MANAGEMENT DISCUSSION AND ANALYSIS

OPERATIONAL REVIEW

GROUP’S OIL PALM AGE PROFILE

GROUP TOTAL

- 8,772 ha (15%)
- 29,731 ha (49%)
- 20,186 ha (33%)
- 1,881 ha (3%)

Weighted average age of palms 9.5

<table>
<thead>
<tr>
<th>Group</th>
<th>FY '16</th>
<th>FY '17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mature (≥20 years)</td>
<td>480,591</td>
<td>347,448</td>
</tr>
<tr>
<td>Mature – Prime (8 – 20 years)</td>
<td>308,416</td>
<td>398,416</td>
</tr>
<tr>
<td>Mature – Young (4 – 7 years)</td>
<td>848,059</td>
<td>842,435</td>
</tr>
<tr>
<td>Mature (≤20 years)</td>
<td>347,448</td>
<td>398,416</td>
</tr>
</tbody>
</table>

CROP PRODUCTION AND PROCESSING

<table>
<thead>
<tr>
<th>Group</th>
<th>FY '16</th>
<th>FY '17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Own FFB</td>
<td>203,758</td>
<td>195,606</td>
</tr>
<tr>
<td>Outside FFB</td>
<td>271,126</td>
<td>273,985</td>
</tr>
<tr>
<td>Malaysian Mill Operations</td>
<td>76,520</td>
<td>73,763</td>
</tr>
<tr>
<td>Indonesian Mill Operations</td>
<td>53,281</td>
<td>27,317</td>
</tr>
<tr>
<td>Group</td>
<td>257,039</td>
<td>277,172</td>
</tr>
</tbody>
</table>

GROUP'S OIL PALM AGE PROFILE

- Immature (1 – 3 years)
- Mature – Young (4 – 7 years)
- Mature – Prime (8 – 20 years)
- Mature (≤20 years)

FFB PRODUCTION (MT)

FFB PROCESSING (MT)
AREA PLANTED AND AGE PROFILE

As at 31 March 2017, the total oil palm planted area in the Group stood at 60,570 hectares. 58.5% of the total planted area is located in Indonesia while the balance 41.5% is located in Sabah, Malaysia. From the total planted area, approximately 82.4% or 49,917 hectares are either young (4 to 7 years) or prime mature (8 to 20 years) with higher yield potential. 14.5% or 8,772 hectares are classified as immature (1 to 3 years). Only 3.1% or 1,881 hectares are above 20 years old and these palms will be replanted accordingly with new and advanced planting materials. The weighted average age profile for the Group is 9.5 years old with the Malaysian and Indonesian operations at 14.4 and 5.9 years old respectively.

CROP PRODUCTION

The total FFB production for the Group in the reporting year was 862,435 mt, which was 1.7% higher than the previous reporting year. FFB production in the Malaysian operations recorded a marginal dip of 3.4% as compared to the previous year to end the year at 464,019 mt. The decline was a result of the prolonged dry weather attributed to the El Niño phenomenon compounded by the ongoing pragmatic replanting programme adopted by the Group. The average yield achieved for the year was 20.1 mt per hectare. A recovery in crop production can be anticipated with the end of the lagged effects from the El Niño phenomenon.

FFB production in the Indonesian operations totalled 398,416 mt, which was 8.4% higher than the prior year. The increase was mainly due to the larger areas attaining maturity, despite some palms affected by the prolonged dry weather, especially in the more matured palms. The Indonesian operations which were still at start-up phase achieved an average yield of 13.9 mt per hectare for the year under review.

CROP PROCESSED

The Group processed a total of 1,010,111 mt (2016: 994,802 mt) in the reporting year. In the Malaysian operations, a total of 659,625 mt (2016: 684,349 mt) of FFB inclusive of external crop, were processed by its four (4) palm oil mills to produce 135,275 mt (2016: 144,875 mt) of crude palm oil (“CPO”) and 32,672 mt (2016: 34,742 mt) of palm kernel (“PK”). The drop of 3.6% in FFB processed was attributed to the decrease in the availability of crop. Processing in Indonesian operations hit 350,486 mt which was 12.9% higher crop processed than previous year. The higher volume of crop processed was attributed to more palms attaining maturity. 76,405 mt (2016: 74,629 mt) of CPO and 13,676 mt (2016: 12,740 mt) of PK were produced in the Indonesian mills.

