Results Review | Plantation | Equity

2Q21 Earnings Review

Overweight◀▶

A quarter of adrenaline-pumping results

- **Overall, the 2Q21 earnings released by companies under our coverage was impressive with eight companies coming in above our expectations.**
- **We believe plantation stocks currently deserve better attention as higher earnings and palm products prices have resulted in several stocks carrying attractive valuations.**
- **We foresee attractive plantations' segment margins seen recently to sustain in the upcoming 3Q21, given higher ASP of palm products and more realistic production expectations.**
- **Maintain OVERWEIGHT given earnings growth estimated to remain firmly on the upside as CPO price is anticipated to stay above RM4,000/MT in the short-term before moderating in the later part of 4Q2021. We have revised average CPO price forecast to RM3,700/MT (RM3,100/MT previously) for 2021 and RM2,950/MT (RM2,700/MT previously) for 2022.**

Performance was impressive

The recently concluded corporate earnings season was remarkable for plantation companies, based on our analysis. Out of ten stocks under our coverage, eight companies reported earnings that were above expectations, with two coming in within our expectation. Earnings were generally higher yoy as improvement in ASP of palm products realised negated the increase in production costs and operational costs as well as lower FFB and CPO production. Expansion in margins and profit contribution from downstream manufacturing segment, aided to the better results for KLK and SIME Plant. Conversely, the improvement in qoq results was generally due to better palm product price realised as well as higher growth in FFB and CPO production during the period. The FFB production growth for GENP and TSH turned out to be positive yoy (Table 3) mainly driven by higher crop from Indonesian estates as more areas came into maturity, whilst existing mature areas moved into higher yielding age brackets. Malaysian estates are still lagging as productivity is wedged by the lag impact of weaker yield from the dry weather experienced in 2019 and lower fertiliser application as well as hiccup in productivity due to labour shortage issues.

Tight palm oil supply in Malaysia set to keep CPO price supported

Apart from lower yield, palm oil production is expected to grow at a slower pace as harvesting and manuring activities is believed to be interrupted by an acute shortage of labour especially in Peninsular Malaysia and Sarawak. The hiring and renewing of workers' permits are being frozen on global fight against prolonged Covid-19 pandemic as borders are closed and inter-state traveling are banned. Besides reopening of major economies, which would take place sooner rather than later, we also believe that tight supply of edible oils and stockpiles compounded by improving demand scenario and rally in soybean oil (SBO) prices, rapeseed oil prices and sunflower oil prices would keep CPO price supported. The palm oil price competitiveness which has large volume and stable supply throughout the year, in our view, has its own benefits, as we believe it has the ability to offset the impact of increasing food commodity prices i.e., to cushion the trade-off issue between the use of agricultural commodities for food and energy.

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Earnings growth outlook firmly entrenched on the upside

We expect plantation's earnings for this year would be more visible given average CPO price achieved up to August 2021 averaging at RM4,123.94/MT vs. RM2,528.56/MT for the same period last year. Fundamentally, the tight inventory level and supply of palm oil would add an upward pressure to palm oil price and, thus, would continue to support the price in the short-to-medium term, in our view, before moderating in the later part of fourth quarter 2021. 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 upward pressure on production and operational costs. There is also a possibility of lower-than-expected production and sales volume as supply/demand is affected by a prolonged pandemic together labour issue remains as a perpetual concern to planters, while margin contraction may well continue 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 the downstream segment.

OVERWEIGHT the sector

We predict that the average CPO price this year would break the 2011's record CPO average price of RM3,278/MT - judging from the CPO price trend, currently trading at much higher than recent historical prices. We have raised our 2021 average CPO price forecast to RM3,700/MT from RM3,100/MT previously, and to RM2,950/MT from MYR2,700/MT initially forecast for 2022. Off note, these changes already reflected in our earnings forecasts in the recent results released in August 2021 - refer Table 2. 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 4Q21. In view of this, we expect plantation companies' earnings to remain firmly on an uptrend for the upcoming results release.

