



REVITALISING THE PALM OIL INDUSTRY THROUGH INDEPENDENT SMALLHOLDERS

Malaysia Young Leaders Programme | April 2018

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Executive Summary (1/2)

INTRODUCTION

Globally, 40% of oil palm is grown by smallholders. Palm oil, the most consumed oil in the world is one of the most productive and versatile crops. This makes the palm oil sector incredibly attractive for smallholder farmers who cultivate the crop in 43 countries around the world. Smallholders typically sell their harvested fruits to dealers, millers or corporations who process the oil for consumer use. Despite its attractive returns, smallholders are often marginalised within the supply chain. This is no different for Malaysia's 235,000 independent oil palm smallholders who are generally defined as having less than 40ha of land and who make up almost 17% of the total land under cultivation.

In contrast to “schemed” or “associated” smallholders who are organised or directly managed by public or private sector parties, independent smallholders are self-organised, self-managed and self-financed, although they may receive some extension services from government agencies or NGOs.

Some of the challenges faced by independent smallholders in Malaysia include immediate pressure to meet global and national certification standards and a lack of sustainable agronomic knowledge, farm training and financial support. They are over reliant on dealers to sell their Fresh Fruit Bunches (FFBs) and have little or no clear relationship with mills or corporate actors in the value chain. Furthermore they are vulnerable to price volatility and lack access to market data. All of these factors combine result in lower quality and yield and a seasonal struggle in independent smallholder communities to make ends meet.

Rapid expansion of land under cultivation to meet global demand for palm oil has increased public and government concern regarding its environmental and social impacts.

Key industry players have developed certification standards such as Roundtable on Sustainable Palm Oil (RSPO) to assure consumers and regulators the commodities are produced sustainably. This has also affected corporate producers in Malaysia who now face constraints in terms of new land concessions which means they must look at sourcing produce from outside of their own large-scale plantations.

To ensure the livelihoods of independent smallholders in Malaysia are preserved and improved, new inclusive business models are needed to address these key challenges and strengthen their position in the value chain.



Executive Summary (2/2)

INDEPENDENT SMALLHOLDERS PALM REVITALISATION ORGANISATION (isPRO)

This proposal recommends a new inclusive business model by establishing the **Independent Smallholders Palm Revitalisation Organisation (isPRO)**. A company limited by guarantee (CLBG), **isPRO** aims to bring together key players from the public, private and civil sectors to provide more choices for independent smallholders when it comes to growing and selling their crops thus improving their livelihoods and the overall state of the palm oil sector in Malaysia.

Key functions of **isPRO** include:

- Organising independent smallholders into clusters for more effective delivery of its services;
- Facilitating Fresh Fruit Bunch (FFB) trading activities between clusters and buyers such as mills;
- Initiating the Sustainable Outgrower Programme (SOP) to match clusters with buyers based on FFB demand and provide contract drafting services to ensure terms that are transparent and fair. The corporate buyers then provide technical assistance, subsidised farming inputs and funding for smallholders to meet certification standards in exchange for guaranteed supply;
- Increasing plantation management options for independent smallholders by connecting them with a pool of service providers. This generates healthy competition, results in transparent pricing and matches supply with demand;
- Making all **isPRO** services and those of plantation management service providers available through a mobile application. Smallholders can also seek instant support through the application and access real time market data.

It is proposed that a five year pilot project be initiated in Perak. The goal for the pilot site is to cover approximately 35% of oil palm planted area owned by independent smallholders.

Financial Highlights

isPRO requires an initial seed funding of RM3 million.

- **isPRO** is expected to achieve profitability during its second year of operations and is estimated to make a total profit of RM9.7million in five years
- For the first five years, 30% of profits (excluding Year 1) will be allocated to the **isPRO** Social Development Fund and this amount will subsequently increase annually. The fund aims to empower independent smallholders through capacity building, research and development and community services.





INTRODUCTION & BACKGROUND

Malaysia Young Leaders Programme (YLP)



- The **Global Institute For Tomorrow (GIFT)** is an independent pan-Asian think tank providing content-rich and intellectually challenging executive education from an Asian worldview.
- GIFT's methodology invites participants to build greater self-awareness and test personal resilience whilst creating robust new business models linked to contemporary challenges and opportunities.
- The Malaysia Young Leaders Program (YLP) is an experiential learning programme designed for young professionals from the public, private and civil sectors to develop their leadership skills whilst engaging in constructive dialogue and cross-sectoral collaboration to overcome key challenges in Malaysian society.

Project Team

- 22 young Malaysian professionals representing multinational and local companies, government bodies and civil society organisations, participated in the Malaysia YLP in Kuala Lumpur and Perak in April 2018.
- In partnership with Wild Asia, participants worked to produce an inclusive business model to integrate independent smallholders into the global supply chain.

NEC

UOB



A platform for constructive dialogue & cross sectoral collaboration

Project Partner : Wild Asia

Wild Asia is a Malaysia-based social enterprise established in 2003 which aims to foster future sustainable development by helping businesses, organisations and consumers to lessen their environmental footprint. Wild Asia's work takes place within key sectors that are closely connected to the negative externalities of the 21st century globalised world and one of the organisation's key activities is improving palm oil traceability.



Wild Asia Palm Oil Initiative

Wild Asia's fundamental goal in their palm oil initiative is to increase the growth of traceable and certified palm oil. This is achieved in three ways:

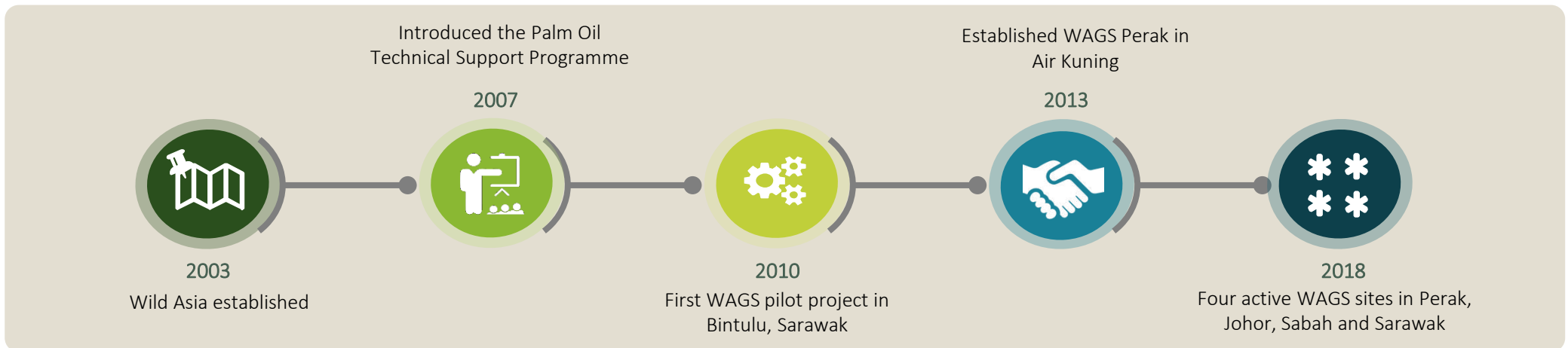
- **Consultancy** – Technical assessments and strategic advice to producers, investors, banks and governments
- **Training** – Designing and running capacity building programmes
- **Implementation** of schemes and projects to promote the adoption of international and national standards

Wild Asia Group Scheme (WAGS)

WAGS is a group management system to support groups of independent smallholders to achieve sustainable production of palm oil. Funded through a partnership model, the scheme promotes sustainable practices among independent smallholders by moving towards RSPO certification.

WAGS Air Kuning, Perak

Adapting to the local challenges in Perak, a three-way partnership model was formed between Cargill, an independent mill and Wild Asia. Cargill funds the certification of independent smallholders that supply to the independent mill. As of 2018, just under 250 farmers are RSPO certified under the WAGS group scheme in Perak.



Scope of Project (1/2)

Programme Objectives

- Gain insights into the key challenges faced by independent smallholders in Perak and explore opportunities for a new scalable Public Private Partnership that would overcome these challenges.
- Develop an inclusive business model to revitalise the livelihoods of independent smallholders, promote sustainability and traceability within the value chain and help integrate smallholders into the global supply chain.
- Produce recommendations that take into account:
 - The balance between commercial sustainability and the social mandate of the business model;
 - Overcoming key challenges faced by independent smallholders without marginalising other stakeholders in the value chain;
 - The potential for replication and scalability in other states across Malaysia and the wider region.



Scope of Project (2/2)

The Malaysia YLP is a one month leadership programme delivered over two modules and combining classroom and field-based learning.

Methodology for Field Project

- Site visits, meetings and focus group sessions with diverse stakeholders to critically evaluate the palm oil sector.
- Information gathering and analysis; business model generation and business planning sessions.

Insights from key stakeholders including:

- Site visits to Sime Darby Plantation Academy in Carey Island, Roundtable for Sustainable Palm Oil (RSPO) Secretariat, Ministry of Plantation, Industries and Commodities (MPIC), Malaysia Palm Oil Certification Council (MPOCC) and the National Association for Smallholders (NASH).
- Participants also met with Orang Asli independent smallholders, harvestors, millers and dealers in Perak.

Outcome

- Development of a business plan with analysis of four key areas: Business Model; Operations & Strategic Partnerships; Organisational Structure, Governance & Social Impact and Financial Analysis & Investment.
- Presentation of highlights of business plan to representatives from the government and the palm oil industry, professionals from international NGOs, dealers, independent smallholders, university students and the media.



Perak, Malaysia



Known as Darul Ridzuan (“*The Abode of Grace*”), Perak is the fourth-largest state in Malaysia. It is divided into 12 administrative districts with Hulu Perak being the largest.

A land marked by natural tropical beauty and rich in culture and history, Perak was developed through tin mining and rubber tree plantations during the British colonial period. It was one of the wealthiest states during the colonial period as much as of Malaya’s mineral deposits were situated there. When the global tin industry collapsed in the 1980s, the local state government diversified the economy towards commodity-based manufacturing.

A major contributor to the state economy is its agriculture industry, specifically rubber, coconut and palm oil. There is an estimated 40,000 independent smallholders whose land covers approximately 118, 321 hectares in Perak.





CURRENT SITUATION & CHALLENGES

Palm Oil and Supply Chain Overview

- Palm oil can be found in about half of all packaged products sold in the supermarket ranging from shampoo to chocolate. Global per capita consumption doubled between 2000 and 2015 to 7.7 kilograms.
- The commercial production of the fruit lasts for 25 years per tree. Once harvested the FFB needs to be transported to the mill for processing within 24 hours to ensure its freshness. This is a key factor for millers as unripe and spoiled fruits are rejected and transported back to the growers.
- A key factor to consider are weather patterns. As palm oil plantations are mostly in tropical countries, heavy rain often floods plantations and hampers harvesting. Dry spells on the other hand negatively impact growth of trees on the plantation thus lowering palm oil production.

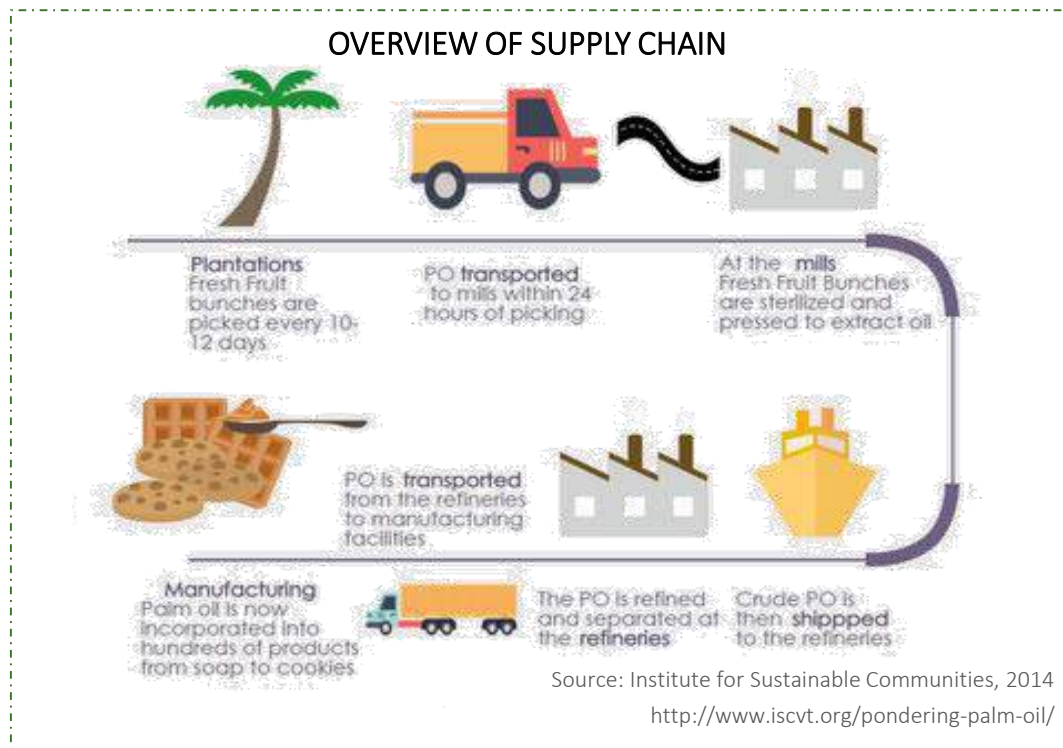
MESOCARP- Fruit Oil

- Biofuel
- Food
- Feed



KERNEL

- Food (margarine, confectionaries, butter substitute)
- Cosmetics
- Detergents

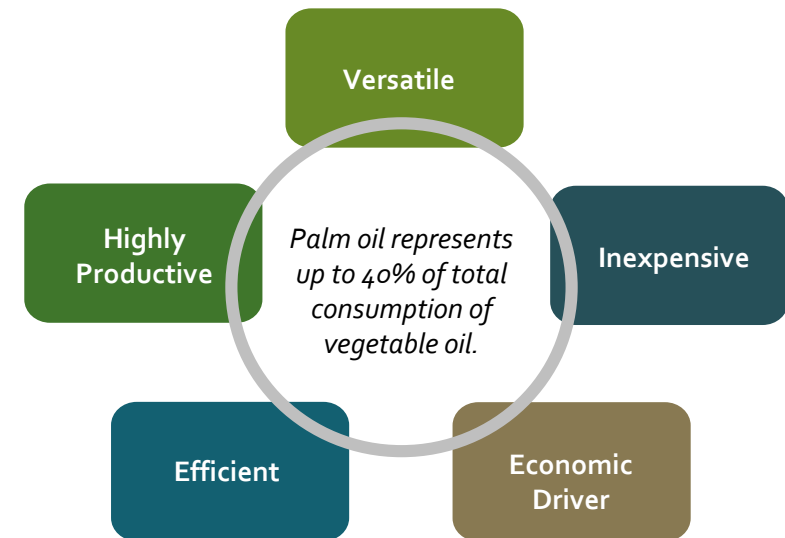


BASIC INDUSTRY TERMS	
Fresh Fruit Bunch (FFB)	The bunch harvested from the oil palm tree. Each bunch weighs from 5kg to 50kg and can contain up to 1500 or more individual fruits.
Crude Palm Oil (CPO)	The oil which is extracted from the reddish pulp of fruit of oil palms and it is similar to the pulp colour because of high inactive vitamin A content.
Palm Kernel (PK)	Edible oil taken from the kernel of the oil palm.
Oil Extraction Rate (OER)	An indicator to reflect production of CPO and PK per hectare in the mill

