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O32.SI - Full Year 2016 Olam International Ltd Earnings Presentation

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PRESENTATION

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

Good morning, ladies and gentlemen. Welcome to Olam International's results briefing on our full year results and quarter results ended December 31, 2016. My name is Hung Hoeng from Investor Relations at Olam International.

I'm pleased to have with me once again the management, senior management team with me. They are seated on my left. If I may just begin to introduce all of them to you. I'm sure you are familiar with them but please bear with me.

On the extreme left at the table is our Group CEO and Co-Founder, Sunny Verghese. On his right is the Executive Director and Group COO, A. Shekhar. On his right is President and Group CFO, N. Muthukumar. And we're also pleased to have some of our senior colleagues in our midst as well in this room.

Just a note on the forward-looking statements; it's taken as noticed and read.

Our agenda today is on the highlights for the full year results, followed by the segmented analysis, as well as the value chain analysis of our results which we give once a year, and the key takeaways.

Without further ado, may I invite Muthu onboard to give you the presentation of our full year results? Thank you.

Neelamani Muthukumar - *Olam International Limited - President, Group CFO*

Thank you, Hung Hoeng. Good morning, ladies and gentlemen. I'm very pleased to welcome you all for the quarter and year ended December 2016 financial results for Olam International.

I'm pleased to announce a very strong set of results for Olam for year ended December 2016 considering a very challenging and volatile market conditions and global commodity markets. Let me move on to the key highlights for 2016.

We had PATMI at SGD351.3 million, which is on very fundamental and significantly improved operational performance, and also due to lower exceptional losses as compared to 2015. But more importantly, the key operational metric that we track, which is operational PATMI, grew 23.1% year-on-year to SGD364 million and grew 155% in Q4, more importantly, to SGD102 million as compared to SGD40 million the same period last year.

We had all our continued effective borrowing initiatives, which are taken during the year and the previous year, had borne fruit and that has resulted in net reduction in our interest cost, and we continue to focus on improving the debt tenure and mix going forward.

We had substantially higher net operating cash flow of SGD1 billion as compared to SGD155 million in 2015. And the FCFF grew by SGD1.6 billion, even though we are at negative SGD418 million at the year end due to increased CapEx investments of close to SGD1.4 billion.

We have continued to execute on our three-year strategic plan for the period 2016 to 2018, and we have been investing both organic and inorganic, primarily in the grains and animal feed business, namely the acquisition of the wheat milling and pasta manufacturing assets in Nigeria, our continued CapEx investment in the new initiative in this platform, which is the animal feed processing plant, and we have -- we had during the year acquired Brooks peanut shelling company in the US, and we have continued to invest in coffee plantations in Brazil, Tanzania, Zambia and Laos, and also continue to invest in our plantations in Gabon both in palm and rubber.

During the year, we have significantly focused on improving shareholder returns. We are pleased to announce that the Board of Directors have recommended a final dividend of SGD0.03, which put together with the interim dividend already announced of SGD0.03 becomes a total of SGD0.06 per share for the full year 2016, as compared to $0.06 that we had announced for 18 months' period for the prior period which was FY2015.

We had also bought close to SGD95 million of shares at very attractive levels, which we are holding now as treasury shares. With this, we hold total treasury shares of SGD190 million in our balance sheet.

Moving on to P&L analysis. We grew the volume during the year by 15% to 14.4 million tonnes, grew revenue by 8% to SGD20.5 billion. The net gain on fair value and biological assets post the restatement that we have had in terms of the change standards from IFRS 41 to IFRS 16 has resulted in only the dairy upstream assets remaining in the biological assets. The rest of the bearer plants have moved on to the PPE, with the residual amount that is there is only fair valuation of the herd that is there for our dairy upstream business in Uruguay and Rusmolco. And also, fair valuation of the fruits on trees, which is there in the almond orchards in Australia.

The EBITDA has grown 11%, the key operation metric for us, to SGD1.2 billion, as compared to SGD1.085 billion for the prior period. Depreciation, amortization had increased as expected because of the various investments that we have done in terms of acquisition of ADM cocoa assets late [2015] (corrected by company after the call), the wheat milling and pasta manufacturing assets in Nigeria, and the Brooks peanut shelling asset that we bought in the US, and predictably, the depreciation and amortization has grown 32% to SGD353 million.

But what is heartening to see is that all our various measures that we have done during the year, as highlighted earlier, has resulted in a net reduction in the interest cost by SGD50 million, even though the overall net debt for the year increased by SGD1.4 billion. And that had resulted in a 10% reduction year-on-year.

The taxation was at SGD94 million. And if we are to really look at taxable profits year-on-year, our effective tax rate has dropped close to 3%. Our ETR effective tax rate now is at 20.5%, as compared to 23.2% for the last year.

Overall, the operational PATMI has grown to SGD364 million, which is a 23% growth year-on-year, as compared to SGD296 million the prior year.

It is very heartening to see that two strong segments to have really fueled the EBITDA growth, which is the confectionery and beverage segment, which had ADM cocoa assets which was fully integrated during the year, as well as the food staples and packaged foods segment which are an all-round improved performance year-on-year.

Moving on to the EBITDA and invested capital analysis on a consolidated basis. We talk about the overall EBITDA at SGD1.2 billion, at an overall invested capital of SGD16.6 billion, 7.7% return at the consolidated level, marginally down from 8.4% year-on-year. Point to be noted here is, despite an increase of SGD2.2 billion in increase in invested capital, the EBITDA there you see has only marginally dropped by 0.7%.

The increase in fixed capital primarily was due to acquisition of wheat milling and peanut shelling assets, as I highlighted earlier, as well as our continuing investments in organic, both in upstream and midstream assets.

The increase in working capital was primarily due to higher volumes. As I'd highlighted, there was 15% increase year-on-year on higher volumes. And despite both organic and post-acquisitions, and also compounded by higher commodity prices, especially in cocoa, coffee and cotton during the year.

Moving on to segmental analysis. Edible nuts, spices and vegetable ingredients had an overall very good year, except tomatoes, that we had called out earlier in Q2 and Q3 already.

