

SECTOR UPDATE

Plantation – Regional

Fast And Furious

CPO prices hit a record high of RM7,786/tonne, according to the Malaysia Palm Oil Board. We attribute the huge spike in CPO prices mainly to the Russia-Ukraine war and export backlog in Indonesia due to the DMO. Reflecting on the higher CPO price assumption of RM4,200/tonne in companies' recent results, we upgrade the sector to MARKET WEIGHT. If CPO prices remain high, we advise investors to go for Malaysia's upstream players for the most benefit.

WHAT'S NEW

- **Another record high.** Malaysia CPO price broke its record high consecutively, landing at RM7,786/tonne as of 1 Mar 22, whereas the spot months future price broke above RM8,000/tonne at RM8,163/tonne, making CPO the most expensive vegetable oil in the world. This surge in vegoil prices, especially palm oil, was driven mainly by sudden supply shortage due to:
 - a) Russia-Ukraine geopolitical tension leading to disruption of sunflower oil supplies.** Ukraine and Russia are the largest exporters of sunflower oil (SFO), contributing close to 60% of the world's SFO production. India and China are the largest SFO importers, contributing around 17% and 11% of global SFO exports. Shipments of SFO from Ukraine are now fully on hold, leading to sudden tightening of vegoil supply in India and forcing India to look for alternatives, ie soybean oil from Brazil and CPO from Malaysia. Even if the war stops, sanctions on Russia may not be lifted immediately. It would take some time for the ports to reopen and the next sunflower planting may not be up to the usual pace.
 - b) Palm oil products exports held back at Indonesian ports due to Domestic Market Obligation (DMO).** Indonesia's new rule, which requires exporters to sell one tonne of CPO/Olein domestically at a stipulated price for every five tonnes of palm products exported in order to obtain export permits, has limited the supply to the global market for time being. Shipments are being held back while exporters are finding ways to meet this new requirement which took effect on 1 Feb 22. After two weeks of implementation, the issuance of exports permits is gaining pace but did not meet the usual export volume, which ranges from 2.5m to 3.0m tonnes/month.
- **Upgrade to MARKET WEIGHT.** We upgrade the plantation sector from UNDERWEIGHT to MARKET WEIGHT after our change of CPO price assumption of RM4,200/tonne for 2022 and recent sector earnings upgrade. Upstream players would benefit the most from high CPO price despite dilution from higher fertiliser cost. Our BUYs are BAL SP, TAPG IJ, and HAPL MK. Among the big-cap plantations in Malaysia, we prefer KLK MK with expectation of a stronger production recovery in FY22 to ride on the current high prices. SDPL MK has the largest CPO volume, so its earnings have the highest leverage to rising CPO prices.

PEER COMPARISON

| Company | Ticker | Rec | Price @ 2 Mar 22 | Target Price | Market Cap (US\$m) | PE | | | ROE | P/B | 2022F Div | Div Yield |
|-----------------------|---------|------|---------------------|-----------------|--------------------------|-------------|--------------|--------------|------|-------|--------------|--------------|
| | | | (RM) | (RM) | | 2021 (x) | 2022F (x) | 2023F (x) | (%) | (x) | (sen) | (%) |
| Malaysia | | | | | | | | | | | | |
| Hap Seng Plantations | HAPL MK | BUY | 2.99 | 3.15 | 570 | 10.7 | 10.4 | 21.2 | 12.5 | 1.3 | 17.2 | 5.8 |
| Kim Loong | KIML MK | HOLD | 2.14 | 2.00 | 493 | 10.8 | 10.4 | 18.1 | 12.9 | 2.5 | 15.4 | 7.2 |
| KL Kepong | KLK MK | HOLD | 27.40 | 28.00 | 7,043 | 13.1 | 16.5 | 20.0 | 19.9 | 2.4 | 99.8 | 3.6 |
| IOI Corporation | IOI MK | HOLD | 4.61 | 5.15 | 6,828 | 20.8 | 18.2 | 23.3 | 14.4 | 2.8 | 13.2 | 2.9 |
| Sime Darby Plantation | SDPL MK | HOLD | 5.22 | 5.45 | 8,607 | 15.4 | 16.3 | 34.1 | 13.6 | 2.1 | 9.8 | 1.9 |
| Sarawak Oil Palms | SOP MK | HOLD | 6.48 | 4.60 | 883 | 7.2 | 11.3 | 20.1 | 19.7 | 1.3 | 23 | 3.5 |
| Genting Plantations | GENP MK | SELL | 9.39 | 7.15 | 2,009 | 19.5 | 22.4 | 37.3 | 8.6 | 1.6 | 25.2 | 2.7 |
| Singapore | | | | | | | | | | | | |
| Bumitama Agri | BAL SP | BUY | 0.77 | 0.85 | 983 | 11.7 | 8.6 | 6.4 | 13.2 | 2.1 | 3.7 | 4.8 |
| First Resources | FR SP | BUY | 1.90 | 2.10 | 2,207 | 19.8 | 13.8 | 10.2 | 14.3 | 1.8 | 9.3 | 4.9 |
| Wilmar International | WIL SP | BUY | 4.45 | 5.50 | 20,632 | 12.82 | 10.40 | 11.04 | 9.74 | 1.04 | 16.1 | 3.6 |
| Indonesia | | | | | | | | | | | | |
| Tripura Agro | TAPG IJ | BUY | 820 | 825 | 1,131 | 17.1 | 14.4 | 8.0 | 15.1 | 2.3 | 30.8 | 3.8 |
| Astra Agro Lestari | AALI IJ | HOLD | 12,300 | 11,070 | 1,645 | 28.4 | 8.8 | 11.8 | 10.0 | 1.1 | 463.8 | 3.8 |
| London Sumatra | LSIP IJ | SELL | 1,515 | 1,100 | 718 | 14.8 | 10.0 | 9.6 | 10.2 | 1.0 | 47.1 | 3.1 |
| Tunas Baru Lampung | TBLA IJ | SELL | 835.00 | 670 | 310 | 5.9 | 5.4 | 7.8 | 12.1 | (0.1) | 25.0 | 3.0 |