The Global Demand for Sustainable Palm Oil

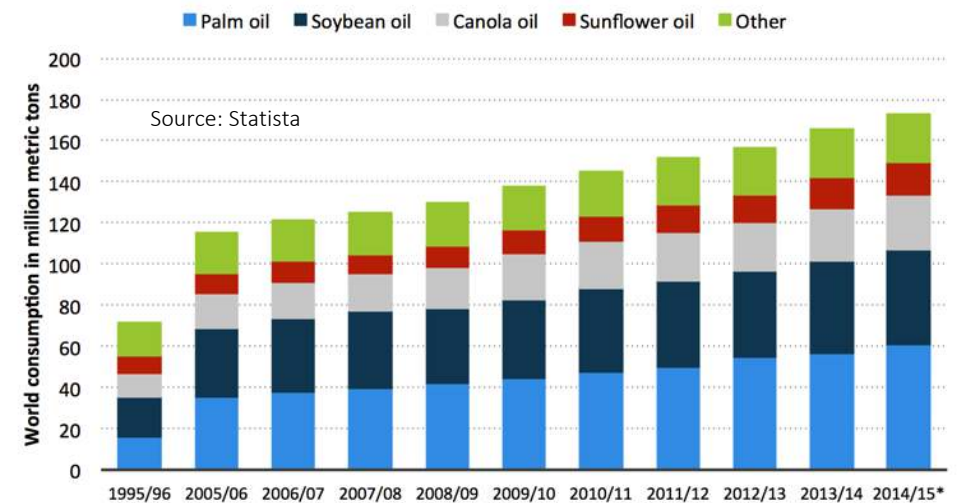
OVERVIEW

- Global production of all vegetable oils doubled in the last 20 years and palm oil is no exception. The global consumption for palm oil rose from 14.6 million tons in 1995 to 61.1 million tons in 2015, making it the most consumed oil in the world. Its main consumers are China, India, Indonesia and the European Union.
- The rapid expansion of the industry has increased public concerns regarding its environment and social impact and increased demand for sustainability and accountability. Actors within and outside the industry have worked on developing and applying global standards on certification for sustainable palm oil such as the Roundtable for Sustainable Palm Oil (RSPO) certification.
- The certification scheme functions as an assurance to consumer groups that the commodities are produced without causing harm to the environment or society. Producers are certified through strict verification process to stringent principles accredited by Certifying Bodies, and can be withdrawn at any time in case of infringement of the standards.
- However palm oil is in many ways inherently more sustainable than other vegetable oils. In comparison to major oil seeds, palm oil is the most productive and economically viable vegetable oil and uses 10 times less land (0.23% of total agricultural land) and produces higher yields per hectare than other vegetable oils.
- Its high productivity attracts many smallholder farmers switch to palm oil production. Globally, around four tonnes of palm oil in every 10 (40%) is grown by smallholders whose incomes are dependent on the companies to whom they sell their FFBs.



Vegetable oils: global consumption by oil type 1995-2015

Global consumption of vegetable oils from 1995 to 2015, by oil type (in million metric tons)



Oil palm is one of the world's most economically viable and versatile crops

Malaysia's Palm Oil Industry

OVERVIEW

- Malaysia is the second largest producer of palm oil in the world. The industry accounts for 5-6% of Malaysia's GDP and is the second largest contributor to external trade. Its main export destinations include India (17.6%), China (11.7%) and the Netherlands (6.4%).
- The last decade had seen rapid expansion of cultivated area in Sabah and Sarawak; while planting in Peninsular Malaysia has slowed because of diminishing availability of new land.
- The crop is the lifeblood of many rural Malaysian communities. Large-scale cultivation of oil palm took off in the 1960s to reduce the country's dependence on rubber. At present, the industry supports more than two million Malaysians (directly and indirectly) across the value chain.

MALAYSIA SUSTAINABLE PALM OIL (MSPO)

- To adapt to the call to meet global sustainability standards, Malaysia launched its own national certification standard aimed at encouraging small and medium-sized producers, who are unable to afford RSPO certification, to adopt sustainability practices.
- The government has made it mandatory for all oil palm growers to be MSPO certified by 2019.
- To date, over 750,000 hectares of planted area are certified accounting for 14.7% of total planted area in Malaysia.

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Malaysia's most successful industrialisation story is not electronics, which is controlled by foreign companies but palm oil, which is controlled by Malaysia.

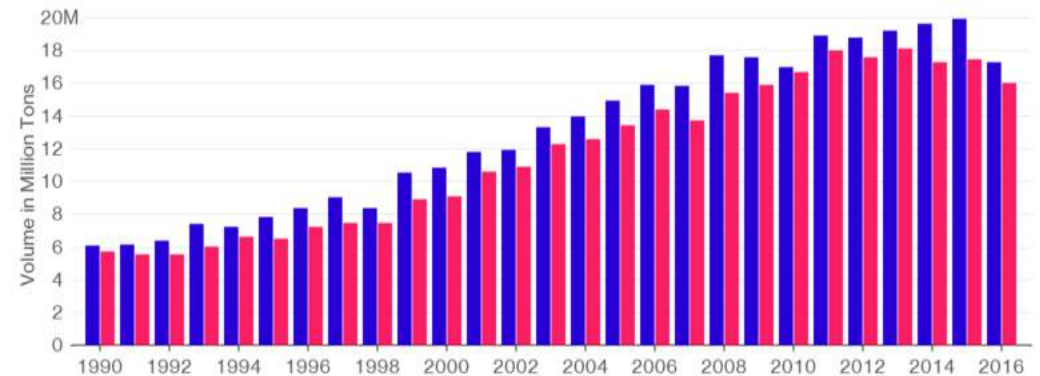
Jomo Kwame Sundaram,
Former United Nations Assistant Secretary-General

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Expansion Accelerates

Malaysian production climbs threefold

■ Production ■ Exports



Source: Malaysian Palm Oil Board

Bloomberg

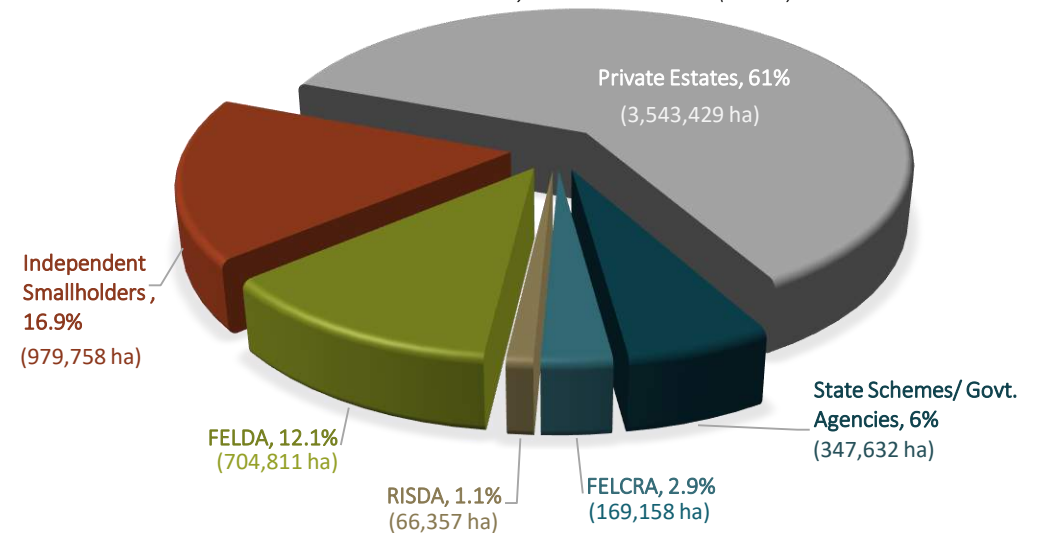
Sustainability standards are now a key industry driver

Independent Smallholders in Malaysia

- In Malaysia, 40% of the total planted oil palm area falls under smallholders. 16.9% is planted by some 235,000¹ independent smallholders who do not belong to any form of organised, local government or federal based schemes.
- Organised smallholders are managed under a central unit and have FFB supply contracts with corporations. Fully organised, the smallholders also have better access to high quality farming input thus produce higher production yield.
- On the other hand, independent smallholders typically have lower yields and face numerous other challenges. They own the land title and manage their own plantations.
- It is also common for independent smallholders to contract a dealer for transportation and labour services.

OIL PALM PLANTED AREA BY CATEGORY, 2017

Source: Malaysian Palm Oil Board (MPOB)



Source: The Palm Scribe



Source: Wild Asia

Independent smallholders are integral to the industry but marginalised at present

Key Challenges faced by Independent Smallholders in Malaysia



Disparate and unorganised

Smallholders cannot leverage on economies of scale due to their scattered locations. It is not uncommon for a farmer to own plantations across different provisions in the state.



Growing pressure to meet certification standards

The lack of financial capacity and infrastructure are major constraints in achieving certification standards (RSPO/ MSPO). Without certification, smallholders are not able to supply and compete in global markets.



No access to market data or guaranteed crop pricing mechanism

Smallholders are reliant on dealers to sell FFBs and have little or no clear relationship with mills. They also lack access to real-time market data.



Inadequate access to suitable financing

The cost to manage plantation, replanting and purchase farming inputs are costly. Lack of access to suitable financing (grants, loans, etc.) forces smallholders to source financial means through informal loan with their dealers.



Labour shortage

Harvesting FFB is labour intensive and fewer young people want to work on plantations choosing urban lifestyles instead. Hiring workers to harvest and collect FFBs are significant costs for smallholders.



Affordability to get high quality seedlings and other inputs

Lack of access to high quality inputs results in lower quality crop and yields leading to lower incomes for smallholders



Lack of agronomic knowledge and farm training

Smallholders suffer from poor farm efficiency and frequent pest and disease outbreaks and are often unaware of industry best practise



Inefficient logistic networks

The lack of quality roads on plantations and access to transportation service providers compounds reliance on dealers and impacts quality of FFBs which must be harvested and transported fresh

Fresh thinking and new business models required to revitalise the livelihoods of independent smallholders



