



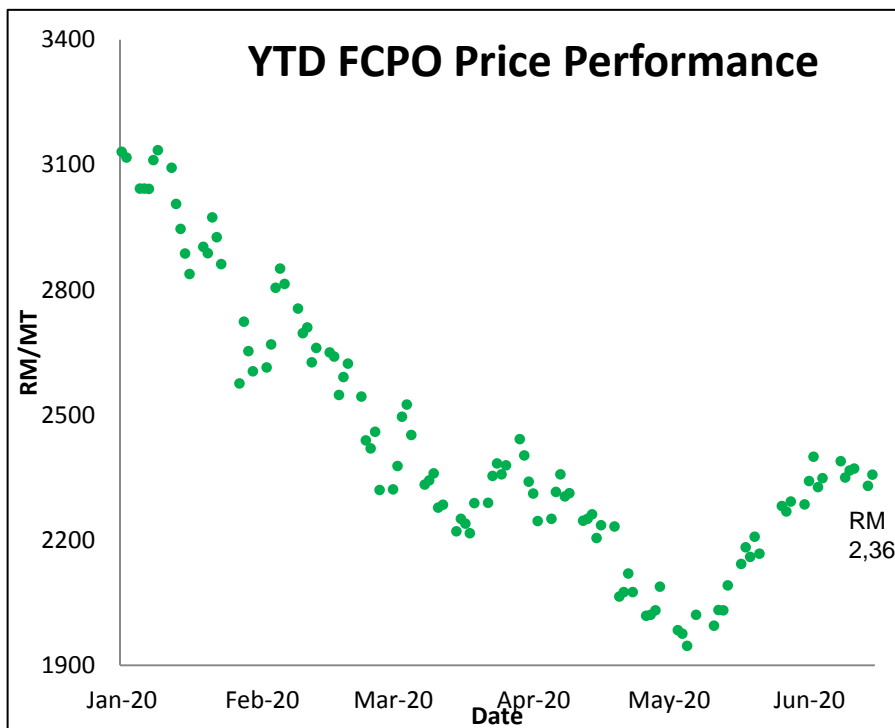
## KF Spotlight : FCPO – Glass Half-Full Halfway Through 2020 By Aron Liew, CFA and Zainal Aiman

In 2019, the benchmark crude palm oil price broke the RM3,000 level for the first time since March 2017 in the last quarter of the year, thanks to positive news on B20 biodiesel mandate by the Malaysian government, improved exports figure, expectation of tighter palm oil supply and a weaker Malaysian ringgit.

Entering into 2020, FCPO kick-off the new year on a positive note, sustaining above the RM3,000 level for the first half of January, on the spillover strength from rival US soybean oil which driven by the positive US-China Phase One trade deal ceremony. FCPO price reached its year's high of RM3,134/MT on 10 January, its highest level since January 2017.

However, the narrative began to change once news on COVID-19 outbreak began to take over as nations around the world implemented forms of lockdowns or restricted movements. This has disrupted the global supply chain and demand. FCPO price fell to a year-low of RM1,946/MT on 6 May 2020, a 30% plunge from the year's high.

Prices began to recover slightly in May as countries around the world began to ease their lockdown measures and both Indonesia and Malaysia reiterated their commitment to implement their biodiesel mandates.



|  |                       |
|--|-----------------------|
| Last Price (RM)                          | 2,367<br>(18/06/2020) |
| High (RM)                                | 3,134<br>(10/01/2020) |
| Low (RM)                                 | 1,946<br>(06/05/2020) |
| Average (RM)                             | 2,442                 |
| YTD-Performance Change (%) (18 Jun 2020) | -22.44                |

Source : Bloomberg

What are the factors that affected FCPO prices so far?



## The Positive Impacts



### Biodiesel Mandate Announcement

- The bullish sentiment surrounding the local palm oil market in the final quarter of last year was carried over into the beginning of this year, making the FCPO market able to sustain the RM 3,000 level at least for the first half of January.
- The positive sentiment was brought by the announcement made by Malaysian government last year to increase the local biodiesel mandate from B10 to B20 for the national biodiesel program.
- The B20, which is a blending of 20% palm methyl esters with 80% of petroleum diesel in the transport sector in Malaysia, was intended to boost the domestic consumption as the mandate is expected to utilise 1.3 million tonnes of crude palm oil.
- In addition, Indonesia also announced its intention to reduce the fossil fuel consumption by 165,000 bpd and implement B30 and B50 programme by January and December this year respectively.



