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Food Producers

Source: Eikon Thomson Reuters

Market data

EPIC/TKR	RE.
Price (p)	332.5
12m High (p)	385.0
12m Low (p)	210.0
Shares Ord (m)	40.5
Shares Prefs (m)	63.6
Mkt Cap Ord (£m)	134.7
Mkt Cap Pref (£m)	64.4
EV ($m)	459.9
Free Float*	33.9%
Market	Main

**As defined by AIM Rule 26*

Description

R.E.A. is engaged in the operation and further development of palm oil plantations in East Kalimantan, Indonesia. The group also operates a stone quarry, and owns coal mining concessions which have been contracted out to significant coal mine operators.

Company information

Chairman	David Blackett
Managing Director	Carol Gysin

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Key shareholders

Directors	31.95%
M and G Investment Mang.	14.97%
Alcatel Bell Pension Fund	10.32%
Artemis UK	8.83%

Next event

Sept-2017	Interim Results

Analysts

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R.E.A. Holdings

All Change From 2019

As weather patterns revert to more normal conditions, REA is hoping to see production levels rise across its oil palm plantations in Kalimantan during 2017. However, full recovery in oil palm production can take up to 18 months, so improvement in production will spread into 2018. Nevertheless, revenues should see growth of more than 20% y-o-y, helped too by contributions from the electricity generating operations and possibly, also by the coal mining activities, as demand for coal grows domestically and abroad, providing support for prices.

- **Strategy**: REA Kaltim, the principal division of REA, is developing a land bank of some 108,000 ha. At the current, accelerated rate of development, the proprietary plantations should be completed by 2021 at circa 60,000 ha.
- **Valuation:** Using an Indonesian risk biased WACC of 12.2%, a valuation range of £4.44 - £4.76 per share is suggested (on the basis of our long run projections for cash flows), depending on the terminal growth rate applied. We would argue for a terminal growth rate range of 1% (bearish outlook), to 3%, more reflective of emerging market growth rates, which are the big consumers of palm oil. The WACC makes no adjustment for REA being listed on the London Stock Exchange and therefore subject to the LSE's good governance requirements.
- **Risks:** Agricultural risk, commodity price risk, and country risk are constants of palm oil production. End 2016 net debt of $205.1m (66.3% of shareholders' funds), is expected to rise again in subsequent years (subject to new equity raises) as the company drives for the completion of its plantations.
- **Investment summary:** REA has scope, with its existing landbank of 108,215 ha, to develop a planted estate of 60,000 ha, possibly 65,000 ha. On the basis of our projections, the group's financial performance undergoes significant change from 2019 forwards. We are assuming some 37,000 ha of mature plantations for end 2019, coupled with stronger agricultural production across the estates, and a firmer CPO price. If these factors align as anticipated, then this will mark the point at which the business becomes self-sustaining: generating sufficient cash to fully meet its obligations on interest payments, preference dividends, estate development and taxation. According to our projections, the plantations will be fully planted by end 2021 (60,000 ha), with a mature area of between 45,000 ha and 46,000 ha, implying that from 2025, the group could be generating free cash in excess of $100m annually.

Financial summary and valuation

Year End Dec ($m)	2014	2015 R	2016	2017E	2018E
Sales	126	91	79	101	125
EBITDA	43	14	17	23	38
Reported EBIT	32	-7	-5	-1	13
Pre-tax Profit	24	-12	-9	-19	-7
EPS (cents)	40	-59	-48	-61	-35
Adj. EPS (cents) **	40	-11.2	1.4	n.a.	n.a.
Dividend per share (p)	7.75	0.0	0.0	0.0	0.0
Net (debt)/cash	-179.2	-196.7	-205.1	-248.4	-281.6
P/E (x)	10.6	-	-	-	-
Planted Hectares (ha)	34,614	37,097	42,846	46,846	49,846
EV/ Planted Hectares ($/ha) *	13,288	12,398	10,838	9,814	9,224

**EV/planted hectare includes Mkt Cap of the 9% Pref Share and DSN 15% Stake*

***** An estimate of earnings before applying the IAS 41 amendment***

Source: Hardman Agribusiness

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Group Results Full Year 2016

The reported results for REA Holdings (REA) for the year to 31st December 2016, were significantly impacted by three powerful drivers. Revenues declined by 12% to \$79.3m (\$90.5m), and pretax profits suffered a reversal of \$21.5m for a loss of \$9.3m (\$12.2m pretax profit).

1. The El Nino weather pattern that impacted the South East Asian region over a longish period from 2H 2014 into 2H 2016, and which resulted in a decline of 22% in FFB produced.

2. The price of palm oil: while the average price per tonne received by the group evolved at circa \$521/mt (FOB Samarinda) in 2016, this was 7.4% higher than the 2015 price of \$485/mt. However, this compares with a 10 year average achieved price of \$664/mt.

3. The adoption of the amended IAS 41 (as of 1st January, 2016). With the elimination of the 'fair value' gains on Biological Assets that flowed from the previous application of IAS 41, and the application of a new depreciation charge on 'Bearer Plants', the reported results were, and will continue to be, negatively impacted until the accumulated fair value gains have been amortised. Comparatives for 2015, restated to reflect the change in the accounting standard, indicate a reduction in pretax results of \$23.8m.

These difficult operating conditions and influences notwithstanding, the group planted a further 5,757 ha of its land bank, and it invested a net \$31.6m (\$34.8m) in its assets. This important progress was supported by an inflow of \$27m of new permanent capital, sourced from the DSN acquisition of a 15% stake in REA Kaltim (REAK) and the placing for cash, of 3.7m new ordinary shares. Additionally, the company improved the maturity profile of its debt portfolio by the exchange of \$13.8m of 2017 \$ Notes for new 2022 \$ Notes, by the repackaging of Indonesian bank loans, and from new debt funding of \$14.4m to refinance maturing debt (a combination of the sale of 2020 £ Notes held in treasury, and loans provided by DSN under the agreement to purchase a 15% stake in REAK). Group net indebtedness increased to \$205.1m (\$196.7m) for a net debt: equity ratio of 66.3% (66.9%).

While the company paid the fixed semi-annual dividends on the 9% Cumulative Preference Shares (which fell due for payment 30th June and 31st December), the directors decided against the payment of a dividend on the Ordinary shares for 2016, noting the difficult conditions experienced by the business during the year.

Palm Oil Operations

Crop Yields

Production levels in 2016 (FFB yields per hectare) were disappointing – strongly influenced by the El Nino weather system during the first three quarters of 2016, and heavy rain within Q4. Across the South East Asian region, palm oil production has been marked by reduced productivity. REA produced 468,374 mt FFB in 2016 compared with 600,741 mt in 2015, a decline of 22%, notwithstanding gathering estate maturities, and increased production area (another 2,154 ha matured during 2016).

Readers will note that for 2015 and 2014, total rainfall was more than 20% lower than the three preceding years, while 2H 2016 rainfall was some 29% higher than for any of the preceding half years.

Rainfall average across estates (mm)

	2016	2015	2014	2013	2012	2011
6 months to 30th June	1,574	1,505	1,295	2,087	1,791	2,011
% of total	45.6%	70.3%	49.7%	61.7%	55.3%	58.9%
6 months to 31st December	1,875	636	1,311	1,298	1,450	1,403
% of total	54.4%	29.7%	50.3%	38.3%	44.7%	41.1%
12 Months to 31st December	**3,449**	**2,141**	**2,606**	**3,385**	**3,241**	**3,414**
Annual Change %	**61.1%**	**-17.8%**	**-23.0%**	**4.4%**	**-5.1%**	**n/a**

Source: REA Company Reports

FFB production for the Indonesian palm oil peer group (see table below), was on average 11% lower for the 2016 year when compared with 2015. The El Nino weather pattern was also a disruptive influence during 2015, but the continuing relative dryness during 2016 had a compounding impact.

FFB Produced (tonnes) (*may include small holders)

Company	2015	2016	% Change
Astra Agro Lestari (Nucleus)	4,200,513	3,726,091	-11%
Dharma Satya Nusantara (Processed FFB)	1,726,000	1,306,000	-24%
Eagle High (Nucleus)	1,261,278	1,150,516	-9%
First Resources (Nucleus)	2,530,357	2,367,767	-6%
Golden Agri (Nucleus)	7,749,536	6,904,929	-11%
REA Holdings	600,741	468,371	-22%
Sampoerna Agro*	n/a	n/a	-21%
Industry Average Change = -11%			

Source: Hardman Agribusiness / Company Reports

A high-quality palm oil estate in East Kalimantan, with an average maturity of circa 10.9 years (REAK), could be expected, under optimal agronomic conditions, to produce in excess of 25 mt of FFB per ha annually. Yields of as high as 30 mt / ha are possible with modern planting material. REA confirms that on the group's newer planted areas, high achieved rates (above 25 mt FFB/ha) of production should be possible as the new planted areas mature. But for 2016, two years of reduced rainfall, followed by excessive rain in Q4 2016, have resulted in significantly reduced output, with consequences for both OER and revenue generation.