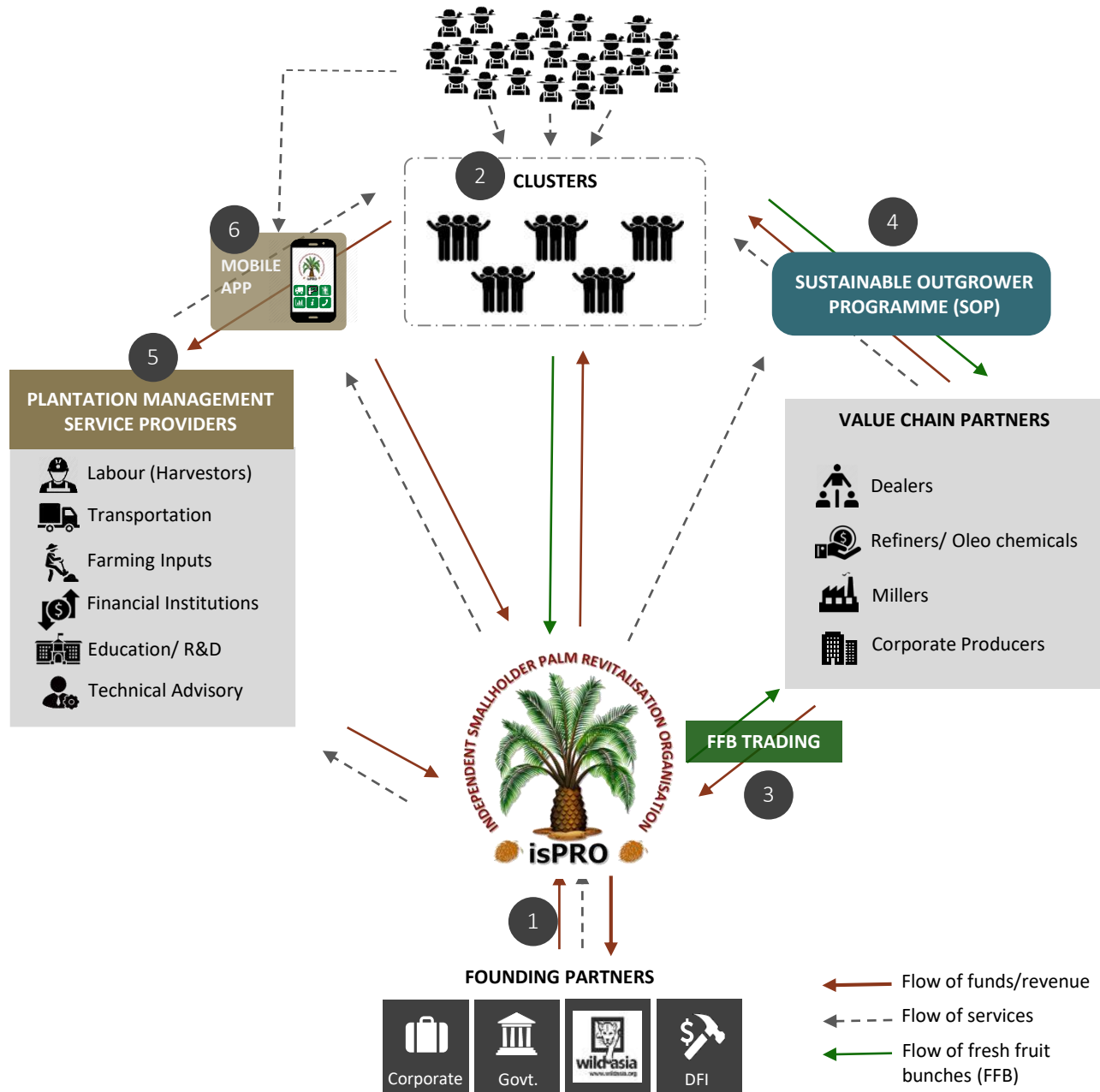
BUSINESS MODEL

Summary

- The proposed business model describes the creation of a new entity, the **Independent Smallholder Palm Revitalisation Organisation (isPRO)**, a company limited by guarantee (CLBG) co-founded by Wild Asia and key industry stakeholders.
- Key functions of **isPRO** include:
 - Organising independent smallholders into clusters for more effective delivery of its services;
 - Facilitation of FFB trading activities between clusters and buyers;
 - Initiating the Sustainable Outgrower Programme (SOP) to match clusters with processors and corporate producers based on FFB demand and provide contract drafting services which protect the interests of the smallholders. The corporations then provide technical assistance, farming inputs and funding for smallholders to meet certification standards in exchange for guaranteed supply;
 - Increase plantation management options by maintaining a pool of service providers. This generates healthy competition, results in transparent pricing and matches supply with demand;
 - Making all **isPRO** services and those of plantation management service providers available through a mobile application.
- All of **isPRO**'s activities address the key challenges faced by independent smallholders. Firstly by strengthening their position in the value chain through the formation of clusters; facilitating FFB trading to ensure fair pricing; matching FFB demand from big players with clusters who can benefit from farming inputs, technical assistance and certification, and by increasing plantation management options for smallholders to manage their plantations more sustainability and productively.



Proposed Business Model



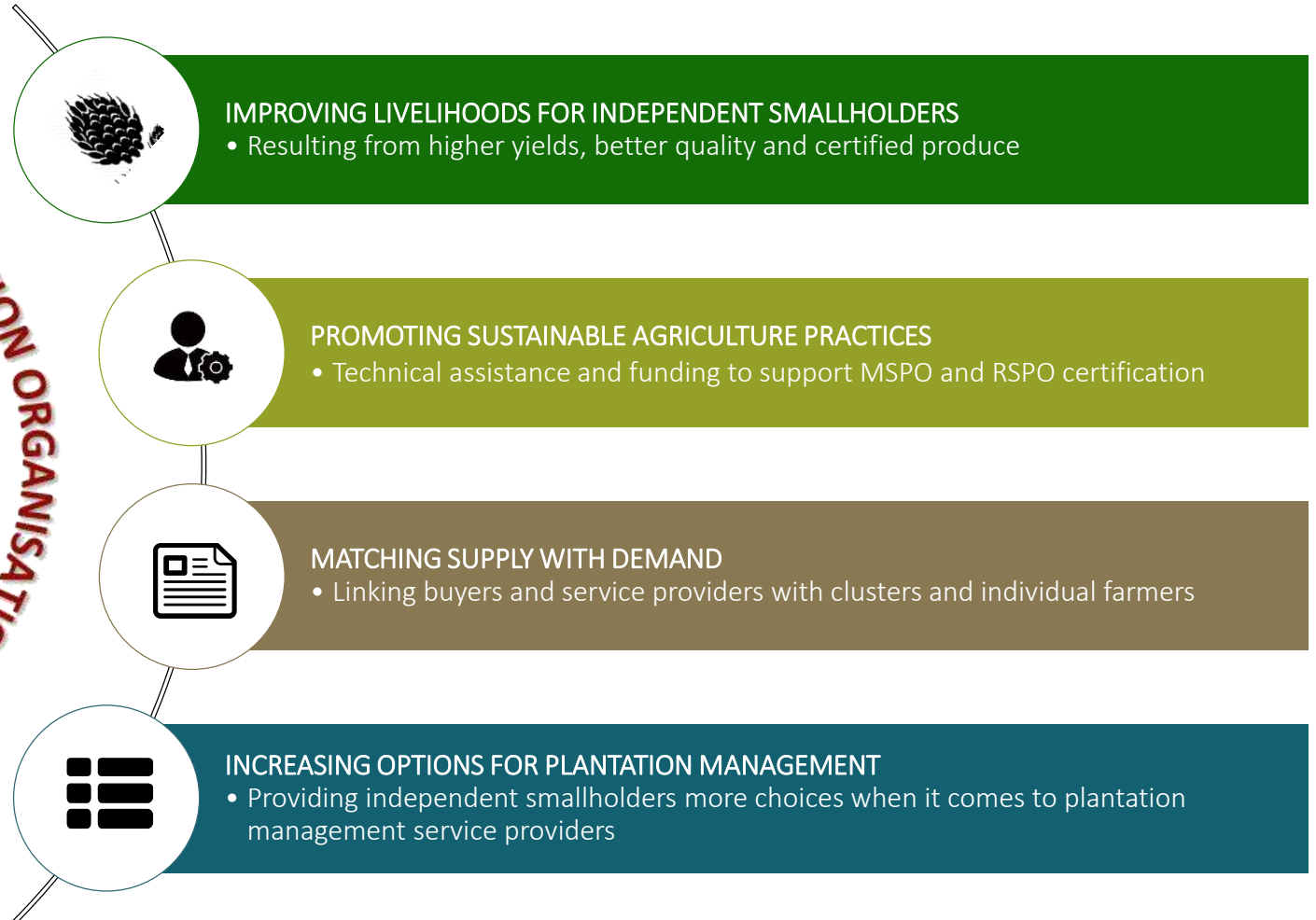
- 1 A new entity, **Independent Smallholder Palm Revitalisation Organisation (isPRO)**, a company limited by guarantee (CLBG) is established with potential seed funding from corporations, government and development finance institutions (DFI).
- 2 Independent smallholders will be grouped into clusters according to land proximity to the mill and size (1 cluster: total area of 1,000 hectares) for more effective delivery of services.
- 3 **isPRO** will facilitate and organise the sales of FFB from clusters to dealership and buyers. A service fee of 1% will be charged each to the cluster and value chain partner. The revenue will be used to fund capital expenditure and cover operational costs.
- 4 The Sustainable Outgrower Programme (SOP) aims to match clusters with buyers based on FFB demand. **isPRO** will provide contract drafting services to ensure terms are transparent and fair to both. Corporations then provide technical assistance, farming inputs and funding for smallholders to meet certification standards in exchange for guaranteed supply. For each successful partnership, **isPRO** will charge a one time fee of RM50/ hectare to the buyer.
- 5 **isPRO** will also act as a bridge between independent smallholders, clusters and plantation management service providers. A commission fee of 5% will be charged to the provider for every service rendered by the smallholders.
- 6 **isPRO**'s services and list of service providers will be made available through a mobile application. Smallholders and clusters have the option to choose service providers through the app without an extra fee.

Introducing the Independent Smallholder Palm Revitalisation Organisation isPRO



*Proposed logo for isPRO

isPRO Value Proposition:



Revitalising the industry by empowering independent smallholders

Formation of Clusters

- The disparate and unorganised nature of independent smallholders mean they cannot leverage economies of scale to access inputs and services or sell their produce.
- This also results in a key challenge for value chain partners (refiners/oleo chemicals, millers, dealers) in dealing directly with independent smallholders.
- The primary objective of **isPRO** is to organise independent smallholders into clusters. **isPRO** will leverage existing groupings and relationships formed by the Malaysian Palm Oil Board (MPOB), Wild Asia and other public, private and civil sector organisations
- Factors to take into consideration in the formation of clusters include:
 - ✓ Land size (Target: 1,000 hectares per cluster)
 - ✓ Proximity of plantations
 - ✓ Location of nearest mills
- In order to align interests, ensure operational excellence and facilitate transparent decision making, it is proposed that each cluster nominates a Cluster Leader to co-manage the clusters with **isPRO**.
- To ensure the scale up of clusters and expand the membership base, strategies to attract independent smallholders include:
 - Roadshows and workshops;
 - Demonstration training;
 - Sharing success stories.



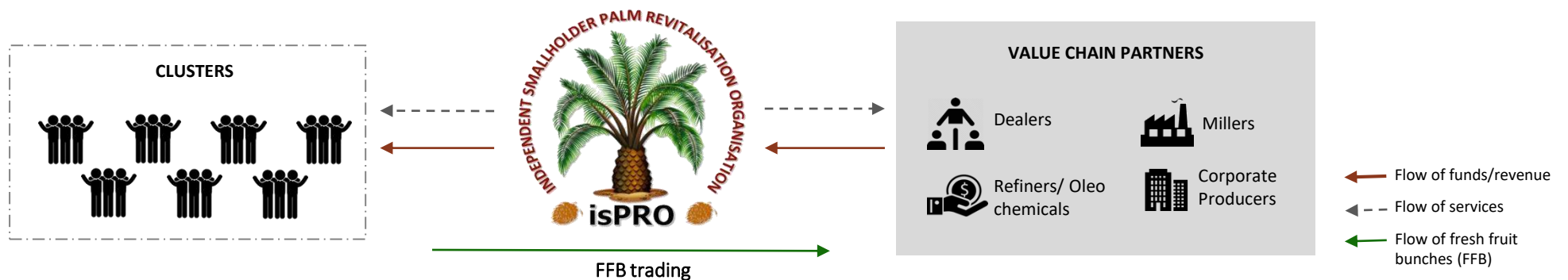
MAIN ROLES OF A CLUSTER LEADER

- ◆ Promote benefits of cluster formation in surrounding communities;
- ◆ Act as main liaison with **isPRO** for FFB trading and SOP contract drafting;
- ◆ Consensus building and dispute resolution within clusters;
- ◆ Ensure adherence to RSPO/ MSPO standards.

Promoting power in numbers for independent smallholders through collective action

FFB Trading

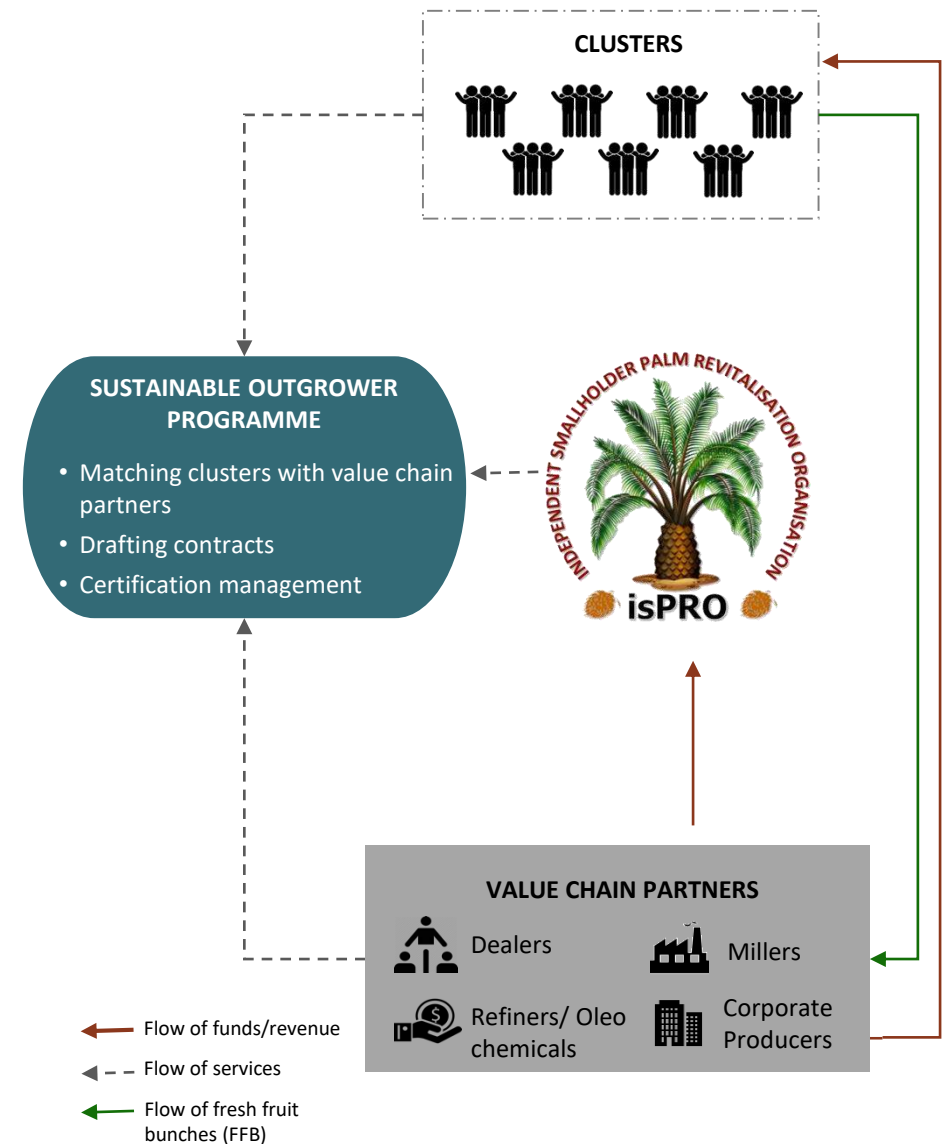
- The current sales of FFB from independent smallholders to value chain partners (dealers, buyers, millers and corporate producers) are ad hoc and often opaque.
- A function of **isPRO** is to facilitate FFB trading between the clusters and value chain partners to ensure **fair pricing structure** while ensuring high quality of FFB.
- The fair pricing structure will take into consideration real time market prices and quality of FFB supplied. This ensures independent smallholders will receive fairer and better prices therefore improving their livelihoods.
- **isPRO** will work with Cluster Leaders by organising and coordinating the FFB sales to value chain partners. A service fee of 2% will be charged for all facilitated FFB sales, 1% paid by clusters and 1% paid by the buyer.