### Supportive Malaysian CPO Export Duties

- Despite the challenging market environment in 2020, Malaysia palm oil market at least can have some breath when the local government has lowered the tax on crude palm oil exports for three times so far this year.
- Except for February this year where the export duties were increased from 5% to 6%, the tax were then lowered from April onwards in a move to boost palm oil exports.
- In April, the export duties were decreased to 5% from 6%, while in May, the tax were lowered to 4.5%.
- In its latest move, the export duty on crude palm oil was lowered to 0% after the reference price for Malaysian palm oil in June was calculated at RM2,122.77, down from RM2,460.89 amid the slump in global edible oil demand.

Source : The Edge Market, Jakarta Post and MPOB Website



## The Negative Impacts



### COVID-19 Pandemic

- In late December 2019, a new virus called COVID-19, which was first detected in the Wuhan province of Mainland China, began to spread swiftly across the world, infecting million of citizens.
- As no vaccines were found yet, and due to the contagious nature of the virus between humans, many countries in the world had imposed lockdown measures to curb the spread of the virus.
- The lockdown measures had indeed turned this health problem into an economic problem, causing global demand-side disruption including palm oil.
- Major palm oil consumers like China, India and Europe exercised lockdown in their nations, causing the drawdown in palm oil consumption.



### Indian Restriction

- Palm oil shipments to the top buyer India has plunged to fresh record low this year amid the COVID-19 lockdown and punitive import curbs.
- In early January 2020, a diplomatic tension between Malaysia and India had caused lower palm oil demand from India since India is one of the largest palm oil buyers in the world.
- Indian government had urged their palm oil refiners and traders to stop buying Malaysian palm oil in retaliation to the former Malaysian prime minister's criticism over India's action towards Kashmir issue.

