Results review

Plantations

Equity

1Q21 Earnings review: Impressive performance

Overweight ▲

- **Overall, 1Q21 earnings released by companies under our coverage was impressive with three coming in above our expectations, six within and one below expectations.**
- **Narrowing of price differential between CPO and SBO in CBOT is inconsequential, due to anticipation of tight supply of global vegetable oils, led by PO from Malaysia as well as improved demand from China that could dictate higher CPO prices, possibly up until July 2021.**
- **We see potential upside to plantations' segment margins in the upcoming 2Q21 earnings season, given higher ASP of palm products and more realistic production expectation.**
- **We upgrade our sector call to OVERWEIGHT from NEUTRAL as rise in earnings and high CPO prices have resulted in several stocks carrying attractive valuations. Maintain unchanged average CPO price forecast of RM2,950/MT for 2021 and RM2,700/MT for 2022.**

Performance was impressive

The recently concluded corporate earnings season was spectacular for plantation companies, in our opinion. Out of 10 stocks under our coverage, 3 companies reported earnings that were above expectations, with 6 inline and 1 came in below our expectation. Earnings were generally higher yoy resulting from greater ASP of palm products and improvement in FFB production. Expansion in margins and profit contribution from downstream manufacturing segment, especially from oleochemical division aided to the better results for KLK and IOI. Conversely, FGV's weaker performance, apart from higher FV charged on LLA, was due to RM65m losses incurred from the processing of external crops as opposed to RM48m gain a year ago – causing a negative milling margin.

Tight supply set to keep CPO price supported

We are of the view that the higher near-term CPO price is possible. Although any price increase could be capped by the narrowing of the price differential between CPO and SBO in CBOT, we believe this is inconsequential. The anticipation of tight supply of global vegetable oils, as well as improved demand from China means CPO price could retain its upward trajectory, possibly up until July 2021. This is in tandem with our view on tight palm oil supply scenario in Malaysia given unresolved labour shortage issues and recent Malaysian government's decision to impose a stricter implementation of Movement of Order Control (MCO) on agribusiness. The MCO is limiting workforce capacity in palm oil mills and refineries to 60% in a bid to curb the spread of COVID-19 and likely hurt palm oil production this year by delaying the harvesting and collecting of FFB. Hence, this will in turn impact productivity and the quality of CPO produced. In light of these developments, we foresee that price for June/July 2021 would trade within a range of RM4,100/MT and RM3,800/MT as opposed to RM2,366/MT and RM2,795/MT during the same period last year.

Noorhayati Maamor
noorhayati@bimbsec.com.my
(603) 2613 1736

Earnings outlook remains exciting

We expect plantation's earnings for this year would be more visible given average CPO price achieved up to May 2021 averaging RM4,095/MT vs. RM2,496/MT for the same period last year. The higher realized price in 2021/22 against 2020 should see plantation segment fetching better margins in FY21 and FY22. Nonetheless, we remain cautious that earnings could be affected by high operational costs and possible lower-than-expected production and sales volume – with labour issue remaining as a key concern when the sector enters high production season in Sep-Nov. On the other hand, there might be margin contraction for downstream players as demand and price (feedstock and selling price) concerns heighten. However, we estimate that higher revenue and better margins expected from oleochemical division, would partially cushion earnings volatility in downstream segment.

OVERWEIGHT the sector

We maintain average CPO forecast for 2021 of RM2,950/MT and RM2,700/MT for 2022. Our base case scenario is for CPO prices to continue their upward trajectory in the short-term – due to tighter supplies and improved demand as discussed earlier – and then moderate in the later part of 3Q21. In view of this, we expect plantation companies' earnings to remain firmly on an uptrend, particularly for 2Q21.

Following the impressive 1Q21 corporate earnings season, we upgrade our call on plantation sector to OVERWEIGHT from NEUTRAL as most stocks under coverage are currently carrying attractive valuations. We have BUY call on HAPL (RM2.17), SOP (RM4.50), IOI (RM4.80), KLK (RM24.40) and SIME Darby Plants (TP: RM5.00), whilst HOLD recommendation on Sarawak Plant (RM2.64), TSH (TP: RM1.23), GENP (TP: RM9.00) and FGV (TP: RM1.30); and non-rated for TH Plant.

Variances in earnings forecast would be due to lower-than-expected production, lower-than-expected ASP realised of palm products and higher-than-expected costs. Risk factors include 1) lower-than expected demand, 2) weakening of crude oil prices, and 3) unforeseen market changes i.e., prolong Covid-19 pandemic and movement restrictions.