FFB Production

	2014	2015	2016	2017e	2018e
FFB Prod' (own) (MT)	631,728	600,741	468,371	578,983	684,345
FFB (purchased) (MT)	149,002	138,657	98,052	120,000	130,000
Total FFB for process (MT)	**780,730**	**739,398**	**566,423**	**698,983**	**814,345**
Own estate FFB mt/ha avg	*22.3*	*20.5*	*14.9*	*17.0*	*19.6*
Total FFB Processed (MT)	774,420	728,871	560,957	684,449	808,879
OER	*21.7%*	*22.2%*	*22.8%*	22.8%	23.0%
Total CPO production (MT)	**169,466**	**161,844**	**127,697**	**156,054**	**186,042**
Palm Kernel Extracted (MT)	**35,764**	**34,354**	**26,371**	**31,454**	**36,646**
Total CPKO (MT)	**12,596**	**12,703**	**9,494**	**11,324**	**13,192**

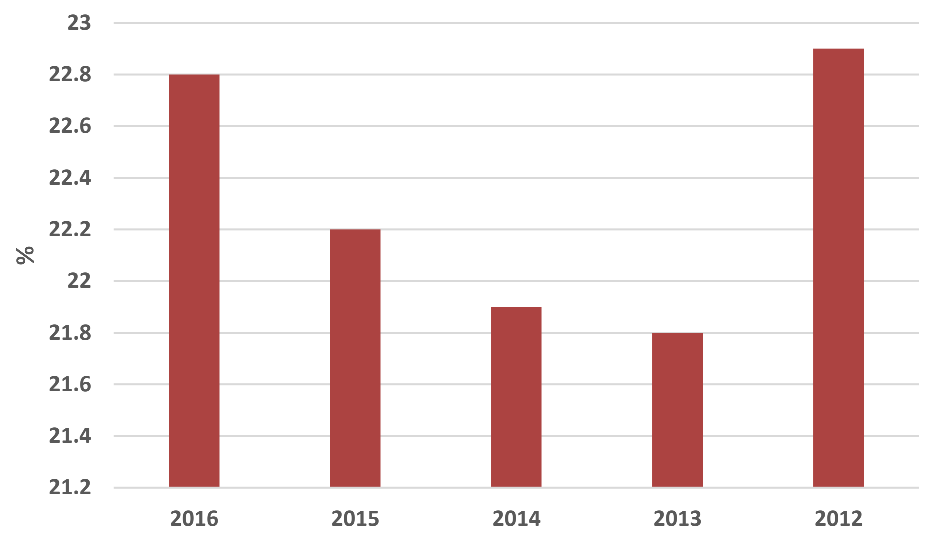
Source: Hardman Agribusiness / Company Reports

There is a knock-on impact from such conditions, with the oil palms taking perhaps 12-18 months to recover from the biological stress induced by abnormally dry conditions, and estate maintenance impacted due to infrastructure damaged by flooding in Q4 2016. With estate roads badly impacted by the Q4 rain, field maintenance operations including the application of fertiliser, were disrupted. Accordingly, we anticipate a knock-on effect on production during 2017 and possibly into 2018, and this is reflected in our FFB production projections (shown above). Our forward projections for group wide productivity (FFB/MT) per ha, are conservatively pitched, remaining below 22 mt/ ha for the lifetime of the model. There is scope for the group to outperform this level.

OER Efficiency

Whilst drought conditions negatively impacted on oil palm estate production, excessive rainfall and flooding (Q4 2016), impacted on the quality of the palm fruit harvested, and in turn, this affected the Oil Extraction Rate (OER). With the heavy rains in Q4 2016 damaging the roads in and around the group's estates, harvesting of FFB and their transfer to the mills was impacted, also leading to a deterioration in OER.

REA Holdings Oil Extraction Rate



Source: REA Annual Reports

While the OER reported for the first half of 2016 was, at 23.8%, at the very top end of sector efficiencies (see table immediately below), the second half's rate of approximately 21.8%, reflected the harsh environmental conditions in Q4, and their impact on both fruit quality and harvesting logistics.

Calendar Year Oil Extraction Rate (%)

	2016	2015	2014	2013	2012
Astra Agro	21.0	21.6	21.9	22.3	22.3
Dharma Satya Nusantara (DSN)	23.9	23.6	23.9	24.3	24.4
Eagle High Plantations	23.8	23.7	23.5	23.5	23.0
First Resources	22.5	22.7	22.8	23.1	23.3
Golden Agri	22.2	22.6	22.8	22.7	22.6
REA Holdings	22.8	22.2	21.9	21.8	22.9
Sampoerna Agro	20.8	21.2	21.7	20.7	20.5
Sime Darby	21.8	21.7	21.9	21.8	21.8
Average	22.4	22.4	22.6	22.5	22.6

Source: Company Annual Reports

Overall the group achieved an OER of 22.8% (22.2%) for the full year 2016, a little ahead of the peer group average.

Achieved rates of OER depend on a number of factors including fruit quality, efficiency of harvesting logistics, efficiency of milling operations and the grading of 3rd party sourced FFB. REA has, over the past two years, undertaken an extensive programme of mill refurbishment. All but one of the four boilers in the group's two older mills have now been reconditioned, and reconditioning of this fourth boiler is expected to be completed within 2017. This refurbishment programme has played its part in the improving profile of OER efficiency in recent years. There may also be scope for the company to strengthen the grading of bought-in FFB. Already it has a large grading team employed across its three mills, but the group is reviewing grading policy and procedures with a view to achieving an appropriate balance between tough commercial grading and the management of supplier loyalty. Our projections are based on a forward OER of 23.5%.

Land & Business Development

During 2016, significant progress was made in respect of estate development, with the planting of a further 5,757 ha, and the preparation of another 1,500 ha for planting in 2017. This meant that the company finished the 2016 year with a total of 42,846 planted hectares. As detailed in the table below (Estate Development), 2016 was notable for a steep acceleration in planting. This was in part enabled by completion of the bunding around the flood prone lower lying areas of the PBJ estate, on which some 3,956 ha were planted, and the construction of water gates to control flooding on these lower lying areas. Partly the acceleration in planting was also possible because the group went into the 2016 year with circa 2,691 ha of cleared land. The group entered the 2017 year with some 1,581 ha of cleared land.

Group Estate

	PBJ	CDM	Total
Cleared, not planted at 1st January 2016 (ha)	2,338	353	2,691
Cleared, during 2016 (ha)	2,110	2,538	4,648
Cleared, not yet planted at 31 December 2016 (ha)	-492	-1,089	-1,581
Planted, during 2016 (ha)	**3,956**	**1,802**	**5,758**

Source: REA Holdings R&A, 2016

During the course of 2017, the group plans to plant a further 4,000 ha, with the activity broadly split between the PBJ and CDM estates.

REA has scope, with its existing landbank of 108,215 ha, to develop a planted estate of 60,000 ha, possibly 65,000 ha. In terms of operational maturity, everything changes for the business when the plantation reaches between 40,000 - 45,000 planted mature ha of palms producing commercial yields of FFB. The company exited the 2016 year with 31,521 mature ha, and by end 2017 this will have risen to an estimated 34,000 ha.

Estate Development

		2014	2015	2016	2017e	2018e
Planted Area (Ha)	Immature	6,339	7,730	11,325	12,770	14,993
	Mature	28,275	29,367	31,521	34,076	34,853
Total Planted Area (Ha)		**34,614**	**37,097**	**42,846**	**46,846**	**49,846**
Planting Achieved/Projected		777	2,236	5,758	4,000	3,000

Source: Hardman Agribusiness / Company Reports

On the basis of our projections, the group's financial performance undergoes significant change from 2019 forwards. We are assuming some 37,000 ha of mature plantations for end 2019, coupled with stronger agricultural production across the estates, and a firmer CPO price. If these factors align as anticipated, then this will mark the point at which the business becomes self-sustaining: generating sufficient cash to fully meet its obligations on interest payments, preference dividends, estate development and taxation. According to our projections, the plantations will be fully planted by end 2021 (60,000 ha), with a mature area of between 45,000 ha and 46,000 ha, implying that from 2025, the group could be generating free cash in excess of $100m annually. Once development has concluded, palm oil plantations can be expected to generate significant surplus cash; REA should be no exception to this rule.

Outsourced FFB

Whereas the group purchased nearly 139,000 mt of FFB from external suppliers in 2015, this important source of additional fruit, shrank to 98,000 m in 2016, also reflecting the impact of the El Nino weather pattern. For 2017 we are projecting a marked uptick in 3rd party supply to some 120,000 mt and this to increase again to 130,000 mt in 2018.

The group develops supply relationships with smallholders and local communities via three distinct schemes:

1. Program Pemberdayaan Masyarakyat Desa (PPMD)

    a. The group introduced this scheme in 2000, to support local co-operatives with access to land for palm oil cultivation. Under the scheme the group provides high quality oil palm seedlings, fertiliser, crop protection inputs and technical assistance.

    b. These support services and materials are provided on a 'loan' basis, albeit interest free, with the cost of the materials and services debited from sale of FFB to the estate mills.

    c. In 2016 supplies of FFB under this scheme totalled 61,000 mt (62% of total 3rd party supply).

    d. In all, the scheme includes 15 smallholder co-operatives.