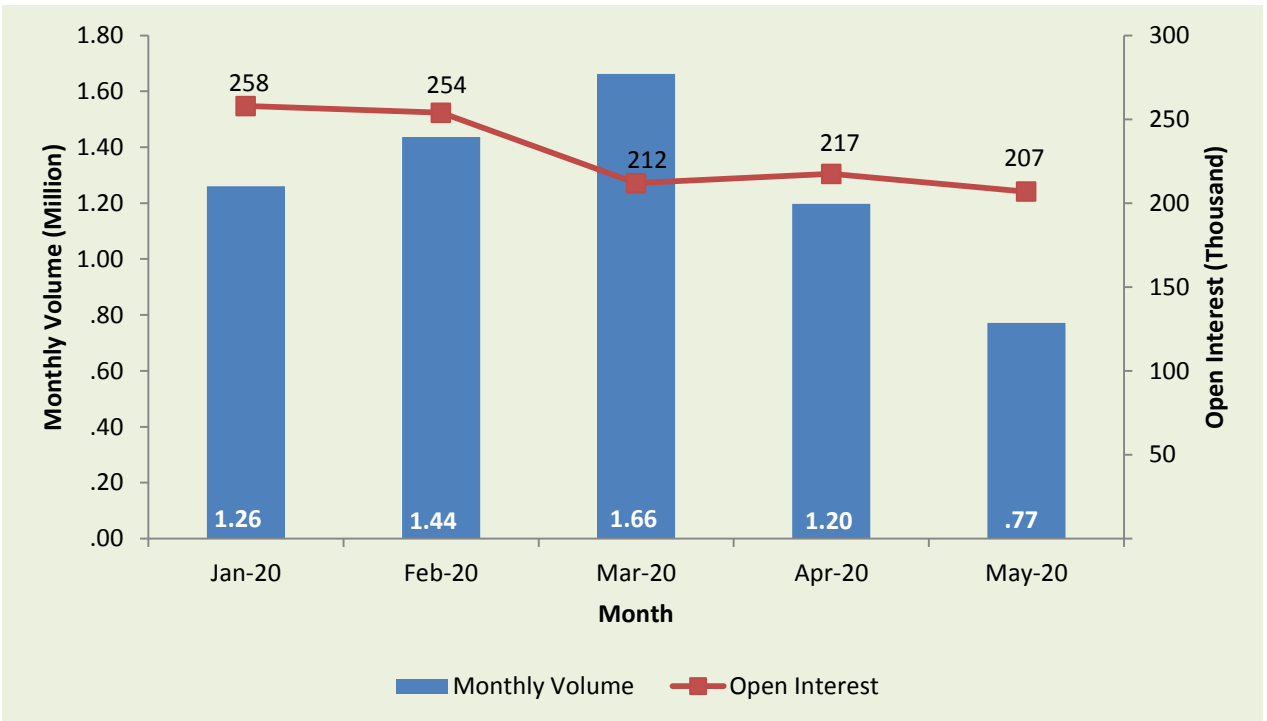


### Crude Oil Prices Plunged

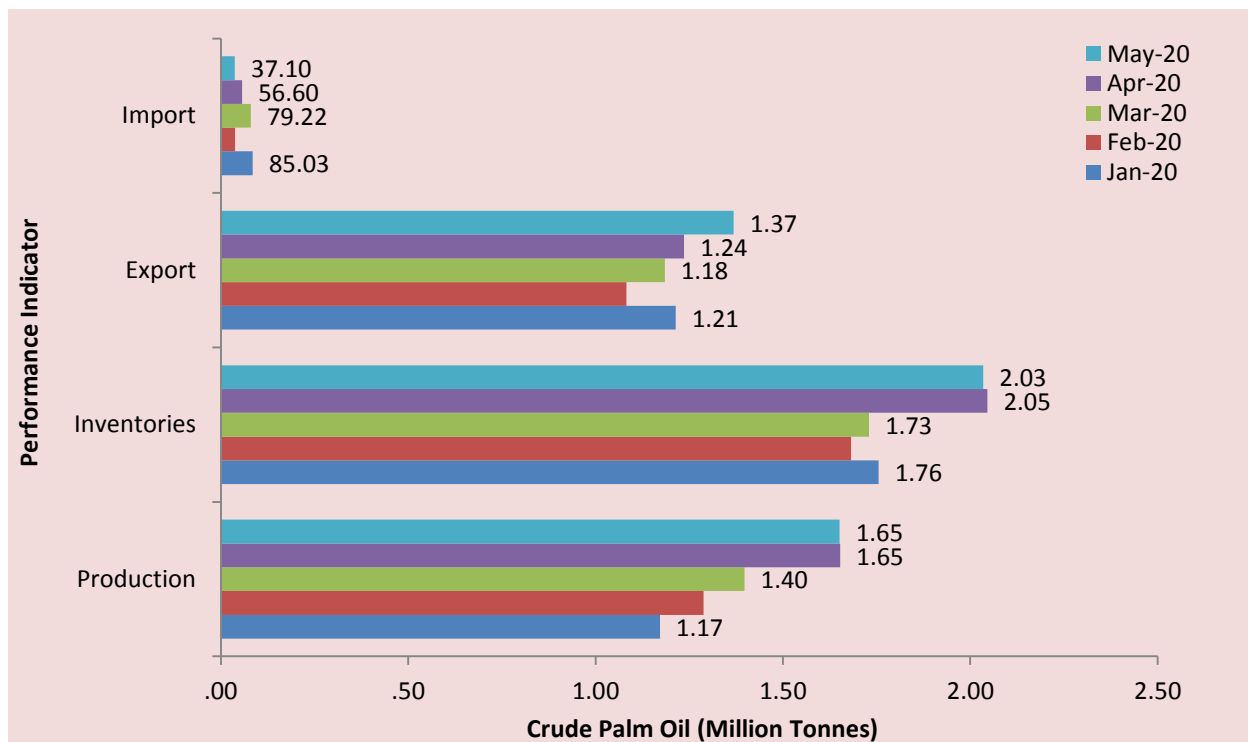
- In early January, crude palm oil prices gained some support due to spillover strength from crude oil prices amid the escalating geopolitical conflicts in Iran with the killing of General Soleimani.
- However, local palm oil began to face some pressure when crude oil prices plunged to a new historic low when the production cut talks between OPEC and its allies collapsed in early April.
- Any deterioration in crude oil prices can cause crude palm oil prices to be under pressure as crude palm oil is used as feedstock in biodiesel fuel.

Source : The Edge Market and Reuters

## Volume and Open Interest in FCPO Market



## Key Performance Indicator of Malaysia's Physical Palm Oil Market



Source : Bursa Malaysia Derivatives and MPOB

## Factors that may impact FCPO price for the rest of the year

### 1) The effect of COVID-19 pandemic on the global supply-demand chain

As the prospect of a vaccine is expected to be developed in at least 12-18 months, global economies and industries will continue to be hit hard by the new normal. Global supply chain disruption in commodities sector, including palm oil is likely to continue and be impacted by the decline in global demand for CPO. According to MPOB, palm oil demand for food and processing in China, and biodiesel in the EU, had slowed down due to the ongoing lockdown measures implemented globally. However, more countries globally are easing their lockdown measures and this will lead to an improvement in demand.