Table 2: Plantations companies results summary

Companies	Reporting Period	Against estimate	Core Earnings Chg.			Earnings Forecast	Rating	TP	Company Commentary
			Qoq	YoY	YTD				
FGVH	1QFY21	Below	<100%	84%	84%	Downgrade	HOLD	1.30	**YoY/Qoq:** FGV's reported a PBT of RM15m in 1Q21 as opposed to LBT of RM163m in 1Q20 mainly due to improved earnings from all sectors – as margins rose owing to better ASP achieved. Nonetheless, the improved earnings were negated by higher FV charged on LLA and FV loss on derivatives amounting RM143.7m (1Q20: RM57.3m) and RM15.1m (1Q20: a gain of RM57.4m) respectively. On qoq basis, the lower profit was due to lower contribution from all sectors. Plantation sector reported a loss of RM50.8m vs. a profit of RM274.7m in 4Q20 on account of lower FFB production and higher FFB purchase costs as well as higher FV charged on LLA of RM143.75m against FV gain of RM87.5m in 4Q20. **Outlook.** We are cautiously optimistic on FGV's plantation sector. We are of the view that FGV may not be able to fetch better margins and to capture fully the rise in CPO price given that 70% of its FFB processed are purchased from third parties.
Genting Plantations	1QFY21	Inline	-29%	-18%	-18%	Maintain	HOLD	9.00	**YoY/Qoq:** GENP's 1Q21 revenue contracted 6% yoy to RM536.6m mainly due to lower sales volume from the Downstream segments on absence of biodiesel sales as well as lower property sales, as revenue recognized was at the early stage of property development (Table 2 and 3). Downstream manufacturing segment registered an EBITDA loss of RM5.9m against a profit of RM14.1m in 1Q20 whilst property segment dropped 8% to RM5.1m resulting from lower sales volume and capacity utilization, as well as lower margins. On quarterly basis, the higher ASP realized of CPO and PK partially negated the drop in earnings that was attributed by a weaker contribution from both plantation and Downstream segment on account of lower FFB production and sales volume respectively. **Outlook:** Although we expect performance of plantation segment to be driven by higher ASP of palm products and improve in production, there is high possibility of continuing margin squeeze in downstream segment on demand and price concerns due to unfavorable palm oil-gas oil (POGO) spread and prolong COVID-19 pandemic, aided by slow uptake in property segment. Conversely, both its Johor and Genting's Premium Outlets may continue to experience lower patronage until concerns on the COVID-19 fully subside. According to management, unbilled sales stood at RM48m as at end-Mar 2021 against RM60m as at end Mar 2020 and RM35m as at end-Dec 2020.
Hap Seng Plantations	1QFY21	Inline	-25%	>100%	>100%	Maintain	BUY	2.17	**YoY/Qoq:** HAPL's 1Q21 core PBT came in higher yoy to RM32.8m against RM2.4m in 1Q20 as revenue increased 19% to RM121.3m on account of higher ASP realized for CPO and PK, despite registering lower sales volume for both products. This was also aided by lower operating expenses of RM91.0m against RM109.7m incurred in 1Q20. On quarterly basis, the 25% drop in core PBT was a result of lower sales volume of CPO and PK, although ASP realized of CPO and PK increased significantly by 22% and 28% respectively to RM3,854/MT and RM2,585/MT. **Outlook:** We believe that HAPL's earnings upside in the next quarter would be more visible as it is highly exposed to movements in palm product prices. The higher palm product price expected in 2021/22 versus 2020 should see HAPL fetching better margins in FY21/22. This is backed by the expected 5% improvement in FFB production of 669k tones in FY21 as opposed to 637k tones in FY20. Conversely, HAPL has a strong balance-sheet with a net cash position, experienced management and one of the largest producers of sustainable palm oil in Sabah. Fundamentally, we believe HAPL has excellent financials to diversify its earnings and contribute to long-term growth, if the need arises.

