AmInvestment Bank

Company report

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PLANTATION

HAP SENG PLANT

(HAPL MK,HAPP.KL)

6 June 2017

Small decline in FFB output in FY17F

UNRATED

Rationale for report: Company update

Price	RM2.59
Fair Value	na
52-week High/Low	RM2.73/RM2.32

Key Changes

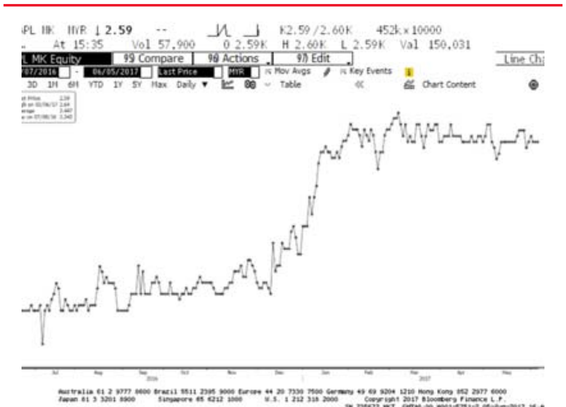
Fair value	na
EPS	na

YE to Dec	FY13	FY14	FY15	FY16
Revenue	443.3	495.6	434.9	503.427
Net profit	97.5	128.3	96.4	124.118
EPS	12.2	16.0	12.1	15.52
EPS growth	-30.5	31.6	-24.8	28.7
Consensus net (RMmil)				
DPS (sen)	10.0	11.0	8.0	8.0
PE (x)	21.8	16.6	22.1	17.1
EV/EBITDA (x)	15.9	12.6	15.7	12.6
Div yield (%)	3.8	4.1	3.0	3.0
ROE (%)	5.1	6.6	4.9	5.9
Net gearing (%)	na	na	na	na

Stock and Financial Data

Shares Outstanding (million)	800.0
Market Cap (RM'mil)	2,072.0
Book value (RM/share)	2.55
P/BV (x)	1.0
ROE (%)	6.2
Net Gearing (%)	na
Major Shareholders	Hap Seng Consolidated (53.0%) Innoprise Corp (15.0%)
Free Float (%)	47.0
Avg Daily Value (RMmil)	0.4

Price performance	3mth	6mth	12mth
Absolute (%)	-4.4	+7.0	+8.4
Relative (%)	-8.7	-2.8	-0.9



Investment Highlights

- **Hap Seng Consolidated held an analyst briefing last week in conjunction with the release of the group's 1QFY17 financial results.**

- **Operating profit of Hap Seng Plantations (HSP) surged by 95% YoY to RM46.2mil in 1QFY17 driven largely by a 37.6% increase in average CPO price and 61.8% climb in average palm kernel price. The group's FFB production rose by 9.6% YoY in 4MFY17. Average realised CPO price was RM3,268/tonne in 1QFY17 vs. RM2,375/tonne in 1QFY16.**

- **Key takeaways from the briefing:**

- **HSP believes that CPO prices are unlikely to fall below RM2,500/tonne in FY17F. The group thinks that average CPO price would be RM2,800/tonne in FY17F. Currently, HSP is selling CPO at spot prices. There are no buyers for CPO at future months. Year to date, average CPO price (MDEX price) has been RM2,928/tonne.**

- **HSP's FFB production is expected to decline by 3.0% in FY17F after bucking industry trends, falling by only 6.6% in FY16. Recall that the plantation industry in Sabah recorded a 15.3% contraction in FFB production in 2016 due to the lagged impact of El Nino.**

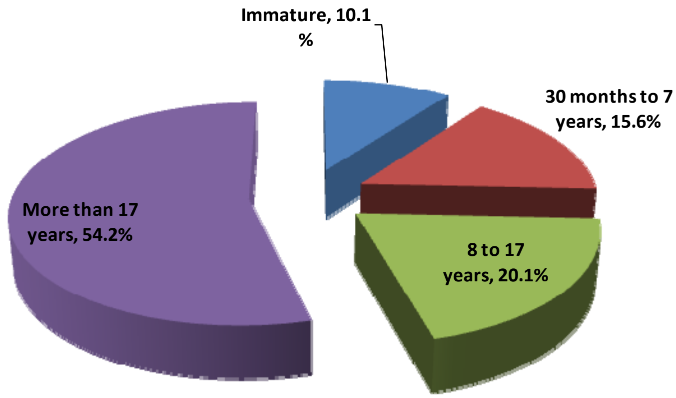
- **HSP is seeing a YoY slowdown in its FFB production in May. FFB yields are expected to soften in the coming two months due to the fasting and seasonal period. The second peak in FFB production is expected to take place in 3QFY17 or 4QFY17. FFB output is anticipated to be stronger in 2HFY17 compared with 1HFY17.**