Fairer and better prices

Sustainable Outgrower Programme (SOP)

- The SOP matches clusters who are already engaged in, or willing to adopt sustainable agricultural practices with value chain partners who are looking to supplement their supply of FFB from external sources.
- **isPRO** plays the role of a broker and supports the drafting of contracts which ensure the interests of both parties are met and crucially, that clusters certification is offset or subsidised by the buyers in exchange for a commitment to supply FFB all time.
- In addition the buyer would also provide inputs (seeds, fertilisers, etc.) and technical assistance to clusters to assure high quality FFBS can be processed.
- **isPRO** would also provide dispute solution services and help buyers to monitor adherence to certification standards by clusters.
- **isPRO** will charge the buyer a one-time fee of RM50/ hectare included in the SOP.



Catalyzes RSPO/ MSPO certification en masse

Core Principles of SOP

The structure of the SOP varies with each cluster's unique characteristics. However, every partnership is guided by the following principles. The way in which each of these principles is addressed defines the overall nature of the SOP and its prospects for long-term viability.

ACCESS TO INPUTS

Value chain partners are incentivised with an assured supply of FFB that meets quality and volume requirements to provide independent smallholders the necessary farming inputs (seedlings, fertilisers).

EXTENSION SERVICES

Effective extensions can equip independent smallholder farmers with the knowledge and tools they need to boost their quality and output volume, whilst promoting the buyer as a committed partner among farming communities. Partners could seek external contractors to provide certain services if they lack capacity.

USE OF CONTRACTS

Contracts can facilitate transparency between parties to ensure long-term partnerships. These must clearly outline the terms of payment and prices to be paid. Similarly, partners should ensure that quality requirements are defined and clusters understand their obligations from the outset.

SMALLHOLDER GROUPING

Farmer grouping can help buyers achieve important economies of scale, to promote cohesion among members through shared values and "peer policing," increasing farmer commitment to the partnership and reducing the risk of side-selling. The selection criteria should consider the cluster's proximity, capacity to supply outputs, and ability to manage resources.

FARMERS MANAGEMENT

Buyers should look for ways to encourage independent smallholders sustained commitment to the relationship and differentiate themselves from their competitors by providing better bundles of services (e.g. extension, inputs and market information), or loyalty programs that reward independent smallholders for improved performance or consistent supply.

POST-HARVEST LOGISTICS

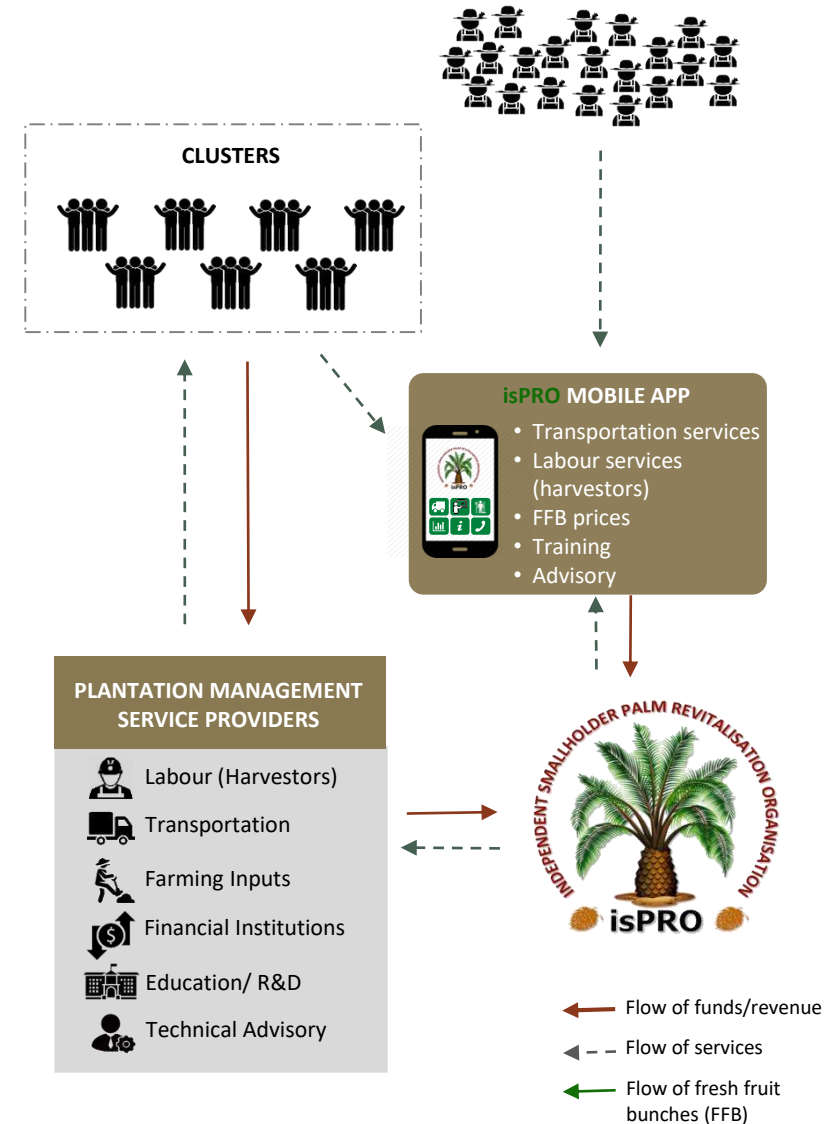
SOP can catalyse the certification of large numbers of independent smallholders with financial support for buyers who would view this as a good investment given the requirements of their own customers when it comes to sustainability and traceability of palm oil.

PROMOTING SUSTAINABLE AGRICULTURAL PRACTICES

A value chain partner's involvement in post-harvest logistical support greatly varies depends on product perishability, quality requirements, existing infrastructure and services and the relative sophistication of participating independent smallholders. Such services can be provided directly or through intermediaries such as lead farmers or NGOs.

Plantation Management Service Providers

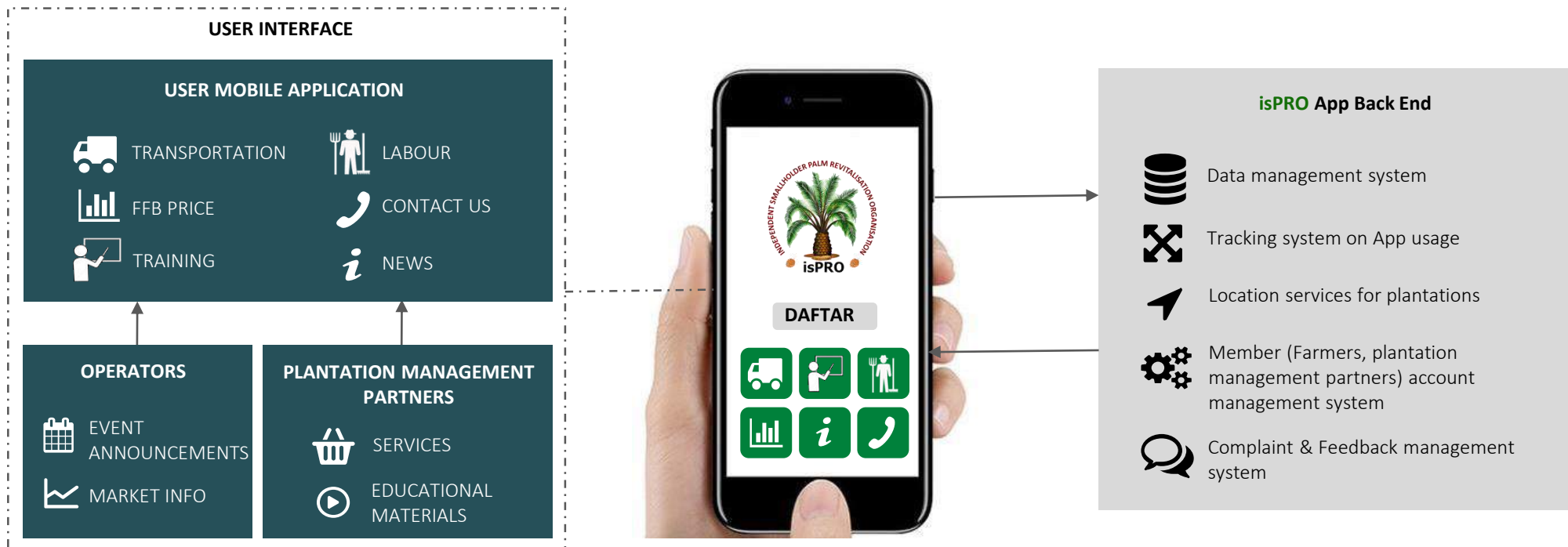
- In the current paradigm independent **smallholders** have extremely limited choices when it comes to accessing service providers.
- Some **smallholders** may wish to farm the land themselves and only seek assistance to plan or harvest for example, whilst others may not live near their land and require end-to-end plantation management services.
- **isPRO** will maintain a pool of service providers and a "menu" of offerings for smallholders to choose from.
- A mobile application will be developed which enables smallholders to browse and access these services.
- **isPRO** will charge service providers a 5% commission for all services rendered either through the app or offline via their directory.



Promotes healthy competition and more options for independent smallholders

isPRO Mobile App

- The **isPRO** mobile application is a centralised system for smallholders to view the directory of plantation management service providers, access real time market data and seek support from **isPRO** when needed.
- **isPRO** can also use the platform to share information and with the support of strategic partners to host a series of educational materials and videos to promote sustainable agricultural practices.
- Data from the mobile app can be used to monitor performance of the partners, map the locations of plantations and track usage of the services provided among the farmers.
- As the user base grows, the data generated can be monetised for research purposes and serve as a revenue stream for **isPRO**.



Opportunity for collaboration with telco and technology companies

Key Stakeholders & Interests (1/2)

	STAKEHOLDERS	CURRENT CHALLENGES	BENEFITS FROM isPRO
UPSTREAM PLAYERS	Independent Smallholders	<ul style="list-style-type: none"> • Pressure to meet certification standards • Inadequate access to farming inputs, financing, market data • Disorganised and disparate 	<ul style="list-style-type: none"> • Subsidised certification through SOP • Fairer better process for FFB • More choice when it comes to plantation management services
	Dealers	<ul style="list-style-type: none"> • High administrative costs to maintain certification of suppliers • Resource planning based on seasonality 	<ul style="list-style-type: none"> • Opportunity to diversify its business and reach larger customer base through isPRO mobile application
	Millers	<ul style="list-style-type: none"> • Pressure from customers to achieve sustainability standards • Unable to trace source of FFB- needs assurance farmers are certified • Low quality of FFB results in poor extraction rate 	<ul style="list-style-type: none"> • Access to smallholders mapping through data from the online platform and trace the FFB origin • Consistent supply of FFB from the formal arrangements through SOP • Goodwill and reputational benefits from supporting a smallholder-centric business model
DOWNSTREAM PLAYERS	Refiners/ Oleo chemicals	<ul style="list-style-type: none"> • Pressure from end consumers to ensure supply is sustainably sourced • Lack of certified suppliers 	<ul style="list-style-type: none"> • Consistent supply of certified FFB through the SOP • Goodwill and reputational benefits from supporting a smallholder-centric business model
	Corporate Producers	<ul style="list-style-type: none"> • Lack of excess land for expansion to increase FFB supply 	<ul style="list-style-type: none"> • Transparent and consistent supply of FFB • Achieve economies of scale through cluster grouping • Access to smallholders mapping and trace the FFB origin • Goodwill and reputational benefits from supporting a smallholder-centric business model

Key Stakeholders & Interests (2/2)

STAKEHOLDERS	CURRENT CHALLENGES	BENEFITS FROM isPRO
Government (Ministerial)	<ul style="list-style-type: none"> • 99% of independent smallholders not MSPO certified • Global pressure for sustainable practices 	<ul style="list-style-type: none"> • Able to certify smallholders en masse to ensure national goal is met within timeframe • Goodwill and trust building with independent smallholder communities
Government Agencies	<ul style="list-style-type: none"> • Difficulty in reaching out to smallholders to offer technical training • Lack of data for farm mapping 	<ul style="list-style-type: none"> • Outreach to smallholders is faster with clusters • Data from the app to be used for satellite mapping of plantations
Plantation Management Service Providers	<ul style="list-style-type: none"> • Informal transactions • Small customer base • High cost of sales 	<ul style="list-style-type: none"> • Organised and structure delivery system through the online platform • Recorded transactions for better business management • Increase customer base and revenues, decreased cost of sales
Technology Companies	<ul style="list-style-type: none"> • Opportunity to collaborate on mobile app as a revenue driver, inroad to new rural customers and build goodwill • Potential to expand app beyond oil palm into other crops 	
Development Finance Institutions	<ul style="list-style-type: none"> • Support sustainable practices in the commodities sector and promote social development • Acceptable rate of return on invested capital • Aligned with mandate from federal government 	
Universities	<ul style="list-style-type: none"> • R&D in palm cultivation and sustainable practices • Opportunities for students to engage with smallholders and exchange knowledge 	
NGOs/ Social Enterprises	<ul style="list-style-type: none"> • Support independent smallholders to improve livelihoods and increase their well-being • Promote knowledge transfer and education in rural communities • Ensure more equitable distribution of profits in agricultural systems 	

isPRO offers benefits to a wide range of stakeholders in the palm oil sector



ORGANISATIONAL STRUCTURE & GOVERNANCE

Summary

- The mandate of **isPRO** is to improve livelihoods of independent smallholders by helping them overcome current challenges.
- Strong governance is pertinent in **isPRO** to ensure alignment of interests of between stakeholders and maintaining operational excellence. Good governance also leads to the sustainability and credibility of **isPRO**.
- **isPRO** will be set up as a Company Limited by Guarantee (CLBG).
- At a national level, **isPRO** is governed by a Board of Directors comprised of representatives from independent smallholders, millers, government agencies, corporate Producers/buyers, and certification councils. An advisory council is formed consisting of agri experts, NGOs, financial institutions, universities and technology companies.
- At the state level, **isPRO** will have on-field units that will be replicated when scaled to different states.