Almonds, which have been doing very well and highly profitable, was -- had a lower contribution compared to prior year due to lower almond prices during the year. However, the peanut business in the US, including the acquired business of Brooks during the year, have all done better than expectation.

Hazelnuts, cashew business have also done very well and compared to plan. And the US dehydrated business, the pepper business in the rest of the world, as well as the dehydrated onion business in Egypt, all have done at plan or better, barring the tomatoes business, which we believe continue to face headwinds due to supply/demand conditions and market overhang on low prices. We expect that trend to continue until the first half of this year.

Overall invested capital increased by SGD180 million on a year-on-year basis, primarily due to the fixed capital investment that we did for acquisition of the peanut shelling assets in the US, it was close to $100 million or SGD140 million.

Moving on to confectionery and beverage ingredients segment. Here the EBITDA rose 43%, with strong contribution both from the cocoa and coffee business. The cocoa results obviously had the consolidation of the cocoa processing business that we acquired from ADM and which had actually performed better than expected, with strong tailwind from good product ratios, although some of it was offset by a lower performance from the cocoa supply chain business.

Here is a tale of two stories. Basically, one is that most of our cocoa bean volumes, which are prior year, was through third party, has now become feedstock for the captive processing business. So the margins hitherto which we had booked in cocoa supply chain are now booked under the cocoa processing assets. That's the number one point. And that has also impacted overall volumes for the cocoa -- for this segment as the third party -- hitherto third-party volumes are now going into the captive processing. And what we book as sales is only the processed volumes, which are lower than the absolute bean volumes that are transferred for processing.

Second part of it is, especially in Q4, the trading conditions have been very against us, and that has negatively impacted both supply chain and trading business in cocoa. And as we speak, that trend is continuing. But in coffee, both midstream and the supply chain business have performed very strongly, and that has been one of the best years we had so far. And heartening to note that the coffee business has also started well in the current year and are positioned to deliver well for the current year as well.

The invested capital grew by [SGD429 million] (corrected by company after the call), primarily driven by the higher working capital both on account of higher prices in cocoa and coffee and also higher volumes of coffee that we are carrying at the year end. Fixed capital also increased due to continued investments that we are doing in coffee plantations across Brazil, Tanzania, Zambia and Laos, and expansion of our very successful soluble coffee business both in Vietnam and Seda in Spain.

Moving on to food staples and packaged foods business. It's very heartening to see a full turnaround of this segment this year. Almost all platforms performed very well. And that has resulted in a 56% absolute EBITDA growth year-on-year in this segment.

There was strong performance from wheat milling operations in West Africa and also the origination business in grains and from Black Sea, the rice trading, the sugar trading, and the dairy supply chain business all delivered very strong results.

The businesses which were underperforming the prior year, which was primarily the palm supply chain and refining business in Mozambique, the dairy upstream business, especially in Uruguay, and the packaged foods business in West Africa, all had turned around during the year and have delivered an improved performance. And they are in the right trajectory to deliver better in 2017.

Overall, the invested capital grew by SGD1.3 billion as compared to last year. Fixed capital was up, mainly due to the acquisition of the wheat milling assets in Nigeria, as I talked about, continued CapEx in the animal feed processing business in Nigeria, the expansion of our wheat milling business in Ghana, and our continued investments of our planting of palm plantations in Gabon. The working capital increased due to higher volumes in grains and sugar trading businesses.

Moving to this segment, industrial raw materials, ag logistics, and infrastructure. You will notice that we have re-christened the segment from just being an industrial raw materials segment to an industrial raw materials, ag logistics and infrastructure. This is primarily to reflect the businesses that we are now trying to do under the overall umbrella of Gabon SEZ platform. And there we are looking at investment in ports, related logistics, warehousing, and silo infrastructure. And we believe that this better reflects the nature of the business that this segment will address going forward.

During the year, the EBITDA was at SGD135 million, down 27%, primarily on lower contribution from cotton and wood products. I had called out earlier, in Q2 and Q3, that the cotton supply chain business and trading business in the US face some headwinds, and that is continuing to have this volatile trading conditions as we speak.

Overall, the wood products business has had reduced margins due to macroeconomic conditions and more so, especially in the last quarter when in India there was this demonetization initiative that has resulted in further illiquidity of the teak business in India, and that has resulted in lower margin for the wood products business.

However, this was partly offset by higher contribution from Gabon SEZ. But what we believe is that both cotton and wood products business are well-positioned and they will -- we hope that they will deliver better performances in 2017.

The invested capital went up by SGD303 million, primarily due to increase in working capital in cotton, because of higher volumes in cotton as well as higher prices. Fixed capital was more or less flat because we had recovered some of our associate investment in Gabon SEZ, but partly offset by our continued investment in planting rubber in Gabon.

I move on to the value chain analysis. As Hung Hoeng had talked about, we present this slice of our business performance on the value chain basis, which is primarily on upstream supply chain and midstream slices.

The first is the upstream segment. In upstream, as you know, we have almond plantations in Australia and the US. We have coffee plantations in Brazil, Tanzania, Zambia and Laos. We have palm plantations in Gabon, we have rubber plantations in Gabon. We have rubber -- palm and rubber plantations through one of the investments in West Africa, in SIFCA. We also have broad-acre row crops planting, which is rice farming in Nigeria as well as peanut farming in Argentina.

So, during the year, the EBITDA declined to SGD79 million, compared to SGD155 million prior year, primarily due to the lower contribution in almond because of lower prices in almond both in Australia and the US, but partly compensated by improved performance from NZFSU.

Most of you will recall that we had restructured the NZFSU business the prior year and we had taken up a restructuring cost, one-time restructuring cost. And I'm heartened to say that the NZFSU business has really turned around very well and it is better than planned in terms of all key operational metrics.

On the overall invested capital, it grew by SGD690 million, primarily on account of almond, coffee, palm and rubber plantation investments during the year.

Moving on to supply chain. We had a SGD503 million of EBITDA as compared to roughly SGD600 million of EBITDA last year. The drop of SGD100 million is again a combination of two things. As I called out earlier, there was a lower performance from cotton supply chain business, especially in the US, that had impacted this segment, as well as partly impacted by a lower performance in contribution from the commodity financial services by around SGD10 million at the EBITDA level.

