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Inside insights

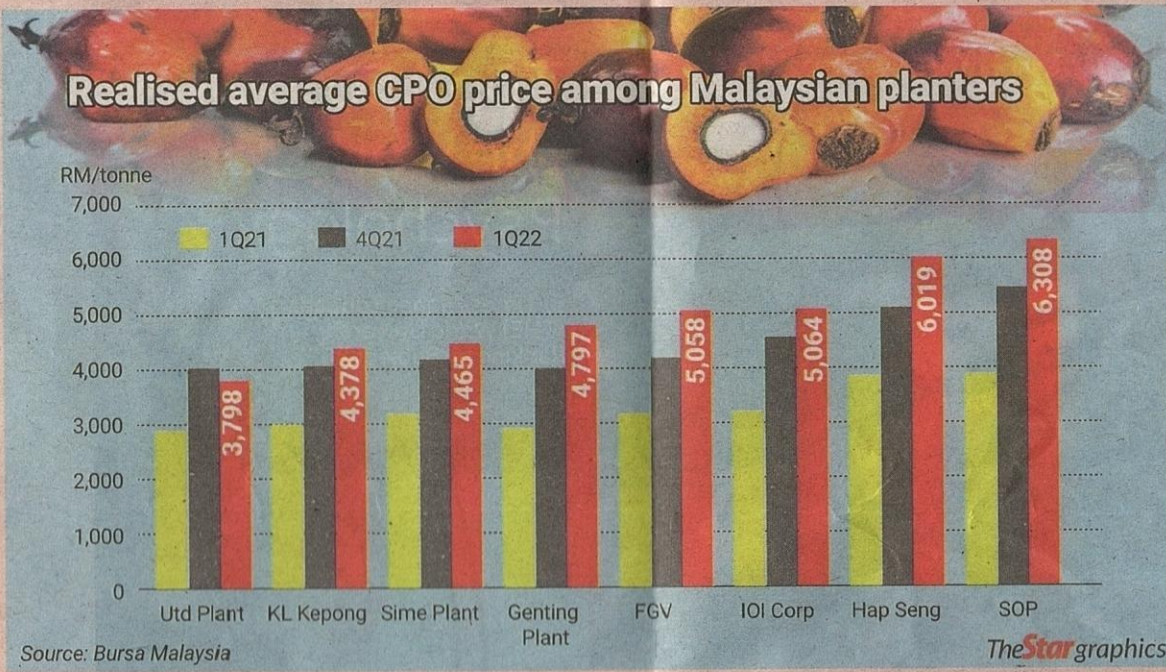
Falling short of expectations

THE Bursa Malaysia Plantation Index (BMPI) has performed remarkably well since the start of 2022 on the back of rising crude palm oil (CPO) prices due to supply constraints in other vegetable oils, the weaker ringgit and curtailed production as a result of labour issues, as well as challenging weather conditions.

Since the start of the year, the BMPI is one of the best-performing indices among the Bursa Malaysia index series, rising by 21.5% in the first five months of the year to close at 7,963.98 points on May 31, 2022.

During the same period, according to prices provided by the Malaysian Palm Oil Board (MPOB), the CPO price increased 29.7% to RM6,680 per tonne from RM5,150 per tonne as at end-December 2021.

Based on the benchmark third-month futures contract, CPO prices



More than 50% tax?

The palm oil companies, despite record-high prices for their products, are not necessarily laughing all the way to the bank like how the glove makers were in 2020/21 during the Covid-19 pandemic.

Today, the cost of production has ballooned not only due to the higher taxes imposed by the state and federal government, which can either be an absolute amount or based on a certain fixed rate which is dependent on the CPO price threshold, but also the income tax rate of 24% as well as a potential additional tax of 9% in the form of the prosperity tax if this year's chargeable income is more than RM100mil.

On a hypothetical basis, assuming a Sabah-based plantation company has a revenue of RM600mil based on 100,000 tonnes of CPO produced this year and fully exported at an average price of RM6,000 per tonne, the company

market futures contract, CPO prices have increased by 34.2% to RM6,312 per tonne from RM4,705 per tonne as at the end of last year.

The rally among plantation stocks also saw major listed companies either hitting multi-year highs or all-time highs, as the BMPI too surged to levels last seen in 2014.

Benefiting from lower taxes

Malaysia is the world's second-largest producer of CPO with production estimated to reach between 18.5 million and 19 million tonnes this year.

On the other hand, Indonesia, with its large land mass and the global leader in CPO production, is expected to see a total output of almost 50 million tonnes this year.

