

SECTOR UPDATE

Plantation – Malaysia

Palm Oil Prices Taking The Lead On Supply Tightness

Palm oil prices at most destination markets have surpassed those of the other three major vegoils (SBO, RSO, SFO) for the first time due to short-term supply tightness. Price movements thus far have been within our expected range. Prices of palm by-products such as palm stearin and palm kernel oil have also strengthened along with higher cocoa prices. CPO prices may weaken, but should remain elevated. Maintain OVERWEIGHT. Top picks: IOI Corporation and Hap Seng Plantations.

WHAT'S NEW

- **CPO prices are the highest among vegoils at the moment.** Palm oil is now the one of the most expensive vegoils at most destination markets, with palm oil prices having surpassed that of the three other major vegoils – soybean oil (SBO), sunflower oil (SFO) and rapeseed oil (RSO). CPO 3<sup>rd</sup> month future price closed at RM4,579/tonne, the highest since 2022. We attribute this to:
  - Buyers are panicking due to a lack of CPO in the market now.** Importers have been holding back from buying in anticipation of weaker palm oil prices in view of the stiff competition from larger production of soybean and dumping of sunflower oil from Black Sea. Palm oil prices did not weaken, but are instead the vegoil price leader in a recent uptrend. This caught the market by surprise and led to panic buying from India as well as Europe rushing to replenish its inventory as well. Thus, low production and high demand have been supporting the current price rally.
  - The market has realised that palm oil production may not recover as expected.** Erratic weather for the past 18 months has continued to stress oil palm trees, especially older age trees. Also, Sabah - the largest palm oil-producing state - is now on high alert for a pest outbreak (sooty mould and mealybug), which has led to declining FFB yields.
  - Indonesia is busy meeting domestic demand, and does not have much spare supply for the global market.** Recently, the Indonesian government has voiced its concerns on low realisation rate of domestic market obligation (DMO) and the controlled increases in cooking oil prices in regions with low supplies. As Lebaran is just around the corner, we notice that Indonesian companies are busy supplying to domestic market after the government raised its concern. Thus, this implies less palm oil for exports, and buyers have to buy from Malaysia. Malaysia palm oil inventory is likely to trend down further in March and April, which is supportive to CPO prices.
- **Skyrocketing cocoa prices to benefit palm oil?** Cocoa prices have skyrocketed lately, reaching its historical high of US\$9,949/tonne, up 135% ytd, due to the supply shortage caused by the volatile weather and inefficient labour. We reckon this may indirectly benefit some of the specialty fats producers; note that palm oil-based cocoa butter is one of the closest alternatives to cocoa butter. Among the Malaysia companies under our coverage, IOI Corporation is one of the major suppliers via its 20%-owned associate Bunge Lodens Croklaan (~4% of FY23 PBT).
- We still expect CPO prices to remain supportive in the short term and we reckon that there are some opportunities for the plantation sector, especially for pure upstream players with good production growth. Our top pick for the sector remains IOI Corporation as it benefits from its strong upstream performance and would see a more stable downstream margin vs its peers. We also like companies with strong dividend yield of 5-8%, such as Hap Seng Plantation and Kim Loong Resources.

PEER COMPARISON

Company	Ticker	Rec	Price @ 3 APR 24	Target Price	Market Cap (US\$m)	PE			ROE (%)	P/B (x)	2024F Div	Div Yield (%)
						2023 (x)	2024F (x)	2025F (x)				
			(RM)	(RM)							(sen)	
Malaysia												
Genting Plantations	GENP MK	BUY	6.11	6.65	1,153	17.63	17.63	15.62	4.81	1.03	17.09	2.80
Hap Seng Plantations	HAPL MK	BUY	1.84	2.25	309	7.00	16.10	9.34	4.71	0.75	11.83	6.43
IOI Corporation	IOI MK	BUY	3.97	4.80	5,178	15.57	14.94	14.04	10.00	2.13	14.71	3.70
KL Kepong	KLK MK	BUY	22.78	24.80	5,251	11.35	15.61	14.92	5.83	1.74	76.30	3.35
Kim Loong	KIML MK	HOLD	2.19	1.95	449	11.59	13.02	12.01	17.38	2.46	15.50	7.08
Sime Darby Plantation	SDPL MK	HOLD	4.35	4.15	6,325	14.48	36.88	18.00	9.64	1.51	14.50	3.33
Sarawak Oil Palms	SOP MK	HOLD	3.07	3.00	575	5.69	9.10	7.12	8.83	0.78	8.62	2.81

Source: UOB Kay Hian

OVERWEIGHT

(Maintained)

STOCK PICKS

Company	Rec	Share Price (RM)	Target Price (RM)
Genting Plantations	BUY	6.11	6.65
Hap Seng Plantations	BUY	1.84	2.25
IOI Corporation	BUY	3.97	4.80
KL Kepong	BUY	22.78	24.80

Source: UOB Kay Hian

CPO PRICE ASSUMPTIONS (RM/TONNE)

	CPO Price (RM/tonne)
2020	2,686
2021	4,408
2022	5,088
2023	3,810

Our forecast:

2024F	4,200
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CPO Price:

MPOB @ 2 Apr 24	4,387
BMD 3 <sup>rd</sup> Month Contract	4,579

Source: UOB Kay Hian

WHAT IS COCOA BUTTER EQUIVALENT (CBE)

- CBE is derived from palm oil and typically contains one or more exotic vegetable fats, i.e., shea, illipe, kokum, and sal butter. These fat components are carefully selected to resemble the triacylglycerol composition of cocoa butter.

