

SECTOR UPDATE

Plantation – Malaysia

MPOB Sep 22: Inventory Nearly Hits Three-Year High On Higher Imports From Indonesia

Malaysian palm oil inventory nearly hit a three-year high mainly due to higher imports from Indonesia. There was strong export growth in Sep 22 as expected, thanks to higher import margins in China and wider PO-SBO price spreads. However, India's exports came in lower mom in Sep 22 due to competition from Indonesia. We expect CPO prices to be supported at the current level as we believe that the recent price hike has factored in the normalising inventory. Maintain MARKET WEIGHT.

MPOB'S SEP 22 STATISTICS

(m tonne)	Sep 22	mom % chg	yoy % chg	9M22	yoy % chg
CPO Production	1.77	2.6	3.9	13.34	0.4
<i>Pen Malaysia</i>	<i>0.96</i>	<i>0.7</i>	<i>5.4</i>	<i>7.46</i>	<i>1.8</i>
<i>Sabah</i>	<i>0.41</i>	<i>7.5</i>	<i>(4.6)</i>	<i>3.01</i>	<i>(3.7)</i>
<i>Sarawak</i>	<i>0.40</i>	<i>2.1</i>	<i>10.2</i>	<i>2.87</i>	<i>1.4</i>
Palm Oil Stocks	2.32	10.5	31.8	2.32	31.8
Palm Oil Domestic Use	0.26	4.8	(9.3)	2.27	(8.5)
Palm Oil Exports	1.42	9.3	(11.9)	11.24	(0.1)
<i>Oleochemical</i>	<i>0.24</i>	<i>10.2</i>	<i>(0.6)</i>	<i>2.05</i>	<i>(5.0)</i>
<i>Biodiesel</i>	<i>0.03</i>	<i>11.7</i>	<i>(43.9)</i>	<i>0.25</i>	<i>(7.1)</i>
Palm Oil Imports	0.13	(9.0)	76.4	0.90	(2.4)
CPO Price (RM/tonne)	3,737	(10.4)	(18.0)	5,531	32.6

Source: MPOB, UOB Kay Hian

WHAT'S NEW

- **Data beat expectations.** The latest data released by Malaysian Palm Oil Board (MPOB) for Sep 22 came in above market expectations, with end-stocks climbing 10.5% mom to nearly a three-year high since Oct 19. This came in above market expectations of 2.26m-2.27m tonnes for Sep 22 Malaysia palm oil inventory, mainly driven by strong imports. We had observed three consecutive months of strong Malaysia palm oil imports (since Jul 22) which coincided with the Indonesian government relaxing its domestic market obligation ratio and its "flush-out" programme since Jun 22 to prevent further inventory build-up during the production peak season in 3Q22.
- **Strong export growth in Sep 22, as expected.** The strongest exports growth mainly came from China (+108.5% mom) given the positive import margins and huge palm oil-soybean oil (PO-SBO) price spread. Having said that, imports from India dropped by 21% mom in Sep 22, as India purchased refined palm oil directly from Indonesian players who had more attractive prices.

ACTION

- **Maintain MARKET WEIGHT.** We expect CPO prices to remain at the current level in the near term. We reckon that the recent hike in CPO prices may have factored in the normalising inventory (especially in Indonesia). Based on GAPKI's announcement, Indonesian palm oil inventory is also normalising at 4.04m tonnes (as of Aug 22).
- **No near-term catalysts for plantation share price performance** with the exception of IOI Corporation (**IOI MK/BUY/Target: RM5.15**) and Hap Seng Plantations (**HAPL MK/BUY/Target: RM2.80**). We expect their financial performance to outperform peers', which will support their share price performances.

