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Small planters gaining attention

BY **Yong Yen Nie**

Current rising crude palm oil (CPO) prices not only indicate that palm oil players are likely to post strong earnings in the coming quarters, but have also caused most palm oil stocks to move up.

Usually, it is the palm oil players with big market capitalisation that draw the attention of investors, given their size and liquidity. The second-tier planters do not generate much buying interest because they are often illiquid.

This time round, however, the fund managers are seeking out the small planters in their quest for undervalued CPO stocks that have been off the radar screen.

Already, several small planters have seen a surge in trading activity. For example, TH Plantations Bhd (THP) and Cepatwawasan Group Bhd have leapt 10.9% and 12.5% m-o-m respectively.

By comparison, big cap IOI Corp Bhd has stayed at the RM5.80 level over the past month while Kuala Lumpur Kepong Bhd has risen 6.8% m-o-m.

THP, IJM Plantations Bhd and TDM Bhd also hit their 52-week highs of RM1.83, RM3.04 and RM2.76 respectively last Wednesday.

"Earnings-wise, the small players showed strong growth across the board in the previous quarter. In addition, their lower price-earnings ratio is making fund managers sit up and take notice. They are looking really attractive," says an analyst from the buy side.

Based on their latest financial results, the historical PER of these counters is in the single digit to low teens compared with the industry average of high teens.

"The PER gap between the large and small planters is widening, with the former getting more expensive," says an analyst.

Industry observers say generally, small plantation players trade at a discount due to several factors, including lower production yield, smaller landbank and tree age profile. THP, for instance, has trees with an average age of 18 years, which is relatively old compared with Genting Plantations Bhd's 12 years and IJM Plantations' 13 years.

Some small planters are hard to ignore as they are now deemed undervalued

"Some small players are also tightly held by a major shareholder or are state-owned, making their stock illiquid and hence do not usually generate a lot of investor interest," an industry observer says.

An analyst says because of their illiquidity, the prices of these stocks also tend to be more volatile.

REUTERS

Nevertheless, analysts opine that the low PER of some small players is hard to ignore, especially those whose fundamentals have improved and which are now deemed undervalued.

Most planters posted significant growth in their earnings in the previous quarter. Genting Plantations' net profit rose 31.7% to RM80.8 million while IJM Plantations' net profit in 2QFY2011 ended Sept 30 jumped to RM47.3 million from RM17.3 million a year earlier.

Apart from improved earnings, industry observers say some players are also looking attractive because of their growing cash pile. TDM, for example, had a cash balance of RM122 million as at Sept 30, 2010.

Recently, research houses have come up with reports on the smaller plantation players, highlighting their valuations.

RHB Research Institute Sdn Bhd, for instance, says THP — the plantation arm of Lembaga Tabung Haji — could be due for a re-rating, especially given the current strength of CPO prices.

Based on forecasts, THP is trading at 7.7 times FY2011 ending Dec 31 earnings per share. "Assigning it a PER of 11 times FY2011, which is the mid-point of its historical average, we arrive at

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a fair value of RM2.30, which is a 42% upside from current price levels.

"Even if we were to value THP at 11 times based on FY2011 consensus EPS, it would still imply a target price of RM1.90 or an upside of 20%, which does not even include its attractive dividend yield of 5% to 8% per annum," RHB Research says.

CIMB Research says the small Sabah planter Cepatwawasan is well placed to ride the CPO's uptrend and double-digit output growth in 2011 due to its young estates.

"Cepatwawasan appears undervalued as it is trading at a 21% discount to its net book value (NBV) of RM1.65 per share and an enterprise value per hectare of only RM35,097, much lower than the recent transacted value of RM59,280 per ha for planted estates in Sabah. Its share price is also 24% lower than the RM1.77 takeover price paid by MHC Plantations Bhd in 2005," it adds.

The research house says using recent transactions of estates as a guide, it derived a sum-of-parts value of RM2.60 per share for Cepatwawasan, but is putting a 20% discount on the stock due to its small market cap and low share liquidity.

"This places the stock at RM2.08, which works out to a forward PER of 14.6 times or a slight discount to the big cap Malaysian planters," CIMB Research says.

According to an analyst, the smaller planters are looking more attractive mainly because of rising CPO prices. "CPO prices are also expected to be sustainable due to poor weather conditions that will dampen productivity. This factor will keep the prices high," he says.

CPO prices broke past the RM3,000 per tonne level in November. YTD, average CPO prices have risen 20% to RM2,660 per tonne from RM2,221 per tonne a year earlier.

According to Malaysian Palm Oil Board (MPOB) statistics for November, palm oil production in Malaysia weakened 10.8% m-o-m and 8.6% y-o-y to 1.46 million tonnes during the month. YTD, local palm oil production stood at 15.8 million tonnes, about 2% lower than the 16 million tonnes recorded in the same period last year.

AmResearch says it is likely that Malaysia's palm oil production will fall below the MPOB's forecast of 17.6 million tonnes for 2010. "This means palm oil inventory in January 2011 will start at a low level," it says.

This also means the small planters are likely to remain in the investing limelight a little longer. E