But at the cocoa supply chain level as I'd called out earlier, bulk of the EBITDA, which were hitherto in this supply chain segment in the last year, has now become more residing in the midstream segment, because this becomes a feedstock for the captive processing for cocoa processing assets.

So what we see is an increasing trend, especially in the cocoa business, as well as in grains business and peanut business, where we see an increasing trend of integrated business, where it is becoming difficult for us to keep this slice as supply chain and midstream, as two separate segments.

So when I talk about midstream next, briefly, you will see this anomaly where we are seeing that the supply chain business seemingly delivering lower numbers, but not so. But actually the hitherto, this contribution which were resident in the supply chain segment is now moving on to the midstream segment.

Also it is, on the invested capital, at around SGD1.7 billion of increase, but that is primarily due to the cocoa bean working capital, which is residing in the supply chain segment, which is destined for transferring to the cocoa processing business going forward. So, in short, the EBITDA is moving to the midstream, whereas the IC is actually residing in the supply chain business.

So, going forward we'll be looking at how to better present this as an integrated supply chain midstream together so as to better present this picture clearly to you all.

Moving on to mid and downstream. It has been a fantastic performance that is more than SGD300 million of increase in EBITDA. As I had highlighted in the supply chain segment, some of this EBITDA growth has come from the transfer of EBITDA margins from the supply chain and cocoa bean business to the cocoa processing business, as well as -- but, however, there has been significantly good performances from West Africa wheat milling business. Both our soluble coffee business in Vietnam and Spain have done very well. All of our peanut shelling and blanching business in the US, whether it's Universal Blanchers, the MMI and Brooks, have done extremely well. And it has been a turnaround performance both in the sugar refining business in Indonesia as well as the palm refining business in Mozambique.

You will see that the invested capital overall has decreased by SGD100 million in spite of increase in fixed capital in this midstream. As you know, we have acquired during the year the wheat milling assets in Nigeria, the peanut shelling assets in the US. But in spite of increase in fixed capital, overall the invested capital has come down, because the erstwhile working capital that we had carried forward post acquisition of the ADM cocoa business late last year has been fully utilized and optimized. And bulk of the inventory that we are carrying forward for the cocoa processing assets is still residing in the supply chain segment. But it has been a healthy 9.7% return as compared to 6.5% year-on-year.

So this is something which we always present you on a year, which gives you the potential of the business that we can deliver going forward. We provide you this gestation mix on all the three segments in terms of upstream, supply chain and midstream. We -- the supply chain business is fully contributing and hence the gestation mix discussion does not apply to supply chain, but I will talk about it in one point briefly.

If you look at the upstream business, that is close to SGD1 billion, which is gestating. As you know, primarily the palm plantation, the rubber plantation investments in Gabon are fully gestating and are not yielding. Close to SGD700 million of investments are gestating, which are including the rice farming business in Nigeria and related -- and some of the businesses, coffee plantations in Brazil, Laos, Zambia and Tanzania. And those, SGD1.7 billion technically of asset which is there, roughly 50% of this is partly contributing or gestating.

More importantly, if you clearly look at here, the fully contributing business is delivering only 5.1%, even though we say that the expected EBITDA on a steady state is 15% to 18%. But actually, if you look at the slice of the fully contributing businesses, so we have the almond business in Australia, which is fully contributing, we have the dairy upstream business both in Uruguay and in Russia, are also part of these fully contributing businesses, the SIFCA business which has the upstream business of palm as well as rubber is included in this contribution, but all of which are actually not fully delivering to potential.

So if you look at -- while the IC, roughly this accounts for a billion dollars out of this $2.1 billion, which are not yielding to full potential, even though they are fully, you know, they are in the process of fully yielding but they are not yielding to full potential. So if all of them turn around during the coming years, we expect the guidance that we have on a steady state base of 15% to 18% will really play out.

If we look at the supply chain business, on an overall segment basis, the EBITDA/IC 8.8%, where as I called out earlier, roughly more than SGD1 billion of invested capital, which is technically to be allocated to midstream which is lying in supply chain which is pertaining to the cocoa bean inventory, if we take that away from the IC of SGD6.5 billion, at SGD503 million, at [SGD0.5 billion], we will be around 10% to 11% of an EBITDA/IC on an adjusted basis, which is really within the range that we had been talking about on a steady state basis.

On the mid and downstream basis, you can see that close to SGD3.4 billion of invested capital is partly contributing. That includes the ADM cocoa assets -- ADM cocoa asset that we had acquired. That also includes the BUA, which is a wheat manufacturing and pasta milling asset that we had acquired during the year, and as well as the peanut shelling assets, the Brooks which were acquired in the US, all are still partly contributing and will move to fully contributing between 2017 and 2018.

So, overall, if you look at close to SGD5.1 billion of invested capital, is actually not fully contributing, and which has the full potential to yield. And going forward, all of this, when they track to their investment thesis, we believe that all which will come to the steady state expected EBITDA/IC returns that we are guiding here in this presentation.

Moving on to balance sheet and cash flow. Overall balance sheet grew by SGD1.7 billion, with net fixed capital growing by SGD829 million and working capital marginally growing at the yearend by SGD222 million.

We grew equity and reserves by SGD610 million. A point to call out here, we had a benchmark issuance of $500 million of perpetual securities which were issued during the middle of the year. And we also successfully refinanced close to SGD2.7 billion of debt that was due to refinance in 2016, very comfortably.

So overall the balance sheet is at SGD19.3 billion, as compared to SGD17.6 billion year-on-year.

On the cash flow analysis, as I had called out in the highlights, we had generated a net operating cash flow of SGD1 billion, clearly, as compared to SGD155 million year-on-year, SGD860 million increase on operating cash flow.

The net interest paid was also lower by SGD130 million. We had a free cash flow generated, before CapEx and investments, we had positive number of SGD650 million, as compared to SGD201 million negative last year, post the ADM cocoa assets acquired late last year.

More importantly, you can see that we have improved FCFE by SGD1.8 billion, even though it is negative at SGD765 million, but that was primarily due to continued investment in CapEx of SGD1.4 billion.