Why Good Governance Matters

What is meant by good governance?

- Good governance is driven by principles such as conducting business with integrity, fairness and transparency and making all the necessary disclosures so as to protect the interest of all stakeholders.
- Organisations, both public and private, should comply with all laws of the land, be accountable and responsible towards stakeholders, and commit to conducting business in an ethical manner. They should focus on balancing stakeholder interests with those of other key stakeholder groups, including customers, communities and supporters.

Why does **isPRO** need governance mechanisms?

- As an intended recipient of investment and funding, mechanisms need to be in place to deliver accurate and transparent information on where funds are being directed and what social impact is created.
- Strong corporate governance is essential to increase the accountability and the transparency of **isPRO** thereby protecting the interests of investors, independent smallholders and value chain partners and ensuring the objectives of the organisation are met through well-established legal norms.
- Good governance will positively influence the reputation of **isPRO** and can mitigate the risks associated with managing funds and working with multiple stakeholders.



Proposed Governance Framework

Good governance is essential to the credibility, success and sustainability of **isPRO**. Within **isPRO**, the following governance framework is proposed to ensure smooth business management and operations.

Objectives

- To ensure agreed upon strategies are carried out in the most effective manner.
- To manage funds invested for long term growth at minimum level of risk so that **isPRO** remains financially sound.
- To align and meet the objectives and expectations of key stakeholders and partners.
- To ensure **isPRO** operates at high level of professionalism both internally and externally.

Principles

- Compliance with all national laws relevant to the business.
- Fulfilling social obligations, including commitment towards partners and stakeholders, commitment towards the community, product safety.
- Advocating management and finance transparency, accountability and disclosure.
- Safeguarding the interests of **isPRO** and its various stakeholders.
- A guide against unethical practices.



Emphasis on good governance is imperative to ensure accountability

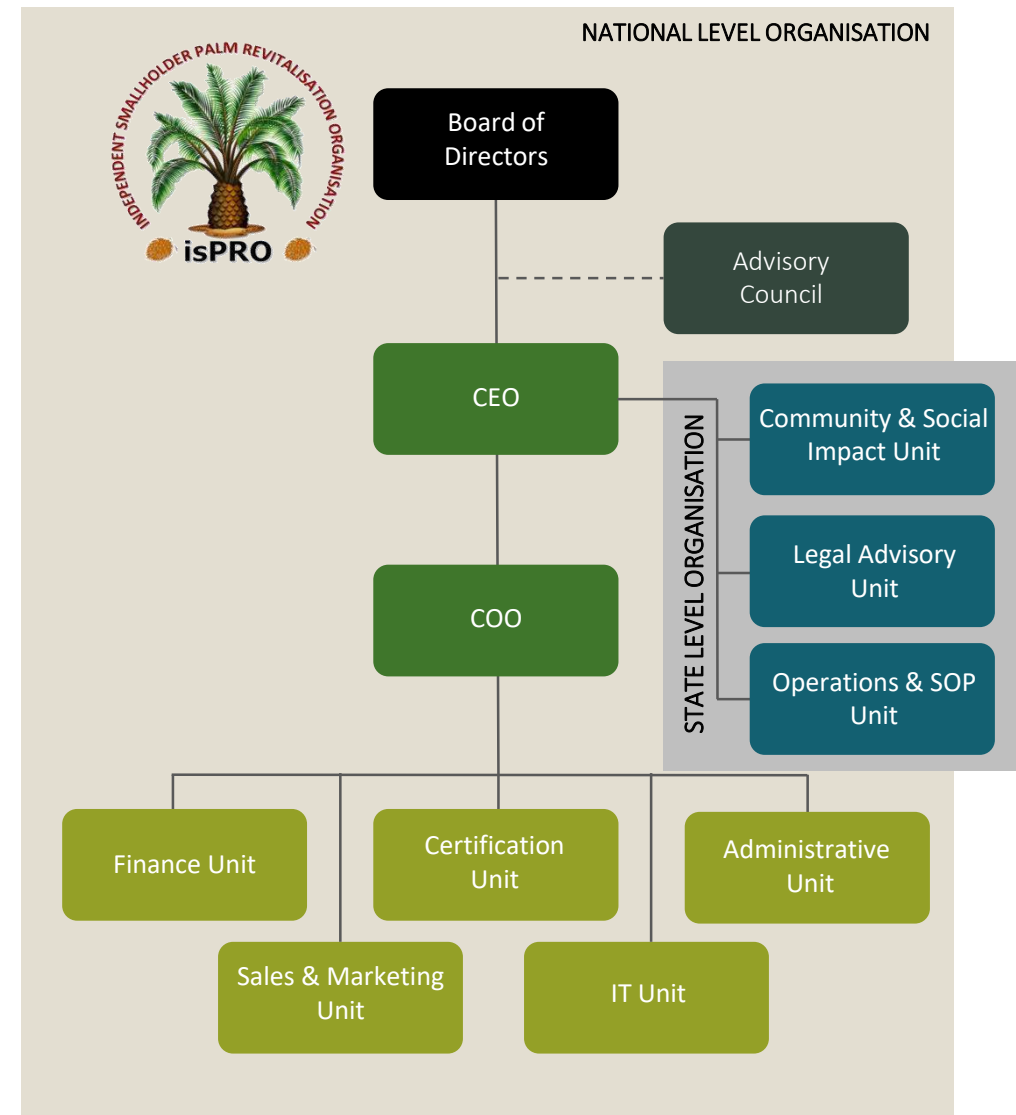
Framework & Organisational Structure of isPRO

FRAMEWORK

- isPRO is a **Company Limited by Guarantee (CLBG)**, where it is incorporated as a public company. Activities of isPRO are in line with the object of 'Promoting commerce and industry' as provided by Companies Commission of Malaysia (SSM).

ORGANISATIONAL STRUCTURE

- The **Board of Directors** is the main governing body of isPRO responsible for corporate governance, overall strategy, policy making, financial oversight, and risk management.
- An independent **Advisory Council** to be made up of representatives from the clusters of independent smallholders, millers, dealers, government, certification councils and corporations to provide oversight and advice to the Board of Directors in decision-making processes based on their respective knowledge and experience.
- The CEO will be responsible for leadership, strategic direction and performance of isPRO.
- The COO will be involved in the daily operations of the business.



Key Roles & Responsibility of the Management Team

Roles	Responsibilities
Chief Executive Officer	<ul style="list-style-type: none"> Responsible for the strategic direction and overall performance of isPRO Manage key stakeholder relationship Reports to the Board of Directors
Chief Operations Officer	<ul style="list-style-type: none"> Second-in-command and responsible for the day-to-day operations efficiency of business
Legal Advisory Unit	<ul style="list-style-type: none"> Responsible for legally representing isPRO, providing legal advice To advise on the compliance of Standard Operating Procedures/Terms Of Reference and policies
Administration Unit	<ul style="list-style-type: none"> Responsible for all administrative tasks within isPRO
Operations & Sustainable Outgrower Programme Unit	<ul style="list-style-type: none"> Responsible for administering the SOP Promotion of the Sustainable Outgrower Programme to clusters and buyers (value chain partners)
Finance Unit	<ul style="list-style-type: none"> Oversee the finance management of isPRO Responsible for budget preparation, financial contracts and forecasting
Sales & Marketing Unit	<ul style="list-style-type: none"> Market overview and implementation strategy Customer relationship management Promotion of the independent smallholder clusters creation
Sustainability/Certification Unit	<ul style="list-style-type: none"> Coordinate with certification bodies (MSPO/ RSPO) and value chain partners to promote certification of independent smallholders Monitor adherence to certification amongst cluster network
Information Technology Unit	<ul style="list-style-type: none"> Manage development and maintenance of mobile application To analyse data gathered from mobile application to be shared with the relevant units in isPRO
Community & Social Impacts Unit	<ul style="list-style-type: none"> To set criteria, coordinate the measurement of and communicate the social impact of isPRO

Transparency & Disclosure

- With financial support from shareholders, and value chain partners, mechanisms need to be in place to deliver information on where money is directed, what services are conducted and what social impact is created.

MONITORING BY THE BOARD

- Regular board meetings to evaluate the performance of the management, operations team and company overall
- Oversight of agreements with producer members, value chain partners and service providers
- Authority on termination and compensation of management team

INTERNAL CONTROLS

- Regular reporting from operational and management team to Board of Directors
- Internal audits to test design and implementation of governance control mechanisms
- Regular checks on clusters to ensure quality control and adherence to SOP contracts and certification standards

PUBLIC DISCLOSURE

- Terms of Reference of Board and Committees
- Audited financial reports included in Annual Reports
- Declarations of interest
- Annual General Meeting held to outline strategic goals and implementation plans.

Disclosure on the deployment of funds ensures the integrity of isPRO



FINANCIAL ANALYSIS & INVESTMENT

Summary

Assessment Year:

5

	Metrics	Results
Investors	Initial Investment	RM 3,000,000
	Net Present Value	RM 1,544,686
	Internal Rate of Return	25.5%
	Payback Period	3.6 years
Business Stakeholders	Avg Gross Margin (%)	16.7%
	Avg Net Profit (%)	23.4%
	Avg Return on Capital Employed	19.8%

- **isPRO** requires an initial funding of RM3 million and no additional funding in the following years.
- **isPRO** is expected to start making profits during the second year and is estimated to make a total profit of RM9.7 million in five years driven by the following revenue streams:-
 - Service fee for all facilitated FFB sales (1% each from clusters and buyers)
 - Commission fee for sourcing plantation management services (5%)
 - SOP facilitation fees (one-off RM50/ hectare)
- For the first five years, 30% of profitability (excluding Year 1) will be allocated for a Social Development Fund and this will increase to 70% subsequently. The fund aims to empower independent smallholders through capacity building and community services.
- **isPRO** is commercially sustainable and is expected to repay the funding within 10 years. Y1 to Y5 at an increase of 75% annually starting from RM150,000, Y5 onwards at RM350,000 until Y10.

Key Financial Assumptions

Revenue Assumptions

- Service fee for all facilitated FFB sales 1% from cluster, 1% from buyers (based on average price of RM495 per tonne)
- Commission of 5% for sourcing plantation management services
- One-time facilitation fees of RM50 per hectare (one-off) from buyers in the SOP

Operating Assumptions

- Mobile app CAPEX estimated at RM500,000
- 30% of allocation to the Social Development Fund from Year 2 onwards
- Allocation for Social Development Fund is excluded in Y1.