Maintain OVERWEIGHT on the sector as most stocks under coverage are currently carrying attractive valuations. We have BUY call on HAPL (RM2.17), SOP (RM4.50), TSH (TP: RM1.23), IOI (RM4.80), KLK (RM24.40), SIME Darby Plants (TP: RM5.00) and GENP (TP: RM9.00), whilst HOLD recommendation on Sarawak Plant (RM2.64), 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) slower-than-expected economic growth and consumption of edible oils, 2) lower-than-expected demand due to changes in government policies of importing countries, 3) higher-than-expected supply and stockpiles of Soybean and SBO, 4) narrowing of the price differential between CPO and SBO, 5) weakening of crude oil prices, and 6) prolonged Covid-19 pandemic with another round of movement restriction worldwide.

Table 2: Plantations companies results summary

Companies	Reporting Period	Against estimate	Core Profit Before Tax Chg. Qoq	YoY	YTD	Earnings Forecast	Rating	TP	Company Commentary
FGVH	2QFY21	Above	>100%	>100%	>100%	Upgrade	HOLD	1.30	**Outlook:** We are positive on FGV's long-term prospect given the continuous effort by management focusing on operational excellence and cost efficiency, in our view, would support its turnaround plan **Our Call:** Given the encouraging results, we revised our FY21/22F earnings forecast higher to RM361m/RM293m from RM177m/RM203m previously as we revisit our ASP of palm products, productions and margin to better reflect our current and future expectations of FGV's business operations. We revised higher our ASP forecast for CPO to RM3,300/MT for FY21 and RM2,950/MT for FY22 from RM2,900/MT and RM2,700/MT previously; whilst cutting our production number by 8% to 4.12m and 4.32m tonnes respectively for FY21/22. Maintain HOLD on the stock with unchanged TP of RM1.30 based on P/B of 1.0x and 3-years average BV/share of RM1.30.
Genting Plantations	2QFY21	Above	>100%	>100%	>100%	Upgrade	BUY	9.00	**Outlook:** We are optimistic on GENP's earnings performance and we expect the catalyst will be plantation segment on higher ASP of palm products and improvement in production. There is high possibility of continuing margin squeeze in downstream segment however, on demand and price concerns due to unfavorable palm oil-gas oil (POGO) spread and prolonged COVID-19 pandemic which have caused slow uptake in property segment and slow sales and patronage of Premium Outlets. **Our Call:** Upgrade to BUY with unchanged TP of RM9.00, based on BV/share of RM5.50 and historical 3-yrs avg. P/BV of 1.65x. Following this result, we revised our FY21/FY22 earnings forecast higher to RM375m and RM351m respectively from RM219m and RM207m previously as we adjusted our production, ASP of palm products, costs and margins assumptions. We cut our production number by 8%/5% to 2.13m/2.23m tonnes respectively for FY21/22 whilst raising ASP forecast for CPO to RM3,150/MT for FY21 and RM2,700/MT for FY22 from RM2,600/MT and RM2,500/MT previously.
Hap Seng Plantations	2QFY21	Above	>100%	>100%	>100%	Upgrade	BUY	2.17	**Outlook:** We believe HAPL's medium-to-long-term prospect remains promising given its 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. **Our Call:** Maintain BUY with unchanged TP of RM2.17, based on 5-years average mean P/B of 1.0x and BV/share of RM2.17. Following this result, we revised our FY21/FY22 earnings forecast higher to RM141m and RM98.9m respectively from RM94.3m and RM86.2m previously as we adjusted our production, ASP of palm products, costs and margins assumptions. We cut our production number by 5% to 634k/650k tonnes respectively for FY21/22 whilst raised ASP forecast for CPO to RM3,650/MT for FY21 and RM3,000/MT for FY22 from RM2,950/MT and RM2,500/MT previously.
IOI Corporation	4QFY21	Above	-2%	46%	76%	Maintain	BUY	4.80	**Outlook:** We believe RBM segment would continue to perform well despite potential margin squeeze on higher feedstock cost and subdued demand for refined palm products in the future. Conversely, the plantation segment is expected to continue to sustain its performance given better palm oil price anticipated in the coming quarter. On a separate announcement, the company had extended the revised timeframe for an additional period of 15 months to utilize the remaining proceeds received from the disposal of 70% of IOI's equity interest held in Loders. This is to enable the Board to further identify and evaluate the feasibility of the potential investments and formulating its Group strategies holistically. **Our call: Maintain** BUY with unchanged TP of RM4.80 based on average 5-yr low P/B of 3.1x and BV/share of RM1.55.

