

30 August 2024

Agriculture | Plantation

Sarawak Oil Palms (SOP MK)

Buy (Maintained)

Undervalued Performer; Maintain BUY

Target Price (Return): MYR3.60 (+28%)
 Price (Market Cap): MYR2.82 (USD583m)
 ESG score: 2.3 (out of 4)
 Avg Daily Turnover (MYR/USD) 0.37m/0.08m

- **Maintain BUY, with new MYR3.60 TP (from MYR3.25), 28% upside and c.4% FY25F yield.** Sarawak Oil Palms' 1H24 earnings beat our and Street estimates, accounting for 58-62% of full-year forecasts. As production continues to ramp up and unit costs moderate, we expect the company to chart stronger numbers in 2H24. Its valuation remains attractive at 7.5x FY25F P/E, vs the peer range of 6-10x.
- **2Q24 core earnings improved 11% QoQ (+106% YoY),** on the back of higher FFB production (+3% QoQ, +11% YoY), CPO ASP (+6% QoQ, +5% YoY) and lower-than-expected unit costs (-16% QoQ, -18% YoY). These drivers, alongside the higher-than-expected interest income in 1H24 (+17% YoY vs our forecast of -22%) resulted in 1H24 core profit growing 99% YoY.
- **2Q24 FFB output rose 3% QoQ and +11% YoY, bringing 1H24 FFB output growth to +10.6% YoY.** YTD-July, FFB growth remained solid at +9% YoY, driven by the peak production cycle. This is above our +7.3% YoY FY24 FFB growth forecast and SOP's original +5-6% YoY guidance. Management however, remains wary of the weather situation in the northern regions, but we note that these areas make up only 8-10% of the total planted area. Taking this into account, we tweak up our FY24 FFB growth estimates slightly to +8% YoY but maintain our 3-4% growth for FY25F-26F.
- **Estimated 2Q24 unit costs have dropped 16% QoQ and 18% YoY,** lower than our flatish assumption for FY24-26, thanks to the improvement in output as well as moderation of fertiliser costs (1H24 requirements bought at prices that were 10% lower YoY). We believe SOP has applied 45-50% of its fertiliser requirements in 1H24 and expect fertiliser application to be on track in 2H. As such, we lower our unit cost assumption by 6% for FY24-25 and 7% for FY26.
- **Downstream outlook.** Although no disclosure was given, management guided that this segment improved QoQ and YoY, and expects it to stay in the black for the rest of the year, driven by its second refinery, which produces higher quality oils (+5% premium), bringing the total downstream capacity to 690k tonnes (+53%). Management however, remains wary of the competition from Indonesian downstream players, given the country's advantageous tax structure. We expect SOP's refinery utilisation rate to remain at 75%.
- **We raise FY24F-26F earnings by 12%, 14% and 14%** after imputing a higher interest income and FFB growth forecast, while expecting unit costs to continue its downward trend in 2H24, on the back of increasing output.
- **Our new TP** is based on 11x 2025F P/E, with a 14% ESG discount built in. SOP is trading at 7.5x FY25F P/E, at the lower end of its peer range of 6-10x.

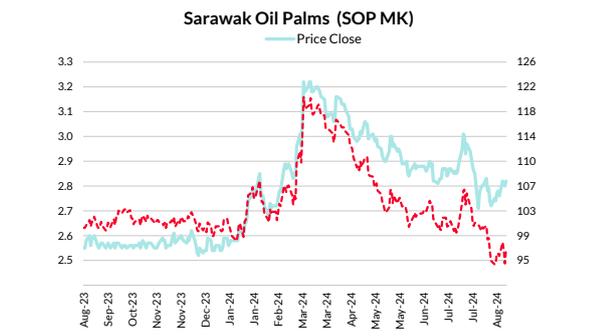
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	8.9	(4.1)	(4.1)	(0.7)	11.5
Relative	(4.8)	(5.9)	(7.1)	(7.3)	(2.2)
52-wk Price low/high (MYR)				2.52	3.22



