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NEUTRAL

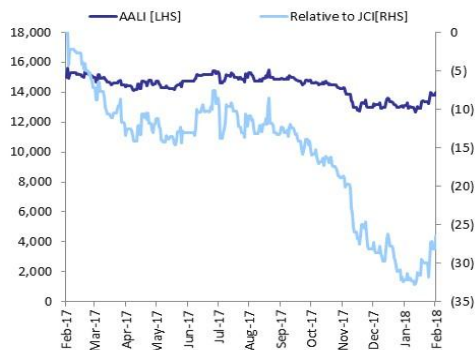
Plantation

Ramping Up The Biodiesel Usage

LSIP relative to JCI Index



AALI relative to JCI Index



Source : Bloomberg



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We met with Mr. Dono Boestami, the President Director of the Oil Palm Plantation Fund Management Agency (BPDPKS), and discussed several issues in the palm oil industry, including Indonesia’s biodiesel program and smallholders’ replanting program. The key takeaways are as follows:

Need to boost biodiesel volumes in the future. From our visit to the Oil Palm Plantation Fund Management Agency (BPDPKS), they stressed the need to boost biodiesel volumes in FY18 in order to support CPO demand and prices. Factors such as China’s preference for soy products, higher import taxes on edible oils in India, and Europe’s black campaign against palm oil have undermined palm oil demand. As such, Indonesia (the largest consumer of palm oil) will need to play a key role in absorbing any lost demand by increasing its biodiesel usage.

Does BPDPKS have enough funds to provide biodiesel incentives? Yes, they stated that they have more than enough funds to support the biodiesel program, but the overhang lies in the regulation. Higher crude oil prices have reduced the current biodiesel incentive to below Rp3,000/liter. The government targets biodiesel absorption of 3.5mn KL in FY18 (+48% YoY), although it is believed realization will be below as rollout of the non-PSO sector is likely to be slow. Assuming FY18 target collection of Rp13tn (70% of it reserved for the biodiesel program), a CPO price of MYR2,700/ton, and a USD60/bbl oil price, we estimate biodiesel volume of 4.0mn KL.

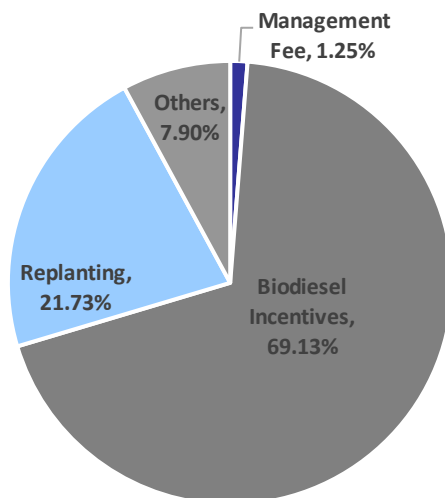
What to expect next? The government targets to broaden the scope of the biodiesel incentive to the non-PSO sector (mining equipment, trains and military vehicles) starting in May 18. As such, we should expect the government to revise Presidential Regulation No.61/2015 on the collection and use of oil palm estate funds soon. Stipulated changes include: 1) streamlining the regulation to incorporate both PSO and non-PSO into the content, 2) revised technical details on the incentive mechanism for both PSO and non-PSO and 3) capping the biodiesel incentive at a maximum of Rp4,000/liter for both PSO and non-PSO. Based on our checks, there have been no reported technical issues related to blending requirements for non-PSO; hence the overhang now lies in the regulation.

Smallholders’ replanting program. The agency has also commenced the replanting program for smallholders and plasma farmers in Oct 17. The goal is to replant a total of 2.4mn Ha, with a replanting target of 185k Ha set for FY18. Among the replanting criterion are: 1) conformance to land legality aspects and sustainability principles, 2) ISPO certification, 3) FFB productivity < 10 tons/Ha and plant density < 80 trees/Ha and 4) the requirement for smallholders to be in a cooperative and have a partner or legal entity. If those criteria are met, the agency will grant a replanting incentive of IDR25mn/Ha.

Maintain neutral. We maintain our neutral stance on the plantation sector in FY18 with a CPO price assumption of MYR2,700/ton.

Company	Ticker	Rec	Target	Market	P/E (x)		P/BV (x)		ROE (%)
			Price (Rp)	Cap. (RpBn)	2018F	2019F	2018F	2019F	2018F
London Sumatra	LSIP IJ	BUY	1,700	8,627.3	8.8	11.0	1.0	0.9	9.8
Astra Agro Lestari	AALI IJ	HOLD	14,800	26,897.5	14.1	14.2	1.4	1.3	9.7
Sampoerna Agro	SGRO IJ	SELL	2,240	4,564.7	16.1	15.1	1.3	1.2	8.0

Exhibit 1. FY18 Funds Usage Breakdown – Rp13tn



Source: BPDPKS

Exhibit 2. Biodiesel Sensitivity Calculation

Assumptions:					
Total Funds Collected by CPO Fund (IDRbn)	13,000				
% Funds Allocated for Biodiesel Subsidy	70%				
Funds Allocated for Biodiesel Subsidy (IDRbn)	9,100				
Funds Allocated for Biodiesel Subsidy (USDmn)	684				
Sensitivity Analysis with Brent Crude Oil Price					
Brent Oil Price (USD/bbl)	30	40	50	60	70
MOPS Crude Oil Equivalent (USD/bbl)	34	45	55	66	76
MOPS Crude Oil (USD/ton)	291	379	468	556	645
MOPS + Alpha (USD/ton)	301	393	484	576	667
CPO Benchmark Price (MYR/ton)	2,700	2,700	2,700	2,700	2,700
CPO Benchmark Price (USD/ton)	643	643	643	643	643
Conversion cost of CPO to FAME (USD/ton)	100	100	100	100	100
Transportation Cost (USD/ton)	26	26	26	26	26
CPO-based price (USD/ton)	768	768	768	768	768
Biodiesel Incentive (USD/ton)	467	376	284	193	101
Biodiesel Incentive (IDR/Liter)	5,471	4,399	3,327	2,255	1,182
Volume of Incentivized Biodiesel (mnKL)	1.7	2.1	2.7	4.0	7.7
Domestic CPO Consumed (mn tons)	1.4	1.8	2.4	3.5	6.7

Source: Danareksa Sekuritas Estimate