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Companies	Reporting Period	Against estimate	Core Profit Before Tax Chg.			Earnings Forecast	Rating	TP	Company Commentary
			Qoq	YoY	YTD				
Kuala Lumpur Kepong	3QFY21	Above	25%	>100%	71%	Upgrade	BUY	24.40	**Outlook:** We are optimistic on KLK's long-term earnings growth prospect. Although weak production and higher costs are expected to continue to be a risk to KLK's earnings, we are of the view that earnings in the next quarter would continue to sustain given higher palm products price i.e., CPO price which is currently trading above RM4,000/MT, may increase the resale value of palm products and fetch better margins to the Group. **Our call:** Maintain BUY with unchanged TP of RM24.40 based on hist. 3-yrs average P/B of 2.3x and BV/share of RM10.61. We tweaked our FY21/22 earnings forecast higher to RM1,335m and RM,206m respectively from RM1,075m and RM981m previously, as we revisited our assumptions on margins, costs and expenses.
TSH Resources	2QFY21	Above	>100%	>100%	91%	Upgrade	BUY	1.23	**Outlook:** TSH is highly exposed to weakness/strength in palm product prices as approximately more than 90% of its revenue and earnings are derived from palm products segment. On that score, we foresee that TSH is set to record strong earnings given higher CPO prices should see TSH fetching better margins, backed by the expected 10% improvement in FFB production of 997k/1.0m tonnes in FY21/22 against 906k tonnes achieved in FY20. **Our call:** Given the encouraging results, we revised our FY21/22 earnings forecast higher to RM120.5m and RM108.5m respectively from RM90.8m and RM87.7m with unchanged Target Price of RM1.23 (Price/Book of 1.1x and BV/share of RM1.12); as we revisit our assumption on ASP of palm products, margins, cost and expenses to be more reflective to current and future expectations. We have raised our FY21/22 ASP forecast for CPO to RM3,280/MT and RM2,700/MT respectively from RM2,950/MT and RM2,500/MT previously. Maintain BUY.
Sarawak Plantation	2QFY21	Inline	63%	>100%	>100%	Upgrade	HOLD	2.64	**Outlook:** We believe earnings performance would be more visible, 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 prices anticipated which are currently trading above RM4,000/MT. **Our call:** Maintain HOLD with unchanged TP of RM2.64 based on P/B of 1.1x and BV/share of RM2.40. Given the encouraging results, we revised our FY21 and FY22 earnings forecast higher to RM79.8m and RM67.5m respectively from RM75.4m/RM66.8m previously as we adjusted our production, ASP of palm products, costs and margins assumptions. We revised higher our ASP forecast for CPO to RM4,050/MT for FY21 and RM3,000/MT for FY22 from RM2,950/MT and RM2,700/MT previously; whilst cut our production number by 12% to 350k and 390km tonnes respectively for FY21/22 to be more reflective to our current and future expectations.
Sarawak Oil Palms	2QFY21	Above	40%	>100%	>100%	Upgrade	BUY	4.50	**Outlook:** Given the current scenario of higher palm products prices, we believe that SOP's earnings upside in the next quarter would be more visible, although there may be margin squeeze in downstream segment on demand and price concerns as well as slow sales and uptake in property segment. **Our call: Maintain** BUY with unchanged TP of RM4.50, based on P/BV of 1.0x and BV/share of RM4.50. Following this result, we revised our FY21/FY22 earnings forecast higher to RM346.5m and RM270.8m respectively from RM287m and RM254m previously as we adjusted our production, ASP of palm products, costs and margins assumptions. We cut our production number by 2% to 1.38m and 1.41m tonnes respectively for FY21/22 whilst raised ASP forecast for CPO to RM3,650/MT for FY21 and RM2,800/MT for FY22 from RM2,950/MT and RM2,500/MT previously.