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Companies	Reporting Period	Against estimate	Core Earnings Chg. Qoq	YoY	YTD	Earnings Forecast	Rating	TP	Company Commentary
IOI Corporation	3QFY21	Above	60%	>100%	84%	Upgrade	BUY	4.80	**YoY/Qoq**: IOI recorded a more than 100% increase in core profit of RM481m in 3Q21 on the back of 41% increase in revenue of RM2.86bn mainly due to higher contribution from all segments, aided by lower effective tax rate. This also was aided by > 100% increase in share of profit from associate, Loders, with a share of profit of RM351m as oppose to RM2.1m in 3Q20 which included a share of one-off gain of RM267.9m from the sale of its refinery in Rotterdam. On quarterly basis, the higher profit contribution from Resources-based Manufacturing (RBM) segment negated the lower contribution from plantation segment, that was due to 28% decrease in FFB production to 550,524MT against 760,743MT for 2Q21. Nonetheless, this was partially negated by higher CPO and PK prices realized of RM3,211/MT and RM2,616/MT respectively vs RM2,992/MT and RM1,982/MT realized in 2Q21. Conversely, the higher profit contribution from RBM segment was due to higher contribution from oleochemical sub-segment on improved margins as well as higher share of results from specialty fats associate, Loders. **Outlook:** Although volatility remains present with the increase concern of ESG issues in the industry, we are positive on IOI's long-term earnings growth prospect. We believe RBM segment would continue to perform well despite potential margin squeeze on higher feedstock cost. Conversely, plantation segment would continue to sustain its performance given better PO price anticipated on the back of higher CPO prices currently
Kuala Lumpur Kepong	2QFY21	Above	6.0%	40.0%	47.0%	Upgrade	BUY	24.40	**YoY/Qoq:** KLK's reported a more than 100% increase in PBT of RM649.3m for 2Q21 vs RM102.6m for 2Q20, on account of higher profit contribution from plantation segments as margin rose to 15.3% from 8.2% in 2Q20 on higher ASP realized of CPO and PK; and higher contribution from Manufacturing and Property segments, as well as higher share of results from joint ventures. On quarterly basis, PBT increased 31% mainly due to 1) higher margins and profit contribution from manufacturing segment on higher revenue and better margins with higher profit contributions from oleochemical division (+54.2% mom to RM199.2m), 2) higher surplus of RM154.6m against RM133k in 1Q21 on sales of plantation land and government acquisition, and 3) a surplus of RM12.2m on FV of an ordinary investment which was previously an associate. **Outlook:** We are optimistic on KLK's long-term earnings growth prospect with positive factors driving key segmental growth on all fronts. We believe plantation segment would continue to sustain its performance given CPO price are currently trading above RM4,000/MT, whilst FFB production is expected to grow significantly by 8% to 4.2m tones in FY21. On the other hand, manufacturing segment demand, especially in oleochemical products, is expected to continue to be satisfactory given increase in hygiene awareness worldwide.
TSH Resources	1QFY21	Inline	-15%	22.0%	22.0%	Maintain	HOLD	1.23	**YoY/Qoq:** TSH's 1Q21 earnings came in higher yoy at RM30.8m, as higher contribution from palm products segment negated the lower contribution from bio-integration and cocoa division, as well as additional cost incurred on Indonesia export levy and duty on CPO of RM25.6m to RM31.9m vs. RM6.2m in 1Q20. This was also aided by lower finance costs of RM9.8m (-19%) and higher share of profits contributions from associate (+11%) amounting to RM1.9m. On quarterly basis, the lower earnings were due to lower contribution from others division, aided by higher cost of sales and lower share of profits from JV and associate. **Outlook:** We believe earnings growth would be driven by expansion in production from Indonesian estates with more planted areas come into maturity and harvesting due to better age profile (Indonesia: 10.0 yrs.; Malaysian: 12.7 yrs.; and Group: 10.6 yrs.). Of note, FFB production in Indonesia grew 8.7% mom to 81.5k tones in April 2021.