PEER COMPARISON

Company	Ticker	Rec	Price @ 11 Oct 22	Target Price	Market Cap (US\$m)	PE			ROE (%)	P/B (x)	2022F Div (sen)	Div Yield (%)
						2021 (x)	2022F (x)	2023F (x)				
Malaysia												
Hap Seng Plantations	HAPL MK	BUY	2.00	2.80	342	7.1	7.0	14.2	12.5	0.8	17.2	8.6
IOI Corporation	IOI MK	BUY	3.68	4.80	4,892	16.6	14.5	18.6	16.5	2.1	13.2	3.6
Genting Plantations	GENP MK	HOLD	5.58	5.90	1,071	11.6	13.3	22.2	8.6	0.9	25.2	4.5
Kim Loong	KIML MK	HOLD	1.72	1.80	356	8.7	9.1	9.7	17.5	1.9	15.4	9.0
KL Kepong	KLK MK	HOLD	19.80	25.25	4,568	9.5	11.9	14.5	19.9	1.6	99.8	5.0
Sime Darby Plantation	SDPL MK	HOLD	4.02	4.75	5,949	11.8	12.6	26.3	13.6	1.5	9.8	2.4
Sarawak Oil Palms	SOP MK	HOLD	2.34	2.47	446	2.6	4.1	7.2	19.7	1.0	23.0	9.8

Source: UOB Kay Hian

MARKET WEIGHT

(Maintained)

STOCK PICKS

Company	Rec	Share Price (RM)	Target Price (RM)
Hap Seng Plantations	BUY	2.00	2.80
IOI Corporation	BUY	3.68	4.80

Source: UOB Kay Hian

CPO PRICE ASSUMPTIONS (RM/TONNE)

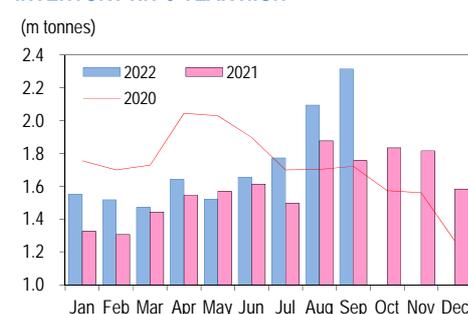
	CPO Price (RM/tonne)
2020	2,686
2021	4,408
Our forecast:	
2022F	5,200
2023F	4,000

CPO Price:

MPOB @ 11 Oct 22	3,643
BMD 3 rd Month Contract	3,522

Source: UOB Kay Hian

INVENTORY HIT 3-YEAR HIGH



Source: Malaysian Palm Oil Board (MPOB)

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ESSENTIALS

- Production peaking.** Malaysia's palm oil production grew 2.6% mom in Sep 22, with Sabah having a higher production growth rate of 7.5% mom (mainly due to less disruption from rainy weather). We expect production to peak in Oct 22 and fall in Nov-Dec 22. We estimate Malaysia's palm oil production for 2022 at 18.0m-18.2m tonnes (9M22: 13.3m tonnes). If rainfall remains high during the La Nina season, followed by the year-end monsoon, Malaysia's production may record negative growth in 2022 vs 18.1m tonnes in 2021.
- Lower exports.** We expect exports to decline in 4Q22 given: a) the winter season, and b) both China's and India's palm oil inventories have returned to normal levels. On top of that, we expect buyers from India to continue to buy from Indonesian players (at least up to Nov 22) given the attractive pricing of refined palm oil.
- Impact from strong US dollar.** The greenback's recent strong performance is not positive to plantation companies, as CPO prices did not react positively to the strengthening of US dollar due to excessive CPO supplies. On the cost side, the stronger US dollar could lead to higher fertiliser cost (as fertilisers are mostly imported). Companies with US dollar-denominated loans may see a slight negative impact on their earnings given the higher interest expenses. Hence, companies may not benefit from the US dollar appreciating against the Malaysian ringgit.
- Budget 2023: Multi-tiered foreign workers levy.** In the recent Budget Malaysia 2023, the government proposed to implement a multi-tiered foreign worker levy by 2023. This will be an additional cost to large plantation companies as they are highly dependent on foreign workers, which could make up 80-90% of their estate workers. Levies may not be a large proportion of the wage component but may put further pressure on companies' cost of production, as cost has been rising due to the higher minimum wage (effective 1 May 22) and higher fertiliser cost.