The average oil extraction rate (“OER”) achieved by the mills in the Malaysian operations was slightly lower at 20.5% (2016: 21.2%) mainly due to poorer fruit formation during the dry period, while the kernel extraction rate (“KER”) was 5.0% (2016: 5.1%). On the other hand, the average OER and KER achieved in Indonesian operations were 21.8% (2016: 24.0%) and 3.9% (2016: 4.1%) respectively.

The kernel crushing plant in the Malaysian operations processed 32,202 mt (2016: 35,311 mt) of palm kernel to produce 14,669 mt (2016: 16,272 mt) of crude palm kernel oil (“CPKO”) and 15,876 mt (2016: 17,455 mt) palm kernel expellers (“PKE”). The average extraction rates for CPKO was 45.6% (2016: 46.1%). Across in Indonesia, the kernel crushing plant which was into its fourth year of operations processed 12,394 mt (2016:12,742 mt) of palm kernels to produce 5,206 mt (2016: 5,311 mt) and 7,187 mt (2016: 6,724 mt) of CPKO and PKE respectively. The average extraction rates achieved in the Indonesian operations was 42.0% (2016: 41.8%).

Overall, the Group achieved average OER and KER of 21.0% (2016: 22.1%) and 4.6% (2016: 4.8%) respectively, while the average extraction rates achieved for CPKO was 44.6% (2016: 44.9%).

OIL YIELD PRODUCTIVITY

Productivity based on oil yield realised for the Malaysian operations was 4.1 mt (2016: 4.4 mt) per hectare in tandem with the decline in production volume, in which both the concurrent years were subjected to the prolonged dry weather attributed to the El Niño phenomenon. The El Niño impact was experienced as early as February 2015 in the Sugut Region, where 65% of the Malaysian operations are located, thus affected both crop production and extractions. Notwithstanding the above, the Group’s oil yields realised in 2017 and 2016 were noted to be 19% and 24% higher than the national oil yield average of 3.7 mt and 3.3 mt per hectare respectively over the same period. The Indonesian operations realised an overall oil yield of 3.0 mt (2016: 3.5 mt) per hectare. This was a result of more young areas with start-up yields coming into maturity, in addition to these palms affected by the prolonged dry weather. For the coming year, the Group’s oil yield is expected to improve after the lagged effects from the El Niño phenomenon.
REPLANTING AND NEW PLANTING

A total of 805.43 hectares (2016: 900.25 hectares) were replanted during the year in the Malaysian operations. The Group continued to adopt a pragmatic replanting policy. Replanting was carried out both in times of low as well as high palm product prices in order to achieve the desired oil palm age profile for the Group. Failure to implement this critical aspect of plantation management will inevitably lead to stagnating yields and declining crop production. All the replanting continued to be carried out in accordance with the environmentally friendly “zero burning policy” where old palm stands are felled, chipped and left to decompose at site. Other best management practices pertaining to replanting were also carried out in accordance with the Group’s agricultural policy. The replanting programme involves only the Group’s internally produced IJM DxP planting materials which have demonstrated early and high yields along with other desirable attributes.

Almost all of the plantable land in the Malaysian operations have been planted. There are no further land-bank for expansion. The Indonesian operations have reached the tail end of its development project. The balance of land-bank approximately 3,000 hectares will be cultivated over the next two years as conditions permit.

CAPITAL EXPENDITURE

The Group recorded capital expenditure of RM90.7 million (2016: RM131.3 million) as stated in the property, plant and equipment section of the financial statements. The expenditure consisted mainly of the development in the Indonesian operations, including the construction costs of the second palm oil mill and related infrastructure establishment. The reduction of amount spent as compared to the prior year was primarily due to the timing of the expenditure incurred for establishing the mills. On plantation development expenditure, the Group incurred RM31.9 million in the current year compared to RM61.7 million incurred in 2016. The lower spend was due to lesser immature areas.

RESEARCH AND DEVELOPMENT

The Group’s Quality, Training and Research Centre (“QTRC”) located in Sandakan with its sub-station in Sugut are testimony that the Group recognises the imperatives of research and development in order to contribute towards sustaining and achieving higher productivity in the longer term and also to implement environmental stewardship in the Group’s upstream practices. While the main focus is directed on oil palm trials for better crop yields, QTRC also provides in-house agronomy and advisory services along with the promotion of integrated pest management (“IPM”). The QTRC sub-station in Sugut Region provides the necessary agro-technical support for the Group’s estates in that region. It also renders support to the Group’s various sustainability initiatives, including engaging with various project collaborators and visiting stakeholders as well as sharing technical know-how to smallholders and surrounding communities as part of the Group’s out-reach programme. A similar support team was established in IPS estate for the Indonesian operations.