Scale of Operations

- Launch of operations at Year 1 with 1 cluster (1,000 hectares planted area by the sixth month)
- 40 clusters with 40,000 hectares planted area by Year 5 (~35% of total planted area in Perak)
- Enrolment growth rate about 35% annually for cluster participation

Cost Assumptions

- Rental of workspace at RM90K per annum at Year 1 with 10% increase every 3 years
- 10 staff in the management and administrative team maintained over the 5 years period.
- 7 on-field staff in Year 1 with periodic increase as cluster participation increases

Investment Requirement

- Initial Seed Funding of RM3million with no subsequent funding is required

Income Statement Projection

	Year 1	Year 2	Year 3	Year 4	Year 5
Revenue	120,275	2,655,500	5,061,000	7,466,500	9,872,000
Less: Cost of Revenue	(429,000)	(619,000)	(759,000)	(899,000)	(919,000)
Gross Profit	(308,725)	2,036,500	4,302,000	6,567,500	8,953,000
Gross Margin	-256.7%	76.7%	85.0%	88.0%	90.7%
Less: Indirect Costs					
Sales & Marketing	(90,000)	(90,000)	(90,000)	(90,000)	(90,000)
Administrative Wages and Salaries (2%)	(768,000)	(829,440)	(895,795)	(967,459)	(1,044,856)
Utilities	(9,000)	(9,000)	(9,000)	(9,720)	(9,720)
Social Development Fund	-	(370,578)	(1,074,654)	(1,774,949)	(2,476,101)
Depreciation	(229,900)	(229,900)	(229,900)	(229,900)	(229,900)
Profit before Interest and Tax	(1,405,625)	507,582	2,002,651	3,495,472	5,102,423
Less: Interest	-	-	-	-	-
Less: Tax		(101,516)	(400,530)	(699,094)	(1,020,485)
Net Income	(1,405,625)	406,066	1,602,121	2,796,378	4,081,939
Net Margin	-8.6%	15.3%	31.7%	37.5%	41.3%
Average Gross Margin (%)		16.7%			
Average Net Margin (%)		23.4%			

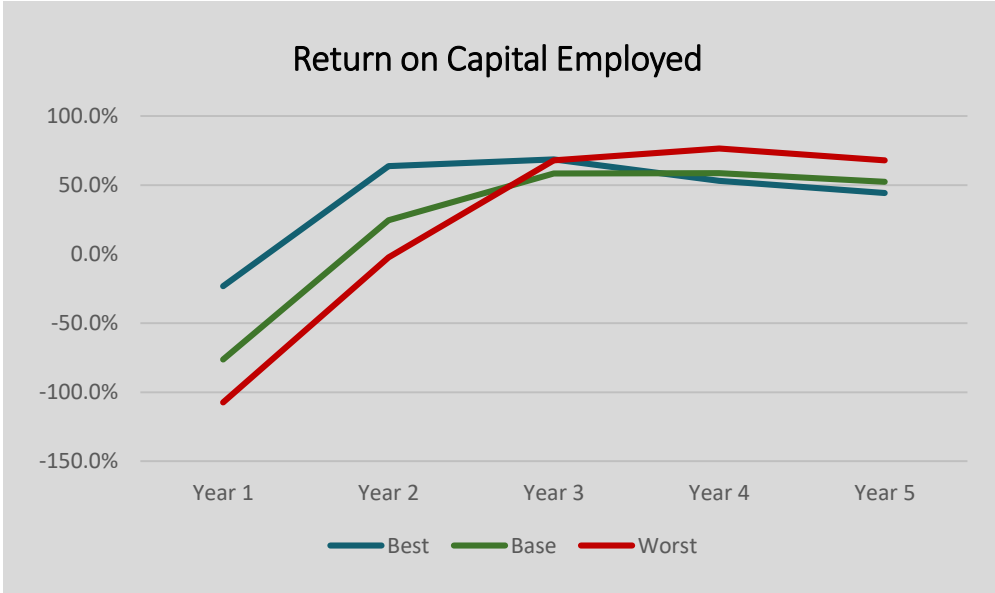
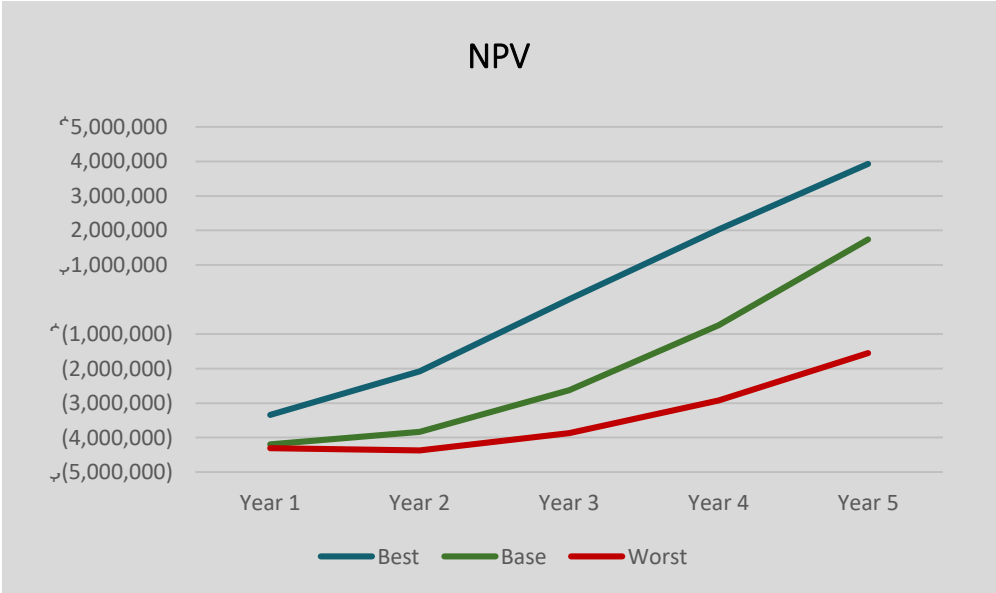
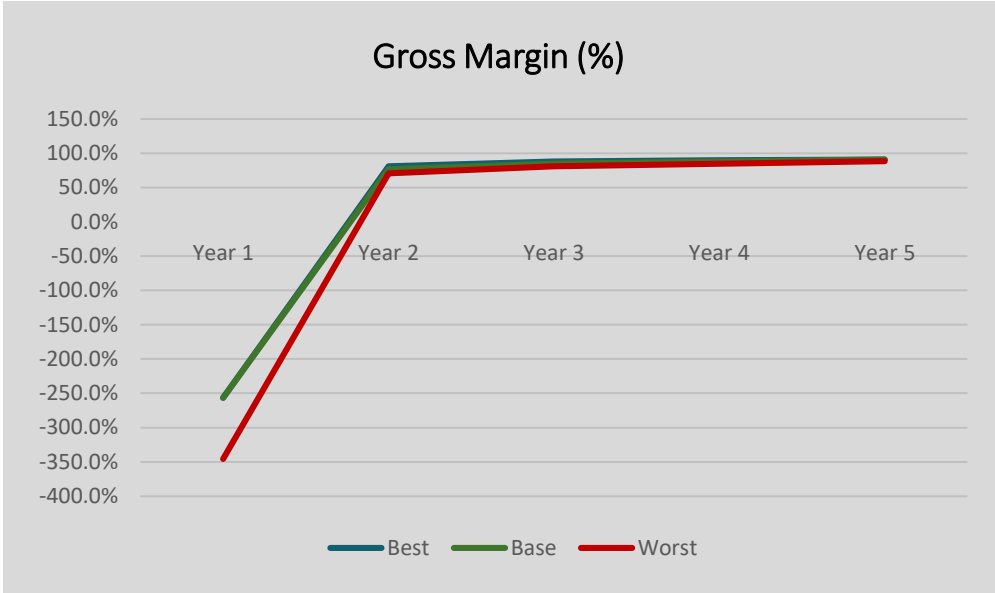
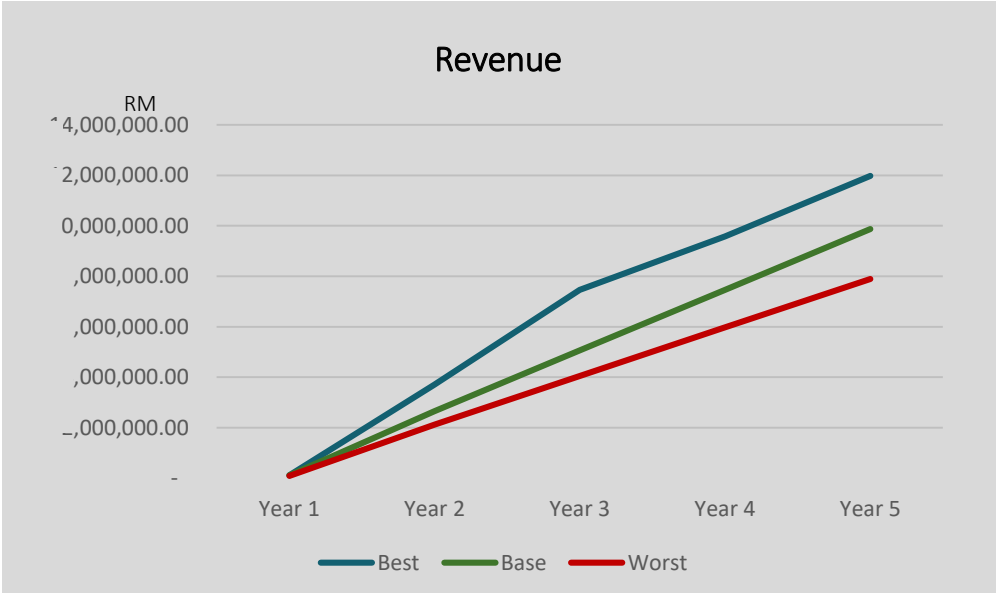
isPRO will reach profitability by Year 2

Cash Flow Projection

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Cash Received from Customer		120,275	2,655,500	5,061,000	7,466,500	9,872,000
Less Cash Paid for:						
Direct Cost		(429,000)	(619,000)	(759,000)	(899,000)	(919,000)
Sales & Marketing		(90,000)	(90,000)	(90,000)	(90,000)	(90,000)
Administrative Wages and Salaries (2%)		(768,000)	(829,440)	(895,795)	(967,459)	(1,044,856)
Utilities		(9,000)	(9,000)	(9,000)	(9,720)	(9,720)
Social Development Fund		0	(370,578)	(1,074,654)	(1,774,949)	(2,476,101)
Interest		6,000	14,000	24,000	36,000	50,000
Tax			(104,316)	(405,330)	(706,294)	(1,030,485)
Cash Flow from Operation:	391,660	(1,169,725)	647,166	1,851,221	3,055,078	4,351,839
Online Service Platform (App)	(500,000)	0	0	0	0	0
Office Renovations & Fittings	(150,000)	0	0	0	0	0
Office Furniture & Equipment	(100,000)	0	0	0	0	0
Vehicles	(400,000)	0	0	0	0	0
Cash Flow from Investing:	(1,150,000)	0	0	0	0	0
Debt issued	0	0	0	0	0	0
Loan Repayments		(150,000)	(200,000)	(250,000)	(300,000)	(350,000)
Cash Flow from Financing:	3,000,000	(150,000)	(200,000)	(250,000)	(300,000)	(350,000)
Beginning Cash	0	2,241,660	921,935	1,369,101	2,970,321	5,725,399
Change in cash	2,241,660	(1,319,725)	447,166	1,601,221	2,755,078	4,001,839
Ending Cash	2,241,660	921,935	1,369,101	2,970,321	5,725,399	9,727,238

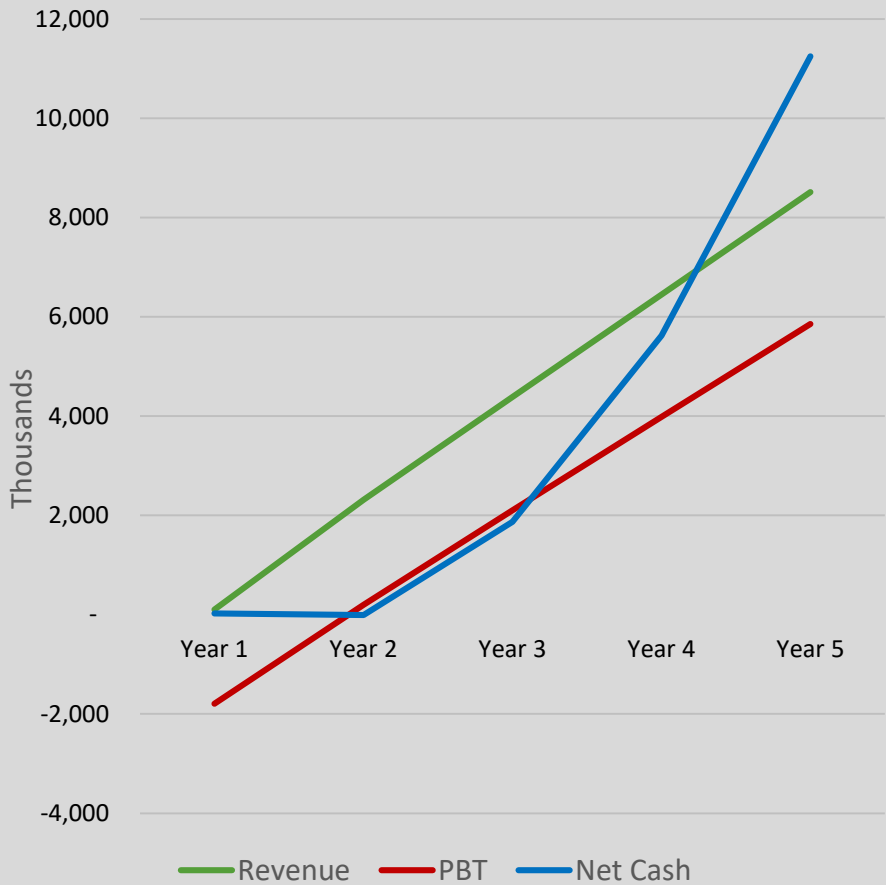
Cash flow from operations is positive from Year 2 onwards


