

SECTOR UPDATE

Plantation – Singapore

What Goes Up Must Come Down

CPO prices have corrected 28% since Indonesia announced the lifting of the export ban. After this CPO price correction, we are seeing some positives emerge to prevent further price deterioration: a) it is commercially viable to increase biodiesel mandate or non-mandatory biodiesel blending, and b) demand recovery is in sight in India and China. But Indonesia's palm oil industry has clearly not benefitted from the high CPO prices over the last six months. Maintain MARKET WEIGHT.

WHAT'S NEW

- **Sharp CPO price correction came earlier than expected.** CPO prices corrected 28% since Indonesia lifted the exports ban. CPO 3-month futures hit a low of RM4,493/tonne yesterday. The sharp correction came earlier than expected. We attribute the sell-down on CPO to: a) the expectation of more exports from Indonesia (which we are yet to see happen) to reduce the high stocks domestically, b) rising recession risk also triggers the fear that demand may weaken further, and c) crops production output in Ukraine and Russia are better than expected. In addition, the sell-down on CPO futures also may be due to the concern of liquidity withdrawal as the Fed tightened the monetary policy.
- **Indonesia's CPO prices corrected more sharply.** Indonesia's domestic CPO net selling prices are estimated to have weakened by 35% since the exports ban was lifted on 23 May 22. This correction is slightly sharper than Malaysia's spot and future prices which declined by 21% and 28% for the same period of time. We attribute this to the oversupply of palm oil domestically in Indonesia as the export is not fast enough to ease the high inventory pressure. Lower ASP and higher taxes have depressed the profit margin for Indonesian-based plantation companies especially the upstream players.
- **Wilmar's food product margins should recover in 2H22 with the correction in feedstock prices.** Wilmar's weak 1Q22 performance was partly affected by the margins compression for its food products due to high feedstock prices despite selling price adjustments. The recent 20-30% agri-commodity price correction should be a big relief to this division and should show good improvement in 2H22. On top of that, China's soybean crushing and soymeal sales have improved in tandem with the recovery in pig farming margin. The recovery in these two segments will be partly offset by the weaker earnings contributions from its upstream. Although the upstream earnings may not be as good as 1H22, it is still much better as compared with 2019 and 2020.

ACTION

- **Maintain MARKET WEIGHT.** CPO prices have weakened as expected and this has a larger negative impact to Indonesian-based plantation companies due to the significantly higher taxes imposed vs its Malaysian peers. In addition, the frequent changes in Indonesia's palm oil policies have significantly affected sales as well. This may have caused low investor interest given the uncertainties in the sector as well as companies' potentially disappointing earnings.
- **Adjusted our valuation.** We have rolled over our valuation to 2023 to better reflect the CPO price downtrend; we expect a lower average CPO price of RM4,000/tonne for 2023 vs RM5,200/tonne for 2022. With this, we have downgraded Bumitama Agri to HOLD with a lower target price of S\$0.65, while maintaining HOLD for First Resources at a lower target price at S\$1.70. We pegged both of the valuation at -2SD from its five-year mean. For Wilmar, we maintain BUY with a target price of S\$5.50 after rolling over our valuation to 2023 and factoring in a lower PE (from 12x to 10x) for its non-China operation while maintaining 26x valuation for the China operation.

PEER COMPARISON

Company	Ticker	Rec	Price @ 22 Jun 22	Target Price	Market Cap (US\$m)	PE			ROE (%)	P/B (x)	2022F Div (cent)	Div Yield (%)
			(\$)	(\$)		2021 (x)	2022F (x)	2023F (x)				
Singapore												
Bumitama Agri	BAL SP	HOLD	0.67	0.65	836	10.2	7.5	5.6	17.8	1.7	3.7	5.5
First Resources	FR SP	HOLD	1.84	1.70	2,089	19.2	13.3	9.8	14.3	1.7	9.3	5.1
Wilmar International	WIL SP	BUY	4.02	5.50	18,152	11.6	9.4	10.0	9.7	0.9	16.1	4.0

Source: UOB Kay Hian

MARKET WEIGHT

(Maintained)

STOCK PICKS

Company	Rec	Share Price	Target Price
Wilmar International	BUY	4.02	5.50

Source: UOB Kay Hian

CPO PRICE ASSUMPTIONS (RM/TONNE)

CPO Price (RM/tonne)	
2020	2,686
2021	4,408
Our forecast:	
2022F	5,200
2023F	4,000
CPO Price:	
MPOB @ 21 June 22	5,233
BMD 3rd Month Contract	4,563

Source: UOB Kay Hian

INDONESIA'S DOMESTIC CPO NET PRICE DIPPED BELOW DPO PRICE



Source: University Bengkulu

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ESSENTIALS

• **Supportive factors are emerging.** We reckon the current price range is more reflective of fundamental factors, which is a reflection of the easing of supply tightness. CPO prices should be stabilising as current prices induce demand from the biodiesel segment, China and India.

