**1.5**		

Notes: FY1 is the current FY estimate
Source: Bloomberg, M&A Securities

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277

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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.*

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A Participating Organisation of Bursa Malaysia Securities Berhad

Level 1,2,3 No.45-47 & 43-6
The Boulevard, Mid Valley City,
Lingkaran Syed Putra,
59200 Kuala Lumpur
Tel: +603 – 2282 1820 Fax: +603 – 2283 1893
Website: www.mnaonline.com.my

Noorhayati Maamor
research@mna.com.my
03-22821820 ext. 277