Source: UOB Kay Hian

MARKET WEIGHT

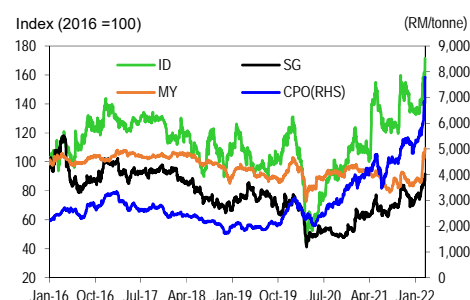
(Upgraded)

CPO PRICE ASSUMPTIONS (RM/TONNE)

| | CPO Price Assumption (RM/tonne) |
|-------|------------------------------------|
| 2022F | 4,200 |
| 2023F | 3,000 |

Source: UOB Kay Hian

PLANTATION INDEX VS CPO PRICE



Source: Bloomberg, UOB Kay Hian

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- Earnings adjustment post results. From the latest results season, most of the plantation companies' earnings came in above our expectations, thanks to the higher-than-expected CPO selling prices. Overall, we raise our Malaysia and Singapore plantation sector earnings forecast by around 26% higher for 2022, and lower our Indonesia plantation sector earnings forecast by around 5% for 2022 due to the dilution impact from DMO.

- Sourcing of labour remains the most challenging issue for Malaysian planters. Based on the briefing updates, the labour shortage situation is unlikely to improve anytime soon. The companies expect an improvement by mid-2Q22 at best and the earliest workers will ready to work at the estates is 3Q22. This is easily 4-6 months behind earlier expectations. Thus, the production recovery from Malaysia will be very marginal.

RISKS

- **Backlog issue and cooking oil shortage issues resolve in Indonesia.** If the backlog issues in Indonesia's ports resolve with the exporters getting export licenses after fulfilling DMO, we expect buyers to turn to Indonesia as Indonesia palm oil products are still at discount compared to those from Malaysia. There is also market talk that the Indonesian government may relook into lowering the percentage of domestic sales from the current 20% once the cooking oil shortage in Indonesia eases.
- **Increase in US soybean planting area.** USDA expects farmers to plant 88m acres of soybeans for 2022, up by 0.8m acres from 87.2m acres in 2021. This may result in higher-than-expected soybean production in the market for 2022 and hence we might see some price weakness in SBO moving forward.
- **Crop losses due to worker shortage.** Based on the recent analyst briefings, we gathered that Malaysia plantation companies have not received any foreign workers up till now due to government-to-government discussions. Companies are only expecting the workers to come in 3Q22, but we reckon that the impact on production recovery would only be in late-22 as companies would still need to train the new workers which would take about 2-3 months.