2. Plasma schemes

    a. Plasma schemes are distinct from PPMD in that it is the group which manages the palm oil cultivations in return for a pre-agreed management fee.

    b. These schemes were established under regulations introduced by the Indonesian state in 2007 to provide greater benefits for the local communities from the palm oil industry.

    c. Plasma schemes are financed by loans to the local community co-operatives, contributed both by the group and by the local development banks.

    d. The co-operatives receive an income based on the value of the FFB harvested by the group, debited for loan repayments and management fees.

    e. The group is currently working towards the development of 13 Plasma schemes for its newer concessions, in addition to 6 more schemes around the already established estates.

    f. At the end of 2016, the group had developed 3,567 ha of plasma cultivations. Four schemes are producing FFB and in total contributed some 9,680 mt of FFB in 2016 (a whisker under 10% of total 3rd party supply).

g. MP Evans, in its defence of the KLK bid, argued that Plasma hectares should be separately valued. To make this argument MP Evans relied on the November 2016 estate valuation, provided by Messrs KHONG & JAAFAR SDN BHD. The Malaysian firm suggested a value of $10,000 / ha for MP Evans' Plasma schemes. Using this logic, would provide an additional $35.67m to the enterprise value of REA Kaltim, or an additional $30.3m to REA's enterprise value, on an equity hectares adjusted basis.

h. While the value contribution of these hectares is reflected in the DCF valuation methodology, a hectare based valuation, could reasonably include the Plasma hectares on the basis that these are somewhat under the control of the sponsoring estate.

3. Direct purchases at mill gates of FFB from independent suppliers

   a. During 2016 the group purchased some 19,760 mt of FFB from independent suppliers (20% of 3rd party supply).

   b. Since 2015, the group has only agreed to purchase FFB from smallholders who have participated in the group's smallholder mapping scheme, an initiative to make the group's FFB supply chain fully traceable. In this way, the production of independent smallholder suppliers can eventually be RSPO certified.

During 2016, the group purchased 93,000 mt (125,000 mt) of FFB, 95% of total 3rd party purchases under these three schemes. The group reports that this represented some $10.4m of revenues for the local communities. This important economic benefit for local communities can be expected to provide strong support for the group's efforts to build and maintain good relationships with the communities neighbouring its estates. The supply of electricity from the group's methane driven generators, also provides another strong shared interest between the community and the group.

Sustainability

REA is fully committed to ensuring all its plantations and mills are in line with RSPO (Roundtable for Sustainable Palm Oil) standard. The Perdana mill has been successfully re-certified this year and it is expected that Cakra mill will be re-certified within the coming months. Certification of the group's mill at Satria has been targeted by December 2017.

Readers will note that the Zoological Society of London (ZSL) undertakes an audit of sustainability across the palm oil producer sector. Using a 'toolkit' defined as Sustainable Palm Oil Transparency Toolkit (SPOTT), it uses publicly available information relating to certification, supply chain traceability and environmental management policies, to generate a score indicating a company's commitment to sustainability and transparency. In October 2016, the group was ranked joint ninth out of 50 palm oil companies. The group gained three points in 2016 by providing maps of concessions and encouraging smallholders to adopt policies of zero burning and no planting on peat soils. Despite this gain, the group ranked slightly lower overall than in 2015 (seventh), due to other companies also improving their overall scores.

In 2016 the group reduced its gross carbon dioxide emissions (y-o-y) by 6.7% and net Greenhouse Gas (GHG) emissions by 17.1%. The group reports that the reduction in GHG emissions is largely due to the increase in credits gained in 2016 for the provision of renewable energy to workers' houses and to local communities by the group's two methane capture / generating facilities. The supply of electricity grew by 73.8% in 2016, following the completion of PLN's distribution infrastructure during 2015.

In 2016, houses had been constructed for 32 workers' families with another 26 planned for 2017. This is alongside community facilities and help with education; the group established a foundation to manage the network of schools across the plantations. Nearly 3,000 children were enrolled in the system in 2016.

REA Kaltim was awarded Class 1 status by the regional governor, following assessment of local plantation companies based on operational, social, and environmental criteria. This recognises the growing strength of the group's community relationship, a 'far-cry' from the village troubles of 2012/13.

Electricity Supply

Operations in 2016

During 2013 the group obtained licences to generate and sell electricity to the state utility PLN for onward sale to the villages surrounding the group's estates. In 2016 revenues from electricity sales amounted to some $563,000 ($233,000 for the first 8 months of operation in 2015). Through its agreement with PLN, the Indonesian state electricity company, the group now supplies power, via a local grid, to 26 villages and sub villages (13,000 households) in areas surrounding the group's estates. In all, REAK operates 7 generators capable of producing 1 megawatt of electricity each, utilising methane from two methane capture plants, both of which were commissioned in 2012. Four of these generators are operated to provide electricity to the group's facilities, but three are dedicated to supplying PLN. The REA 2016 Report and Accounts note that "PLN, may…be able to increase its power capacity requirement to eight megawatts". The company has scope to increase the production of methane and electricity by installing a third methane capture plant at the Satria Mill, the most recently constructed.

Payment for the electricity supplied to PLN is at fixed rates, which are set by Indonesian state regulations, and is received by both the group, and the local district power company: Perusda. Currently, PLN pays the group approximately $0.07 per kilowatt hour.

There is potential for natural growth in respect of electricity supply as a result of incremental consumption as uptake per connected household increases, and as further households install meters, and new villages are connected to the local grid.

Growth Opportunity

For 2017 we are projecting revenues for the electricity generating business of no more than $600,000, rising to $1m annually by 2019 (and then unchanged for the life of our profit and loss model). We believe this is conservative. Potentially revenue growth will be further boosted as all households are ultimately connected, and demand per household grows as consumers purchase additional appliances etc. In addition, PLN has been considering linking the regional transmission network to the new local grid; in that event REAK could install further generating capacity and would be able to deliver electricity into the regional network 24 hours/day and 7 days/week, increasing revenue from electricity sales materially. We have assumed, for valuation purposes, that by 2020/2021, the company is supplying six megawatts of electricity to PLN.

Electricity Supply in Indonesia

The Indonesian media note that PLN's 10-year plan for electricity supply across the country anticipates the supply of electricity, by independent power producers (like REA), continuing to feature prominently in the overall mix of sources. It is also noted that the country will focus on developing power plants that can tap into local sources of energy for electricity generation (again like REA). In the same context, there is reportedly an upwards revision of the use of renewable energy in power projects, with renewables now targeted to be 22.5% of the total energy mix by 2025. REA's power operations, conform to all these requirements.

Valuation

With tariffs unchanged at $0.7m per megawatt of supply, but with 6 megawatts supplied annually from 2020/21 onwards, the business could be producing revenues of more than $2m in the early years of the 2020s. This is double the rate that we have built into our P&L forecasts. On this assumption however, and using a discount rate of 12%-12.5% with a growth rate of 2.5%, the implied cash flows from this expanded operation would produce a NPV of $16.3m.

While this business is dependent on the palm oil mill waste, it is otherwise a separate revenue stream and in our view, deserves to be separately assessed for valuation purposes.

Coal and Stone Interests

The group holds interests in respect of two stone deposits (andesite and limestone), as well as two coal mining concessions.

The andesite stone and coal mining concessions are held by Indonesian concession holding companies. These holding companies are owned presently by REA's local partners, and therefore are not consolidated. REA has the right, subject to the satisfaction of certain conditions, to acquire 95% of each of the holding companies, at the original cost to the local partners. In the Strategic Report (2016 Annual Report and Accounts) the company notes that recent changes to Indonesian regulations relating to foreign investment in mining, will make it unlikely that the necessary conditions for ownership can be satisfied at present. The company also states that it is confident "that such conditions could over time be successfully renegotiated without material loss to the group".

The concession holding companies have been financed by loans provided by REA, on terms such that no dividends or other distributions or payments can be made by the holding companies, without the prior agreement of REA.

The limestone concession is held by an independent Indonesian 3rd party with which REA has indirectly concluded an exclusive offtake agreement.

The stone and coal interests are managed by an Indonesian subsidiary company: PT KCC Resources Indonesia ("KCCRI"). This company is 95% owned by a UK subsidiary company of REA's, KCC Resources Ltd. The remaining 5% is owned by local partners in Indonesia.

Any profits deriving from the coal and stone interests will accrue to REA Holdings via the ownership structure described above, and not via REA Kaltim.

Regulatory Regime

Stone quarrying is classified as a mining activity by the Indonesian Ministry of Energy and Natural Resources. Mineral and coal mining activities are governed under the Mining Law. The business entity holding a mining licence must be an Indonesian legal entity. A key feature of the Mining Law is that a privately held company can only hold one licence (i.e. one IUP/IUPK) and only companies listed on the Indonesian stock exchange are entitled to hold more than one licence.

