

SECTOR UPDATE

Plantation – Regional

Flip-flopping On DMO Policy

The Indonesian government announced the demolition of the DMO policy yesterday, along with an increase in the CPO export levy in order to subsidise household unbranded cooking oil. In the past, when Indonesia increased exports levy, CPO prices rose on the excuse that higher prices would compensate for the higher levy. But with the weak demand sentiment now, CPO prices may not see a positive reaction. This would burden Indonesian upstream players as they would need to bear the export levy. **Maintain MARKET WEIGHT.**

WHAT'S NEW

- **The flip-flopping.** The Indonesian government had made a few announcements for the palm oil products in order to secure domestic supplies of domestic cooking oil. The latest changes are as below:
 - On 16 Mar 22, it announced the removal of domestic price obligation (DPO) and only set Rp14,000/litre for household bulk cooking oil. The price difference between the actual market price and price control will be subsidised by funds collected from the export levy.
 - On 17 Mar 22, it announced the demolition of the domestic market obligation (DMO) for palm oil products, meaning that all export volume restrictions on palm oil products will be removed.
 - The CPO export levy was raised, effective 18 Mar 22. The maximum total crude palm oil export duties will be increased to US\$675/tonne (still awaiting final confirmation) from the current US\$375/tonne. The Indonesian government had also added a new bracket for CPO prices of between US\$1,000-1,500/tonne.
 - Allocation of Rp7.28t from CPO fund to subsidise bulk and unbranded cooking oil. Each month, about 202m litres of cooking oil will be subsidised for six months to keep prices at or below Rp14,000/litre.

COMMENTS

- **Weakness in CPO prices.** By removing the DMO for palm products, we reckon that this would allow for more global palm oil supply which may soften the international CPO pricing. Indonesia's palm oil exports account for about 65% of its total palm oil production, whereas the domestic consumption for food products only contribute about 15% of its total palm oil production. We reckon that the shortage of cooking oil in Indonesia was mainly due to the pricing and marketing strategy taken by the cooking oil producers as most of the cooking oil producers and refiners are suffering with thin or negative operating margin.
- **Impact from higher CPO levy.** The Indonesian upstream players would suffer the most impact as they are the ones who bear the export tax and levy. With the export levy structure being effective from 18 Mar 22, the Indonesia's CPO reference price for Mar 22 is at US\$1,432/tonne, and the CPO export levy and duty will increase from US\$375/tonne to US\$535/tonne. Based on our estimation, the CPO reference price for Apr 22 will be closer at US\$1,700/tonne or higher and hence the maximum duty and levy will be US\$575/tonne.

PEER COMPARISON

Company	Ticker	Rec	Price @	Target	Market Cap (US\$m)	PE			ROE (%)	P/B (x)	2022F Div (sen)	Div Yield (%)
			17 Mar 22 (RM)	Price (RM)		2021 (x)	2022F (x)	2023F (x)				
Malaysia												
Hap Seng Plantations	HAPL MK	BUY	2.40	3.15	457	8.57	8.36	17.02	12.45	1.02	17.20	7.17
Kim Loong	KIML MK	HOLD	1.78	2.00	410	8.99	8.68	15.08	12.92	2.11	15.40	8.65
KL Kepong	KLK MK	HOLD	25.00	30.00	6,423	11.94	15.02	18.25	19.90	2.18	99.80	3.99
IOI Corporation	IOI MK	HOLD	4.14	5.15	6,130	18.65	16.36	20.91	14.45	2.50	13.20	3.19
Sime Darby Plantation	SDPL MK	HOLD	4.90	5.45	8,076	14.41	15.31	32.03	13.55	1.94	9.80	2.00
Sarawak Oil Palms	SOP MK	HOLD	5.36	4.60	732	5.99	9.32	16.59	19.73	1.09	23.00	4.29
Genting Plantations	GENP MK	SELL	8.55	7.15	1,828	17.75	20.39	33.98	8.59	1.49	25.20	2.95
Singapore												
Bumilama Agri	BAL SP	BUY	0.75	0.85	960	11.42	8.41	6.24	17.82	1.83	3.70	4.93
First Resources	FR SP	BUY	1.98	2.10	2,304	20.63	14.35	10.59	14.25	1.92	9.30	4.70
Wilmar International	WIL SP	BUY	4.61	5.50	21,420	13.29	10.77	11.44	9.74	1.07	16.10	3.49
Indonesia												
Triputra Agro	TAPG IJ	BUY	795	860	1,104	16.56	13.92	7.73	15.12	2.24	30.80	3.87
Astra Agro Lestari	AALI IJ	HOLD	12,150	11,070	1,635	28.07	8.65	11.63	10.01	1.13	463.79	3.82
London Sumatra	LSIP IJ	SELL	1,370	1,100	654	13.42	9.03	8.72	10.19	0.92	47.12	3.44
Tunas Baru Lampung	TBLA IJ	SELL	805	670	301	5.73	5.20	7.49	12.07	(0.05)	25.00	3.11

Source: UOB Kay Hian

MARKET WEIGHT

(Maintained)

TOP PICKS

	Price (Icl Crcny)	Target Price (Icl Crcny)
HAPL MK	2.40	3.15
BAL SP	0.75	0.85
FR SP	1.98	2.10
TAPG IJ	795	860

Source: UOB Kay Hian

CPO PRICE ASSUMPTIONS (RM/TONNE)

