

SECTOR UPDATE

Plantation – Malaysia

Palm Oil Production Upcycle Coming Soon

End-Feb 23 inventory came in lower than market expectations but still failed to lift CPO prices, mainly due to the weakness in oilseeds and other vegoils. The lower inventory was mainly due to lower imports and high domestic consumption. We expect strong production in the upcoming months as La Nina has ended. We also expect demand to improve in Mar 23, with Malaysia players benefitting from a slowdown in Indonesian exports. Maintain MARKET WEIGHT.

MPOB'S FEB 23 STATISTICS

(m tonne)	Feb 23	mom % chg	yoy % chg	2M23	yoy % chg
CPO Production	1.25	(9.4)	10.0	2.63	10.1
Palm Oil Stocks	2.12	(6.6)	39.6	2.12	36.6
Palm Oil Domestic Use	0.34	7.4	59.8	3.82	5.9
Palm Oil Exports	1.11	(2.0)	0.5	17.98	7.6
<i>Oleochemical</i>	<i>0.23</i>	<i>8.1</i>	<i>(0.1)</i>	<i>0.12</i>	<i>(73.5)</i>
<i>Biodiesel</i>	<i>0.01</i>	<i>3.2</i>	<i>(67.2)</i>	<i>0.44</i>	<i>492.1</i>
Palm Oil Imports	0.05	(63.8)	(65.0)	1.26	1.2
CPO Price (RM/tonne)	3,908.0	(1.0)	(26.8)	3,915.0	(30.6)

Source: MPOB, UOB Kay Hian

WHAT'S NEW

Feb 23 Malaysia palm oil inventory came in below market expectations. This was mainly due to lower imports and better domestic consumption. Some of the key highlights are:

- **Inventory: Lower than market expectations**, mainly due to lower-than-expected imports and higher domestic consumption. Large government spending on food items for flood victims is likely to have boosted domestic consumption of palm oil, in addition to higher consumption during the Chinese New Year festivities.
- **Production: Within market expectations**, given that the market had factored in the higher than usual rainfall in mid-Feb 23, which previously led the CPO prices to recover by 12% in Feb 23 alone.
- **Exports: Within market expectations**, with the market entering a quiet month with lesser working days.

Malaysia Palm Oil Outlook for Mar 23:

- **Higher production** on the back of: a) catch-up in harvesting after the rains, and b) start of the high crops cycle. However, the production is expected to be lower than our initial forecast, factoring in high rainfall in the first week of Mar 23.
- **Exports:** Malaysia may capture a larger export market share in Mar 23 as Indonesia players are slowing down their exports due to the current attractive domestic pricing.
- **End stock:** Expecting to be lower mom as exports growth will be higher.

ACTION

- **Maintain MARKET WEIGHT.** We expect CPO price to linger between RM3,500-4,300/tonne for 1H23. Having said that, we recommend investors to accumulate on high dividend-yielding companies when share prices weaken, given the strong cash flow generated over the past two years.
- Our top pick for the sector remains IOI Corporations as we reckon that the strong downstream margin as compared to its peers would be able to cushion the softening upstream earnings for 2023.

PEER COMPARISON

Company	Ticker	Rec	Price @ 10 Mar 23	Target Price	Market Cap (US\$m)	PE			ROE (%)	P/B (x)	2023F Div	Div Yield (%)
			(RM)	(RM)		2021 (x)	2022F (x)	2023F (x)			(sen)	
Malaysia												
IOI Corporation	IOI MK	BUY	3.80	4.80	5,218.4	14.9	17.2	17.1	16.5	2.1	11.5	3.0
Genting Plantations	GENP MK	HOLD	5.96	5.90	1,183.0	11.3	17.2	18.0	9.1	1.0	15.2	2.5
Hap Seng Plantations	HAPL MK	HOLD	1.89	2.30	334.4	7.2	10.6	13.2	11.0	0.8	10.7	5.7
Kim Loong	KIML MK	HOLD	1.82	1.80	389.9	9.6	10.2	10.5	17.5	2.1	14.2	7.8
KL Kepong	KLK MK	HOLD	20.70	23.40	4,938.9	10.3	14.1	14.3	16.6	1.6	72.6	3.5
Sime Darby Plantation	SDPL MK	HOLD	4.25	4.60	6,502.6	14.1	15.6	15.9	13.8	1.6	16.4	3.9
Sarawak Oil Palms	SOP MK	HOLD	2.49	2.47	490.4	4.6	7.2	5.8	15.8	0.7	13.9	5.6

Source: UOB Kay Hian

MARKET WEIGHT

(Maintained)

STOCK PICKS

Company	Rec	Share Price (RM)	Target Price (RM)
IOI Corporation	BUY	3.80	4.80

Source: UOB Kay Hian

CPO PRICE ASSUMPTIONS (RM/TONNE)

	CPO Price (RM/tonne)
2020	2,686
2021	4,408

Our forecast:

2023F	4,000
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CPO Price:

MPOB 2022 average	5,088
MPOB @ 10/3/2023	4,164
BMD 3 rd Month Contract	4,182

Source: UOB Kay Hian

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ESSENTIALS

- From the recent Palm Oil Conference 2023, there are two schools of thoughts from the speakers:
 - Bullish:** a) Lower growth in palm oil output moving forward, higher biodiesel consumption in Indonesia (looking at the implementation of B40 mandate in Jun/Jul 23), higher demand in China and India in 2H23 and potentially El Nino by end-23.
 - Bearish:** a) Huge soybean production coming up from Brazil, and b) current high inventory level in the oilseeds market.
 - Our view from this event:** We reckon that CPO price would be higher in 2H23, with inventory level starting to normalise in destination countries. This will be coupled by lower-than-expected CPO output as we expect that yield recovery may not be as good given the prolonged rainy weather and reduction in fertiliser application over the last three years.
- Possibly stronger output in the short term.** The subsiding rain coincides with the end of La Nina, and we expect production would be strong in the next 2-3 months on the back of a catch-up in harvesting activities in the estates. While Mar-Apr 23 would be the fasting month with production usually coming in lower, we reckon that the production would still be good in Mar-Apr 23. The difference this year is that companies will be compensating harvesters with higher commission to reward and retain them given the strong output from the oil palm trees.
- Stronger exports.** Malaysia may gain some of the exports market as Indonesia's exports are not aggressive given that Indonesian domestic prices are more attractive than export prices. In addition, Pakistan, which has not been active in buying, is "very close" to signing the IMF agreement which would unlock other bilateral and multilateral financing avenues for Pakistan to shore up its foreign exchange reserves. We reckon that this may boost some of the palm oil export to Pakistan, given that the palm oil export to Pakistan had been low for the past few months due to funding limitations.

SECTOR CATALYSTS

- Potential El Nino.** Based on National Oceanic and Atmospheric Administration (NOAA), there's around a 60% chance of El Nino by Sep-Nov 23. El Nino would bring dry weather in the palm oil producing countries and we do not expect any immediate impact on the palm oil output. The impact of El Nino on palm oil output would only be reflected in 4-6 months, resulting in lower FFB production. Having said that, we reckon that the market may react and lift the CPO prices if El Nino is expected, as the market would expect palm oil supply to be weaker in 2024.
- Higher biodiesel and renewable diesel demand.** Indonesia has increased its biodiesel mandate for 2023 to 35% (B35) from 30% in 2022, but the market expects Indonesia to introduce B40 soon, which will add an additional 1.8m-1.9m kl to demand. This could translate to total palm oil usage of 12.9-13.0m tonnes, or 31% of Indonesia's production (up from 22% in 2022).
- Black Sea war.** A continuation of the Black Sea war would be supportive for vegoil prices. However, assuming the Black Sea war ends, the market will then be flooded by a huge vegoil supply.

ASSUMPTION CHANGES

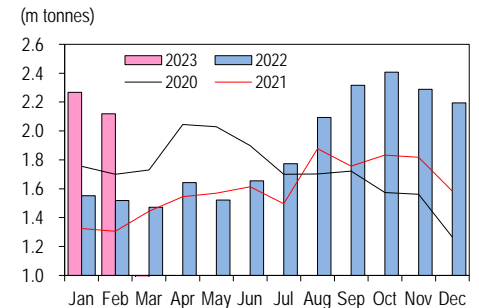
- No change to CPO ASP assumptions.** We maintain our CPO price assumptions at RM4,000/tonne for 2023.

CPO PRODUCTION BY REGION

(m tonne)	Feb 23	mom % chg	yoy % chg	2M23	yoy % chg
CPO Production	1.25	(9.4)	10.0	2.63	10.1
Pen Malaysia	0.68	(4.8)	6.8	1.39	9.0
Sabah	0.33	(11.3)	17.5	0.69	12.0
Sarawak	0.25	(17.6)	9.8	0.55	10.4

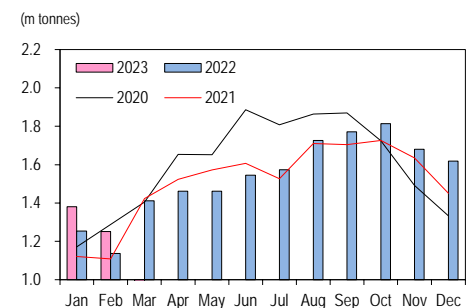
Source: MPOB

MALAYSIA PALM OIL INVENTORY CAME IN LOWER THAN MARKET EXPECTATION



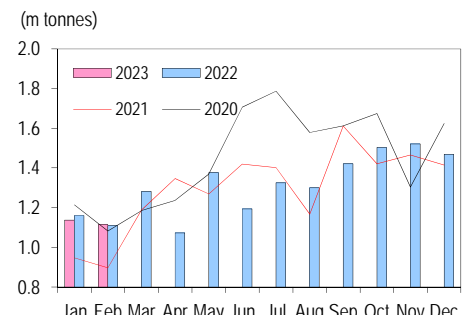
Source: Malaysian Palm Oil Board (MPOB)

MALAYSIA PALM OIL PRODUCTION



Source: MPOB

FLAT EXPORTS MOM



Source: MPOB

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