Moving on to gearing. We are 1.99 levels, marginally higher than the 1.96 levels we were at this time last year. Point to note here is that this is despite the increase of net debt by SGD1.4 million. And, however, adjusting for readily marketable inventory of roughly SGD6 billion and secured receivables of SGD1.3 billion, our adjusted net debt to equity is a very healthy level of 0.73 times.

Our liquidity position remained strong. We have close to SGD7.3 billion of unutilized bank lines, and overall available liquidity of SGD16.8 billion, roughly SGD13.6 billion of gross debt split into SGD6 billion of short-term, and roughly SGD7.7 billion of long-term debt.

We continue to optimize both our debt tenure and mix and to rebalance both our long-term and short-term debt, especially considering the rising interest scenario. And we will be working to match both fixed capital and working capital needs.

So, ladies and gentlemen, in summary, a very strong operational performance in 2016, backed by strong growth in confectionery and beverage segment and food staples and packaged foods compared to 2015; of 11% increase in EBITDA, 23% in operational PATMI year-on-year; a 34% increase in EBITDA on Q4 the same period; and more importantly, 155% increase in Q4 on operational PATMI over the prior period, has been the highlights of this year, which reflects the fundamental and intrinsic strength of the strategy and the diversified portfolio that we have, especially considering very volatile global market and commodity conditions.

We continue to focus on turning around underperforming businesses. We had successfully turned around many businesses, which were underperforming in 2015, in 2016. We will focus on some of the underperforming businesses in cotton as well as in SVI in tomatoes, and we'll ensure that the gestation businesses reach full potential as we had discussed in the gestation mix slide.

The debt optimization initiatives that we have done over the last 24 months has really successfully reduced our interest costs and our effective interest rate, despite a very high asset base. But going forward, we see that there will be an increased interest rate regime and we will see -- and we are taking enough steps and measures to how to address that issue going forward.

We will stay focused on executing our three-year 2016 to 2018 strategic plan and continue to invest in prioritized platforms. Thank you.

QUESTIONS AND ANSWERS

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

Thank you, Muthu. We will now take your questions. If you have a question, please raise your hands and let us know your name and where you represent and a microphone will be brought to you.

Jeevan Vasagar - *Financial Times - Media*

Jeevan Vasagar, Financial Times. Thanks very much. I have three questions.

One is, could you give us a bit more color on the underperforming businesses and what you're going to do to turn them around, cotton and tomato you mentioned?

Secondly, could you give me a sense of your outlook for coffee and cocoa prices this year?

And thirdly, what's the impact on the business of the moratorium on forest clearance in Gabon? Thank you.

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

Okay. So, the first question is on the underperforming assets. The underperforming assets are basically the OTP, Olam Tomato Processors, in the US. And that is a function of market conditions and also a function of our configuration of assets in OTP. So as far as market conditions are concerned, there's still excess supply and a surplus supply situation, both in terms of Chinese production as well as US production and EU production. We expect that overhang in stocks to be cleared over the course of the next 12 months. And we should get the market back in balance subsequent to that.

The second issue is really the raw tomato prices in the US, despite a surplus crop, has been quite strong, because the growers in California are organized under the California Tomato Growers Association, and they negotiate these prices before the season starts with the processors.

So those processors who have some mix of raw material production themselves, so, some of the processors have their own tomato farming. We are involved in tomato farming but only through our contract growers. So we have a very large ag operation that helps them grow the tomatoes and increase the productivity and we manage their harvesting and everything else, but we're not directly involved in tomato growing.

And therefore, when CTGA prices in tomatoes are high, our capacity to extract decent margin gets limited. So that's the function of how the negotiations between the cotton -- between the California Tomato Growers Association and the processors take place. So, progressively over the next few years, we will increase our participation in getting some of our production grown ourselves either through contract growing or through leased farming ourselves. So that is something that we will do.

We are also changing our product mix more to value-added products, including canned -- different kinds of tomato canning, as well as seasonings and sauces beyond just making ketchup-based or industrial tomato paste. So, change in product mix, change in some percentage of the tomatoes that we use in our factories being grown by us in a variety of models, and then hopefully a better negotiated settlement with the California Tomato Growers Association to have a more fair distribution of the margins in this business between the growers and the processors, would be the three things that we are planning to do.

So we would expect that the trajectory of performance of OTP with the revived market conditions that we anticipate will happen over the course of the next 12 months, which is why Muthu, in his commentary on tomatoes, said that the first half is still going to be tough for the business, and we hope conditions will start improving from the third, fourth quarter of 2017. But there's a clear turnaround plan that we are working on at this point in time as far as the tomato business is concerned.

The cotton business is more cyclical. So we have a very strong cotton business. Globally we are the second largest cotton company. We're the largest cotton ginner in the world. Most of the cotton businesses in Olam did extremely well last year, with the exception of the US. And there were some cyclical conditions in the US which impacted our performance last year.

But as far as the overall cotton business is concerned, our Australian business, our CIS business, our Indian business, our Chinese business, our African business, are all doing extremely well, and we hope that the cyclical conditions that we faced in the cotton business in 2016 in the US will not repeat itself in 2017. And therefore, overall we are looking for a better year in cotton compared to 2016. But it's a very solid business with a differentiated strategy and we expect cotton's performance in 2017 to be back to its normal trend line.

And I think you mentioned one more business? Yes. So the second question was about coffee and cocoa prices. So I'll start with coffee.

We have revised our S&D, our supply and demand numbers in coffee as far as Arabica coffee is -- as far as Robusta is concerned, by about 1 million bags. So our total deficit for both Robusta and Arabica put together is now, for the 2017, 2018 crop, gone up to about 5.2 million bags. So this will be supportive for the market.

So, despite -- and we also know that in Brazil we have alternative bearing years. And this year is going to be a low-bearing year. And therefore, the Brazilian Arabica crop is going to decline by about 6 million, 7 million bags this year, but that is something that is well-anticipated and already priced in.