Source: Bloomberg

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (MYRm)	5,308	5,124	4,585	4,531	4,638
Recurring net profit (MYRm)	501	302	388	337	336
Recurring net profit growth (%)	8.9	(39.8)	28.5	(13.2)	(0.3)
Recurring P/E (x)	4.95	8.32	6.48	7.46	7.48
P/B (x)	0.8	0.7	0.7	0.6	0.6
P/CF (x)	3.32	6.82	3.84	4.74	4.81
Dividend Yield (%)	3.2	1.7	3.5	3.5	3.5
EV/EBITDA (x)	2.53	4.69	3.58	3.62	3.31
Return on average equity (%)	15.7	8.8	10.6	8.6	8.0
Net debt to equity (%)	net cash	1.8	net cash	net cash	net cash

Source: Company data, RHB

Overall ESG Score: 2.3 (out of 4)

E: GOOD

While Sarawak Oil Palms is committed to no further development on peat areas, 45% of its landbank is still planted on peat. The company has reported a reduction in greenhouse gas (GHG) emission intensity since 2017 for its estates but has seen an increase of such from its milling and downstream operations. The company is fully Malaysian Sustainable Palm Oil-certified for its mills and estates.

S: MODERATE

Sarawak Oil Palms is committed to free, prior and informed consent for all its employees. Its fatality accident rate has remained low, while the lost time injury frequency rate continues to trend lower. The company has not had any major labour issues in the last two years.

G: GOOD

33% of SOP's board members are independent, and 44% of its members are women. Additionally, it provides full disclosure on director remuneration, which includes salaries and bonuses and on a named basis. The company has an in-house investor relations team and holds briefings regularly, embodying good transparency and disclosure practices.

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Figure 1: SOP's results review

FYE Dec (MYRm)	2Q23	1Q24	2Q24	QoQ (%)	YoY (%)	1H23	1H24	YoY (%)	Comments
Revenue	1,175.3	1,325.5	1,139.5	(14.0)	(3.0)	2,382.4	2,465.0	3.5	Thanks to higher FFB production (+11% YoY), CPO ASPs (+3% YoY) and PK ASPs (+9% YoY)
EBIT	60.5	121.7	135.7	11.5	124.2	131.5	257.4	95.7	
EBIT margin (%)	5.1	9.2	11.9			5.5	10.4		
EI	(2.9)	(15.3)	0.8	>100	>100	(8.0)	(14.6)	(82.6)	EIs include a fair value gain on derivatives of MYR7.4m and bearer plants written off of MYR9m, offset by a fair value gain on biological assets of MYR1.6m
Pretax profit	66.8	112.4	144.7	28.8	>100	134.3	257.1	91.5	
Pretax margin (%)	5.7	8.5	12.7			5.6	10.4		
Tax	(16.2)	(28.9)	(35.4)	(22.4)	>100	(37.0)	(64.3)	(73.7)	
Effective tax rate (%)	(24.3)	(25.7)	(24.4)			(27.6)	(25.0)		
Minority interest	(2.5)	(4.0)	(3.7)	8.2	(48.7)	(5.0)	(7.7)	(54.9)	
Net profit	48.1	79.5	105.7	33.0	>100	92.3	185.1	>100	
Core profit	51.0	94.8	104.9	10.7	>100	100.3	199.7	99.2	Above our and Street expectations, at 58-62% of FY24F
Net margin (%)	4.3	7.2	9.2			4.2	8.1		
Operational Stats									
FFB production	264,453	286,086	294,694	3.0	11.4	525,188	580,780	10.6	Above our projection of +7.3% YoY and management's original guidance of +5-6% YoY
CPO production	86,293	94,909	94,808	(0.1)	9.9	169,638	189,717	11.8	
PK production	18,315	20,771	19,744	(4.9)	7.8	36,205	40,515	11.9	
CPO price, MYR/tonne	3,948	3,913	4,157	6.2	5.3	3,932	4,035	2.6	
PK price, MYR/tonne	2,324	2,267	2,826	24.7	21.6	2,342	2,547	8.8	