ACTION

- **Upgrade to MARKET WEIGHT.** We reckon that the current RM7,786/tonne CPO price may not be sustainable. The elevated price is likely to stay longer and higher than expected. This will continue to drive investors' appetite towards plantations stocks which has underperformed for last three years. Our BUYs are BAL SP, TAPG IJ, and HAPL MK.
- We had previously adjusted target prices upwards to reflect the higher CPO price assumption of RM4,200/tonne in our result notes issued during the results season in the last two weeks. In this note, we also increase our target price for Kim Loong (KIML MK) to RM2.00 (previous: RM1.30) to reflect the same increase in CPO price assumption.
- **The beta.** Should the high prices remain for longer periods, pure upstream players would have higher leverage and beta to the CPO uptrend. Among companies under our coverage, SDPL MK, HAPL MK, TAPG IJ and AALI IJ are those with higher earnings sensitivity towards CPO prices.

COMPANIES 2021 RESULT SUMMARY

| | 2021 Core Net Profit | yoy % chg | ---- Net Gearing Ratio ---- | | CPO ASP (USD/tonne) | FFB production ('000 tonnes) | CPO production ('000 tonnes) | FFB growth (%) | CPO growth (%) | FFB yield (tonne/ha) | OER (%) |
|------------------------------|----------------------------|--------------|-----------------------------|-------------|---------------------------|------------------------------------|------------------------------------|----------------------|----------------------|----------------------------|------------|
| | (RMm) | | 2020 (x) | 2021 (x) | | | | | | | |
| Malaysia | | | | | | | | | | | |
| Hap Seng Plantations | 200 | 189.1 | Net cash | Net cash | 1,057 | 593 | 133 | (6.9) | (8.1) | 18.3 | 20.45 |
| Sarawak Oil Palms | 484 | 123.1 | 0.20 | 0.15 | 1,093 | 1,245 | 384 | (8.3) | (1.6) | n.a | n.a |
| IOI Corporation (1HFY22) | 733 | 34.6 | 0.29 | 0.18 | 1,031 | 2,794 | 628 | (10.9) | (10.8) | n.a | n.a |
| Kuala Lumpur Kepong (1QFY22) | 551 | 103.1 | 0.24 | 0.45 | 846 | 4,232 | 1,086 | 7.8 | 2.6 | 21.43 | 21.75 |
| Genting Plantations | 449 | 86.3 | 0.33 | 0.17 | 825 | 2,018 | n.a | (3.2) | n.a | n.a | n.a |
| Sime Darby Plantation | 2,338 | 175.1 | 0.40 | 0.33 | 889 | 9,128 | 2,373 | (1.6) | 0.42 | 18.49 | 21.59 |
| Singapore | | | | | | | | | | | |
| Bumitama Agri | Rp1,677b | 45.9 | 0.50 | 0.33 | 684 | 3,374 | 1,052 | 1.8 | 2.6 | 19.63 | 22.6 |
| First Resources | US\$161.1m | 61.6 | 0.22 | 0.02 | 523 | 3,368 | 869 | 2.9 | 1.6 | 17.2 | 22.7 |
| Indonesia | | | | | | | | | | | |
| Astra Agro | Rp2,504b | 201.4 | 0.24 | 0.09 | 600 | 4,327 | 1,473 | (6.6) | 3.1 | 22.7 | n.a |

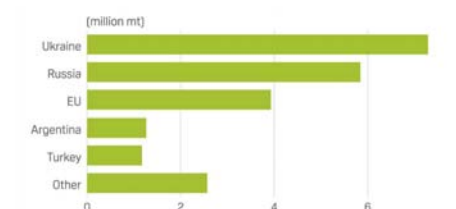
Source: Respective companies, UOB Kay Hian

EARNINGS SENSITIVITY WHEN CPO PRICES (% CHANGE ON EARNINGS)

| (%) change from our current earnings based on CPO price of RM4,200/tonne | RM5,500/tonne | Potential Fair Value |
|--|---------------|----------------------|
| | | (RM) |
| Malaysia | | |
| SDPL MK | 83.1 | 9.98 |
| HAPL MK | 73.3 | 5.46 |
| GENP MK | 68.3 | 12.03 |
| SOP MK | 61.0 | 7.41 |
| KLK MK | 60.7 | 45.00 |
| KIML MK | 42.0 | 2.92 |
| IOI MK | 16.9 | 6.02 |
| Singapore | | (S\$) |
| BAL SP | 33.5 | 1.86 |
| FR SP | 24.4 | 3.95 |
| Indonesia | | (Rp) |
| TAPG IJ | 88.9 | 1,558 |
| AALI IJ | 68.3 | 18,631 |
| LSIP IJ | 54.2 | 1,712 |

Source: UOB Kay Hian

TOP GLOBAL SUNFLOWER OIL PRODUCERS



Source: USDA

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