The Group’s long term oil palm breeding, selection and progeny testing programme will enable it to improve the oil palm planting materials to meet its present and future requirements to ensure better yields and other desired oil palm characteristics. The seed production unit in QTRC is able to produce over 1.5 million DxP seeds annually derived from Deli Dura and AVROS pedigrees. The seed production unit had been accredited with SIRIM’s MS157:2005 certification. Selected mother palms from the genetic blocks located in Sijas Estate had also been certified by SIRIM and were being used for commercial seed production. For the last 14 years, the entire oil palm planting material requirements in the Group’s Malaysian operations including in all the replanting programme, as well as the Group’s allowable requirement in the Indonesian operations were all planted with IJM DxP planting materials.

Fertiliser recommendations were based on soil and foliar analysis coupled with technical observations from field visits. The recommendations are prepared by the agronomist and the team in QTRC as part of agronomic and technical advisory services for the estates. QTRC staff were also responsible for estate field audits, pest and disease census and reviewing the quality grading of crops received by the palm oil mills. In addition, QTRC also acted as a training centre for many agronomic and plantation management programmes for the Group’s employees.
OUTLOOK

The Group remains confident that the long term prospect for the palm oil industry is promising as palm oil continues to be the most edible oil, healthy vegetable oil, a price leader and with the demand fundamental forecasts continue to be positive. The global vegetable oils demand is expected to grow at a Compounded Annual Growth Rate ("CAGR") of 3% to over 200 million metric tonnes by 2025. Palm oil’s market share will be driven by a robust long term fundamentals with population growth and per capita income continue to chart its growth, rendering the impetus for higher palm oil demand in the long run.

Notwithstanding the above, the business relating to commodities will have factors that the Group will not be able to control. Changes in macroeconomic policies along with other government interventions throughout the world will continue to have major consequences on both the financial and commodity markets. Looking ahead, palm product prices will continue to be influenced by its relative pricing vis-a-vis other competing edible oils such as soybeans as well as crude petroleum oil. Developments on macroeconomic policies, especially in the USA and the biofuel policies can also cause knee-jerk reactions to prices.

Since the last quarter of year 2016 the impact of the El Niño had eased. This was evident by the increase in crop production. Consequently, commodity prices had softened significantly.

Moving forward, the Group will intensified efforts focused on harvesting and milling activities in the Group’s Indonesian operations while returning to sustain high yields post the El Niño phenomenon from its Malaysian operations. Growth in FFB production is expected from the young plantings and larger areas coming into maturity from the Indonesian operations while a pragmatic replanting programme will continue to be the mantra for the Group as matured oil palm areas are replanted with better planting materials in the Malaysian operations.

The availability of workers remains one of the key challenges for the plantation sector. In order to sustain high productivity and address labour issues, the Group focuses on implementing site-specific agro-management practices and continue to expand the use of mechanisation focused on site-specific in-field crop evacuation while introducing competitive harvesting rates and adopting different approaches in engaging and recruiting workers.

By going beyond traditional boundaries in plantation management, the Group shall continue exploring digitalisation in certain day-to-day upstream activities to increase efficiency and productivity and reduce dependency on workers. This will help to enhance harvesting supervision, reduce paperwork and improved transparency.

The Group’s oil palms tree will continue to be nourished using science-based approach in nutrient management while numerous soil and water conservation initiatives will be implemented and enhanced at site-specific areas in order to sustain yields and improve productivity.

As the Group moves forward, it will continue to deliver its value proposition as a resilient and a highly competitive mid-sized plantation player with respectable social environmental footprints. The Group is confident that with continuous improvements in productivity and it holding steadfast in implementing best management practices together with cost effective strategies, it would be able to ride out of any challenges ahead. The Group expects the profitability level for the coming financial year to be satisfactory barring unexpected adverse volatility in both palm product prices and foreign exchange rates.

JOSEPH TEK CHOON YEE
Chief Executive Officer & Managing Director

Passion, perseverance and purpose driven