Coal Interests

REA holds rights in respect of 2 coal mining concessions:

1. Kota Bangun (Central East Kalimantan)
    a. The land area within this concession extends to some 4,400 ha.
    b. The inferred coal resources have been assessed at some 1.7 million tonnes, but we understand that potentially economically recoverable reserves may be greater.

c. The deposits are classed as having low sulphur content, with a gross calorific value of between 6,800-7,800 kilocalories per kg.

d. Extraction is by open-cast mining.

2. Liburdinding (South-east Kalimantan)

a. The land area within this concession extends to some 1,000 ha.

b. The inferred coal resources have been assessed at some 14.7 million tonnes, but the quality of these resources suggests they are unlikely to be commercially utilised in the near term.

c. The deposits are classed as having high sulphur content, with a gross calorific value of between 5,800-6,200 kilocalories per kg. Sulphur content impacts negatively on price. Sulphurous gases (primarily sulphur dioxide) produced by the combustion of fossil fuels are the major cause of acid rain. There are two principal methods to reduce sulphur emissions when burning coal: the first is through crushing/washing the coal which physically separates some of the sulphur from the coal. The second method is through the use of "scrubbers", which remove most of the sulphur from the combustion gases before they are released into the atmosphere.

d. Extraction is by open-cast mining.

Rights in respect of a third coal concession, the Muser concession (also in South-east Kalimantan), acquired together with the rights over the Liburdinding concession, have been allowed to lapse. The company took the view that the cost of extending the Muser licences was not supported by the economic prospects for the concession. The coal deposits in the Muser concession were deemed to have an even higher sulphur content that the Liburdinding concession deposits.

Current Operations

In the past twelve months, the price of coal has enjoyed a significant recovery. The coal sector information site, Coal Spot.com (http://coalspot.com/) notes that the Indonesian (thermal) coal price reference (as set by the Indonesian Director General of Minerals and Coal) is up $23.65 / mt at $75.46 / mt (compared with June 2016). Readers should note that this price reference has been reduced from a 2017 high of $86.23/ mt, and down $8.35 / mt on the May 2017 price reference of $83.81/mt.

REA states in the 2016 Report and Accounts that it expects operations at the Kota Bangun concession to resume in the near future. The project agreement signed in 2013, with a 3rd party operator to develop and operate the concession, (which remained inactive after the slump in the coal price 2014-2016), has now been novated to a second 3rd party operator, who will fund the resumption of mining at the Kota Bangun site. REA expects the coal mining site to be 'dewatered' shortly, with a resumption in coal extraction soon thereafter.

Under this newly novated agreement, REA will receive an agreed payment of circa $9.00 per tonne of coal produced from the concession, with an upside ratchet based on certain coal index values. For every $5/mt increase in the value of certain coal grades, the price REA will receive escalates by $1/mt. There are virtually no costs associated with these revenues, so that they should substantially accrue to the bottom line. Readers will note that during the period that the international traded price of coal fell from $87/mt (in January 2014), to a low of $53/mt (in January 2016), the concession was inactive and has only attracted interest on the basis of the price increases over the last 12 months, implying that this agreement will remain dependent on the 3rd party operator, being able to achieve an economic price for the coal recovered.

In respect of the Liburdinding concession, the group continues to hold discussions with “several potentially interested parties”. The group’s aim is either to “divest the concession in its entirety” or to conclude an operating agreement similar to the Kota Bangun model, which would provide the group with a minimum revenue from the concession.

Balance Sheet Carrying Value

The coal companies are included in the 2016 Report and Accounts at a value of $22.773m ($20.903m), before a provision against a loan to these companies of -$3m (-$3m). The loan provision was introduced as a precaution, in the event (during a period of low coal prices) that the likely returns from the coal businesses over a reasonable timescale, would be insufficient to justify the loan carrying values. As the activities have been financed entirely by loans from REA, it might have been concluded that greater, or further provisions, would have been made. However, the company took the view that the value of the stone deposits, and the cross-guarantees between the three concession companies, gave sufficient substance to obviate the need for further provisioning.

Once the company is able to demonstrate an established pattern of revenues from the concessions, including the stone concessions, it may become possible for these provisions to be written back. The company will be looking to establish such a pattern of revenues over the next few years.

Providing that the international price of coal remains at a level which makes the recovery of coal from the Kota Bangun concession economic, these assets should finally make a contribution to the group profit and loss account. It is to be hoped that the Liburdinding concession can also become the subject of a 3rd party operating agreement, similar to the Kota Bangun agreement, providing the group with a second coal income stream.

Indonesian Coal Sector

Indonesia, is one of the world's largest producers and exporters of coal, and a leading exporter of thermal coal. Global demand for coal is largely driven by the power generation sector: some 39% of global electricity is produced by coal-fired power plants. This is in turn, driven by economics: coal is abundant, it is relatively easy to produce, and thus relatively low cost, with less expensive infrastructure relative to other energy resources.

Indonesian coal reserves are about the 10th largest in the world, constituting some 3.1% of total proven global coal reserves according to the 2016 BP Statistical Review of World Energy. The largest deposits of Indonesian coal resources are to be found in South Sumatra, South Kalimantan, and East Kalimantan (where the REA concessions are located). There are a number of smaller pockets of coal reserves on the islands of Sumatra, Java, Kalimantan, Sulawesi and Papua.

A significant portion (60%) of the country’s exported coal consists of a medium-quality thermal coal (between 5100 and 6100 cal/gram) and a low-quality thermal coal (below 5100 cal/gram). This is in the category, sub-bituminous coal. A large proportion of this coal is exported to China and India. Domestic use of coal remains relatively small in Indonesia, with exports accounting for between 70% and 80% of total coal produced. The main export destinations for Indonesian coal are China, India, Japan and Korea.

Indonesian Coal Production and Exports

Year	Indonesian Coal Production (mt)	Indonesian Coal Exports (mt)	Exports as % of National Production
2007	217	163	75.12%
2008	240	191	79.58%
2009	254	198	77.95%
2010	275	210	76.36%
2011	353	287	81.30%
2012	412	345	83.74%
2013	474	402	84.81%
2014	458	382	83.41%
2015	461	366	79.39%

Source: Indonesian Coal Mining Association (APBI) & Ministry of Energy and Mineral Resources (Indonesia)

At the current rate of production, the Indonesian Ministry of Energy estimates that Indonesian coal reserves will be fully exploited within 85 years. During the commodities boom of the 2000s, there was a significant expansion of coal production in Indonesia. Ultimately, as the Chinese economy, and global economy slowed, a supply glut occurred, from which the Indonesian sector is now just recovering. The Indonesian coal industry is dominated by a few big producers and with many small players, owning mines and concessions (mainly in Sumatra and Kalimantan), in a significant second tier. REA's coal interests, perhaps rather typical within this second tier.

Coal Pricing

The 2018 revenues ($1.5m) projected by Hardman for the REA coal and stone operations, assume that the Kota Bangun concession will ship between 100,000-200,000 mt of coal annually (over a 5-10 year period), with REA receiving a 'royalty' payment of circa $9/mt. This would imply a revenue opportunity of up to $1.9m. Readers will note that prices have been significantly firmer across the first five months of 2017, compared with any year before 2013. However, prices were firmer in November ($84.9 mt) and December ($101.7 mt).

Indonesian Government's Benchmark Thermal Coal Price (US$ MT)

By Month	January	February	March	April	May
2012	109.29	111.58	112.87	105.61	102.12
2013	87.55	88.35	90.09	88.56	85.33
2014	81.90	80.44	77.01	74.81	73.60
2015	63.84	62.92	67.76	64.48	61.08
2016	53.20	50.92	51.62	52.32	51.20
2017	86.23	83.32	81.90	82.51	83.81

Source: Ministry of Energy and Mineral Resources (Indonesia)

During the four months to April 2017, coal imports into China rose by 33% year-on-year, although this pattern is expected to slow as Chinese domestic coal production begins to rise during the year. Notwithstanding the likely negative impact of declining Chinese import volumes on international traded prices, it is believed that China is committed to its policy of intervening in domestic coal production (by cutting working days in the coal mines), in order to support the coal price and make the coal sector a profitable business for miners (when the coal price falls below 535 yuan - approx. USD $78 - per tonne).

Indonesia Coal Sector Outlook 2017

As reported by Reuters Commodities (Wed May 24, 2017), Indonesia's coal production is expected to climb 5% in 2017 and 2018 from an estimated 440 million tonnes in 2016, as miners ramp up output due to improved prices. These volumes are in excess of a production cap of 413 million metric tonnes as set by the National Development Planning Agency for the current year. Reuters reports that the agency has set a production cap of 400 million tonnes from 2019 onward in an effort to secure domestic supply. Domestic consumption is expected to increase to 101 million tonnes this year from 90.6 million tonnes in 2016, amid government concerns for national energy security. Officials from the country’s Natural Resources Ministry were quoted by Reuters as stating that “Coal ... will be part of the backbone of (Indonesia's) energy sovereignty”.