However, due to the local demand for cooking oil, Indonesia has taken several steps to secure domestic supply and the ban on palm oil exports, which ended early this week, was one of them.

In March, Indonesia raised the maximum palm oil export levy to ensure domestic cooking oil supply as well as to control domestic market prices.

A higher progressive rate was introduced if the reference price for the CPO is at least US\$1,050 (RM4,613) per tonne to a maximum levy of US\$375 (RM1,648) for prices above US\$1,500 (RM6,590).

Previously, the Indonesian gov-

ernment imposed a maximum export levy of US\$175 (RM769), which kicks in when the reference price hits US\$1,000 (RM4,393) per tonne.

Indonesian palm oil exporters are also required to pay an export tax on palm oil shipments on top of the export levy.

The maximum export tax is currently US\$200 (RM879) a tonne. Hence, assuming a CPO price of US\$1,500 (RM6,590) and above, an Indonesian planter is subjected to a total tax of US\$575 (RM2,526) per tonne.

This reduces the planter's profit significantly.

Effectively, the taxes and levies translate to about 38.3% if prices are at US\$1,500 (RM6,590) per tonne.

Malaysia too imposes various taxes and this includes an export tax of 8% when prices exceed RM3,450 per tonne, a windfall profit tax of 3% when prices exceed RM3,000 in the Peninsula and RM3,500 in Sabah and Sarawak.

In addition, a cess of RM16 per tonne is also imposed on CPO produced. In addition, planters in Sarawak and Sabah are subjected to a sales tax of 5% and 7.5%, respectively, if the CPO price is above RM1,500 per tonne.

Hence, assuming the same CPO price of RM6,590 per tonne in

Malaysia (equivalent to the US\$1,500 per tonne in Indonesia), a Peninsula-based planter will be subjected to about 9.9% in all sorts of taxes and levies, while a planter based in Sarawak and Sabah will have in total 14.6% and 17.1% taxes imposed on them.

Indeed, at the current CPO market price, the effective tax rate for Malaysian planters is much lower than in Indonesia.

Realised price matters most

Based on data provided by the MPOB, the average CPO price for the recently concluded first-quarter 2022 (1Q22) reporting quarter was RM6,051 per tonne.

However, a check on major listed companies announcing their quarterly results showed that among the eight large companies that were reviewed, the average price ranged from a low of RM3,798 per tonne for United Plantations Bhd to as high as RM6,308 per tonne for Sarawak Oil Palms Bhd or SOP.

In essence, the realised price among the eight companies ranged from a discount of 37.2% to a premium of 4.3% from MPOB's average price during the quarter as seen in the chart.

In 4Q21, when prices were less volatile, these planters too found it difficult to match the average

MPOB price of RM5,154 per tonne, as the eight planters reviewed had an average price that was between a discount of 21.8% to a premium of 6.1%.

Compared with the same quarter in 2021, based on MPOB's average price of RM3,895 per tonne in 1Q21, the realised average price range was between RM2,892 per tonne to as high as RM3,885 per tonne.

All eight companies had a lower realised price than what MPOB's average price showed for the quarterly periods.

In an upward price cycle, planters do know that the good times like these are never ever-lasting, and hence, most of them would have made forward market sales when prices started to climb above RM4,000 per tonne.

As prices went parabolic due to cost pressures and supply shocks, so did the cost of production, especially those related to fertilisers, while disruption was also experienced in harvesting the fresh fruit bunches.

Hence, for some, although the time the forward sale was done was "a good price" for delivery in the future months, the actual cost of production when the fruits were harvested was much higher than the time when the future price was locked-in, resulting in a margin squeeze.

exported at an average price of RM6,000 per tonne, the company will make some RM1.6mil in cess payments, fork out RM45mil in sales tax to the state government, pay RM48mil for the export levy, and suffer another RM7.5mil in windfall tax.

Assuming the cost of production is RM2,800 per tonne, the company would make some RM217.9mil in pre-tax profit.

As this is well above the RM100mil threshold for the one-off prosperity tax and assuming the chargeable income is the same as the pre-tax profit, the taxman will collect RM71.9mil in total taxes this year.

The company itself will show a net profit of RM146mil. As a percentage of operating profit of RM320mil, the company's total compliance cost (income tax, prosperity tax, windfall tax, cess payment, sales tax, and export levy) of RM174mil is more than the profit attributable to the shareholders – an effective tax rate of 54.4%.

No wonder planters are not comfortable with the sky-high CPO price as it has only resulted in them being subjected to a never-ending increase in compliance cost, be it in the form of taxes, levies, or cess payments.

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