

## Plantation sector

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### Rising supply will be a concern

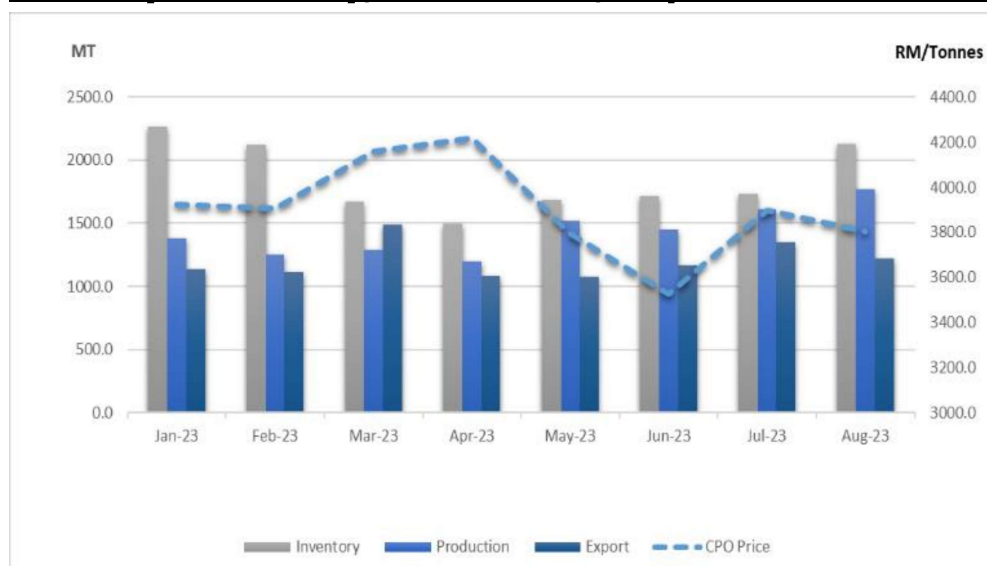
- Review.** CPO production demonstrated favourable increase of +6.1% QoQ (2Q23: 4.2m tonnes compared to 1Q23: 3.9m tonnes). We attribute the better production as a result of improvement in labour shortages. Looking ahead, we anticipate a stronger growth in CPO production, with projected +24.0% QoQ increase in 3Q23. The projection is based on the comparatively lower base production figures in 2Q23, coupled with expectation of seasonally stronger yields in the upcoming quarters.
- Exports in palm oil recorded decline of -11.0% QoQ to 4.2m tonnes 2Q23. We believe the slowdown was primarily dragged down by sluggish demand from China and India, attributed to inflationary pressures and economic uncertainties. Additionally, the less competitive pricing of palm oil compared to other vegetable oils also attributed to the weakness. During the period of April to May 2023, soybean oil premium against palm oil reached an all-time low, averaging around USD 257/tonne. Nonetheless, we expect exports to experience robust growth (+19% QoQ) in 3Q23 due to festive seasons in late-September to October 2023.
- Palm oil inventory experienced a notable -19.1% QoQ decline in 2Q23, reaching a total of 4.9m tonnes after production plunged in April 2023. Moving forward, we anticipate increase in palm oil inventory (+24.7% QoQ), notching 6.1m tonnes in 3Q23 in line with the higher production.

### Soybean Oil vs Palm Oil Price Spread (USD/tonne)



Source: Bloomberg, Apex Securities

### Monthly Inventory, Production, Export and CPO Price)



Source: MPOB, Apex Securities

- **Outlook.** Average CPO price maintained its downward trajectory, from RM3,996/tonne in the 1Q23 to RM3,846/tonne in 2Q23. Overall, we believe the slight drop in CPO price was attributed to expectation of higher production outweighing the strengthened soybean price and export growth expectation. Our full-year 2023 forecast for CPO price were unchanged at RM3,800/tonnes in anticipation of additional supply that impacts the market in 2H23.
- **Valuation & Recommendation.** We maintain our **Neutral** view on the sector for remainder of 2023 as we expect recovery of FFB production will offset by softening CPO price coupled with accumulating inventory level. For stocks under our coverage, we retain **HOLD** recommendations for **Kuala Lumpur Kepong Bhd (FV: RM 19.20)**, **Hap Seng Plantations Holdings Bhd (FV: RM1.80)** and a **SELL** call for **Sarawak Plantations Bhd (FV:1.80)**. We keep our **BUY** call on **United Plantation Bhd (FV: RM17.40)** due to its inexpensive valuation and high dividend yield prospects. The Plantation sector is trading at forward PERs of 20.8x/16.8x for 2023F/2024F and is currently close to its historical 3-year average of 17.1x; implying the sector has been fairly valued at the moment.
- **Key Risk.** Unpredictable weather patterns affect FFB production, lower tax rate and import duties of Indonesia threatens local CPO demand, shortage of labour and rising operational cost.
- **Summary.** Over the near-term, the plantation sector will remain under pressure, due to geopolitical uncertainty as well as rising supply. Nonetheless, we believe uptick in CPO price are in the cards in 2024, due to the potential implication from El-Nino phenomenon on production and hence, we deemed the plantation sector to be attractive for a longer-term investment horizon. We continue to favour plantation stocks with solid fundamentals with decent yields.

### Top Picks

Company	Price (RM)		P/E (x)			Dividend Yield (%)	Target Price (RM)	Potential Upside / Downside
	as at 29Sep23	2022	2023F	2024F				
United Plantation Bhd	16.64	10.10	14.37	14.31	5.91	17.40	4.57%	
Kuala Lumpur Kepong Bhd#	21.4	19.54	18.00	18.63	4.71	19.20	-10.28%	
Hap Seng Plantations Bhd	1.88	20.00	14.32	14.32	4.91	1.80	-4.26%	
Sarawak Plantations Bhd	2.09	11.24	10.83	9.61	3.69	1.80	-13.88%	

# Kuala Lumpur Kepong Bhd data based on FYE Sep

Source: Apex Securities Bhd, Bloomberg