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ESSENTIALS

- **Key highlights from our recent meetings and conference in China.** Note that despite the overall subdued demand for palm oil in China due to the prevailing macroeconomic conditions and the abundance of alternative vegetable oils in the market, there are enduring preferences for palm oil in the market. This demand is not easily supplanted by other vegetable oils due to the unique characteristics of palm oil, such as its higher boiling point which makes it more suitable for frying and cooking applications where high temperatures are involved. Additionally, palm oil's natural composition makes it highly versatile in various food processing and industrial applications that are not easily replicated by other oils. It is estimated that about 200,000 tonnes of monthly demand for palm oil monthly in China (equivalent to 4.8m tonnes p.a., accounting about 6% of global palm oil consumption) fall under this category of non-substitutable demand.
- **How are other vegoils/crops doing?**
  - a) **Soybean.** All eyes are now on soybean production from South America, given the anticipated record-high soybean production in 2024. Based on our channel checks, some market players are expecting soybean production to be higher at about 160m tonnes, which is higher than Brazilian Association of Vegetable Oil Industries and US Department of Agriculture expectations of 153m-155m tonnes. During the recent China Global Oils and Oilseeds summit, some speakers expect to see better soybean meal demand in 2H24, driven by higher hog breeding.
  - b) **Sunflower oil.** We understand that there is still ample cheap sunflower oil supply to China and India coming from Russia.

ACTION

- The KLCI Plantation Index has risen by a modest 5% ytd, in contrast to the notable 20% rally in CPO prices. This disconnect can be attributed to lingering earnings uncertainties, particularly within integrated plantation firms. The downstream operations of these companies face challenges in maintaining healthy margins amidst elevated feedstock prices. Additionally, investor sentiment appears to display signs of fatigue, as evidenced by the disparity between plantation company performance and the robust trajectory of CPO prices in recent years. This trend is further compounded by a shift in investment focus towards other burgeoning sectors.
- We still expect CPO prices to remain supportive in the short term and maintain our OVERWEIGHT recommendation. We still see some opportunities for the plantation sector, especially for pure upstream players with good production growth. Our top pick for the sector remains IOI Corporation as it benefits from its strong upstream performance, and its downstream margin will remain stable vs its peers. We also like companies with strong dividend yields of 5-8% such as Hap Seng Plantation and Kim Loong Resources.

SECTOR CATALYSTS

- **Never-ending weather risk with La Nina expected.** Although El Nino will impact 2024, the market is now also looking at the potential of La Nina happening in 2H24 which may disrupt vegoil supply in the 2024/25 season. If a strong La Nina happens in 2H24, this would bring dryness/drought and affect the soybean supply in Argentina, Southern Brazil and Midwest US.

ASSUMPTION CHANGES

- **No changes to CPO ASP assumptions.** We maintain our CPO price assumption at RM4,200/tonne for 2024.

OUTBREAK OF SOOTY MOULD AND MEALYBUGS CAN CUT FFB YIELD BY 30%

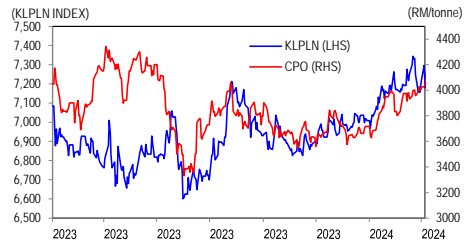
**URGENT ALERT: Outbreak of Sooty Mold and Mealybugs in Sabah Oil Palm Plantations**

Annual MPOA-MPOB R&D/Sustainability Forum held on 19th March 2024, a significant outbreak and rapid spread of both Sooty Mold and Mealybugs.

- Sooty Mold, a prevalent issue in Sabah, has been directly linked to the resurgence of Mealybugs, exacerbating the situation. This infestation poses a severe threat to the health and productivity of our plantations.
- Reports indicate a staggering decline in photosynthesis rates that **can range from 58 to 78%, accompanied by a corresponding drop in FFB yields, which can plummet by as much as 30%.** However, it is reassuring to note that these adverse effects can be mitigated through timely intervention and appropriate treatments. To address this critical situation, researchers are recommending the implementation of the following measures:

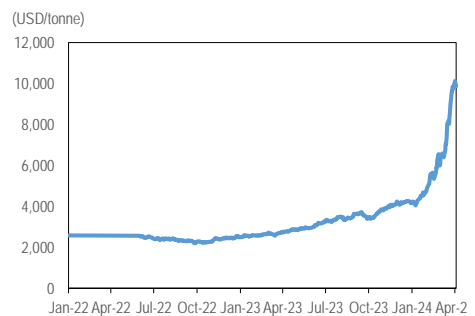
Source: MPOA

KL PLANTATION INDEX VS CPO PRICES



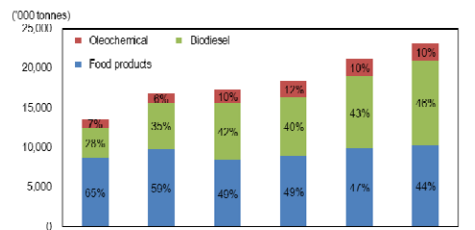
Source: Bloomberg

RECORD HIGH COCOA PRICES



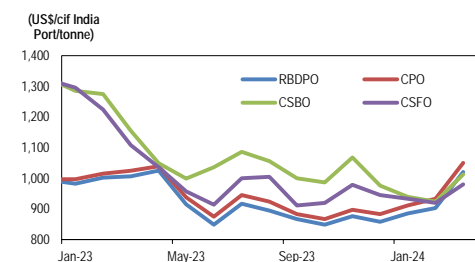
Source: Bloomberg

INDONESIA DOMESTIC USE DRIVEN BY BIODIESEL MANDATE



Source: GAPKI

VEGOIL PRICES AT INDIA PORT



Source: SEA

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