SECTOR CATALYSTS

- Weather risk.** If triple-dip La Nina happens, this may result in:
 - Malaysia's lower-than-expected Malaysia palm oil production.** We expect a slower-than-expected yield recovery from the older trees and lower oil extraction rate (OER). Hence, Malaysia's palm oil production may come in lower than market expectation at around 18.0m tonnes (market expectation: 18.3m-18.7m tonnes)
 - Indonesia's production growth may suffer from crop losses.** Recall that some Indonesian palm oil mills were closed or refused to take in external crops in 2Q22 due to the internal stockpile. Hence, a lot of fruit were left on the trees to rot. This would affect production in the upcoming months as harvesters would need to spend more time to trim the branches and may also affect production yield moving forward. Hence, we expect Indonesia's palm oil production growth to come in lower than market expectations.
 - Brazil's oilseed production for 2023.** Brazil's oilseed production may be lower than expected if La Nina happens, due to the drier weather.
- If the Ukrainian Black Sea grains exports deal is not extended, global supplies may again be disrupted and prices for oilseeds and grains could rally again. This could spill over to vegoil prices as well.

ASSUMPTION CHANGES

- No change to CPO ASP assumptions.** We maintain our CPO price assumptions at RM5,200/tonne and RM4,000/tonne for 2022 and 2023 respectively.

RISKS

- Brazil is expected to produce record-high soybean.** Estimates for the soybean crop, of which planting has already started, signal that oilseed production should reach 152.4m tonnes in the 2022-23 season, up from 125.5m tonnes in last year's estimates. The expected area for soy is 42.9m ha, up from the 41.5m ha estimated for the 2021-22 crops.

PRODUCTION PEAKING



Source: MPOB

STRONGER EXPORT IN SEP 22



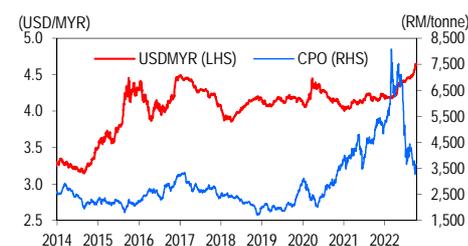
Source: MPOB

% OF COMPANIES FOREIGN WORKERS VS TOTAL WORKERS

Company	% of Foreign Workers
Sime Darby Plantations	61.1
Kuala Lumpur Kepong	63.1
IOI Corporation	60.9
Genting Plantations	75.4
Hap Seng Plantations	84.7

Source: Companies' Reports

STRONG USD NO LONGER BUOY CPO PRICE



Source: Bloomberg

EARNINGS IMPACT TO 1% APPRECIATION ON USD

Company	Earnings Impact (%)
Sime Darby Plantations	(1.5)
Kuala Lumpur Kepong	(0.8)
IOI Corporation	(0.6)

Source: Companies' Reports

- **Potentially higher Ukraine oilseed production for 2023.** Ukraine's sunflower seed acreage is expected to increase in the next marketing season. The Ukrainian Grain Association also expects an increase in soybean planted areas for the 2023-24 crops to 1.4m ha from 1.2m ha in the 2022-23 marketing years. The increase in sunflower seed and soybean acreages in the next season is mainly because farmers expect good profitability of both crops.
- Higher demand from biodiesel and renewable diesel may lead to higher-than-expected vegoil consumption and mitigate the concerns of a recession.

MALAYSIA: PALM OIL EXPORTS BY DESTINATION

('000 tonne)	Sep 22	mom % chg	yoy % chg	9M22	yoy % chg	Remarks
TOTAL	1,420	9.3	(11.9)	10,240	(8.9)	
China	264	108.5	12.70	1,012	(20.8)	Higher mom thanks to higher import margin.
India	185	(21.0)	(50.40)	2,074	(16.5)	Lower mom as Malaysia players' loss market share to Indonesian players.
EU	83	(36.0)	(38.60)	1,064	(12.2)	
Japan	51	(8.8)	40.50	409	30.3	
Pakistan	31	(38.8)	(51.60)	356	(25.0)	
US	15	56.9	(49.20)	126	(41.9)	Higher mom due to higher demand to replace soybean oil in non-biofuel sectors.
Others	790	14.2	7.3	5,198	(1.2)	

Source: MPOB, UOB Kay Hian

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