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## Inventory declines but exports still weak

Both CPO production and palm oil exports trended higher mom in May but remained lower yoy. Palm oil inventory declined to the lowest level in 62 months but is poised to rise again in the next few months as oil yield recovers further. The USDA cut its beginning inventory and raised consumption estimates for US soybean for 2016/17E but raised its world vegetable oil inventory marginally. El Nino has dissipated. We maintain our CPO ASP assumption of RM2,400/MT in 2016-18E, plantation stock TPs and sector NEUTRAL rating. We maintain our SELL ratings on FGV and GENP on valuation grounds.

### CPO mom production growth trimmed by lower OER

In May, CPO production grew by a more moderate 4.9% mom to 1.36m MT (versus 16.9% in March and 6.7% in April) as the impact of higher FFB yields in the Peninsular, Sabah and Sarawak were partially offset by lower OERs. Due to the impact of extreme dry weather conditions brought about by El Niño, CPO production in May and the first five months of the year were 24.6% and 16.8% lower yoy. Ytd production of 6.06m MT is 32% of Oil World's forecast of 18.93m MT for 2016, pointing to a potential 40%:60% split between the first and second half of the year instead of the usual 45%:55%.

### Exports increased 9.3% mom, inventory declined to 1.65m MT

Palm oil exports in May increased by 9.3% mom but declined yoy, indicating still weak demand overseas. China, India and the EU, which together accounted for almost 49% of total Malaysian exports, imported less compared to May last year. The weak CPO production and palm oil export growth contributed to a decline in palm oil inventory from 1.80m MT in April to 1.65m MT, a 62-month low.

### El Niño has dissipated, 75% chance of La Niña during fall/winter

According to the 9 June US NOAA/CPC advisory, El Niño has dissipated and ENSO-neutral conditions have returned. There is however a 75% chance of La Niña during the fall and winter of 2016-17, with forecasts favouring a weak or borderline moderate La Niña at this stage. A strong La Niña event will create extreme wet conditions in the western Pacific and extreme dryness in the eastern Pacific.

### Peer comparison

Stock	Stock code	Rating	Sh Pr # (RM)	TP (RM)	Mkt Cap (RMm)	Year end	Core PE (x) CY16E	Core PE (x) CY17E	EPS growth (%) CY16E	EPS growth (%) CY17E	EV/EBITDA FY16E (x) ^	P/BV FY16E (x) ^	ROE (%) CY16E	DY (%) CY16E
Sime Darby	SIME.MK	HOLD	7.52	7.11	46,708	June	22.2	16.0	29.3	38.7	15.1	1.5	6.8	3.3
IOI Corp	IOI.MK	HOLD	4.33	4.24	27,541	June	21.0	19.5	20.4	7.7	17.8	5.2	23.9	2.8
KL Kepong	KLK.MK	HOLD	23.20	21.70	24,766	Sept	22.5	19.6	13.8	14.7	11.7	2.5	11.0	2.2
Felda Global	FGV.MK	SELL	1.45	1.17	5,290	Dec	24.6	14.9	>100	64.4	9.3	0.8	3.4	5.5
Genting Plant	GENP.MK	SELL	10.50	8.84	8,165	Dec	22.6	19.1	74.2	18.1	14.9	2.0	8.7	1.1
IJM Plant	IJMP.MK	HOLD	3.33	3.42	2,935	March	22.7	15.3	100.7	49.0	12.6	1.8	11.8	3.0
Hap Seng Plant	HAPL.MK	HOLD	2.38	2.20	1,904	Dec	15.2	13.9	29.8	8.9	8.6	1.0	7.8	4.2
Wilmar *	WIL.SP	Not Rated	3.36	n.a	21,235	Dec	12.9	11.6	13.9	11.6	12.3	1.0	7.7	2.8
Golden Agri *	GGR.SP	Not Rated	0.38	n.a	3,942	Dec	16.2	13.8	0.0	17.6	10.1	0.6	3.6	2.2
Astra Agro **	AALI.U	Not Rated	15,550	n.a	24,487	Dec	14.3	12.0	177.0	18.9	8.4	1.8	14.5	2.1
Mkt Cap weighted average (excl FGV)							21.9	17.8	28.8	24.1	14.8	2.7	12.2	2.8

\* S\$ \*\* IDR # Share prices as at 10 June 2016 ^ FY17E for IJMP

Source: Company, Affin Hwang forecasts, Bloomberg

Affin Hwang Investment Bank Bhd (14389-U)  
(Formerly known as HwangDBS Investment Bank Bhd)