But overall, we are friendly to coffee prices and we expect, particularly in Robusta's case, there to be growing supply/demand imbalance that will be played out a bit more as we go through the year. Most of this information is already partly in the price but we think there is still some room for prices to adjust given the deficits that we are expecting of almost 5.2 million bags.

We see a lot of heaviness in stocks in the consuming countries and destination markets, but we see a big tightness of supply in the producing countries. Overall, we still see a deficit of about 5.2 million bags.

As far as cocoa is concerned, as you know, in 2016, we had a significant shortfall in the mid-crop in the principal producing countries in West Africa, including Cote D'Ivoire and other parts of Africa. And that resulted in a 2016 deficit of roughly between 285,000 tonnes to 300,000 tonnes. We have had very, very good weather since then. And the 2017, 2018 crop we expect will be a bumper crop, almost a record crop, both in Cote D'Ivoire, Ghana and most of the producing countries.

So we expect a fairly significant surplus. So, from a very major deficit in 2016, 2017, we see a swing to a fairly substantial surplus in 2017, 2018. And this has also been compounded by the fact that, in Cote D'Ivoire, there has been significant defaults by customers, and as a result, almost 350,000 tonnes, according to government records, has come back for reselling in the market, because as the prices fell, a lot of customers defaulted on those contracts. So that is also putting an overhang on prices.

Much of this has been reflected in the way cocoa prices have moved in the last quarter of the year. We saw a GBP440 drop in the cocoa market in that last quarter, in the London market. So that will play out, but most of it is already now seen as far as the market is concerned. There's also a fairly substantial large spec, net short position, almost 50,000 lots, which will also keep the market depressed and provide overhang on prices. But a lot of this news is now already in the price, but we are expecting a substantial surplus for cocoa in terms of supply and demand in the 2016, 2017 year.

I think your final question was on forest in Gabon. As most of you know, we had, in the middle of December a report issued by Mighty Earth and Brainforest -- Mighty Earth is part of Waxman Strategies in the US. It's an NGO. And they attacked our palm and rubber operations in Gabon, that we were deforesting in Gabon to plant palm and rubber. And they also alleged that our supply chain, where we are sourcing palm oil in Asia, we didn't have proper processes to validate the supply base in terms of their sustainability practices.

So, subsequent to the report, as you know, we, on the same day the report came out, issued a fairly comprehensive response to that report. And then after that, we engaged with Mighty and we engaged with the many other interested stakeholder groups since that period until now, and this week or last week you saw that we had issued a press release on the agreement that we reached with Mighty.

So I just want to clarify a couple of issues with regard to that agreement. First, Olam will only develop its palm plantations under six conditions, or rubber plantations for that matter, any tropical forest -- any tropical plantations, only under six conditions.

Firstly, we will not develop our plantations in what we call high conservancy value areas. So the first rule is, no HCV. No high conservancy value. The second rule that we have is, no HCS. No high carbon stock areas will we be converting into palm plantations or rubber plantations or any other tropical crop plantations.

The third condition that we have is we will not develop any plantations in peat areas. So, no peat. So that is a third boundary condition. The fourth boundary condition that we have is, no burning under any circumstance. So that's the fourth boundary condition.

The fifth boundary condition is, no exploitation. And exploitation here includes communities where we are setting up our plantations. So we have a very elaborate, free prior informed consent process that not only recognizes customary land rights or legal land rights of the communities involved where we are putting up our plantation projects, but also -- but also customary or traditional land rights.

So if their forefathers farmed that land 50 or 100 years ago, the government took over that land and the land now belongs to the government, they resettled those communities or those villages, these farmers will still have a customary right that we recognize. Even though they don't have a legal right, they have a customary or a traditional right which we will recognize.

So in our palm plantations in Gabon, we did that for two out of our 21 villages that were involved in that project where it was developed and we recognized their traditional rights and, accordingly, did not develop plantations where although we had the legal title, the government had given us a legal title and we had that legal title.

So that is the conditions under which we will develop our palm plantations. So in Gabon, the phase one of our project was to develop 50,000 hectares of a nucleus palm plantation. And we had planted 45,000 hectares so far. And we have set aside -- we were given 100,000 hectares of land by the government.

We have set aside the balance of 55,000 hectares because we believe that our assessment on HCV, HCS, et cetera showed that these 55,000 hectares at high conservancy value or carbon stock areas and therefore, they should be preserved and protected.

So when you do an HCV analysis, we have to follow six principles of HCV analysis, you know, first, we have to have a biodiversity assessment of the concession that we were given. And this is a very elaborate process. We start with the aerial LIDAR mapping but then we have an army of zoologists and botanists doing the transects of the forestry and inventorizing every toad and tick and plant and species in that forest and then drawing up a detailed biodiversity map in one square meter area resolution. So it's a very disaggregated HCV analysis.

And then we do it across landscape analysis, we do a landscape analysis, we do an ecosystem and ecosystem services analysis, we do a rare species analysis, we do a cultural analysis, we do a social analysis. So all of that is part of the HCV and it's not just a self-assessment that we do.

We had the HCV resource network do a peer review, it's an anonymous peer review, right?

And this is the first plantation in the world that had done a peer review of the HCV resource network. We had the high carbon study plus study group which has eminent scientists who came and visited the plantation and came with a conclusion that our Gabon plantation, because of the set aside, I said we set aside 55% of the area, the average set-aside in Indonesia is 3%.

In our rubber plantation in Gabon, we set aside 67% of the area, we planted only 33%. Right? And that again, compares to an Asian average of 4% set asides, so they came and said that this is the most sustainable plantation that they have seen.

Now, we cannot convince all of the extreme NGO groups who say that not one tree or one stick can be cut. Gabon is in a situation where they have 35% of the people living below the poverty line. They have roughly 38% rural unemployment. They have massive rural-urban migration issues because there is no livelihood in the rural areas. The government -- the economy is dependent entirely on oil and gas and their studies show that the oil and gas reserves that they have will run out in 30 years, if they are very aggressive, 40 years, so they have a small window to broad base and diversify their economy.

And we are saying that we are not going to be felling forests to develop our palm plantations, but they are secondary logged out forests, if there's low ecological value forests, and it meets our five or six conditions of no HCV, no HCS, no peat, no burning aspect process et cetera, then we think it is right to develop a sustainable agricultural plan so we will not go into countries where the government does not have a land use plan.

