GROUP FINANCE DIRECTOR'S REVIEW

ACCOUNTING POLICIES

The Directors continue to review the appropriateness of the accounting policies adopted by the Group having regard to developments in International Financial Reporting Standards. There were no new standards or amendments effective and relevant in 2017 that had a material impact on the Group's accounting policies and disclosures.

RESULTS

Revenue at US$17.7 billion was 12% up on 2016. Gross revenue, including 100% of revenue from associates and joint ventures, which is a measure of the full extent of the Group's operations, increased by 9% to US$37.9 billion. This increase was largely from Astra with its gross revenue, including 100% of revenue from its associates and joint ventures, rising 10% to US$30.9 billion, reflected in all businesses, except financial services which was little changed from the previous year.

Underlying operating profit from the Group's parent company and subsidiaries, excluding non-trading items, which amounted to a net gain of US$11 million (2016: US$25 million), was US$277 million higher at US$1,752 million. Astra's underlying operating profit increased by 18% to US$1,675 million, contributed largely by its heavy equipment, mining, construction and energy business as significantly stronger coal prices led to improved performances in its construction machinery and mining contracting business as well as its mining operations. The Group's Direct Motor Interests contribution saw a 5% decline in underlying operating profit as the strong results achieved by Cycle & Carriage Singapore were offset by the loss in Cycle & Carriage Bintang. Newly acquired Vinamilk contributed a dividend of US$9 million.

Net financing charges, excluding those relating to the Group's consumer finance and leasing activities, increased by US$8 million to US$47 million, mainly due to the higher levels of average net debt at the Group's parent company and Astra parent company. Interest cover excluding the financial services companies remained strong at 32 times (2016: 29 times), calculated as the sum of underlying operating profit and share of results of associates and joint ventures divided by net financing charges.

	2017			2016		
	Underlying profit US$m	Non-trading items US$m	Total US$m	Underlying profit US$m	Non-trading items US$m	Total US$m
Revenue	17,701	–	17,701	15,764	–	15,764
Operating profit	1,752	11	1,763	1,475	25	1,500
Net financing charges	(47)	–	(47)	(39)	–	(39)
Share of results of associates and joint ventures	562	16	578	346	34	380
Profit before tax	2,267	27	2,294	1,782	59	1,841
Tax	(489)	–	(489)	(337)	(6)	(343)
Profit after tax	1,778	27	1,805	1,445	53	1,498
Attributable to:						
Shareholders of the Company	788	23	811	679	23	702
Non-controlling interests	990	4	994	766	30	796
	1,778	27	1,805	1,445	53	1,498

The Group's share of underlying profit of associates and joint ventures increased by US$216 million or 62% to US$562 million, due mainly to the improved contribution from Astra's associates and joint ventures with a return to profitability at Permata Bank and higher profits from its automotive businesses. The associates and joint ventures of the Group's Direct Motor Interests saw a decline in contribution, due mainly to lower automotive profit in Truong Hai Auto Corporation which faced a very competitive environment in Vietnam ahead of the removal of import tariffs in January 2018, partly compensated by improved real estate results. Siam City Cement's contribution was down, following one-off restructuring expenses and lower domestic volumes and prices, coupled with higher energy costs. Refrigeration Electrical Engineering Corporation reported higher contributions from all its businesses.

The effective tax rate of the Group, excluding associates and joint ventures in 2017 was 28%, compared to 23% in the previous year. Excluding non-trading items, the Group's effective tax rate was 29%, compared to 23% in 2016. The effective tax rate in 2016 was lower due to a new tax incentive on fixed asset revaluation that gave rise to deferred tax assets within the Group's Indonesian subsidiaries.

The Group's underlying profit attributable to shareholders for the year was 16% up at US$788 million. The Group's profit attributable to shareholders was US$811 million compared to US$702 million in 2016 after accounting for net non-trading gains of US$23 million due largely to investment property revaluations and net gains arising on the disposal of interests in certain companies and investments, partly offset by impairment charges. The net non-trading gain in 2016 of US$23 million arose from the sale of land and investment properties revaluations.

DIVIDENDS

The Board is recommending a final one-tier tax-exempt dividend of US¢68 per share (2016: US¢56 per share), which together with the interim dividend will give a total dividend of US¢86 per share (2016: US¢74 per share) for the year. Shareholders have the option to receive the dividend in Singapore dollars and in the absence of any election, the dividend will be paid in US dollars.

CASH FLOW

Cash inflow from the Group's operating activities was US$1,655 million, US$238 million higher than the previous year, mainly due to higher inflows from Astra's financial services and heavy equipment, mining, construction and energy businesses.