## Sector Update

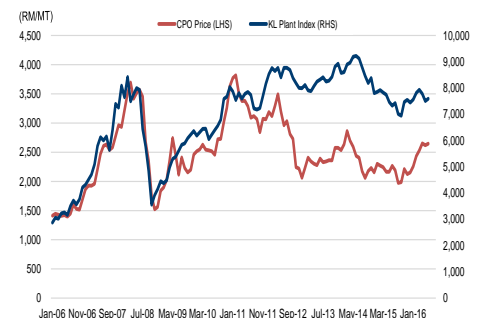
# Plantation

## NEUTRAL (maintain)

### Absolute Performance (%)

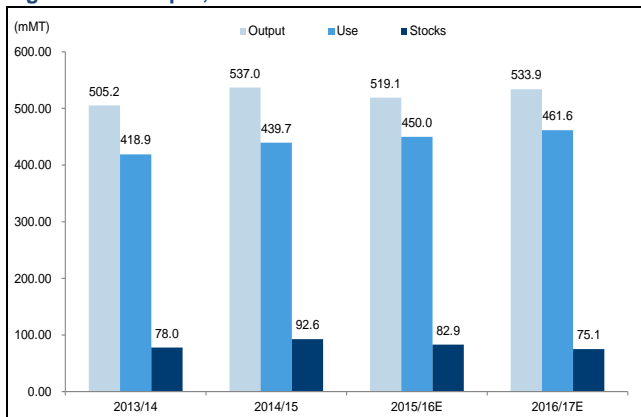
	1M	3M	12M
FGV	+2.1%	-0.7%	-24.5%
GENP	-0.6%	-4.6%	+5.9%
HAPL	+0.9%	+1.3%	-4.8%
IJMP	-4.3%	-7.0%	-7.8%
IOI	+3.6%	-10.2%	-7.4%
KLK	+1.1%	-3.3%	+7.9%
SIME	-0.3%	-4.2%	-11.8%

### CPO Price vs KL Plantation Index

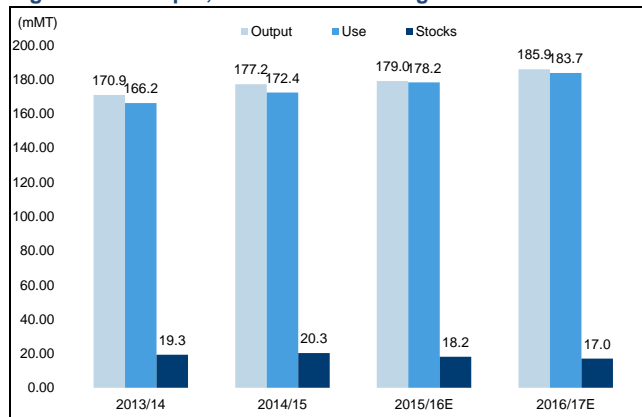


Source: Affin Hwang, Bloomberg

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**Fig 1: World output, use and stock of oilseeds**

Source: USDA

**Fig 2: World output, use and stock of vegetable oils**

Source: USDA

### Price outlook hinge on yield recovery and demand growth

It is generally expected that FFB yield will continue to improve until Sept/Oct but some planters are expecting a more gradual recovery due to significant impact of the last strong El Nino event. Lower FFB yield recovery in the coming months may cap inventory build-up and support CPO prices until the end of the year. For the 2016/17E season, both the USDA and Oil World forecast higher production of oilseeds and vegetable oils even though stock-usage ratios may be flat to tighter due to low beginning inventories and higher consumption. On the demand side, the Malaysian government's plan to push biodiesel usage from B7 to B10 is positive. But export demand for both Malaysian and Indonesian palm oil is still key and that is correlated to global economic growth and sentiment. Soybean closed at the highest level in almost two years last Friday after the USDA cut its US beginning inventory and raised consumption estimates, and pegged its average price forecast for soybeans 40 cents higher at the midpoint for 2016/17E. Its world vegetable oil closing inventory estimate for 2016/17E is raised marginally.

### Maintain CPO ASP assumption and sector NEUTRAL rating

We maintain our CPO ASP assumption of RM2,400/MT in 2016-18E, plantation stock target prices and sector **NEUTRAL** rating. Across our coverage universe we still do not have BUY-rated names. **IOI** has rebounded after it dropped the suit against the RSPO and is maintained at HOLD. **FGV** is still a SELL progress in cost cutting and profit enhancement is seen in the coming quarters. **GENP** has excellent FFB production growth prospects, but remains a **SELL** at current levels due to its unappealing valuation.