	CPO Price Assumption (RM/tonne)
2022F	5,200
2023F	4,000

Source: UOB Kay Hian

INDONESIAN PALM OIL MARKET AT A GLANCE

('000 tonnes)	2021	2022F
Open Stock	4,867	4,129
Production	51,300	52,656
CPO	46,888	48,035
CPKO	4,412	4,561
Imports	59	60
Domestic Use	18,422	19,971
Food	8,954	8,991
Oleo	2,126	2,163
Biodiesel	7,342	8,817
Exports	33,674	29,809
CPO	2,482	913
Refined PO	25,481	23,596
Lauric Oil	1,510	1,290
Biodiesel	167	63
Oleo	4,036	3,947
Ending Stock	4,129	7,007

Source: GAPKI

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ACTION

- **Maintain MARKET WEIGHT.** Even though we reckon that we might see some weakness in CPO prices, thanks to the U-turn policy by the Indonesian government on DMO and the hike in CPO export levy, we reckon that CPO prices are unlikely to see a sharp correction in 1H22 in view of the global vegetable oil tightness.
- We reckon that the pure upstream Indonesian players would get impacted the most from Indonesia's changes on DMO and the export levy structure. Companies under our coverage would be Bumitama, London Sumatra and Triputra Agro.
- Integrated companies with Indonesia exposure under our coverage, First Resources, Astra Agro Lestari, Kuala Lumpur Kepong, Genting Plantations, Sime Darby Plantations and IOI Corporations will also be affected with lower upstream margin. Downstream margin would remain stable, where the export levy on refined products is still lower than CPO.
- We had provided the companies' exposure in Indonesia (refer to right column) and the scenario studies of the impact on companies' earnings and net CPO ASP after implementing the changes on the export levy structure based on the percentage of companies' exposure in Indonesia (refer to below).

SECTOR CATALYSTS

- **Increase in US soybean planting area.** The US Department of Agriculture 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 soybean oil moving forward.
- **Prolonged Russia-Ukraine war** could further tighten the global oilseed and vegoil supplies and this would prolong the upcycle in vegoil prices. Ukraine and Russia are entering the critical month of sunflower planting which should start in April, and the prolonged war could hamper the coming planting season. Ukraine's and Russia's sunflower oil exports account for 10% of global vegoil exports.

POTENTIAL IMPACT OF LEVY ON COMPANIES' NET CPO ASP

CPO Price based on Bursa Malaysia		COMPANIES NET CPO ASP BASED ON GEOGRAPHICAL EXPOSURE									
(RM/tonne)	(US\$/tonne)	100% Malaysia (MY)	100% Indonesia (ID)			50% MY : 50% ID			30% MY : 70% ID		
			Before (US\$/tonne)	After (US\$/tonne)	% Change	Before (US\$/tonne)	After (US\$/tonne)	% Change	Before (US\$/tonne)	After (US\$/tonne)	% Change
4,200	1,005	924	739	739	0.0	832	832	0.0	869	869	0.0
5,000	1,196	1,100	855	795	(7.0)	978	948	(3.1)	1,027	1,009	(1.8)
5,500	1,316	1,211	941	821	(12.8)	1,076	1,016	(5.6)	1,130	1,094	(3.2)
6,000	1,435	1,321	1,060	900	(15.1)	1,190	1,110	(6.7)	1,243	1,195	(3.9)
7,000	1,675	1,541	1,300	1,100	(15.4)	1,420	1,320	(7.0)	1,468	1,408	(4.1)

Source: UOB Kay Hian

SCENARIO STUDY: IMPACT OF THE CHANGE IN EXPORTS LEVY ON OPERATING PROFIT

		Before changes in export levy				After change in export levy		
		Planter A	Planter B	Planter C	Planter D	Planter B	Planter C	Planter D
CPO production	tonnes	60,000	60,000	60,000	60,000	60,000	60,000	60,000
- Malaysia exposure	(%)	100	0	50	70	0	50	70
- Indonesia exposure	(%)	0	100	50	30	100	50	30
Based on CPO ASP Assumption of RM4,200/mt or US\$1,005/mt								
Operating Profit	(RMm)	114.6	71.0	92.8	101.5	56.2	85.4	97.1
Changes in earnings	(%)					(20.79)	(7.95)	(4.36)
Based on CPO ASP Assumption of RM5,500/mt or US\$1,211/mt								
Operating Profit	(RMm)	192.6	117.8	155.2	170.1	83.3	137.9	159.8
Changes in earnings	(%)					(29.25)	(11.10)	(6.1)

Source: UOB Kay Hian

MALAYSIAN COMPANIES WITH INDONESIA EXPOSURE

% of operation	Upstream	Downstream
Kuala Lumpur Kepong	60	5
Genting Plantations	55	Nil
Sime Darby Plantations	27	20
IOI Corporations	12	Nil

Source: Companies' reports

NEW INDONESIA EXPORT LEVY STRUCTURE

CPO Reference Price (US\$/tonne)	CPO		RBDPO		Olein	
	Levy	Duty	Levy	Duty	Levy	Duty
0-750	55	0	38	0	35	0
751-800	75	3	54	0	51	0
801-850	95	18	70	0	67	0
851-900	115	33	86	2	83	0
901-950	135	52	102	12	99	5
950-1,000	155	74	118	26	115	17
1,001-1,050	175	93	134	40	131	40
1,051-1,100	195	116	150	56	147	44
1,101-1,150	215	144	166	70	163	57
1,151-1,200	235	183	182	100	179	81
1,201-1,250	255	200	198	117	195	92
1,251-1,300	275	200	214	117	211	92
1,301-1,350	295	200	230	117	227	92
1,351-1,400	315	200	246	117	243	92
1,401-1,450	335	200	262	117	259	92
1,451-1,500	355	200	278	117	275	92
> 1,500	375	200	294	117	291	92

Source: MoF, Indonesia

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