The Observer

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Is there a viable RPT deal after all?

Related party transactions (RPT) are poised to be a common in the days ahead given many businesses are anticipated to struggle with earnings dips as the COVID-19 health crisis is showing no sign of abating – and with concerns over a potential second wave attack escalating.

Recall our June 12 revelation as to how RPT were embarked upon as a vehicle by major shareholders (very often, company founders) to bail out unprofitable personal businesses in their stable.

As a follow-up to that, allow us to throw the question if there are indeed genuine RPTs out there – those that are financially-sound and are truly intended to reward shareholders, particularly those in the minority realm.

Unfortunately, the truth is such that most literature on RPTs tend to paint such corporate exercises in an unpleasant light.

Pointing to the very fact that RPTs have the potential to be abusive, the International Corporate Governance Network (ICGN) stresses that disclosure, review by independent directors and a shareholder vote are important ingredients to protect the interest of minority shareholders.

In principle, however, RPTs are neither intrinsically good nor bad. They can have legitimate purposes in promoting the company's own long-term value creation and success.

But obviously, as history has proven time and again, they can also be subject to abuse – by the executive management or controlling owners – in a way that can negatively affect the company and its minority shareholders as well as its creditors.

The Eversendai RPT game plan

Let us examine if Eversendai Corp Bhd – the latest listed entity to court the RPT controversy – deserves our benefit of doubt.

For the record, the steel structure and civil construction firm inked a purchase agreement on 30 June to acquire liftboat operator Vahana Offshore (M) Sdn Bhd for RM235 million, the purchase price of which will be settled via the issuance of 770.49 million new redeemable convertible preference shares (RCPS) at 30.5 sen each.

However, the price tag of RM235 mil works out to an earnings multiple of close to 50 times Vahana's earnings which is deemed to be on the high side considering the current economic/financial climate.

This is because Vahana Offshore's FY19 earnings are based on the contributions of only one vessel (namely, Vahana Aryan) while the other vessel, Vahana Arjun, will only be built by June 2021.

Despite Eversendai's founder, executive chairman and managing director Tan Sri AK Nathan having come out in the open to argue passionately on the long-term benefits of Vahana Offshore's acquisition, sceptics are quick to associate the RPT exercise as not being beneficial to Eversendai's dwindling financial performance, and hence, to minority shareholders.

There is no hiding that the company's earnings (in terms of net profit) plummeted 80.5% during FY19 to RM13.7 million (FY18: RM70.24 million) with 8.8% decrease in revenue to RM1.55 billion (FY18: RM1.71 billion).

Eversendai attributed the dismal performance to "lower revenue contributed by the energy sector which has decreased significantly by 81.1% and losses incurred due to very low utilisation of the Ras Al Khaimah fabrication yard facility (in the United Arab Emirates) caused by the delay in the timing of new project awards by external parties."

For its Q1FY20 ended 31 March 2020, Eversendai slipped into the red with a net loss of RM10.14 million (Q1FY19: RM11.41 million) with its revenue shrinking 42.8% to RM228.5 million from RM399.63 million in the same period of the previous year.

Above all else, its share price is languishing in the 27 sen to 30 sen range even after having recovered from an all-time low of 14 sen on 16 March at the height of the COVID-19 market sell-off.

Notwithstanding the headwinds stemming from a slowdown in global trade, Eversendai expects a rebound from the current slump given the group's order book value stands at a historical high of RM2.9 billion (with about 44.5% of the value coming from its traditional Middle East stronghold).

In a media conference to announce the RPT exercise on 10 February, Eversendai's Nathan expressed confidence that the recurring income from Vahana Offshore would boost the group's earnings, and in turn bolster shareholders' confidence.

As announced on 30 June, Vahana Offshore is expected to contribute 25% or more of the net profits of Eversendai going forward.

However, minority shareholders should note that there is no profit guarantee and as such these projections may very well be wishful thinking on the part of the major shareholder. It would be good if such RPTs come with profit guarantees to comfort and give confidence to the minority shareholders.

Reaching the verdict

Obviously sceptics would argue that the outlook of the industry remains challenging at this point of time – with the lingering clouds of global economic and financial uncertainties – hence, the risks seem to outweigh the benefits. Probably, minority shareholders need to delve deeper into details of the acquisition given "the devil is always in the details".

In all fairness, regardless if a RPT will ultimately be boon or nightmare to the minority shareholder's fraternity, the company's board – in particular, its independent directors – should avail themselves as the first line of defence to determine if the exercise merits a green light.

According to the ICGN, the company's board should consider the following:

- Are there strong business reasons for the company to enter into the proposed RPT;

- A statement from the board/independent board committee that the terms of the RPT are fair to the company and its shareholders;

- A confirmation that the terms and conditions of the transactions are established on an arm-length basis, and that similar conditions would have been applied for a transaction with an unrelated party; and

- Whether the RPT is expected to have an impact on the independence of corporate directors that are involved in the transaction.

At a glance, the Vahana Offshore RPT transaction and issuance of RCPS do not seem to be detrimental to the interest of minority shareholders.

The purchase consideration does not result in an outflow of cash from Eversendai as it involves the issuance of 770.49 million RCPS in Eversendai at 30.5 sen each.

The RCPS shall have a tenure of 10 years with cumulative preferential dividend of 3% per annum and is convertible into ordinary shares in Eversendai at a conversion ratio of two RCPS to one Eversendai share.

And most importantly, the proposals are subject to and conditional upon approvals being obtained from the shareholders of Eversendai at an extraordinary general meeting (EGM) to be convened.