- Potentially more demand from biofuel segment.** Palm oil-gasoil (POGO) prices spread is turning negative, which means it is commercially viable to start non-mandated biodiesel blending. This is also encouraging amid the fuel shortage due to Black Sea Tensions. Just a week ago, Argentina has raised the biodiesel blending mandate on the backdrop of supply scarcity together with high diesel prices.
- Demand recovery is seen in China** after the palm olein price premium to soybean oil narrowed significantly. The price premium has dropped from around Rmb4,000/tonne in late-April to around Rmb1,900/tonne currently. After the sharp price decline, demand for palm olein in China has been improving over the past weeks. China's palm oil inventory is at its historical low of 203,300 tonnes as at 17 Jun 22 vs the usual level of 400,000-600,000 tonnes. If the demand recovery sustains, China may need to increase the import of palm oil to meet the demand.
- India may increase palm oil imports as margins turn positive.** The positive import margins should encourage higher palm oil imports by India. This price correction comes at a time when India usually increases import of vegoil to meet the high festive demand. Similar to the situation in China, palm oil inventory in India was also at a low level of 240,865 as at end-Apr 22 vs its usual 600,000-700,000 tonnes of inventory. Negative import margin has stopped India from importing palm oil.

ASSUMPTION CHANGES

- **CPO ASP assumptions.** We maintain our CPO price assumptions at RM5,200/tonne and RM4,000/tonne for 2022-23 respectively.

SECTOR CATALYSTS

- Higher-than-expected US green diesel demand.
- Stronger-than-expected commodity cycle.

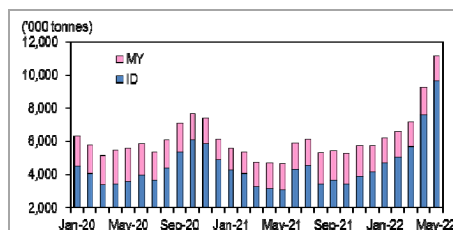
REVISED RECOMMENDATION AND TARGET PRICES

	Recommendation		Target Price	
	Revise	Previous	Revise	Previous
Bumitama Agri	HOLD	BUY	0.65	0.96
First Resources	HOLD	HOLD	1.70	2.30
Wilmar International	BUY	BUY	5.50	5.50

Source: UOB Kay Hian

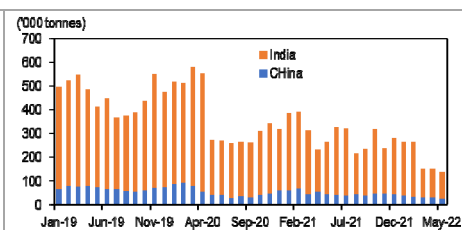
HIGH PALM OIL INVENTORIES AT PRODUCING COUNTRIES WHILE RECORD LOW AT TWO MAJOR CONSUMING COUNTRIES

PALM OIL INVENTORIES IN INDONESIA AND MALAYSIA



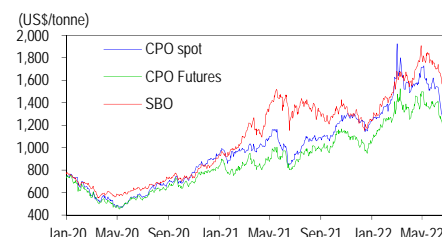
Source: MPOB, GAPKI

PALM OIL INVENTORY IN INDIA AND CHINA



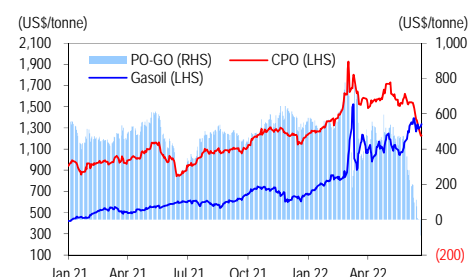
Source: SEA, EPANSUN

CORRECTION IN AGRI COMMODITY PRICES



Source: Bloomberg

BETTER POGO SPREAD COULD SEE NON-MANDATORY BIODIESEL BLENDING



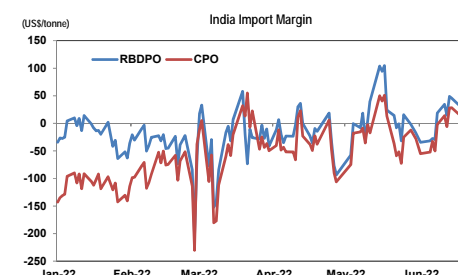
Source: Bloomberg

PALM OIL PRICE PREMIUM TO SBO IN CHINA NARROWED SIGNIFICANTLY (RMB/TONNE)



Source: Bloomberg

BETTER IMPORT MARGIN IN INDIA



Source: Bloomberg

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