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Companies	Reporting Period	Against estimate	Core Earnings Chg. Qoq	YoY	YTD	Earnings Forecast	Rating	TP	Company Commentary
Sarawak Plantation	1QFY21	Inline	-22%	53%	53%	Maintain	HOLD	2.64	**YoY/Qoq:** SPLB's 1Q21 core PBT increased 96% yoy to RM19.8m as higher ASP realized for CPO and PK were more than offset by a 0.2% and 4.1% declined in CPO and PK sales volume to 30.9k tones and 6.3k tones respectively. Conversely, the 47% increase in revenue of RM145.5m against RM98.9m in 1Q20, negated the higher cost incurred in production and operating cost amounting to RM126.3m (+41.95% yoy). On quarterly basis, a tad decline in profit was attributed by a lower productions and sales volume of CPO and PK despite a higher realized ASP of CPO and PK as well as higher cost of sales and distribution expenses during the period **Outlook:** We believe earnings performance would be sustained, in view of 1) its harvestable areas and crops profile has improved, hence will generate better yield and production growth, and 2) any earnings downside would be mitigated by the higher CPO price anticipated which are currently trading above RM4,000/MT. Off note, about 700ha has been considered as normalized as at end April, 2021 - bring the remaining area to be normalize YTD of c. 2,035ha (end 2020: 2,735ha).
Sarawak Oil Palms	1QFY21	Inline	23%	71%	71%	Downgrade	BUY	4.50	**YoY/Qoq:** SOP's 1Q21 PBT came in higher yoy to RM113.0m against RM96.3m in 1Q20 mainly due to higher ASP realized of palm products sold as well as lower finance costs of RM8.7m as opposed to RM12.3m incurred in 1Q20. On quarterly basis, although revenue dropped 4% to 788.3m from RM820.4m in 4Q20, PBT increased more than 100% qoq, resulted from higher ASP realized of palm oil products sold and absence of impairment loss recognized during the quarter. This was also aided by lower cost of sales of RM645.6m (-7.7%) as well as administrative expenses of RM7.9m against RM9.6m previously incurred in 4Q20. **Outlook:** We are positive on the performance of SOP although there may be margin squeeze in downstream segment on demand and price concerns. Nonetheless, given the current scenario of higher palm products prices, we believe that SOP's earnings upside in the next quarter would be more visible, aided by FFB production that is expected to increase by 4% yoy to 1.41m tones in FY21.
Sime Darby Plantation	1QFY21	Above	12%	>100%	>100%	Upgrade	BUY	5.00	**YoY/Qoq:** SDPL's 1Q21 core PBT improved significantly to RM713m against RM298m in 1Q20 mainly attributed to 1) higher contribution from upstream operations, as margin increased significantly (refer Table 2) on higher ASP realized of palm products, 2) improved result from Downstream segment due to higher contribution from bulk business and trading operations in Asia Pacific and higher premiums from sale of RSPO products, and 3) lower finance cost of RM14m vs. RM38m in 1Q20. On quarterly basis, the improved results from upstream segment have negated the lower contribution from downstream segments on account of higher selling prices realized and better cost control. **Outlook:** Although ESG issues would continue to be the main key concerns for plantation industry, we believe that any earnings downside would be mitigated by the higher price anticipated for palm product prices in upstream segment which are currently trading above RM4,000/MT, supported by growth in production especially from Indonesian estates.
TH Plantation	1QFY21	Inline	-91%	-88%	-88%	Maintain	Non-Rated	NA	**YoY/Qoq:** THP recorded PBT of RM25.4m in 1Q21 against a loss before tax of RM14.5m in 1Q20 mainly due to higher ASP realized of FFB, CPO and PK. On quarterly basis, the higher PBT was supported by gain in fair value change in biological assets of RM14.89m against RM28.96m loss in 4Q20; aided by lower impairment of assets by RM8.6m to RM0.09m and lower operating expenses of RM3.57m against RM7.03m in 4Q20. Nonetheless, revenue dropped 9.2% qoq to RM131m on lower CPO and PK sales volume, despite achieving higher ASP realized for CPO, PK and FFB **Outlook:** As THP's earnings are highly correlated to ASP of palm products and production, we believe earnings would be sustained in this financial year given current CPO prices are trading at multi-year high and trade above RM4,000/MT. This is also aided by the on-going progress of THP's Strategic Recovery Plan, in our view, that would make its earnings target justifiable.