Table 2: Plantations companies results summary

Companies	Reporting Period	Against estimate	Core Profit Before Tax Chg. Qoq	YoY	YTD	Earnings Forecast	Rating	TP	Company Commentary
Sime Darby Plantation	2QFY21	Above	25%	>100%	>100%	Upgrade	BUY	5.00	**Outlook:** Although ESG concerns puts pressure on valuations, in our opinion, certain context or scenario appear to be overplayed. We are expecting a better performance in subsequent quarters on higher price anticipated for palm product prices, as well as growth in FFB production especially from Indonesian estates. **Our call:** Given the encouraging results, we tweaked our FY21/22 earnings forecast higher to RM1,899m and RM1,661m respectively from RM1,391m and RM1,349m with unchanged TP of RM5.00 (P/B of 2.5x and BV/share of RM2.00); as we revisit our assumption on ASP of palm products, margins, cost and expenses to be more reflective to current and future expectations. We have raised our FY21/22 ASP forecast for CPO to RM3,577/MT and RM2,880/MT respectively from RM2,891/MT and RM2,592/MT previously.
TH Plantation	2QFY21	Inline	>100%	>100%	>100%	Maintain	Non-Rated	NA	**Outlook:** We believe earnings performance would be sustained in this financial year given current CPO prices are trading at multi-year high and trade above RM4,000/MT with cost efficiencies measures in place. 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. **Our call:** We have non-Rated recommendation on the stock.

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 (%)	
	2Q21	1Q21	2Q20	QoQ	YoY	2Q21	1Q21	2Q20	QoQ	YoY
SIME Plant	2,455,404	2,207,333	2,470,348	11.2	-0.6	3,632	3,185	2,361	14.0	53.8
IOI	727,653	550,524	865,502	32.2	-15.9	3,648	3,211	2,370	13.6	53.9
KLK	968,438	900,153	1,014,300	7.6	-4.5	3,444	2,997	2,239	14.9	53.8
FGV	1,058,327	742,426	1,188,296	42.5	-10.9	3,333	3,172	2,309	5.1	44.3
GENP	532,902	440,800	500,281	20.9	6.5	3,250	2,916	2,325	11.5	39.8
HAPL	148,750	130,284	152,708	14.2	-2.6	4,365	3,854	2,321	13.3	88.1
TSH	255,151	228,188	219,082	11.8	16.5	3,441	3,010	2,099	14.3	63.9
THP	180,012	139,221	218,063	29.3	-17.4	3,424	3,283	2,236	4.3	53.1
SOP	315,753	293,781	344,644	7.5	-8.38	4,414	3,885	2,357	13.6	87.3
Sarawak Plant	77,753	68,636	89,398	13.3	-13.0	4,221	3,819	2,333	10.5	80.9

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	3.96	27,386.23	1346.7	1899.3	1661.4	20.3	14.4	16.5	3.0%	9.9	5.00	**Buy**
IOI Corp	4.00	24,931.51	1394.3	1033.7	1018.8	17.9	24.1	24.5	2.6%	13.5	4.80	**Buy**
KLK	21.34	23,002.11	772.6	1334.9	1206.4	29.8	17.2	19.1	2.3%	7.3	24.40	**Buy**
FGV	1.39	5,070.93	146.2	361.3	293.1	34.7	14.0	17.3	2.2%	3.5	1.30	Hold
TH Plantations	0.56	490.54	14.0	44.4	40.6	35.1	11.0	12.1	0.0%	2.4	NA	Non-Rated
Genting Plant	7.64	6,854.59	254.4	374.9	351.4	26.9	18.3	19.5	2.7%	5.2	9.00	**Buy**
Hap Seng Plant	1.89	1,511.41	90.3	140.5	98.9	16.7	10.8	15.3	3.7%	5.4	2.17	**Buy**
TSH Resources	1.11	1,531.99	79.5	120.5	108.5	19.3	12.7	14.1	1.4%	5.5	1.23	**Buy**
SOP	3.65	2,086.61	204.1	346.5	270.8	10.2	6.0	7.7	1.6%	8.6	4.50	**Buy**
Sarawak Plant	2.40	669.68	61.0	79.8	67.5	11.0	8.4	9.9	4.2%	10.4	2.64	Hold

Note: ^Closing price (afternoon session) as at 3 September 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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