- **HSP's production cost per tonne (ex-mill) is estimated to be RM1,300 to RM1,400/tonne in FY17F against RM1,159/tonne in FY16. This is due to the drop in FFB production and higher wages. HSP recorded a high production cost of RM1,558/tonne in 1QFY17 (1QFY16: RM1,498/tonne) due to increases in cost of repairs, maintenance and wages. The group carried out repairs and maintenance of some of its bridges and roads, which were damaged by the wet weather.**

- **Fertiliser costs are expected to decline in FY17F. Average fertiliser cost is estimated to be RM865/tonne in FY17F vs. RM1,100/tonne in FY16.**

- **HSP is interested in acquiring oil palm estates in Sabah. However, the issue is pricing. Recent market transactions valued planted landbank in Sabah at more than RM70,000/ha. HSP's cash reserves stood at RM161.6mil as at end-March 2017. The group has zero borrowings.**

CHART 1: AGE PROFILE OF OIL PALM TREES IN MALAYSIA



Source: Company

DECENT PLANTER

Hap Seng Plantations (HSP) is expected to benefit if CPO prices stay resilient. This is due to its relatively low production cost per tonne.

In terms of valuation, HSP is currently trading at an FY18F PE of 14.8x (based on consensus EPS of 17.5 sen) compared with IJM Plantations' 20.2x and TSH Resources' 18.5x.

HSP's balance sheet is clean. As the group has not embarked on any acquisition since its IPO, HSP has zero borrowings and cash reserves of RM161.6mil.

HSP declared a gross DPS of 8 sen in FY16, which was the same as FY15. The group's gross DPS ranged from a low of 8 sen to a high of 11 sen in the past five years. These translated into yields of 3.1% to 4.2%.

KEY TAKEAWAYS FROM BRIEFING

❑ ***FFB production to decline by 3.0% in FY17F***

HSP's FFB production rose by 9.6% YoY in 4MFY17. In comparison, CPO production in Malaysia climbed by 18.2% YoY in 4M2017.

In spite of the 9.6% YoY improvement in 4MFY17, HSP is expecting its FFB output to inch down by 3% in FY17F. The group's FFB production is anticipated to ease in the coming few months due to seasonal factors and fasting period.

The decline in HSP's FFB production in FY17F is in contrast to the upbeat production outlook given by the other plantation companies.

We believe that this is due to the fact that HSP was not adversely affected by the lagged impact of El Nino in FY16. Hence compared to other companies, the group may still be facing lingering effects of El Nino in FY17F.

HSP's FFB production only fell by 6.6% in FY16 compared with a contraction of 15.3% recorded by the industry in Sabah.

Interestingly, HSP's oil extraction rate (OER) dipped from 22.1% in 1QFY16 to 19.7% in 1QFY17. This was due to effects of heavy rains since October 2016.

❑ ***Production cost per tonne to increase in FY17F***

HSP's production cost is estimated to be RM1,300/tonne to RM1,400/tonne in FY17F compared with RM1,159/tonne.

The increase in production cost per tonne can be attributed to the drop in FFB production in FY17F and higher cost of wages, which could not be offset by the decline in fertiliser costs.

Dragged by a global glut, fertiliser prices have been soft. HSP's average fertiliser cost is envisaged at RM865/tonne in FY17F compared with RM1,100/tonne in FY16.

❑ ***Interested in M&As***

HSP is interested in acquiring plantation land in Sabah. However, the issue is pricing. Recent market transactions valued planted landbank in Sabah at more than RM70,000/ha.

Felda Global acquired 8,478ha of land in Sugut from Golden Land Bhd for RM655mil in FY15. The purchase consideration translated into an enterprise value of RM73,000 to RM74,000/ha.

HSP is not expected to face problems financing any acquisition of landbank as the group has cash reserves of RM161.6mil.

❑ ***Replanting about 1,412ha of oil palm trees in FY17F***

HSP is expected to replant about 1,412ha of ageing oil palm trees this year. Currently, about 54.2% of the group's planted areas consist of oil palm trees that are more than 17 years old.

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