Table 3: FFB Production and ASP realised of CPO – Qoq and YoY performance

Calendar year	FFB Production			Changes (%)		Average Selling Price Realised of CPO (RM/MT)			Changes (%)	
	1Q21	4Q20	1Q20	Qoq	YoY	1Q21	4Q20	1Q20	Qoq	YoY
SIME Plant	2,207,333	2,295,924	2,117,688	-3.9	4.2	3,185	2,664	2,605	19.6	22.3
IOI	550,524	760,743	631,954	-27.6	-12.9	3,211	2,992	2,704	7.3	18.8
KLK	900,153	973,744	890,733	-7.6	1.1	2,997	2,703	2,572	10.9	16.5
FGV	742,426	1,042,001	711,745	-28.7	4.3	3,172	3,059	2,669	3.7	18.8
GENP	440,800	598,227	449,209	-26.3	-1.9	2,916	2,589	2,619	12.6	11.3
HAPL	130,284	178,081	131,980	-26.8	-1.3	3,854	3,148	2,814	22.4	37.0
TSH	228,188	255,008	207,727	-10.5	9.8	3,010	2,779	2,599	8.3	15.8
THP	139,221	194,586	164,678	-28.5	-15.5	3,283	2,859	2,580	14.8	27.2
SOP	293,781	325,944	293,667	-9.9	0.04	3,885	3,235	2,679	20.1	45.0
Sarawak Plant	68,636	83,089	65,271	-17.4	5.2	3,819	3,178	2,643	20.2	44.5

Source: Companies, BIMB Securities

Table 4: Peer comparison – stocks under coverage

Companies	Price	Market Cap	Net Profit (RM m)			PER (x)			Div. Yield	ROE	Target Price	Rating
	(RM)	(RM m)	FY0	FY1	FY2	FY0	FY1	FY2	(%)	(%)	(RM)	
SDPL	4.50	30,980.59	1346.7	1390.9	1349.5	23.0	22.3	23.0	1.8%	9.9	5.00	**Buy**
IOI Corp	4.06	25,404.39	600.9	1055.9	1033.6	42.3	24.1	24.6	2.0%	6.5	4.80	**Buy**
KLK	22.00	23,728.19	772.6	1075.0	981.6	30.7	22.1	24.2	2.3%	7.3	24.40	**Buy**
FGV	1.35	4,925.00	146.2	176.5	203.1	33.7	27.9	24.3	2.2%	3.5	1.30	Hold
TH Plantations	0.51	446.34	14.0	44.4	40.6	31.9	10.0	11.0	0.0%	2.4	NA	Non-Rated
Genting Plant	7.89	7,078.89	254.4	219.1	206.5	27.8	32.3	34.3	1.6%	5.2	9.00	Hold
Hap Seng Plant	1.95	1,559.39	90.3	94.3	86.2	17.3	16.5	18.1	3.6%	5.4	2.17	**Buy**
TSH Resources	1.13	1,559.60	79.5	75.3	68.3	19.6	20.7	22.8	1.3%	5.5	1.23	Hold
SOP	3.92	2,240.59	204.1	287.0	254.1	11.0	7.8	8.8	1.5%	8.6	4.50	**Buy**
Sarawak Plant	2.45	683.63	61.0	75.4	66.8	11.2	9.1	10.2	4.1%	10.4	2.64	Hold

Note: ^Closing price (afternoon session) as at 3 June 2021
Source: Bloomberg, Companies, BIMB Securities

DEFINITION OF RATINGS

BIMB Securities uses the following rating system:

STOCK RECOMMENDATION

BUY	Total return (price appreciation plus dividend yield) is expected to exceed 10% in the next 12 months.
TRADING BUY	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain.
HOLD	Share price may fall within the range of +/- 10% over the next 12 months
TAKE PROFIT	Target price has been attained. Fundamentals remain intact. Look to accumulate at lower levels.
TRADING SELL	Share price may fall by more than 15% in the next 3 months.
SELL	Share price may fall by more than 10% over the next 12 months.
NOT RATED	Stock is not within regular research coverage.

SECTOR RECOMMENDATION

OVERWEIGHT	The Industry as defined by the analyst's coverage universe, is expected to outperform the relevant primary market index over the next 12 months
NEUTRAL	The Industry as defined by the analyst's coverage universe, is expected to perform in line with the relevant primary market index over the next 12 months
UNDERWEIGHT	The Industry as defined by the analyst's coverage universe, is expected to underperform the relevant primary market index over the next 12 months

Applicability of ratings

The respective analyst maintains a coverage universe of stocks, the list of which may be adjusted according to needs. Investment ratings are only applicable to the stocks which form part of the coverage universe. Reports on companies which are not part of the coverage do not carry investment ratings as we do not actively follow developments in these companies.

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BIMB SECURITIES SB (290163-X)
A Participating Organisation of Bursa Malaysia Securities Berhad
Level 32, Menara Multi Purpose, Capital Square,
No. 8 Jalan Munshi Abdullah,
50100 Kuala Lumpur
Tel: 03-2613 1600 Fax: 03-2613 1799
http://www.bimbsec.com.my

Azharuddin Nordin
Head of Research