### Key risks

Key downside risks to our NEUTRAL sector rating and stock calls include (i) weaker-than-expected demand and higher-than expected production lowering prices of vegetable oils; (ii) decline in CPO production that is not offset by higher CPO selling prices; (iii) delays in implementation of biodiesel mandates in Indonesia and Malaysia; and (iv) unfavourable policies and taxes. Key upside risks include a strong rebound in the global economy as well as demand for and prices of vegetable oils.



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## Focus Charts

Fig 3: Key palm oil statistics – May 2016

	Apr16	May16	mom change		May15	May16	yoy change		YTD (Jan - May) ('000 MT)		
	('000 MT)	('000 MT)	('000 MT)	%	('000 MT)	('000 MT)	('000 MT)	%	2015	2016	%chg
Production	1,301.3	1,364.6	63.3	4.9	1,810.7	1,364.6	(446.1)	(24.6)	7,281.6	6,058.0	(16.8)
Export	1,172.9	1,282.4	109.5	9.3	1,613.6	1,282.4	(331.2)	(20.5)	6,134.9	6,155.8	0.3
Stock	1,803.9	1,645.6	(158.3)	(8.8)	2,248.6	1,645.6	(603.0)	(26.8)	2,248.6	1,645.6	(26.8)
Avg Price (RM/MT)	2,652.5	2,620.0	(32.5)	(1.2)	2,165.5	2,620.0	454.5	21.0	2,229.2	2,498.3	12.1

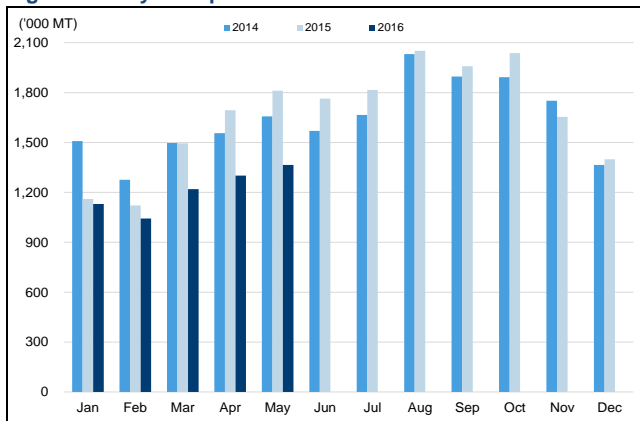
Source: MPOB

Fig 4: Exports to key destinations – May 2016

Destination (MT)	2015				2016				Change (%)		
	Mar	Apr	May	Jan-May	Mar	Apr	May	Jan-May	May16		
									mom	yoy	Jan-May16
China PR	132,722	262,713	359,660	1,036,113	141,962	104,923	105,905	510,494	0.9	(70.6)	(50.7)
India	297,549	87,391	342,859	1,110,131	328,127	179,540	310,495	1,259,022	72.9	(9.4)	13.4
Japan	31,296	41,801	60,606	219,375	34,583	27,817	32,806	174,690	17.9	(45.9)	(20.4)
Netherlands	63,879	61,430	191,064	544,389	67,709	49,982	30,899	356,729	(38.2)	(83.8)	(34.5)
Pakistan	60,387	64,562	58,385	272,152	44,882	72,225	76,567	279,804	6.0	31.1	2.8
United States	49,213	77,324	45,410	288,891	60,554	50,213	59,126	277,583	17.8	30.2	(3.9)
European Union	112,938	130,520	267,245	819,482	128,392	100,645	117,416	740,438	16.7	(56.1)	(9.6)