The country has a 35-gigawatt power development programme in place, of which, the Reuters’ report states that circa 40% is now under construction. By 2024, Indonesia’s domestic requirement for coal use for power generation is expected to roughly double to 151 million tonnes from 73.2 million tonnes in 2016, according to state power utility Perusahaan Listrik Negara (PLN).

Stone Interests

The stone interests comprise a concession over a substantial deposit of high grade andesite stone located to the north east of the SYB northern plantations, and an exclusive offtake agreement in respect of a much smaller limestone deposit adjacent to the PBJ plantations.

Limestone Deposit

The limestone deposit concession is held by an independent Indonesian 3rd party with which an exclusive offtake agreement has been concluded by REA. The concession has been estimated to contain deposits of between 1.2 million and 1.5 million tonnes of limestone. There may be additional deposits in adjacent areas, and it may be possible to extend the concession into these areas.

The independent 3rd party contractor has the exclusive rights to quarry the concession, but has agreed that all the stone quarried, will be transferred to the PBJ estate for crushing (by the same contractor), and then it will be sold to KCCRI. KCCRI will then sell the crushed limestone to PBJ and other group companies in the vicinity of PBJ, as well as to external customers. This crushed limestone will be used to harden roads on the PBJ estate and other group estates with reasonable access to PBJ. Production is expected to commence during Q3 2017.

Andesite Stone Concession

REA has owned the concession to quarry and crush a very substantial andesite stone deposit since 2014.

The name 'Andesite' is derived from the Andes mountain range, where the rock was originally discovered. However, Andesite rock can be found in Central America, Mexico, Japan, Indonesia, the Philippines, New Zealand, the US Pacific Northwest, and the Caribbean. Andesite rock will form in regions above subduction zones. A subduction zone is an area of tectonic plate collision where the more dense plate follows a path underneath the less dense plate. For example: where an oceanic plate margin is being pushed under a continental plate or a less dense oceanic plate. This formation usually occurs after oceanic plates melt, creating magma. When the magma erupts to the surface, it creates a fine-grained rock that crystallizes quickly. Andesite rock is used for many construction purposes, including, specifically, aggregated gravel for roadbeds.

The initial challenge for REA, is to gain access to these Andesite deposits. Currently, the concession site can be accessed via a former logging road, but this requires investment to make it suitable for sustained operations. The cost of upgrading the road will vary according to the size of trucks (weight of stone) expected to operate on the road. Large, heavy load bearing vehicles, will require a stronger, more expensive road than one being plied by smaller vehicles. A two-phase strategy would see an upgrade for smaller vehicles, thus permitting the release of cash from the concession, for a more significant upgrade of the road in due course. In 2014, the group estimated that the cost of upgrading the road to support heavy duty trucks, would amount to some $3m.

Once access is feasible, REA proposes to transfer crushed stone from the concession site to a stock pile in order to supply the CDM estate, other accessible REAK estates, and external customers. The company notes that the agricultural operations can utilise significant quantities of crushed andesite stone in their building and infrastructure construction programmes. The company also believes that there will be good external demand for the crushed andesite for road building and for use as a concrete aggregate.

Balance Sheet Carrying Value

The carrying value of the Stone company is shown in the 2016 Report and Accounts as $17.435m ($17.435m). The Stone company has provided a guarantee in respect of the amounts owed to the group by the two coal concession companies.

Group Leadership

Mr David Blackett, a non-executive director since 2008, was appointed Chairman 1st January 2016, on the retirement of Mr Richard Robinow, who continues to serve as a non-executive director on the Board. Also serving as a non-executive director since 1st January 2016 is Mr John Oakley, formerly Managing Director. The continuing presence of Mr Robinow and Mr Oakley on the Board of Directors, ensures continuity in the generational management transition of the company.

Ms Carol Gysin was appointed to the Board as Managing Director in February 2017, after the resignation of Mr Mark Parry. Ms Gysin is very familiar with REA having served as the group Company Secretary for the past 8 years. During this period, Ms Gysin has been a frequent visitor to the group's plantations and regional offices, allowing her to establish a close dialogue with all the senior operational and supervisory arms of the group's businesses. It is our understanding that Ms Gysin has implemented a revised reporting structure across this network to ensure that there is a fully integrated response to new information or changes in operating conditions for the group's widespread operations.

Mr Parry resigned from his position with the company after the authorities in East Kalimantan expressed concerns that he may have acted outside the scope of his work permit. His period as Managing Director was marked by a strong recent uptick in the pace of development and rising efficiencies. However, Mr Parry's sudden resignation for apparently infringing the terms of his work permit, underscores the specific sensitivities of operating in Indonesia. In this context, it is reassuring to note that the Board of REA Kaltim, which now comprises 4 directors, includes three Indonesian nationals, the fourth being a British ex-patriate, who has an Indonesian family.

Michael St Clair-George has also joined the board as the senior independent non-executive director. Mr St Clair-George has over 40 years' experience in the agriculture and plantation sector in South East Asia, having worked for 25 years with Harrisons & Crosfield and Harrisons Malaysian Plantations Berhad as finance director and then president director of Sipef NV's Indonesian operations. He spent 10 years as managing director at Sipef NV and recently was on the board of New Britain Palm Oil Limited.

Appropriately for a business which has all its operating divisions in Indonesia, it should be noted that 4 of the 9 most senior members of the operational and supervisory management teams in Indonesia and Singapore, are either Indonesian citizens or permanent residents with strong connections and commitments to REA's business operations in the country, and to Indonesia as a country. This group includes Mr Luke Robinow, son of Richard Robinow. Mr Robinow has made Indonesia his home, he is bi-lingual with Indonesian and English, and he is both a member of the Board of Commissioners (Indonesian supervisory board), and an active member of the senior management team in the region. The Robinow family has had a long involvement in Indonesia, stretching back to the 1960s, and with ownership of some 27.4% of the ordinary shares in issue, it has a significant commitment to the business.

Noting the growing maturity of the group's estates, and the final push to complete development across the newer estates, the group has revised the roles of the senior managers on the estates. All estate agricultural operations now fall under the remit of the former manager of immature estates, who was responsible for the development of the PBJ and CDM estates, including the impressive achieved planting rate in 2016. The former head of mature estates, is now responsible for all estate support operations, including relations with the local community and smallholders, as well as certain estate administrative functions previously undertaken by Mark Parry.

Conclusion of DSN Transaction

During December 2016, Pt Dharma Satya Nusantara TBK (DSN) completed its acquisition of a 15% stake in REA's principal operating subsidiary in Indonesia, PT REA Kaltim Plantations (REAK). The agreements between the group and DSN received regulatory approval and were completed on 2 December 2016. As a result, subsidiaries of DSN have acquired, by a combination of subscription for new shares and acquisition of existing shares, a 15% equity interest in REAK. The overall consideration for the interest acquired, amounted to the equivalent of $15 million in cash, with up to a further $850,000 payable depending upon the recovery by REAK of certain overpaid tax amounts prior to 1 January 2018. Under the provisions of the agreement (between REA and DSN) governing the transaction, DSN has made loans to REA Kaltim, to the value of some $12.0m, and during the course of 2017, we expect another $16.85m of loans to be contributed by DSN, in line with its obligations under this agreement.

DSN can acquire up to 49% of REAK within the next 5 years (subject to agreement regarding amongst other things, the price at which further shares can be acquired).

Revenue Formation Projections To 2018

Revenue Formation					
$'000	**2014**	**2015 (Restated)**	**2016**	**2017e**	**2018e**
CPO Price	665	485	521	570	590
CPKO Price	820	744	1,111	1,000	1,000
CPO Revenue	114,212	78,413	66,530	88,951	109,765
PK Revenue	10,326	9,445	10,547	11,324	13,192
Coal and Stone	0	0	0	0	1,500
PLN	1,327	0	563	600	700
Other Income		2,952	1,100		
TOTAL REVENUE	**125,865**	**90,515**	**79,265**	**100,874**	**125,157**

Source: Hardman Agribusiness / Company Reports

The coal and stone revenues indicated for 2018 ($1.5m) assume that the Kota Bangun concession will ship between 100,000-200,000 mt of coal annually with REA receiving a 'royalty' payment of circa $9/mt. Any revenues from the stone concessions would be an additional benefit.

The CPO prices shown in the table below, are the assumed 'actual average received prices' for the years detailed. Translated into CIF Rotterdam values, these received averages imply $738/mt and $758/mt CIF Rotterdam for FY17 and FY18, based on the average discount to CIF Rotterdam for the years 2014-2016 as detailed below.

Crude Palm Oil Pricing			
	CIF Rotterdam ($/mt)	**REA Average Received Price ($/mt)**	**Discount ($/mt)**
2014	818	665	153
2015	614	485	129
2016	704	521	183
Average implied Discount per mt CPO ($)			**155**

Source: Hardman Agribusiness / Company Reports

CPO Forecast

We have forecast an average price of $738/mt (CIF Rotterdam) for 2017. The average price during the period January to end May, was approximately $752/mt. Production has not returned as quickly as some commentators were predicting and this has provided a degree of support for the price during 1H 2017.