Scenario Analysis

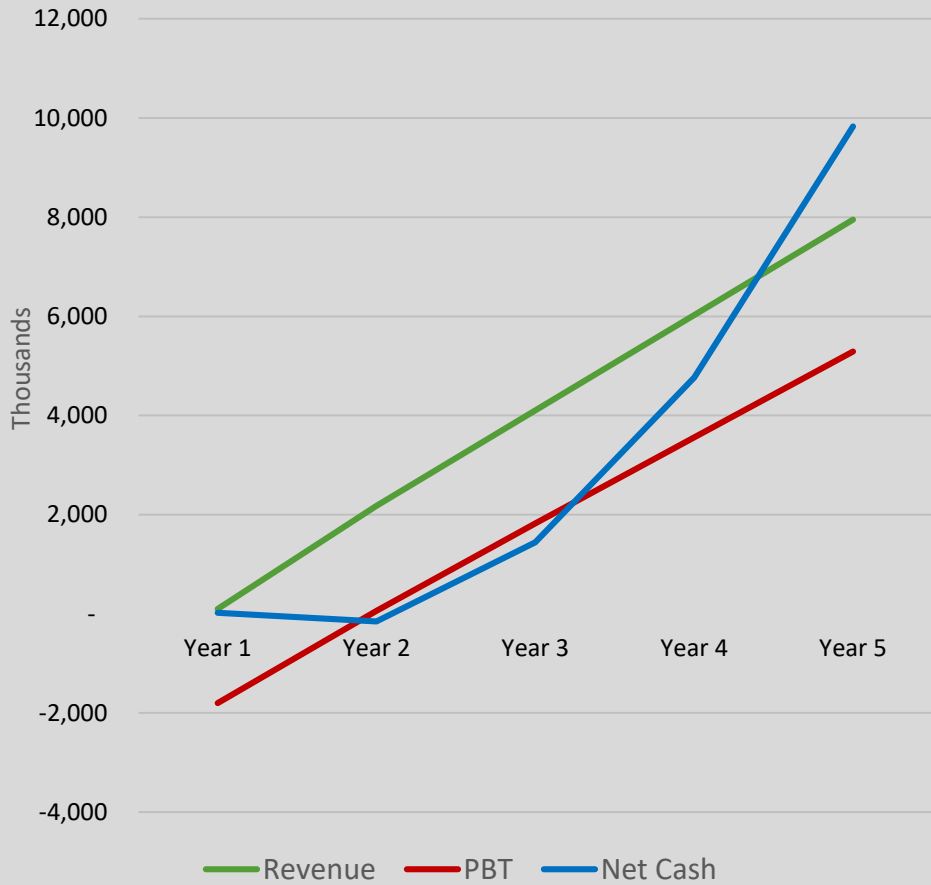


Sensitivity Analysis

Sensitivity 1:  FFB price by 20%



Sensitivity 2:  Clusters participation by 20% across 5 years



Consistent revenue stream despite market volatility



SOCIAL IMPACT & COMMUNITY BENEFITS

Summary

- Efforts to integrate independent smallholders into the supply chain have typically fallen within the remit of NGOs, social enterprises and the government. However they continue to be marginalised from the value chain and livelihoods at risk from the challenges they face.
- **isPRO** is a commercial and social driven entity that addresses the key challenges independent smallholders face and strengthen their position in the value chain.
- **isPRO** Social Development Fund aims to empower independent smallholders, strengthen the value chain and community services through these key activities:
 - Capacity Building and Extension Services
 - Research and Development
 - Community Development
- It is proposed that a social impact measurement methodology be implemented in addition to the production of a yearly integrated report in order to capture and apply lessons learned to other states in Malaysia where **isPRO** expands.
- Furthermore reporting social impact and performance can serve as a powerful marketing tool and contribute to **isPRO**'s efforts to spread awareness on integrating independent smallholders into the global supply chain.



Expected Economic and Environmental Impact

Economic Impact

- The model will prevent production risks faced by smallholders by providing them with high quality farming inputs and good agricultural practices to ensure better yield.
- Increase in production and quality of yield coupled with guaranteed market for their FFB will support an improvement in their livelihoods.
- Higher production of sustainable palm oil contributes to Malaysia's export value.
- Potential to develop more smallholders who are commercially oriented and nurture the spirit of entrepreneurship through the training services.



Environmental Impact

- Efficient use and allocation of all resources reduces wastage and promotes a less polluting agricultural system.
- Ensuring correct application and high quality agrochemicals thereby supporting soil health and productivity while reducing the risk of groundwater pollution.
- Less stress on forested land as corporate producers source from independent smallholders and provide farming inputs to increase production on existing land.



isPRO improves smallholder livelihoods and overall improvement on the environment

isPRO Social Development Fund

The **isPRO** Social Development Fund is a vehicle to redistribute financial surplus towards strengthening the palm oil value chain and improving the livelihoods of independent smallholders.

Its three main areas of activity will be:



Capacity Building & Extension Services

- Funding educational activities in collaboration with Wild Asia and other partners to promote sustainable agricultural practices amongst independent smallholder communities.
- These activities will also be leveraged to identify and attract smallholders to form clusters.
- Cluster leaders will play a key role in designing and delivering many of these programmes so as to demonstrate the benefits of involvement with **isPRO**.



Research & Development

- In collaboration with universities, government agencies like MPOB and private corporations such as Sime Darby and BASF, the fund will be utilised to launch an “Independent Smallholder Oil Palm Centre of Excellence”
- The Centre of excellence will focus on R&D related to inputs such as seeds, equipment such as harvesting tools. Combating pests using sustainable agricultural practises as well as mechanisation and IT solutions deemed suitable for smallholders.



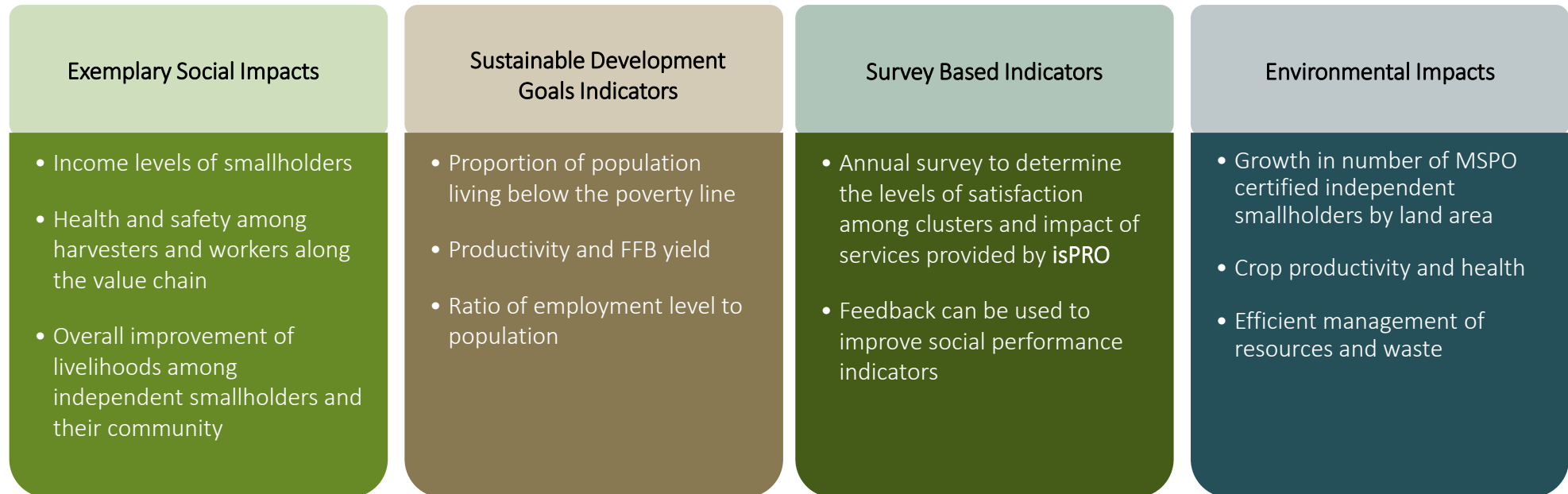
Community Development

- The fund will also be utilised to for a variety of development activities within independent smallholder communities.
- These may include community infrastructure projects such as improved road systems and drainage within plantations.
- Social services such as education, elderly care and housing
- Collaboration with the public and private sector to offer subsidized life, health or crop insurance.

isPRO is a force for positive social impact in Malaysia’s palm oil sector

Measuring Social Impact

- As the operations of **isPRO** scales, a social impact measurement methodology and production of a yearly report is proposed in order to capture and apply successful partnership models to other states.
- The potential indicators can include but not limited to social impact, sustainable development goals, survey based indicators and environmental impact.
- Reporting of the monitored impact indicators can serve as a point of reference and powerful marketing tool to **isPRO**'s efforts to spread awareness on integrating independent smallholders into the global supply chain.



Measuring socio economic impact to capture and apply lessons learned as the organisation scales to other states



IMPLEMENTATION PLAN

Implementation Timeline

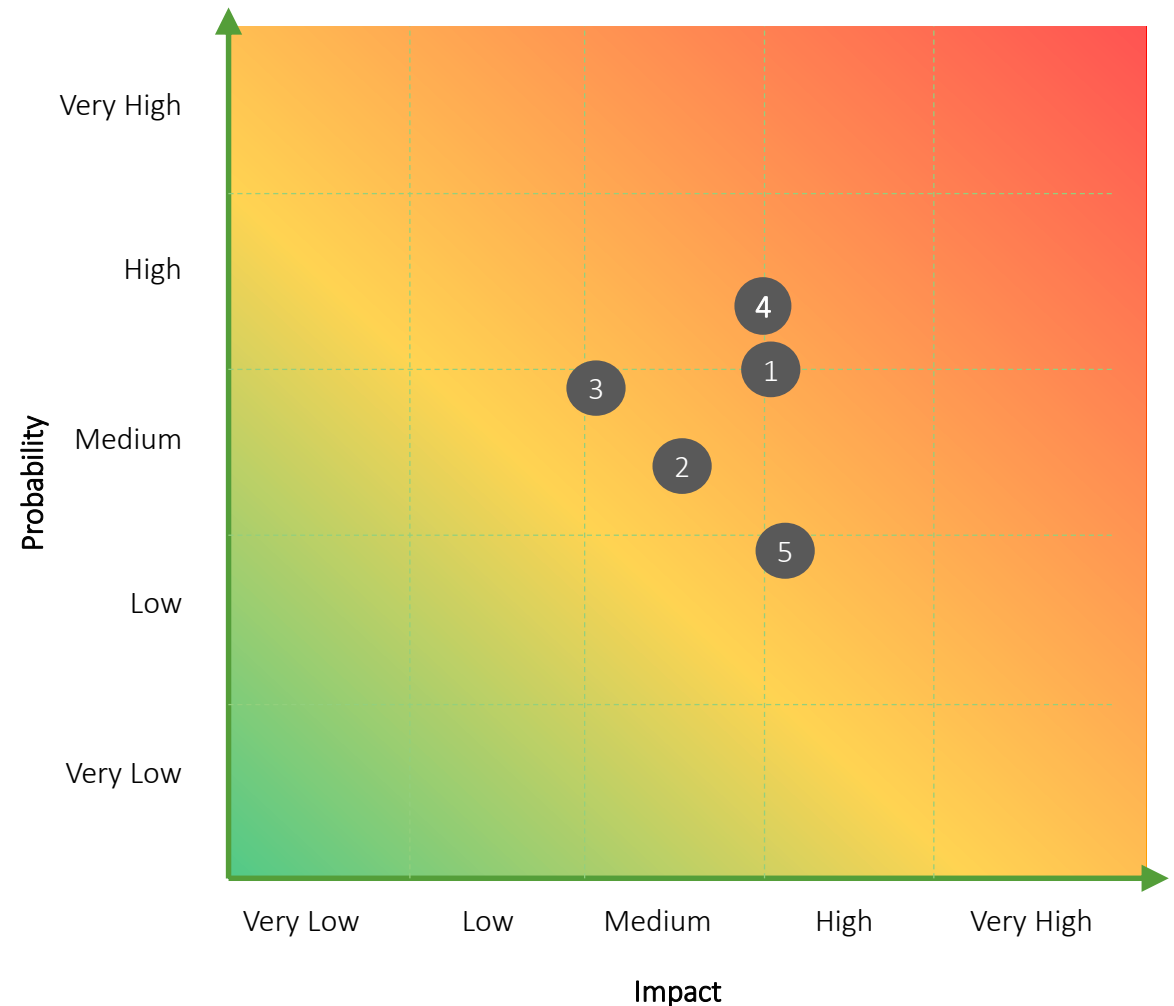
Focus Area	Phases	Year 1				Year 2				Year 3 - 10	
		Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Sales & Marketing	Develop marketing materials										
	Organise roadshows and townhall sessions										
Operations & Strategic Partnerships	Establishment of on-site office in Perak										
	Map out location of mills and all location of oil palm plantations										
	Start FFB trading										
	Launch plantation management services										
	Start Sustainable Outgrower Programme (SOP)										
	Formation of clusters: 1st Site target area (Target land size 1,000/Ha)										
	Formation of clusters: 2nd Site target area (Target land size 10,000/Ha)										
	Formation of clusters: 3rd Site target area (Target land size 20,000/Ha)										
	Training and knowledge transfer to independent smallholders										
Organisational Structure & Governance	Establish isPRO as company limited by guarantee (CLBG)										
	Establish Board of Directors and Advisory Council										
	Review governance and organisational framework										
	Secure key isPRO management and op-field team										
Financial Analysis & Investment	Secure the funding and necessary capital										
	Annual financial reporting for Board of Directors										