The net cash outflow from investing activities was US$2.3 billion, US$1.5 billion higher than the previous year mainly due to the Group's investment in Vinamilk. Capital expenditure and investments mainly comprised:

- US$66 million for the purchase of intangible assets, which included US$52 million for the acquisition costs of contracts in Astra's general insurance business and US$37 million for the purchase of leasehold land use rights for use by Astra's businesses and Cycle & Carriage Bintang;
- US$745 million of property, plant and equipment mainly by Astra comprising US$513 million of heavy equipment and machinery for its heavy equipment, mining, construction and energy businesses, US$113 million of equipment and network development for its automotive businesses and US$75 million to develop its agribusiness;
- US$162 million for additions to investment properties in Astra (mainly for Menara Astra) and US$50 million for additions to bearer plants in Astra;
- US$14 million mainly for investments in Astra's mining subsidiaries;
- US$669 million for investments in associates and joint ventures which included US$44 million for Astra's subscription to Permata Bank's rights issue, Astra's acquisitions and capital injection of US$481 million including Bhumi Jati Power and investments in toll roads. The Company also participated in Siam City Cement's rights issue and purchased additional shares for US$138 million;
- US$1.6 billion for investments, mainly the purchase of a 10% interest in Vinamilk for US$1.2 billion and other investments by Astra's general insurance business.

The contribution to the Group's cash flow from disposals for the year amounted to US$454 million which arose mainly from the sale of other investments by Astra's general insurance business and disposal of subsidiaries as well as associates and joint ventures by Astra.

The cash inflow from financing activities was US$823 million, compared to US$307 million of cash outflow in the previous year mainly due to a higher drawdown of borrowings to finance the investment in Vinamilk. In 2017, the net cash inflow from borrowings and the receipt of US$68 million from non-controlling interests for the investment in Astra Land Indonesia were offset by higher dividends paid to non-controlling interests and dividends paid by the Company.

TREASURY POLICY

The Group manages its exposure to financial risk using a variety of techniques and instruments, to mitigate foreign exchange and interest rate risks and to provide a degree of certainty about costs. The investment of the Group's surplus cash resources is managed to minimise principal risk while seeking to enhance yield. Appropriate credit guidelines are in place to manage counterparty risk.

When economically sensible to do so, borrowings are taken in local currency to hedge foreign exposures on investments. A portion of borrowings is denominated in fixed rates. Adequate headroom in committed facilities is maintained to facilitate the Group's capacity to pursue new investment opportunities and to provide some protection against market uncertainties. Overall, the Group's funding arrangements are designed to keep an appropriate balance between debt and equity from banks and capital markets, both short and long term, to give flexibility to develop the business.

The Group's treasury operations are managed as cost centres and are not permitted to undertake speculative transactions unrelated to underlying financial exposures.

The Group's financial risk factors are set out on page 79.

FUNDING

The Group is well financed with strong liquidity. The Group's consolidated net debt, excluding borrowings within Astra's financial services subsidiaries, was US$819 million in 2017, representing a gearing of 6%, compared to net cash of US$709 million in 2016. The Company's net debt was US$1.2 billion compared to net cash of US$154 million at the end of 2016. The change from net cash to net debt in the Group and in the Company was due primarily to the investment in Vinamilk. Net debt within the Astra's financial services operations decreased slightly to US$3.4 billion at the end of 2017.

At the year-end, the Group had undrawn committed facilities of some US$2.7 billion. In addition, the Group had available liquid funds of US$2.6 billion.

BALANCE SHEET

The Group continues to have a strong balance sheet. Shareholders' funds increased by 12% to US$6.4 billion. Property, plant and equipment increased by US$432 million to US$3.4 billion, mainly due to the purchase of heavy equipment and machinery. Interests in associates and joint ventures grew by US$564 million to US$4.3 billion, from the Group's share of profits, subscription to Permata Bank's and Siam City Cement's rights issues and the purchase of new and additional interests, including Bhumi Jati Power and investments in toll roads. Non-current investments increased by US$1.5 billion to US$2.0 billion due mainly to the Group's investment in Vinamilk. Trade debtors increased mainly due to higher receivables from heavy equipment stocks. Stocks increased marginally, in anticipation of higher sales demand for heavy equipment and higher inventory days in Astra's automotive businesses. Trade creditors increased mainly due to higher purchases of heavy equipment stocks.

RISK MANAGEMENT REVIEW

A review of the major risks facing the Group is set out on page 42.

Adrian Teng
Group Finance Director
1st March 2018