A note of caution: the expected y-o-y production gains following the El Nino weather pattern, and the competition from soya bean oil, has the potential to push the CPO price downwards later this year. Imports of soybeans to China, the world's largest buyer, were up 25% (y-o-y) to 9.59 million tonnes for May, according to Chinese customs data. This was the single largest monthly volume of imports, at least since 2010 (Thomson Reuters). While China is believed to have imported 1.29 million mt of palm oil during Q1 2017 (Oil World), up 9.3% on Q1 2016, USDA is projecting Chinese import formation for the whole of the 2017 year, unchanged.

Profit & Loss Account Projections To 2018

By 2018 revenues are projected to grow strongly on a return to more normal cropping levels and a firmer CPO price. However, the changes to the P&L, introduced by the amendment of the IAS 41 will impact on reported profits markedly.

Amendment to IAS 41

In June 2014, the International Accounting Standards Board (IASB) published amendments to 'Agriculture: Bearer Plants' (IAS 16 and IAS 41). Effective from the beginning of 1 January 2016, Bearer Plants, formerly classified as Biological Assets in the Balance Sheet, are now divided into PP&E Structure and PP&E Planting, and are treated as an investment cost, and are subject to depreciation, instead of being accorded a fair value valuation, as previously. The impact on REA's profit and loss account is expected to be significant. Whereas formerly, the application of IAS 41 resulted in a positive impact on the P&L, the new treatment has resulted in a significantly enlarged depreciation charge to the reported P&L, and this will mark the pattern of reporting for some years to come. Comparatives for 2015, restated to reflect the change in the accounting standard, indicate a reduction in pretax results of $23.8m.

Across the plantation sector, companies have responded in different ways, with many palm oil producers simply writing off the built-up value in Biological Assets in one significant adjustment; REA has decided to do this incrementally. Because of the marked impact this policy will produce on the reporting of earnings per share, we propose to show earnings per share with this additional depreciation and before the additional depreciation. See table below for illustration.

Profit & Loss (IAS 41 Amendments Effect Demonstration)

	IAS 41 Amendments (as reported in Annual report)		Pre IAS 41 Amendments (for demonstration purpose only)		
Year Ended 31st Dec	**2016 A**	**2015 A (Restated)**	**2016 ***	**2015 A**	**Comments**
$m					
Revenue	**79.3**	**90.5**	**79.3**	**90.5**	
Net (loss)/ gain arising from changes in inventory value	0.6	-1.1	0.6	-1.1	
Cost of production					
Depreciation	-21.0	-21.7	-11.0	-9.1	2016: Estimated depreciation charge pre IAS 41 Amendments
	-50.9	-61.4	-50.9	-63.3	
Gross profit	**8.1**	**6.2**	**18.0**	**17.0**	
Gross margin %	10.2%	6.9%	22.7%	18.7%	
Biological assets valuation	0.0	0.0	0.0	13.1	2016: Assume to be the same level as 2015 for comparison purposes
Other operating income	0.0	0.0	0.0	0.0	
Distribution costs	-1.1	-1.1	-1.1	-1.1	
Administrative expenses	-12.0	-11.7	-12.0	-11.7	
Operating profit	**-5.0**	**-6.6**	**4.9**	**17.2**	
EBITDA	16.8	14.1	17.0	27.3	
Investment revenue	1.7	0.3	1.7	0.3	
Finance costs	-6.0	-6.0	-6.0	-6.0	
Profit before tax	**-9.3**	**-12.2**	**0.7**	**11.5**	
Tax	-2.0	-0.7	-0.2	-6.6	
Profit for the year	**-11.3**	**-12.9**	**0.5**	**4.9**	
EPS (cents)	-48.2	-59.0	1.4	-11.2	
Dividend (GBp)	0.0	0.0	0.0	0.0	
Attributable to:					
Ordinary Shareholders	-17.8	-20.9	-6.6	-4.0	
Preference Shareholders	7.4	8.5	7.4	8.5	
Non-controlling interests	-0.9	-0.5	-0.3	0.4	
	-11.3	**-12.9**	**0.5**	**4.9**	

*Pre IAS 41 Amendments Statement is only an estimate to what the results might be before the implementation of the amendments

Source: Hardman Agribusiness

Administration & Distribution Costs

Readers will note that we expect Admin and Distribution costs to remain largely similar to recent levels, indicating that management is bearing down on costs. However, the weak Rupiah: $ exchange rate has benefited reported Admin costs, and these do remain vulnerable to upside pressure (in reported terms) should the Rupiah strengthen against the US$.

Administration Costs ($'000)

	2015	2016	2017e	2018e
Net foreign exchange losses	818	1,290	1,000	1,000
Net credit for additional pension contributions	-2,267	-	0	0
Loss on disposal of PP&E	49	12	0	0
Indonesian operations	11,556	9,621	10,200	11,000
Head office	6,160	5,377	5,500	5,500
	16,316	**16,300**	**16,700**	**17,500**
Amount incl as additional PP&E	-4,614	-4,313	-4,593	-4,813
% Admin Expenses to be capitalised	*28.3%*	*26.5%*	*27.5%*	*27.5%*
Admin Expenses as reported in P&L	**11,702**	**11,987**	**12,108**	**12,688**

Source: Hardman Agribusiness / Company Reports

Financial Metric Forecasts

$'000	2015 (Restated)	2016	2017e	2018e
EBIT	-6,553	-5,026	-1,140	13,146
EBIT Margin (%)	-7.2%	-6.3%	-1.1%	10.5%
EBITDA (before Inventory Valuation)	15,239	16,198	22,903	38,157
EBITDA Margin (before Inventory Valuation) %	16.8%	20.4%	22.7%	30.5%

Source: Hardman Agribusiness / Company Reports

Interest Cover

	2015 (Restated)	2016	2017e	2018e
Interest Cover (P&L Interest, inc. pref div)	-0.5	-0.4	0.0	0.5
Interest Cover (After BA, P&L Interest, exl. Pref div)	-1.2	-1.2	-0.1	0.7

Source: Hardman Agribusiness / Company Reports

Rising finance costs, with increased borrowings, and without any assumption of exchange rate benefit (see table below for benefit to historic P&L from exchange rate movements relative to outstanding loans and bonds), can be expected to tip the P&L into a loss before tax, for both 2017 and 2018, and this will likely have implications for the dividend policy in respect of the ordinary shares. We are not assuming a return to the payment of ordinary dividends before 2019.

Borrowings

$'000	2015 (Restated)	2016	2017e	2018e
Exchange Rate Benefit	7,640	9,092	0	0

Source: Hardman Agribusiness / Company Reports

Profit & Loss				
Year Ended 31st Dec	**2015 (Restated)**	**2016**	**2017 e**	**2018 e**
$m				
Revenue	**90.5**	**79.3**	**100.9**	**125.2**
Net (loss)/ gain arising from changes in inventory value	-1.1	0.6	0.0	0.0
Cost of production				
Depreciation	-21.7	-21.0	-24.0	-25.0
	-61.4	-50.9	-64.6	-72.8
Gross profit	**6.2**	**8.1**	**12.2**	**27.3**
Gross margin %	6.9%	10.2%	12.1%	21.9%
Biological assets valuation	0.0	0.0	0.0	0.0
Other operating income	0.0	0.0	0.0	0.0
Distribution costs	-1.1	-1.1	-1.3	-1.5
Administrative expenses	-11.7	-12.0	-12.1	-12.7
Operating profit	**-6.6**	**-5.0**	**-1.1**	**13.1**
EBITDA	14.1	16.8	22.9	38.1
Investment revenue	0.3	1.7	0.3	0.2
Finance costs	-6.0	-6.0	-17.6	-20.0
Profit before tax	**-12.2**	**-9.3**	**-18.5**	**-6.7**
Tax	-0.7	-2.0	-2.0	-2.0
Profit for the year	**-12.9**	**-11.3**	**-20.5**	**-8.7**
EPS (cents)	-59.0	-48.2	-60.9	-34.7
Dividend (GBp)	0.0	0.0	0.0	0.0
Attributable to:				
Ordinary Shareholders	-20.9	-17.8	-24.7	-14.1
Preference Shareholders	8.5	7.4	7.3	7.2
Non-controlling interests	-0.5	-0.9	-3.1	-1.7
	-12.9	**-11.3**	**-20.5**	**-8.7**

Source: Company Report, Hardman Agribusiness

Cost of Production

REA has traditionally been one of the most efficient operators within the listed palm oil sector. Its cash cost per mt of CPOe, remains below $400/mt (according to our projections) out to 2018, with the increase on 2015 attributable to rising investment in fertiliser and higher numbers of harvesters as the mature estate grows. Readers will note that cost per hectare evolved lower in 2016, while cash cost per mt CPOe rose. This reflected the lower levels of fruit production following the El Nino weather pattern. In 2017 the principal driver of the increase in cash cost of production, will be an increased investment in fertiliser. In 2018, as estate productivity returns to more levels, then our projections suggest the cash cost will fall closer to the 2015 level.