Source: Company data, RHB

Figure 2: Key assumptions

	FY22	FY23	FY24F	FY25F	FY26F
FFB production, tonnes	1,193,846	1,226,566	1,324,473	1,374,322	1,419,309
% change	-4.2%	2.7%	8.0%	3.8%	3.3%
Effective CPO price (MYR)	5,136	3,832	3,900	3,800	3,800

Source: Company data, RHB

Emissions And ESG

Trend analysis

In 2023, Scope 1 emissions decreased to 269k tonnes of CO2 equivalents (2022: 282k tonnes of CO2 equivalents) and Scope 2 emissions also decreased to 24.5k tonnes of CO2 equivalents (2022: 38.7k tonnes of CO2 equivalents)

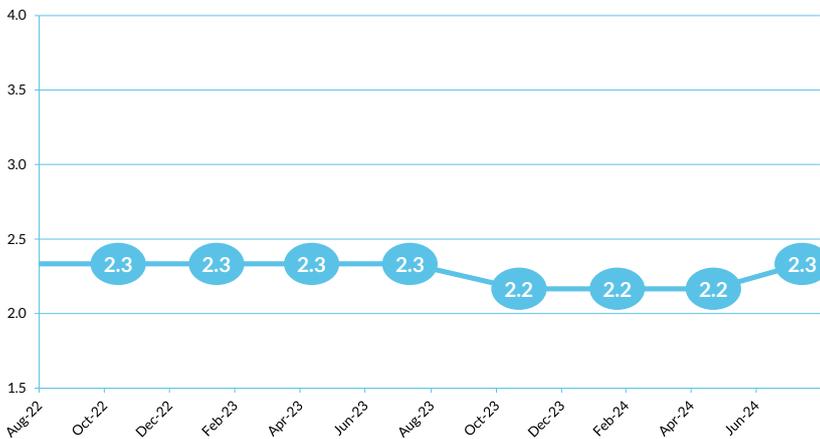
Emissions (tCO2e)	Dec-21	Dec-22	Dec-23
Scope 1	237,413	281,756	269,481
Scope 2	31,877	38,742	24,956
Scope 3	na	na	-
Total emissions	269,290	320,498	294,437

Source: Company data, RHB

Latest ESG-Related Developments

- **Sustainability certification:** As of end 2023, 100% of SOP's operations are MSPO certified.
- **Traceability:** As of end-2023, SOP managed to achieve 45.0% traceability to plantation for CPO and 47.0% for PK and getting all the POMs ISCC re-certified.
- **Reducing GHG emissions:** SOP is committed to reducing GHG emissions with the installation of methane capture facilities (five more to be completed from 2024) to reduce emissions at all mills.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-08-12	Buy	3.25	2.83
2024-05-19	Buy	3.30	2.90
2024-02-29	Buy	3.20	2.84
2023-11-29	Buy	2.95	2.58
2023-11-20	Buy	2.80	2.59
2023-08-28	Buy	2.85	2.55
2023-07-23	Buy	3.00	2.60
2023-05-22	Sell	2.00	2.46
2023-04-18	Neutral	2.50	2.46
2023-03-01	Neutral	2.75	2.55
2022-11-28	Buy	3.00	2.60
2022-09-11	Buy	3.00	2.54
2022-08-28	Buy	3.10	2.75
2022-08-10	Buy	4.65	2.68
2022-05-24	Buy	7.25	3.93

Source: RHB, Bloomberg

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(1) they do not have any financial interest in the securities or other capital market products of the subject companies mentioned in this report, except for:

Analyst	Company
-	-

(2) no part of his or her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.



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