RISK ANALYSIS & MITIGATION

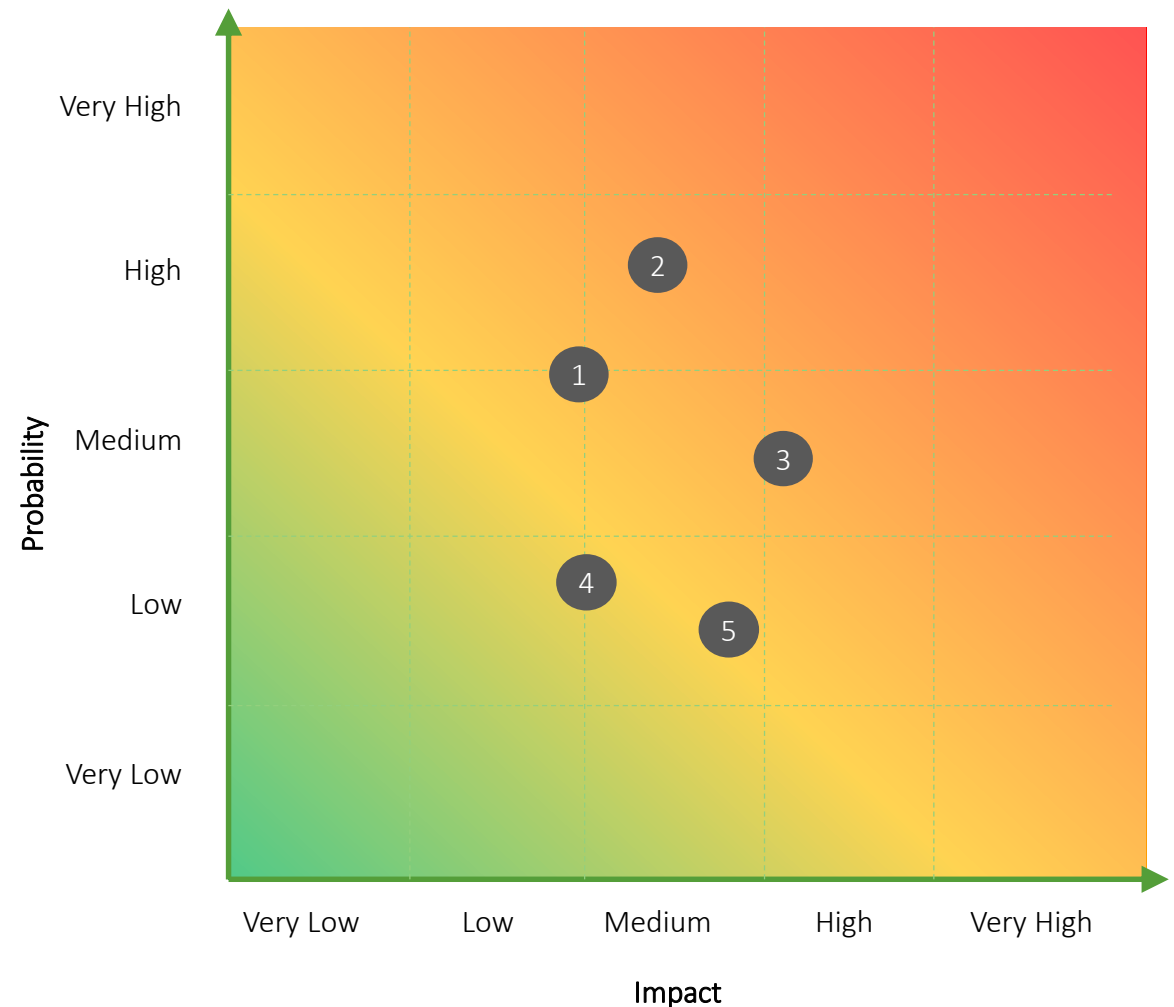
Operational Risks & Mitigation

- 1 Risk:** Inconsistent supply of quality FFB from clusters
Mitigation: Provide technical support and farming inputs to independent smallholders. Regular quality inspection of plantations.
- 2 Risk:** Lack of participation from smallholders to join the clusters
Mitigation: Promote **isPRO**'s benefits and work with organisations who have existing relationships with the smallholders.
- 3 Risk:** Exploitation of independent smallholders in SOP
Mitigation: Strict vetting process and set expectations to be made explicit in contract for all partners
- 4 Risk:** Risk of contract default by clusters or value chain partners
Mitigation: Establish trust by providing complimentary services such as training and reinforce the added benefits from the SOP in the long run
- 5 Risk:** Lack of participation of value chain partners in SOP
Mitigation: Propose tax exemption as an incentive for corporate producers to engage in SOP



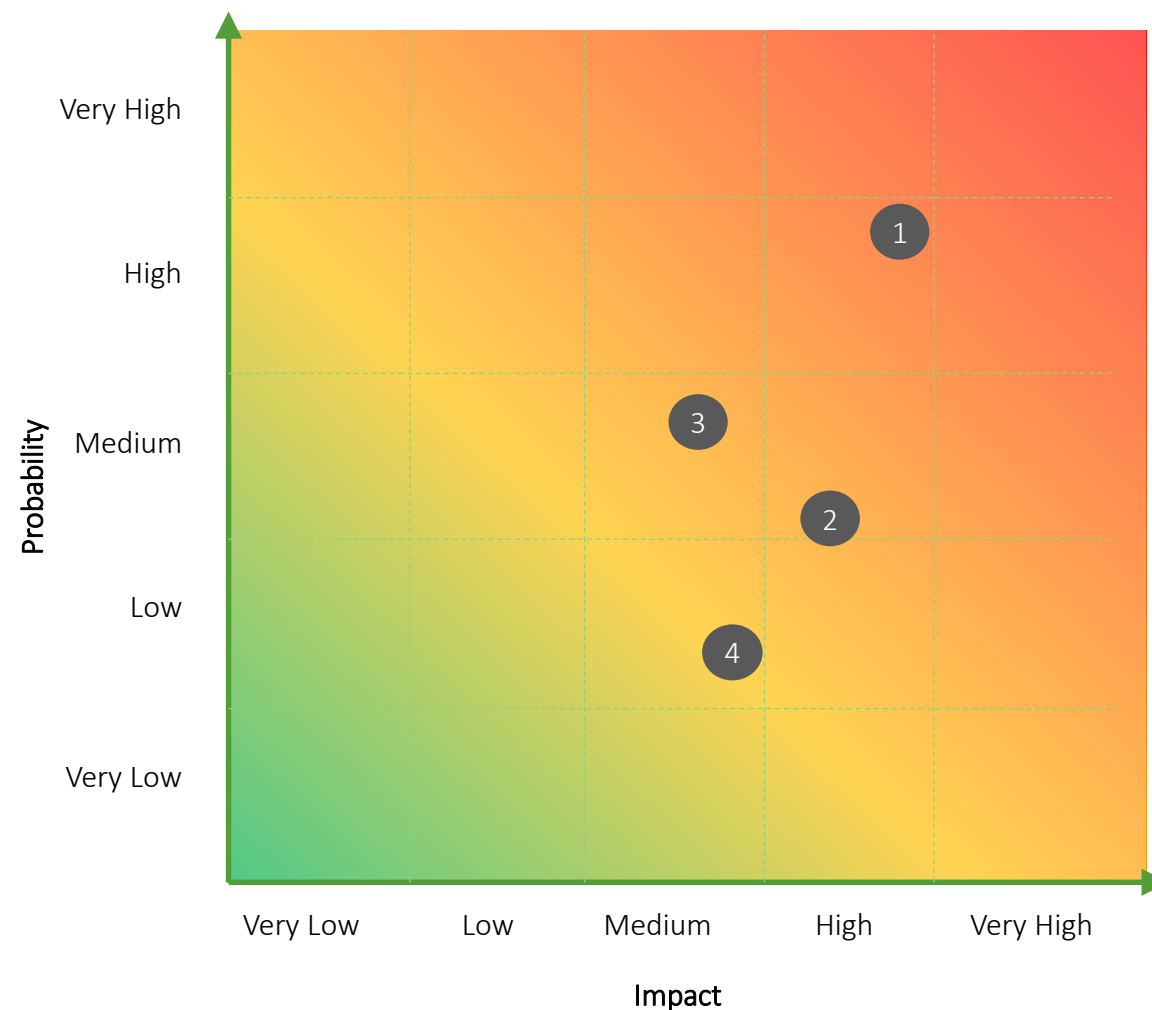
Governance & Organisational Risks & Mitigation

- 1 Risk:** Lack of alignment between management team and local on-field team
Mitigation: Quarterly meeting, training and regular communications to ensure team is aligned.
- 2 Risk:** Lack of capacity to reach out to independent smallholders
Mitigation: Develop the local technical on-field team to take lead. Start with small number of smallholders and scale as team trainers and technicians are developed.
- 3 Risk:** Non-compliance by Board Members
Mitigation: Yearly audit requirements and regular performance review
- 4 Risk:** Reputational risk due to poor conducts and inefficiency
Mitigation: Regular performance monitoring and offer training for isPRO's staff
- 5 Risk:** Changes and uncertainties in political landscape
Mitigation: Maintain a positive relationship with government



Financial and Investments Risks & Mitigation

- 1 Risk:** Fluctuation of FFB and CPO pricing
Mitigation: Increase FFB trading volume and develop alternative revenue streams
- 2 Risk:** Challenges securing initial capital
Mitigation: Emphasis opportunity to financiers to drive significant social benefits; approach development funding institutions (DFIs), look at availability of impact investors, soft loans
- 3 Risk:** Investors might have vested self driven interests
Mitigation: Ensure contractual terms are made clear to all stakeholders
- 4 Risk:** Financial supporters may question the disbursement of funds used
Mitigation: Transparent reporting and disclosure through annual reports and communications
- 5 Risk:** Increased costs of products and services due to inflation
Mitigation: Cost optimisation and adjust unit process





CONCLUSION

Critical Drivers for Success

isPRO offers innovative solutions to address the key challenges independent smallholders face. The business model strengthens smallholder's position in the value chain, benefits other key players downstream by leveraging economies of scale, offering more choice and matching supply with demand, all while promoting sustainable agricultural practices and greater traceability.

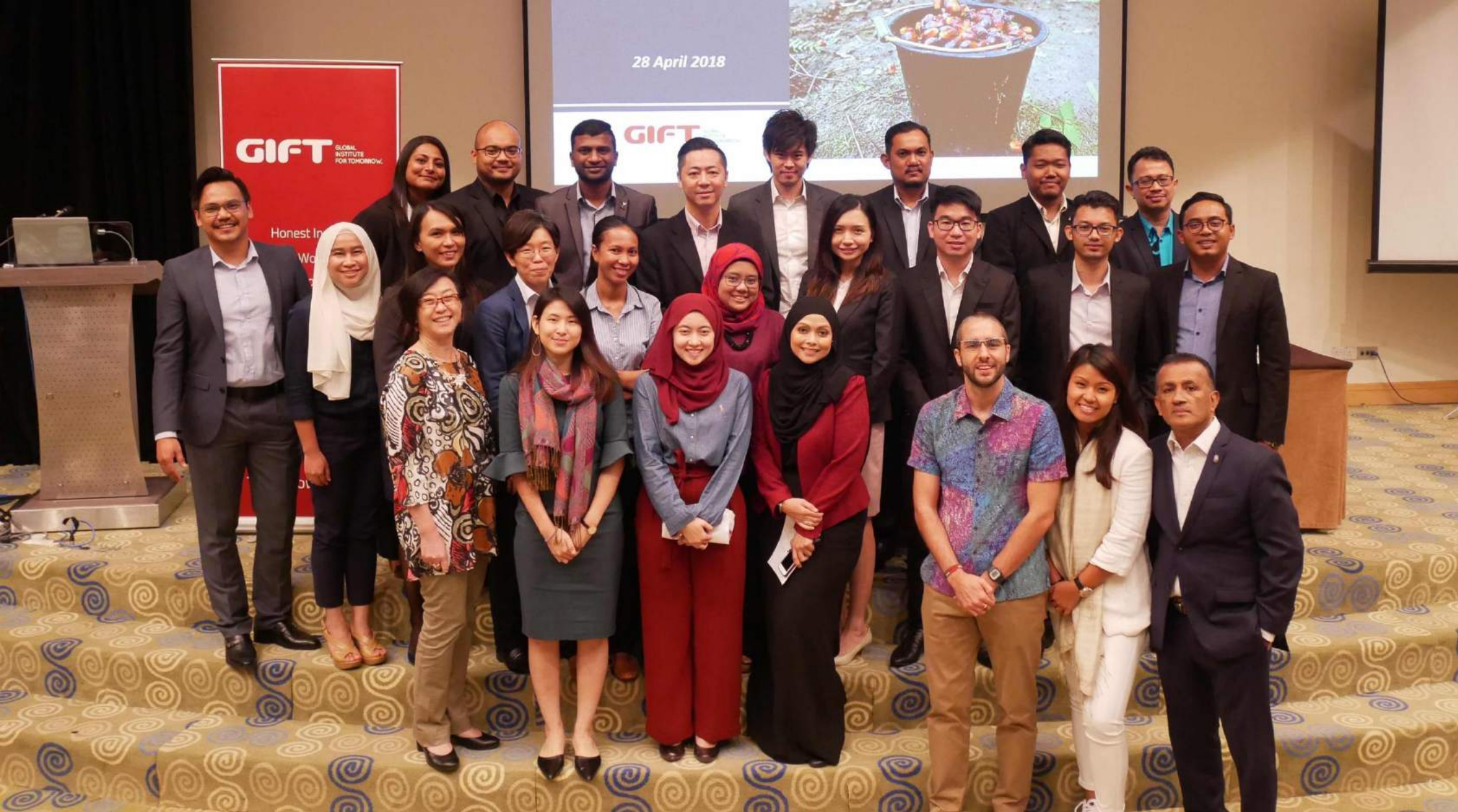
Besides being a financially viable business, **isPRO's** activities can revitalise the palm oil industry in Malaysia and serve as an example for other palm oil producing countries.

Key drivers for success include:

- Convening a consortium of founding members and drafting a constitution imbedded with checks and balances to ensure the interests of all stakeholders, especially independent smallholders, are protected;
- Securing the initial funding to establish **isPRO** and begin implementation of pilot site in Perak;
- Organising the independent smallholders into clusters for efficient delivery of services and to leverage economies of scale;
- Securing partnerships with corporations for a successful Sustainable Outgrower Programme;
- The identification of risks and development of mitigation measures to address these quickly and efficiently.

The creation of **isPRO** presents a compelling case for key industry players especially those mandated to ensure independent smallholders meet certification standards, and corporate growers facing land constraints. It is now recommended that further due diligence be conducted to assess the recommendations in this proposal and support be garnered amongst key players in the value chain with a view to establishing **isPRO** before funding and launching a pilot project in Perak to test and refine the proposed business model.





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