Cost of Production ($/mt)				
	2015 (Restated)	**2016**	**2017e**	**2018e**
Direct Cash cost per CPOe	-352	-371	-386	-359
Cost per hectare	-2,637	-2,279	-2,600	-2,767

Source: Hardman Agribusiness / Company Reports

Balance Sheet Projections To 2018

Readers will note that our projections indicate that the Net Debt/Equity ratio will continue to widen (in the absence of any increase in the equity base), as total borrowings increase in order to fund the development of the plantations and to meet financing costs.

By end 2018, without any increase in permanent capital, the D/E ratio could push beyond 114% according to our projections. The Indonesian banks appear to take a highly commercial approach to the percentage of total capital they are willing to provide to plantation development, in competition with other sources of capital. Noting the medium term cash generative profile of the REA palm oil operations, as the operations progressively mature, it may be practical for the company to continue to expand its operations with a widening D:E ratio.

In 2017, the group is expecting to refinance some $10m of its Sterling Notes, which are maturing this year. Already, REA has exchanged some $13.8m of its 7.5% US Dollar Notes 2017 with the new 7.5% US Dollar Notes 2022. Along with the repackaging of the group's Indonesian bank facilities, now $95.3m, these actions have helped to extend the maturity profile of the group's borrowings.

Balance Sheet

Year Ended 31st Dec	2014 (restated)	2015 (restated)	2016	2017 e	2018 e
$m					
NON-CURRENT ASSETS					
Goodwill	12.6	12.6	12.6	12.6	12.6
Intangible Assets	0.0	0.0	4.2	4.1	3.1
Biological Assets	0.0	0.0	0.0	0.0	0.0
Property, Plant & Equipment	459.1	468.9	471.9	480.4	491.3
Prepaid Operating Lease Rentals	33.9	34.3	34.2	34.5	34.8
Indonesia Stone and Coal Interests	31.3	35.3	37.2	38.2	39.2
Deferred Tax Assets	8.9	15.7	12.8	12.8	12.8
Non-Current Receivables	2.7	1.4	3.1	3.1	3.1
	548.5	568.1	576.0	585.8	596.9
CURRENT ASSETS					
Inventories	16.2	11.2	15.8	15.2	14.4
Biological Assets	2.3	2.1	2.0	2.0	2.0
Investments	0.0	2.2	9.9	1.5	1.5
Trade & other receivables	25.5	29.1	42.6	42.2	41.0
Cash & equivalent	16.2	15.8	24.6	10.8	16.6
	60.1	60.3	94.8	71.6	75.6
TOTAL ASSETS	**608.7**	**628.4**	**670.9**	**657.4**	**672.5**
CURRENT LIABILITIES					
Trade and other payables	17.8	27.0	43.4	43.2	42.4
Current Tax Liabilities	2.6	3.4	0.3	0.3	0.3
Bank Loans	40.3	50.9	28.6	33.8	41.6
Sterling notes	14.7	0.0	10.1	0.0	0.0
US dollar notes	0.0	0.0	20.0	0.0	0.0
Other Loans & Payables	1.2	0.1	0.5	0.2	1.4
	86.2	81.4	103.0	77.4	85.7
NON-CURRENT LIABILITIES					
Bank loans	60.6	72.0	97.8	135.4	166.6
Sterling notes	37.7	55.9	37.0	37.0	37.0
US dollar notes	33.5	33.6	23.6	23.6	23.6
Deferred tax liabilities	77.2	86.1	80.8	80.8	80.8
Other loans & payables	6.8	5.6	19.0	34.9	34.9
	215.8	253.2	258.3	311.7	342.9
TOTAL LIABILITIES	**302.1**	**334.6**	**361.3**	**389.2**	**428.7**
TOTAL EQUITY	**306.6**	**293.8**	**309.6**	**268.2**	**243.8**

Source: Company Report, Hardman Agribusiness

Net Debt

$000	2014 R	2015 R	2016	2017e	2018e
Total Debt	196,432	212,430	229,679	259,205	298,205
Cash	16,224	15,758	24,593	10,779	16,583
Net Debt	180,208	196,672	205,086	248,426	281,622
Net Debt/Equity (inc. pref in equity)	58.8%	66.9%	66.3%	92.6%	115.5%

Source: Company Report, Hardman Agribusiness

Cash Flow Projections To 2018

Management is committed to fastest possible development of the group's land bank, and as noted above, we anticipate that this will result in continued pressure on the Balance Sheet and specifically the D:E ratio. The tough realities of operating the businesses with reduced harvests and sub-optimal estate infrastructure, following the 2 El-Nino years and subsequent heavy rains in Q4 2016, is evident in the table below. Net cash from operations is reduced to a level that is inadequate to support investment in estate development and to satisfy the company's obligations to providers of capital. Instead group borrowings, continue to rise. We have included in our assumptions for 2017, loans to REA Kaltim, from DSN to the value of some $17.8m, as expected under the DSN transaction.

Cash Flow

Year Ended 31st Dec	2015 (restated)	2016	2017 e	2018 e
$m				
NET CASH FROM OPERATING	**20.1**	**2.6**	**-2.7**	**9.7**
Interest received	0.3	1.7	0.3	0.2
Proceeds from disposal of PP&E	2.5	0.1	0.0	0.0
Purchase of PP&E	-32.3	-31.1	-31.6	-33.9
Expenditure on Biological Assets	0.0	0.0	0.0	0.0
Expenditure on prepaid operating lease rentals	-1.3	-0.4	-1.0	-1.0
Investment in Indonesian stone & coal	-4.0	-1.9	-1.0	-1.0
CASH FROM INVESTING ACTIVITIES	**-34.8**	**-31.6**	**-33.3**	**-35.7**
Preference dividends paid	-8.5	-7.4	-7.3	-7.2
Ordinary dividends paid	-4.2	0.0	0.0	0.0
Repayment of borrowings	-9.6	-11.0	-3.1	-6.0
Proceeds of issue of ordinary shares	6.8	13.0	0.0	0.0
Proceeds of issue of preference shares	7.8	0.0	0.0	0.0
Redemption of US dollar notes	0.0	0.0	-20.0	0.0
Issuance of Sterling notes, by exchange	39.9	0.0	0.0	0.0
Redemption of Sterling notes	-39.9	0.0	-10.1	0.0
Proceeds of issue of sterling notes (net of cost)	4.1	1.9	0.0	0.0
Purchase of sterling notes	-2.2	0.0	0.0	0.0
Payment on termination of hedging contract	-10.2	0.0	0.0	0.0
Net Sale and repurchase of US dollar notes	0.0	-0.1	0.0	0.0
New bank borrowings drawn	30.3	14.9	45.9	45.0
Proceeds of sale of shareholding in subsidiary	0.0	14.0	0.0	0.0
Loan from related parties	0.0	12.4	16.9	0.0
CASH FROM FINANCING	**14.5**	**37.8**	**22.2**	**31.8**
NET INCREASE IN CASH	**-0.3**	**8.9**	**-13.8**	**5.8**
Cash b/f	16.2	15.8	24.6	10.8
Effect of exchange rate	-0.2	0.0	0.0	0.0
CASH BALANCE C/F	**15.8**	**24.6**	**10.8**	**16.6**

Source: Company Report, Hardman Agribusiness

Borrowings

	2015 R	2016	2017 e	2018 e
Bank Loan	122,940	126,399	169,223	208,223
Sterling Notes	55,853	47,140	37,040	37,040
US Dollar Notes	33,638	43,694	23,646	23,646
Loans from related parties		12,446	29,296	29,296
New Bank Borrowings	30,326	14,939	45,924	45,000
Repayment of Bank Loan	-9,620	-11,004	-3,100	-6,000
Repayment of Sterling Notes		0	-10,100	0
New Sterling Notes Issuance	4,086	1,922		
Purchase of Sterling Notes	-2,158			
New dollar Notes		-89		
Repayment of US Dollar Notes		0	-20,048	0
New Borrowings from related parties (DSN)		12,446	16,850	
NET DEBT/ (Net Cash)	**196,673**	**205,086**	**248,426**	**281,622**
Interest on cash	259	1,742	256	220
Interest on bank loans	-8,130	-12,617	-14,781	-18,872
Interest on Sterling Notes	-5,042	-5,184	-4,209	-3,704
Interest on US Dollar Notes	-2,716	-2,899	-2,862	-2,010
Interest on Loan from related parties		-273	-1,461	-2,051
Other financial costs	-2,572	-251	-1,000	-1,000
Exchange rate Benefit	7,640	9,092	0	
Interest to pay	-10,820	-12,132	-24,313	-27,637
% Interest to be Capitalised	*45%*	*51%*	27.5%	27.5%
Interest included into Balance Sheet	-4,869	-6,127	-6,686	-7,600
Interest costs for P&L	-5,951	-6,005	-17,627	-20,037

Source: Company Report, Hardman Agribusiness

Valuation Discussion

In the discussion below we review the current valuation of REA using the DCF methodology, the sum of parts methodology, and we reference recent M&A activity. The sum of parts and DCF methodologies suggest that the current valuation of the group's operations, is at a discount of circa 18%-28% to underlying value. The M&A references indicate that the palm oil operations (REAK) are trading at a steeper discount, in a range of 21.8% - 48.4%. The sector M&A data imply a control premium of 24.5%, which if applied to REA's planted estates, would produce a value of $13,493 per planted hectare, compared with $10,838 at 7th June 2017.