So the big issue was if the Gabon government starts to sway the Pandora's box, it is a thin edge of the knife and you are going to open this up to what happened in Indonesia. But the government of Gabon is saying that by 2020, they will only develop 1% of their forest land. They have 23 million hectares, 90% is forest. The balance of 10% is swamps and infertile area that they cannot plant.

So they have over the past 100 years, given forest concessions, the people have come and logged those forests so there are logged out forests, secondary forest areas, and that is where we are developing a palm plantation. And even there, because when somebody goes and gets a logging concession and logs a forest, there are 350 species of trees that you'll find in a forest typically, and in a very heavy forest, more than 1,000 species.

Of this, probably 40 to 50 species are commercially exploitable. Of that, only 10 species are liquid. So when these guys go into forest and clear the forest, they will only go for harvesting the very liquid species.

So this NGO in their report had shown some big trees being cut. Obviously, there will be a lot of big trees in a logged-out forest that will be cut because they have been left as not of any economic value. But more importantly, even if it is logged out, if that tree has any conservancy value, this is a high conservation species value, we will protect it. We will not cut it down.

So we had then engaged with Mighty team and they started with the position not one tree, one stick can be cut, now they have moved to a more balanced position. In turn, we have said that we have put a moratorium on developing any further land. See now, they wrote a 70-page report without setting foot in Gabon, which for me is incredulous, but they did that.

Now, they are willing and accepted that they will come to Gabon. They will have a multi-stakeholder consultation process in Gabon and they will -- after that assessment is done, we will take a moratorium for a year of not developing any new plantation in those forested areas secondary logged out, low ecological worth value forested areas, until those multi-stakeholder consultations are done.

Both in our palm plantation and rubber plantations. So we planted 45,000 hectares, we will plant another 5,000 hectares in Gabon but in savannah land, not in the forested areas, and we will plant 1,000 hectares that we have already cleared in rubber but after that, we are putting a moratorium for 12 months.

Now, if the high conservancy -- HCS approach group which is developing the carbon threshold for both tropical forests, humid regions like Indonesia, Malaysia, which they have almost come to a conclusion and they are likely to issue a report on what they think is -- this is a multi-stakeholder approach group -- what is the carbon threshold for those conditions.

But within that HCSA, they have got a high forest working group, which is supposed to develop an HCS threshold for high forested cover nations and that is very different from a deforested nation like Indonesia.

You cannot have the same HCS threshold for a high forest cover nation versus a highly deforested country like Indonesia or Malaysia.

So this group is now in the final stages of issuing a report on what is the HCS threshold and we have said and committed, we will follow that standard in Malaysia, Indonesia and similar tropical humid areas where the standard will be applicable.

But within that group, there is the high forest working group and they have to develop a standard for Africa, which they have not made any progress on. We are observers to the high forest working group deliberations, they are deadlocked, they have not made progress, we have invited them, the government of Gabon has invited them, the Republic of Congo has invited them to come to Africa and through a multi-stakeholder approach process determine what is the appropriate standard for Africa in terms of HCS because they are all very high forested. Papua New Guinea and Cameroon and Nigeria and sorry, Cameroon and Gabon and DRC and ROC are all part of this high forest cover coalition of nations, but then you need to develop a standard for that.

So we are hoping that in the 12 months we have a moratorium, this group will actually come up with a standard for high forest working group. We are not going to wait forever, right?

If in 12 months, they are making progress and they are likely to come to a standard, we have said in our agreement that we will extend our moratorium. If you know that the standard is imminent, if however, we believe that it is deadlocked, and they are unlikely to develop any standard, we will work with the other NGO groups, whether it's accounting -- accountability network or the forest alliance network. There are various others who are also trying to do the same thing.

So we will work with all of these stakeholder groups to see that they develop an appropriate standard for Africa through a multi-stakeholder consultation process, balancing forest conservation. Olam is all for forest conservation but we want to balance forest conservation with sustainable agricultural development with poverty reduction, with preventing rural -- reducing rural urban migration and creating livelihoods in the rural areas, we want to balance all of these objectives.

Whether Olam opens a Pandora's box and not all of these governments are struggling with employment generation. They are going to open this Pandora's box. It is better for responsible companies like Olam or Sime Darby or others to go and invest and do this responsibly, than have irresponsible players go and develop this opportunity.

So we can hold our hand to our heart and say we have developed one of the most sustainable palm oil plantations anywhere in the world and most observers, independent observers, have gone and visited the plantation, believe it, this is the case.

Now on the second delegation, which is on the Indonesian supply chain, we are a very, very small player. Indonesia and Malaysia put together, produces 55 million tonnes of palm oil. Globally, palm oil production is in excess of 60 million tonnes.

In 2016, we sourced and traded 250,000 tonnes. We are an insignificant player. That does not excuse us from being responsible in the way we source. So we have agreed that we will disclose the name of our suppliers, which we have done. We have already disclosed the name of our mills to WRI but everybody who discloses with WRI their mills, does it on an anonymous basis to encourage all people to start disclosing their mills.

And the WRI helps us to do a risk assessment of those mills.

And the high-risk mills category, then we do verification on the ground whether they conform to our sustainable palm oil policy and all of the other good conservation practices that we are talking about.

We have also laid out a time bound plan in terms of what we will complete by 2018 and 2020, let me just give you an example. We have hired --- we are in the process of finalizing hiring Proforest to do a validation of our mills.

Now, they have told us that they have the capacity and the bandwidth to do 12 mills a year. We have more than 800 mills or 900 mills that we will be sourcing from. Small quantities, but that's the number of mills. So that will take a very, very long time.

So we are going to supplement that by hiring more people who can do the traceability and verification, but more importantly, all the palm oil companies are similarly engaged in efforts to do the traceability to the mills and then from the mills, to the people who supply to those mills. So rather than all of us do our own independent verifications, we want to see whether these NGOs that are doing these verifications for each of us can create a clearing house system where they can say that we have verified these mills and we verified the mills of these suppliers.

