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Plantation stocks 'due for major correction'

Fund manager sees palm oil prices hitting 2008 lows

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MALAYSIAN plantation stocks have been on a six-year rally. Tan Teng Boo thinks a serious correction is long overdue.

The managing director of global fund manager icapital.biz has long been bearish on world equity in general and Bursa Malaysia in particular, but has usually focused on the big picture. Last week, he turned more specific.

Mr Tan is not the only doomsayer out there, but he has been bearish for quite a while. In many ways, it's a reflection of world equity markets in general and a consequence of the global printing of money after the global financial crisis.

This time, the fund manager has zoomed in on plantation stocks.

First off, Mr Tan points at the physical palm oil market which has been bearish since 2011: October futures have even dipped below RM2,000 (S$790) a tonne.

Mr Tan thinks that the price could reach its 2008 lows "which is a long way down from RM2,000". Yet, he notes that the KLSE Plantation Index "has hardly fallen from its all-time highs".

It should be noted, however, that Mr Tan wrote this before the government scrapped export taxes on palm oil last Friday, a move that sent three-month futures' prices back over RM2,000 a tonne.

Even so, one suspects that the fund manager would still remain suspicious of the high valuations of certain plantation stocks. Case in point: Genting Plantations, the plantation arm of the gaming conglomerate, is capitalised at RM7.8 billion and posted net earnings of RM311 million for the last 12 months.

But "if a price-earnings ratio of 15 is applied, the market capitalisation of Genting Plantations would only be around RM4.6 billion".

Or take heavyweight and institutional investor favourite KL Kepong. Mr Tan notes that it is capitalised at RM23.5 billion and reported earnings of RM1.08 billion. Again, affixing a 15 times PE ratio to the stock, Mr Tan says, it would be worth only "around RM15 billion".

United Plantations, another institutional favourite, is capitalised at RM5.7 billion with earnings of RM263 billion. Mr Tan's market barometer of a 15 times PE ratio would value the firm at RM3.9 billion.

Mr Tan concludes soberly. "Whether you call it a bubble, speculation or irrational exuberance, the fact of the matter is the same.

"They are overvalued, some by a humongous amount, some by a lesser quantum. And when exit time comes, the exit door will be very small and many will be squashed in the stampede to get out."