Ratings

MARC Ratings affirms ratings on Sime Darby Plantation

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MARC Ratings has affirmed Sime Darby Plantation Berhad's (SD Plantation) corporate credit rating at **AAA** and Perpetual Subordinated Sukuk Programme rating of up to RM3.0 billion at **AA**$_{IS}$. The two-notch rating differential between SD Plantation's corporate credit rating and the Perpetual Sukuk programme rating is in line with MARC Ratings' methodology on notching principles of subordinated and hybrid instruments. The ratings carry a **stable** outlook.

The ratings affirmation considers SD Plantation's very strong market position in upstream oil palm cultivation, well-established track record as an integrated oil palm player, and strengthening balance sheet structure. The ratings also incorporate healthy cash flow generation stemming from sizeable and geographically diversified planted areas, despite crude palm oil (CPO) price volatility. The corporate credit rating benefits from a one-notch uplift on implicit support from parent Permodalan Nasional Berhad.

SD Plantation remains the world's largest oil palm plantation company with a total planted area of 577,344 ha (Malaysia: 51%; Indonesia: 33%; Papua New Guinea/ Solomon Islands (PNG/SI): 16%) as at end-June 2023. MARC Ratings views positively the group's favourable tree maturity profile: the average oil palm age at its plantations currently stands at 12.2 years with about 29% of its trees aged between nine to 18 years (prime age) and 44% aged below eight years (immature and young matured age).

The rating agency notes that SD Plantation practices consistent replanting to ensure continued healthy fresh fruit bunch (FFB) production. In this regard, SD Plantation undertakes a replanting programme of 4%-5% p.a. of its total plantation area, largely focusing on its Malaysian and Indonesian plantations. Replanting cost of about RM950 million in 2023 is largely funded internally.

For 1H2023, group performance was impacted by a 21.4% y-o-y decline in CPO price to RM3,824/MT that led to a revenue decline of 16% y-o-y to RM8.4 billion. Coupled with the prolonged labour issues in Malaysia and the higher labour and fertiliser costs, pre-tax profit fell to RM736 million (1H2022: RM2.2 billion). This has also led to a lower group operating profit margin of 7.4% (1H2022: 18.6%). The rating agency notes that SD Plantation's downstream segment has continued to record low margins and expects margin pressures to remain given the stiff competition in the segment.

MARC Ratings projects CPO price to range between RM3,700/MT and RM3,900/MT over the next 12-15 months; given the current production cost of around RM2,500/MT, SD Plantation has sufficient buffer to generate positive cash flow. While the group has largely addressed labour shortages for its plantations, the required labour expertise needed for field work, particularly in harvesting, has not been fully met. This has weighed on production metrics with FFB production declining by 3% y-o-y to 3.86 million MT in 1H2023. MARC Ratings understands that it would take nine to 12 months to optimise harvesting capabilities.

The group's cash flow from operations (CFO) of RM695 million (1H2022: RM1.1 billion), coupled with cash balances of RM668 million, is sufficient to meet its near-term loan obligations without resorting to external funding. Consolidated borrowings stood at RM8.2 billion, translating to an adjusted gross debt-to-equity ratio of 0.43x as at end-1H2023. CFO debt and interest coverages stood at 0.2x and 4.3x. The group is expected to continue with its deleveraging plan through proceeds from non-core asset disposals. MARC Ratings projects SD Plantation's leverage position to improve to about 0.35x.