So these guys are sustainable and therefore, you can buy from them. Rather than each of us do that and it will take us 40 years or 50 years to trace and track every mill and every farmer who supplies to each of these mills. So I think there is an effort to see whether sectorally, we can combine our forces to establish this traceability as well.

So, to conclude, we have agreed on three things. One, that they will offer a moratorium for 12 months in the palm oil plantations, and we will extend it for another six months if the HCSA group is imminently going to issue HCS standard for high forest cover nations for both palm and rubber in Africa.

The second thing that we said is we will commit to meeting our timelines in the milestones that we have talked about in terms of verifying our third-party supply chain sourcing of palm oil in Asia.

The third thing that we have said is we had a grievance procedure where any farmer or community that is being impacted by any development that we have done in the plantation or any third party supplier sourcing that we have done, there was a grievance procedure that we had established but that was an anonymous -- sorry, that was the grievance procedure where whoever is complaining, will have to tell us who is complaining so that we can go and meet them and fix the problem.

But we have been told that because the government of Gabon is involved in our Gabon plantation project, anybody who complains is complaining actually against the government and therefore, they are afraid to complain. So they are not going to complain if it's not anonymous.

So we have agreed that we will make a grievance and public complaints procedure anonymous so that people without any fear or favor, can make the complaints and we will find a way of how we can reach them to address the problem as promptly as we can. So that is the third thing that we said we will do.

In turn, Mighty Earth has agreed to suspend their campaign against Olam. So second, they have agreed to withdraw the point of association complained that the file with the Forest Stewardship Council.

Three, they have recognized a sovereign right for Gabon to develop their agricultural sector in a sustainable basis, balanced with forest conservation and recognize the right for poverty reduction and preventing rural urban migration. And they also agreed that they will visit Gabon and have a multi-stakeholder approach to consulting with government civil society and all other stakeholder groups involved to develop what is an appropriate balanced approach to having forest conservation objectives met along with sustainable agriculture development and poverty reduction.

We've also engaged with all the mainstream NGOs. So, as you know, NGOs will have different views and they will be single issue advocacy groups and there will be groups in the center and groups in the far right and groups in the far left. We have tried to engage as many of them as possible. So we did meet with at least 20 NGOs and I have explained to everybody our position, have invited everybody to come and visit our plantation operations, I have made the commitments and said that we will issue progress reports against the commitments that we are making as far as third party supplier sourcing, et cetera, is concerned.

So that is where we are on the last point.

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

Thank you, any other questions?

I have two questions that just came up on the webcast, a follow up to the questions on cocoa and coffee. On cocoa, with your comments on the prices going forward, how is it going to impact your cocoa trading operations?

The second question is on coffee, but let's take the cocoa one first.

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

So our cocoa business as you know is now an integrated business. In the past, we are mainly a supply chain trader in cocoa and we were not in the midstream processing piece. Now, we are a fully integrated business. We are not in chocolates, but we are in cocoa bean sourcing and trading, and we are also in cocoa processing.

So we believe that the low prices and the margins for our integrated business is going to be a function of what happens to cocoa differentials, what happens to cocoa ratios both in terms of combined ratios and separately, butter liquor ratios and powder ratios.

We saw in the last quarter of 2017 very high product ratios and combined ratios, 3.15 was where it ended in the fourth quarter. So our processing business, because of the very high ratios, did extremely well last year. The ratios since then have come down. The ratios in January was 3, the ratios we expect the first quarter will end up at probably 2.75 and then Q3 and Q4, we see a further decline in ratios to around probably 2.45 kind of levels.

But because bean prices have come down very significantly, the processing and crush margins as you call it in soybean, the processing margin, the grind margins here, we still believe, will be quite robust. Although there will be declining product ratios over the course of Q3 and Q4. We have sold most of our production to the first half, we will be now selling for the second half but the declining bean prices -- the significant decline in bean prices, the processing margins still look quite healthy.

But there will be tough trading conditions on the trading side of our business, but overall, as an integrated business, we believe that we can navigate this quite successfully over the course of the next 12 months.

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

This question is on coffee beans. What is the main driver of the growing deficit in Robusta coffee beans?

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

Yes, so one was the impact of El Nino and the reduction in the conilon crop in Brazil. So we have had two years of very poor Robusta conilon crop production in Brazil which is a big driver. We had a significant shortfall in Vietnam, which is the second biggest producer of Robusta coffee. That crop is now reviving. There are some unseasonal rains now, but the crop is now reviving.

But a combination of poor crops over a two year, three-year period has resulted in the S&D for coffee and the end-use ratio. So today, if you look at the Robusta end-use ratios, we estimate we will end in 2017, 2018 season with about 26.5% and 27%. That is one of the historically very low end-use ratios.

We expect Arabica end-use ratios to be between 32%, 33%. Overall coffee end-use ratios are at the lower end of a historical trend and that is largely on account of the fact that the S&D mostly from the supply side has been an issue.

Demand has been fairly predictable, nothing major has happened to demand, unlike in cocoa where you have seen chocolate demand last year come down by 3% because of very high cocoa prices. Overall, globally, about 2.5% but it declined in Europe by 3.1%, the chocolate consumption, because of very high prices.

Now that cocoa prices are very low and ingredient prices are very low, we would expect a revival in chocolate consumption in 2017, 2018 compared to 2015 and 2016 when ingredient prices, cocoa ingredient prices, were quite elevated.

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

The next question is on edible nuts and the impact of weather. The first one is on cashew production in Vietnam, which has been affected by droughts. How is production going to be impacted and what is the impact on Olam?

The second question is Californian weather, which is the reverse that is happening there, what is the impact on our own production?

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

So as you know, cashew prices run up quite significantly over the course of the last 12 months. So white wholes 320s, which is the reference grade of cashew kernels, moved from something like $3.20 per pound to about $4.60 per pound. So cashews are creating a historically high levels, largely on account of a deficit that was there and very strong consumption.

But as we have seen in the past, the cure for high prices is high prices. So with cashew prices at $4.60, we will see some destruction of demand and rationing of demand. To give you an example, Costco, which is one of our customers, increased the shelf price for the cashews, white wholes 240s that they sell in the shelf, by about 27% in the last one month -- 27%.