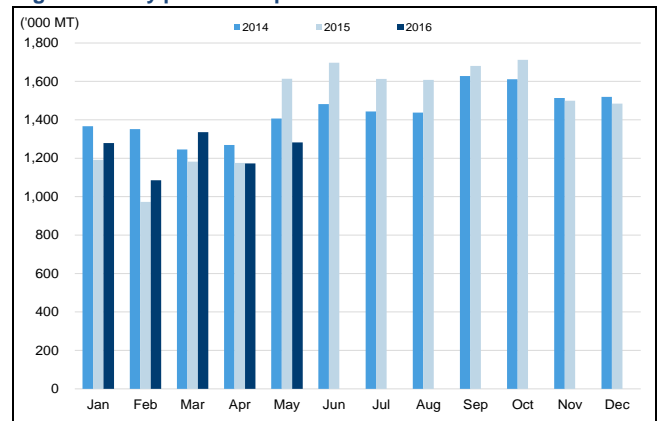
Source: MPOB

Fig 5: Monthly CPO production



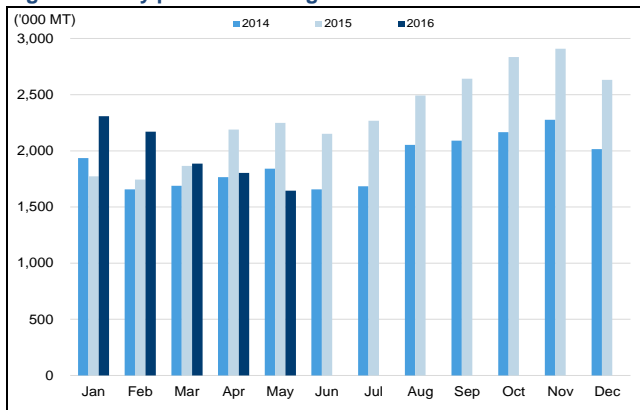
Source: MPOB

Fig 6: Monthly palm oil exports



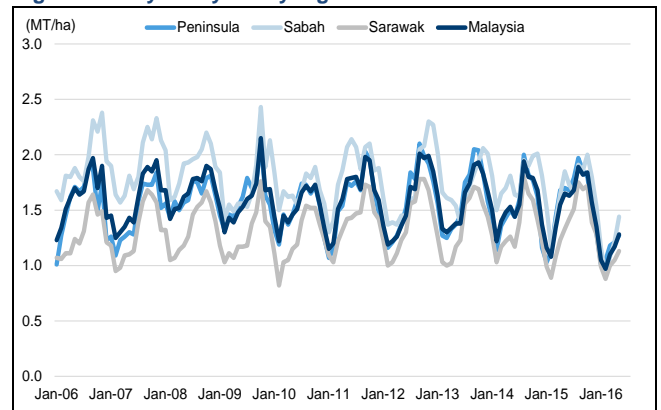
Source: MPOB

Fig 7: Monthly palm oil closing stocks

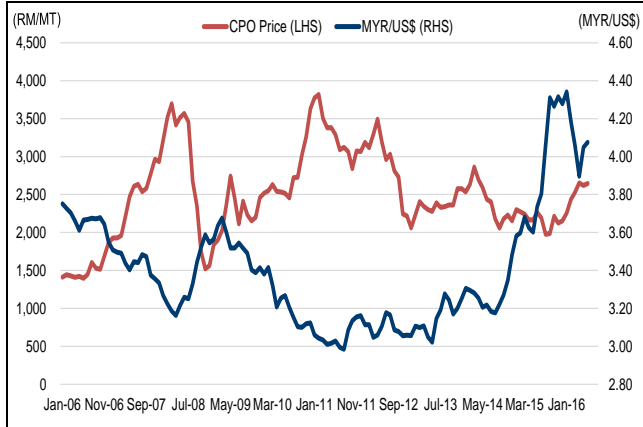


Source: MPOB

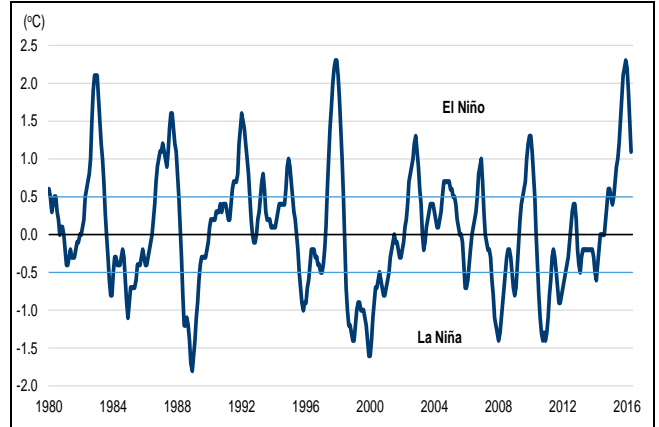
Fig 8: Monthly FFB yield by region



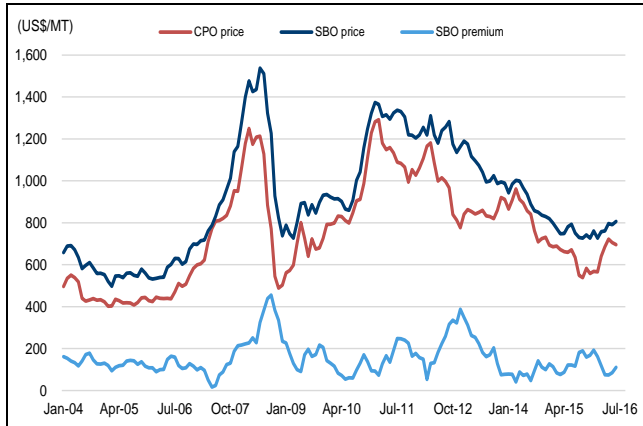
Source: MPOB

**Fig 9: CPO price versus USD/MYR exchange rate**

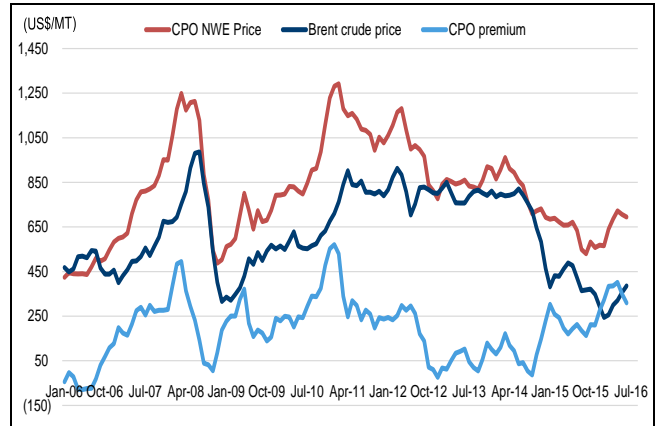
Source: MPOB, Bloomberg

**Fig 10: Observed SST anomalies in Niño-3.4 regions**

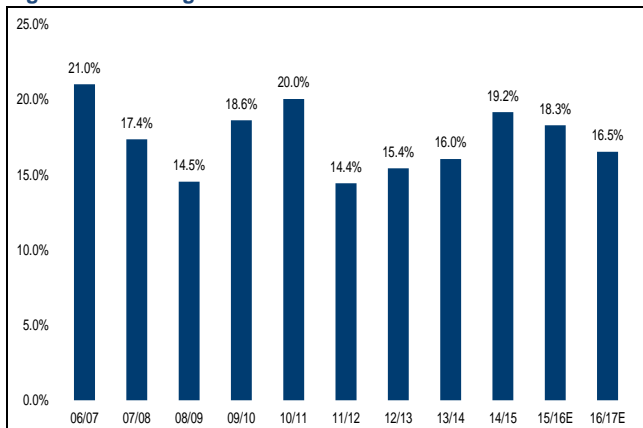
Source: US NOAA

**Fig 11: Soybean oil price, CPO price & soybean oil premium**

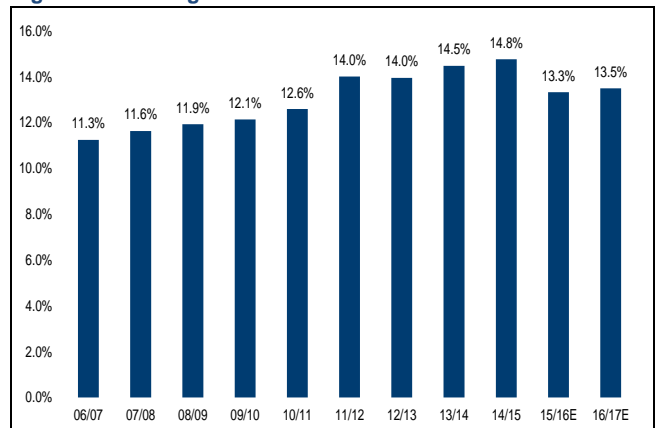
Source: Oil World, Bloomberg, Affin Hwang estimates

**Fig 12: CPO premium over Brent crude**

Source: Oil World, Bloomberg, Affin Hwang estimates

**Fig 13: Stock/usage ratio of 10 Oilseeds**

Source: Oil World

**Fig 14: Stock/usage ratio of 17 Oils & Fats**

Source: Oil World

**Equity Rating Structure and Definitions**


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<b>BUY</b>	Total return is expected to exceed +10% over a 12-month period
<b>HOLD</b>	Total return is expected to be between -5% and +10% over a 12-month period
<b>SELL</b>	Total return is expected to be below -5% over a 12-month period
<b>NOT RATED</b>	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

*The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.*

<b>OVERWEIGHT</b>	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
<b>NEUTRAL</b>	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
<b>UNDERWEIGHT</b>	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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