### 2) Implementation of Biodiesel Mandates

The Malaysian mandate to manufacture biofuel with a 20% palm oil component - known as B20 - for the transport sector was first rolled out in January, and was set to be fully implemented across the country by mid-June 2021. Nevertheless, the country, through the Malaysian Biodiesel Association, has decided to delay the implementation amid the Movement Control Order (MCO) adopted by the Malaysian government but has recently announced that it will resume the roll out in September 2020.

Meanwhile in Indonesia, the government recently unveiled a \$186 million injection as well as hiked its palm oil export levy by \$5/mt to \$55/mt in May as it pledged to continue with its B30 biodiesel mandate. However, the recent plunge in crude oil prices in Q1 2020 made the edible oil less appealing as a biodiesel feedstock. The Malaysian Biodiesel Association also told Reuters that it expected exports for palm biodiesel to fall to 500,000 tonnes this year, down from 609,777 tonnes in 2019.

### 3) Prospect of Lower Production Might Provide Some Cushion

Despite the setbacks that cloud the market, several positive factors can provide some breather for the local palm oil market. One of them is the prospect of lower production figures in 2020. The latest May figures from MPOB has already begun to show a mere reduction in production of 0.10% from 1,652,771 tonnes in April to 1,651,328 tonnes in May. This is due to the impact of the low fertiliser application in 2019 and dry weather in the middle of 2019, resulting in diminished oil palm fruit yields in 2020.

The brief suspension of Sabah oil palm estates and mills due to COVID-19 pandemic also adds to the disruption of supply. In addition, as a labour-intensive industry where more than 70% of the country's plantation workers come from outside Malaysia, the ongoing COVID-19 pandemic would further increase the labor shortages as palm oil companies are generally unable to recruit new foreign workers and thus causing more palm oil supply disruption.

*Source : MPOB, The Edge Market and The Star*

## 4) Performance of Malaysian Ringgit

Malaysian Ringgit has been underperforming against a basket of currencies for the most part of this year, though it has recovered some ground and strengthened against the USD in May. As an open economy, Malaysia remains vulnerable to external weaknesses brought upon the COVID-19 pandemic and trade disputes among the major economies. This could weaken the Malaysian Ringgit, which is a positive factor for CPO price. The weaker currency may entice global demand for crude palm oil as it may be viewed as relatively cheaper to other related commodities.

## 5) Expected Improvement in Palm Oil Exports to India

Following a formation of new government in Kuala Lumpur, the animosity between Malaysia and India is seen dissipated which eventually can improve the palm oil demand to the world's second largest palm oil buyers. In mid May 2020, Malaysia agreed to sign a deal to purchase a record of 100,000 tonnes of Indian rice, while according to Reuters, leading Indian importers contracted up to 200,000 tonnes of crude palm oil from Malaysia which are to be shipped in June and July. In addition, the local palm oil is also now available at discount to supplies from Indonesia which on May raised its palm oil export levy by \$5 per tonne.

## 6) Zero Export Tax Making Malaysian Palm Oil More Attractive

In managing the country's stock level and stabilize the CPO price, Malaysian government had announced on early June a 100% exemption on export duty on crude palm oil, crude palm kernel oil and processed palm kernel oil from July 1, 2020 to Dec 31, 2020. The decision was announced as part of an economic stimulus package known as National Economic Recovery Plan (Penjana) to revitalize industries badly hit by the coronavirus pandemic including palm oil. According to many analysts, the move can further improve Malaysia's palm oil exports as the local CPO is now about \$15 cheaper than rival Indonesia, which this month raised its export levy by \$5 to \$55 per tonnes.

*Source : MPOB, The Edge Market and The Star*

## A Short Term Price Outlook for FCPO



Source : Bloomberg

FCPO has been on a downward trend since the beginning of the year and reached a year low of RM1,939 in end-April. Based on the MACD, a bullish divergence was formed, resulting in an upward trend since early-May.

In the near term, we expect to maintain its upward momentum and we see strong resistance level at RM2,400 level. If this level is broken, expect FCPO to rise further and may challenge the next resistance level of RM2,540. We continue to maintain a positive outlook for FCPO price in the near-term and expect FCPO price to trade around the range of RM2,200 to RM2,400.

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