So obviously with the higher sticker price shock, there will be a rationing of demand and disruption of demand over time. And therefore, the prices will go back to an equilibrium.

But on the specific question about Vietnam, we believe the Vietnam crop is a little bit late and a late crop typically would mean a shorter crop, but we have a good crop in India which is another big producer. We have a very good crop across the Southern Hemisphere, Tanzania, Mozambique, et cetera. We finished the season, so that is a very good crop.

We are expecting a very significant growth in the crop in West Africa, which is a very big producer of cashews. So overall, we are expecting a surplus of about 275,000 tonnes as far as cashews is concerned, which is a very high surplus that is emerging. But if Vietnam crop is short, that will take off some of the surplus. But nevertheless, in most scenarios we would expect the surplus crop situation this year in cashews.

So I think people will start beginning to reflect that as far as cashew prices are concerned going forward.

(Multiple speakers)

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

Yes, so the harvest has been delayed, and typically, we have a narrow window to harvest. The harvest has been delayed. And we are gearing ourselves to harvest quicker, including require to harvest in the night.

So in Australia, harvesting in the night -- so we have made arrangements for having lights to be able to allow us to harvest and you must understand the scale of this. We've got 31,000 acres of almond plantations in the US. So it's a very large, large area to really harvest. But we expect -- the crop is looking extremely good, so we are positive about the size of the crop. And if we can get all the crop from the trees and have a successful harvesting program, then I think we should all be quite happy.

So we will wait and see. It's all hands on deck now to make sure that in the window that we have, we can successfully complete the harvesting process.

Yes, so California almonds, we have had some of the best weather. So you will know that California, 6 years we have had a drought. The water table receded, massive water shortage -- almond is a very water-intensive crop and needs 12.5 megaliters per hectare of crop. So there was severe stress on all Californian agriculture over the last 5 years, 6 years.

Now, from a situation of real bad drought conditions, we have now had just the opposite. We've had some massive rains, high heavy snow packs, dams being and reservoirs being full. Some dams and reservoirs having spills because there is just too much water.

So from famine to feast. Very good for almond production and productivity but this is the bloom period for almonds and the bloom is a three-week period. In that three-week period if there's rains, then the bloom gets impacted.

In the three-week period, the bees need at least 6 days to fly and do their business of cross pollinating. If there are rains, the bees will not fly. If the wind speeds are above 15 miles an hour, the bees will not fly. If it is cloudy conditions, the bees will not fly.

So everybody's fingers are now crossed, will we get 6 days, 7 days where the bees can go and do their job or will there be continuing rains during the bloom period which will affect the crop?

Right now, the crop looks good. I mean, the bloom looks good, or the blossom looks good. We have to see whether this will be actually converted into setting and that is a function of how effectively cross pollination will happen with the bees over the next two weeks. So the next two weeks, this is something that keeps us awake every night on how good the bees will be.

Unfortunately, I can't give the bees overtime and ask them to work longer and harder. They only fly from morning, probably 10 o'clock, to afternoon, 2 o'clock. After that, they rest.

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

That's a very interesting comment, because in Singapore we have some very active bees in the some parts of the country that are affecting people's livelihood.

We have a question obviously, the last but not the least question on palm prices. Sunny, would you like to comment?

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

Yes, as you saw, palm prices have run up largely on account of a very, very severe El Nino that we had in 2015 and that has resulted in 5.2 million tonne reduction in Indonesia and Malaysia. And that is very conservative estimate. Most market participants have put that reduction in crop because of that El Nino impact at closer to 6 million tonnes. Our number is 5.2 million tonnes.

But we see there will be a revival in the production. If you saw the last serial El Nino in 1997, 1998, there was a sharp recovery in palm oil production in Malaysia and Indonesia post that last similar strength intensity El Nino that we had.

But at that time, there was a lot of planting et cetera that was happening. And that sharp revival was also because of the significant additional planting that have happened that year. We have not seen the same sharp recovery but we will see that recovery come up. And our estimate is that Malaysian production, which fell to 17.4 million tonnes, we expect that production will revive by about 2.4 million tonnes this year to about 19.8 million tonnes. So that will be a very sharp recovery.

We see Indonesian production, which decreased by 3.5 million tonnes because of El Nino to 31.5 million tonnes, to revive to 35 million tonnes in 2017, 2018.

So we expect Malaysian and Indonesian production to revive by about 5.9 million tonnes, to about 54.8 million tonnes. That is our house view and number. And this will then, in the second half of the year, put some pressure on palm oil prices because we will see inventories building up.

We will see fairly strong prices in Q1 as suggested. We also see he competing alternatives in terms of the soft oil prices, all giving up value. And if you saw, during the El Nino, we lost about -- we lost say 6 million tonnes of production if you will take the estimates of the market, 6 million tonnes of production. We had 3 million tonnes growth in demand for palm oil, which is 9 million tonnes. And then we had 2 million tonnes diverted to biofuel production in Indonesia, 11 million tonnes.

And that 11 million tonnes disappearance was made up by 3 million tonnes increase in soft oil production, sunflower, rapeseed, soybean oil. And it was also 3.8 million tonnes was what the Chinese Government reduced its stockpile by having both soybean oil auctions and rapeseed oil auctions.

And 4 million tonnes was the reduction in end use inventory. So the 11 million tonnes shortfall was made up by this 11 million tonnes in this form and manner. And that resulted in elevated prices.

But we expect that after this first quarter, we will begin to see market start factoring in what the S&D -- prospective S&D is going to look like. And we are bearish to palm oil prices beginning late second quarter and definitely into the second half of this year.

Hung Hoeng Chow - *Olam International Limited - General Manager, IR*

All right. Is there a question on the floor?

If you are happy with all our answers, I would like to call this briefing to a close and we thank you for your participation today.

Sunny Verghese - *Olam International Limited - Co-Founder and Group CEO*

Thank you.

Neelamani Muthukumar - *Olam International Limited - President, Group CFO*

Thank you.

A. Shekhar - *Olam International Limited - Executive Director, Group COO*

Thank you.

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