DCF Methodology

For the purposes of this report, we have revised down the WACC previously used for arriving at cash flow based valuation outcomes for REA, from 13% to 12.2%, in the light of a declining yield on the 10-year Indonesian bond.

WACC Calculation

	%	Comments
Risk Free Rate	6.95%	Indonesia 10-yr Gov bond
Palm Sector Beta	0.55	Average of Leading Palm Sector Companies in Indonesia
Market Premium (Indonesia)	8.82%	Stern NYU
CoE	11.79%	
Country Risk Premium	3.13%	Stern NYU
CoE	14.92%	
CoD	10.25%	
We	41%	
Wd	59%	
WACC	**12.2%**	

Source: Hardman Agribusiness

Applying this WACC to our long-range cash flow projections, a valuation range of £4.44 - £4.76 per share is suggested, depending on the terminal growth rate applied. We would argue for a terminal growth rate range of 1% (bearish outlook), to 3%, more reflective of emerging market growth rates, which are the big consumers of palm oil. The WACC continues to be conservative, as its drivers are all firmly based on Indonesian risk indicators, and this makes no adjustment for REA being listed on the London Stock Exchange and therefore subject to the good governance requirements of the London exchange.

Valuation – Market Cap (£m)

	Terminal Growth Rate						
	0.0%	0.5%	1.0%	1.5%	2.0%	2.5%	3.0%
9.5%	367	374	381	389	399	410	422
10.0%	323	329	335	341	349	357	367
10.5%	284	288	293	298	304	311	319
11.0%	248	252	256	260	265	270	276
11.5%	216	219	222	225	229	234	239
12.2%	175	177	180	183	186	189	193
12.5%	159	161	164	166	169	172	175
13.0%	135	136	138	140	143	145	148
13.5%	112	113	115	117	119	121	123
14.0%	91	92	94	95	97	98	100
14.5%	72	73	74	75	77	78	80
15.0%	54	55	56	57	58	59	61

Source: Hardman Agribusiness

Valuation – Share Price (p)

	Terminal Growth Rate						
	0.0%	0.5%	1.0%	1.5%	2.0%	2.5%	3.0%
9.5%	906.4	922.7	940.8	961.2	984.3	1010.7	1041.2
10.0%	797.8	811.1	825.7	842.1	860.6	881.5	905.4
10.5%	700.2	711.0	723.0	736.3	751.1	767.8	786.7
11.0%	612.0	620.9	630.7	641.6	653.6	667.0	682.2
11.5%	532.1	539.5	547.5	556.4	566.2	577.1	589.3
12.2%	432.1	437.8	444.0	450.8	458.2	466.4	475.5
12.5%	393.0	398.1	403.7	409.7	416.3	423.6	431.7
13.0%	332.2	336.5	341.1	346.2	351.7	357.7	364.3
13.5%	276.4	280.0	283.9	288.1	292.7	297.6	303.1
14.0%	225.1	228.1	231.3	234.9	238.7	242.8	247.3
14.5%	177.6	180.2	183.0	185.9	189.1	192.6	196.3
15.0%	133.8	136.0	138.3	140.8	143.5	146.4	149.5

Source: Hardman Agribusiness

DSN Interest / Sector M&A Activity

Noting that DSN can acquire up to 49% of REAK within the next 5 years (subject to agreement regarding amongst other things, the price at which further shares can be acquired), readers will note that the palm oil business operations are trading at an implied discount to the valuation levels evidenced by recent sector M&A activity.

There has been much discussion of the November 2016 valuation provided for MP Evans estate in East Kalimantan by Messrs Khong & Jaafar SDN BHD, as a component in the company’s defence against the valuation placed on it by KLK in the course of its bid for the UK listed company. The Khong & Jaafar SDN BHD valuation of the MP Evans East Kalimantan estate out turned at $21,000 per planted ha. While this sets one reference for palm oil plantation valuation, so too does the price achieved by MP Evans for its interests in PT Agro Muko. In December 2016, MP Evans announced the sale of its 36.84% share in PT Agro Muko, (equivalent to 7,200 planted ha) to joint venture partner, the Belgian Sipef group, for the sum of US$100 million or

$13,860 per ha. The Agro Muko transaction provided strong validation for the 21st November, 2016 valuations provided by Khong & Jaafar SDN BHD, at which time it valued Agro Muko at $13,100 per ha.

The Agro Muko valuation on a per planted hectare basis, was close also to the value implied by the KLK offer of £7.40 for each MP Evans ordinary share. Adjusting the KLK offer for cash on the MP Evans balance sheet (from the NAPCo stake disposal), and for the value of the Malaysian property interests, the value per planted hectare (equity share basis) outturns at circa $13,090.

The KLK bid for MP Evans, and the Agro Muko transaction, both point to a value per planted (Indonesian) hectare (in the context of M&A activity), in a range of $13,000 to $14,000 per planted ha. This contrasts with the current capital markets weighted average planted hectare value of $11,135, for REA's Indonesian peer group.

Indonesian Peer Group EV/ Planted Hectares

Company	EV/ha ($)
Anglo-Eastern Plantations	6,604
Astra Agro Lestari	9,957
Austindo Nusantara Jaya Agri	10,590
Bakrie Sumatera Plantations	7,700
Bumitama Agri	11,155
Dharma Satya Nusantara	8,156
Eagle High (BW Plantation)	9,107
First Resources	14,292
Golden Agri	15,779
London Sumatra Indo	6,075
MP Evans	13,690
Provident Agro	6,558
R.E.A. Holdings	10,838
Salim Ivomas Pratama	6,413
Sampoerna Agro	6,138
Sawit Sumbermas Sarana	40,503
Sipef	14,343
Socfinasia	8,089
Weighted Average	**11,135**

Source: Hardman Agribusiness and Thomson Reuters 9th June, 2017

The Indonesian peer group trades in a wide EV/ha range of $6,075 to $40,503, with a weighted average EV/planted hectare of $11,135, implying a 24.5% control premium for the Agro Muko transaction. It is interesting to note that the MP Evans EV/ha remains between the level of the KLK bid value and the Agro Muko transaction value, with the market noting that KLK is steadily increasing its stake in the UK company. Applying a 24.5% control premium to our adjusted EV/planted hectare for REA, would give $13,493.

By comparison with the valuation achieved in the Agro Muko transaction in December 2016, REA's plantation assets are trading at an implied discount of 21.8% (see calculation below), June 7th, 2017.

Readers will note also, that the current enterprise valuation of REA's 85% holding in its East Kalimantan plantations (adjusted for non-palm oil operations): $10,838 / planted ha (see table below), stands at a discount of 48.4% to the $21,000 / ha proposed by Khong & Jaafar SDN BHD for MP Evans' 10,250 ha East Kalimantan estate.

Adjusted EV/Equity Planted Hectares 7th June 2017	
	US$ m
REA Holdings Market Cap (Ordinary shares)	173.2
REA Holdings Market Cap (Preference shares)	82.3
REA Net Debt (end Dec 2016)	205.1
	460.6
Loans Contributed By Non-Controlling Shareholders (DNS)	12.4
EV Adjusted for Non-Controlling Shareholders Loan	448.2
Value For Electricity Operation (Hardman Agribusiness Estimates)	16.3
Balance Sheet Carrying Value of Stone & Coal Operations	37.2
Adjusted EV for REA Holdings Palm Operations	394.7
REA Holdings holds 85% Share of Planted Hectares	
85% of end 2016 Planted Hectares	36,419
Adjusted EV / Planted Hectare (US$)	10,838

Source: Hardman Agribusiness

Sum Of Parts Methodology

The sum of parts valuation calculation below implies that REA's current EV stands at a discount of some 17.5% to this calculation of the value of the group's portfolio of business assets.

Sum of Parts Valuation 7th June 2017	
Palm Operations	
Adopting Agro Muko Transaction Value ($/ha) for Valuation Driver	13,860
Total Planted Hectares	42,846
Total Value for Palm Operations ($m)	**593.8**
REA Holdings' Equity Share	85%
Estimated Value for Palm Operations ($m)	**504.8**
Value for Electricity Operations (Hardman Estimate) ($m)	**16.3**
Balance Sheet 2016 Carrying Value for Stone & Coal Interests ($m)	**37.2**
Estimated Total Sum of the Parts ($m)	**558.3**
Current Enterprise Value ($m)	**460.6**

Source: Hardman Agribusiness

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