As such, shareholders shall have a final say in the acceptance of the proposals – unlike some instances where the RPT does not trigger any of the thresholds in the listing requirements to warrant an EGM for their approval.

Devanesan Evanson
Chief Executive Officer

MSWG AGM/EGM Weekly Watch 27 July - 31 July 2020

For this week, the following are the AGMs/EGMs of companies which are in the Minority Shareholders Watch Group's (MSWG) watch list.

The summary of points of interest is highlighted here, while the details of the questions to the companies can be obtained via MSWG's website at www.mswg.org.my.

Date & Time	Company	Quick-take
27.07.20 (Mon) 09.00 am	Pegasus Heights Bhd (AGM)	The Group reported a lower loss in FY19 due to the better result of the Centrepoint Seremban Mall with improved occupancy rates from 65.3 % in FY18 to 75.4% in FY19
27.07.20 (Mon) 10.00 am	Sapura Resources Bhd (AGM)	The Aviation and MRO business segments recorded higher losses in FY20 were due to the restriction in air travel and MCO as a consequence of the COVID-19 pandemic.
27.07.20 (Mon) 02.30 pm	Affin Bank Bhd (AGM)	Affin's ROE is one of the lowest in the industry while its cost to income ratio is one of the highest in industry. In addition, its net interest margin is expected to be under pressure amid current low interest rate environment.
28.07.20 (Tue) 09.00 am	Teck Guan Perdana Bhd (AGM)	It registered a y-o-y decline of 9.36% in revenue to RM273.65 million vs RM301.90 million in the preceding year due to lower sales volume and selling price. Nevertheless, net profit is higher at RM3.16 million compared to RM2.52 million in the preceding year attributed to higher operating margin. Will we see a positive surprise in its FY21 operating performance if FFB production and average selling price improve going forward?
28.07.20 (Tue) 10.30 am	Quality Concrete Holdings Bhd (AGM)	QC's has recorded lower pre-tax loss of RM1.4 million compared to pre-tax loss of RM10.5 million in the year before. The prospect of it making a turnaround remains murky in FY21.
28.07.20 (Tue) 11.00 am	Kumpulan H&L High-Tech Bhd (AGM)	The lower revenue of its manufacturing division was contributed by the decline in Precision Engineering Moulding (PEM) segment due to the slow-down in demand from Malaysia and compounded by the trade war between China and the United States.

29.07.20 (Wed) 10.00 am	Axiata Group Bhd (AGM)	Axiata is leveraging on digitisation, analytics and data modelling to identify growth opportunities.
29.07.20 (Wed) 10.00 am	George Kent (Malaysia) Bhd (AGM)	More proactive measures needed to address the declining top-line and bottom-line results since FY2019.
29.07.20 (Wed) 11.00 am	Inix Technologies Holdings Bhd (AGM)	Inix extended its 12 months financial period to 18 months from 1 August 2018 to 31 January 2020. It recorded a lower revenue of RM8.049 million for FY20 compared to RM 9.45 million in FY18. Net loss was lower at RM 2.74 million compared to net loss of RM 15.29 million in FY18 due to reduction in the impairment of receivable and administrative expenses. It has suspended ex Group MD Mohd Anuar Mohd Hanadzlah who is currently a non-independent non-executive director of the company on 18 March and putting him under investigation. In turn, Mohd Anuar is suing Inix for defamation and is claiming for general damages of RM1 million and other damages to be determined by the court. At the meantime, there will be five additional resolutions to be tabled at its AGM, one of which is to remove Mohd Anuar from the Board, while the rest pertaining to the appointment of four new directors. The future of Inix remains uncertain.
29.07.20 (Wed) 11.00 am	Sapura Industrial Bhd (AGM)	The Company will strengthen its R&D capabilities to develop new innovative products and solutions that will expand the range of product offerings, thus giving the Company a unique advantage in today's highly competitive and fast-evolving market.
29.07.20 (Wed) 11.00 am	G3 Global Bhd (fka Yen Global Bhd) (AGM)	It has been registering losses for years with a net loss of RM16.39 million in FY19 compared to RM17.11 million in FY18. It intends to

		expand further into the ICT business especially in AI and Data Analytics. As global and local demand rises for Smart Technology (AI, mobility, smart IoT) to manage efficiency and cost, it hopes to see continuous growth in revenue especially demand for AI in view of current COVID-19 outbreak.
29.07.20 (Wed) 02.00 pm	Astro Malaysia Holdings Bhd (AGM)	Analysts have deemed the recent acquisition of iFlix by Tencent is not a threat to Astro given the latter's extensive market reach and position. Nevertheless, it continues to face stiff competition from easily accessible pirated content.
29.07.20 (Wed) 02.00 pm	Minda Global Bhd (AGM)	It has been incurring losses every year since FY14 and registered a higher net loss of RM37.8 million in FY19 compared to a loss of RM15.9 million in FY18. One of the key concerns is its huge allowance for impairment losses in respect of trade receivables as at the end of FY19 amounted to RM53.7 million. This represents 82.7% of total outstanding trade receivables of RM64.9 million.
30.07.20 (Thur) 10.00 am	Sapura Energy Bhd (AGM)	The Group will continue to bid for more renewables, decommissioning, marine terminal and large volume EPCIC projects, while keeping the options to scale back based on demand.
30.07.20 (Thur) 10.00 am	CYL Corporation Bhd (AGM)	The plastic packaging manufacturer faces declining profit margin and revenue for the past five years. It slipped into red with pre-tax loss of RM1.5 million in FY18 then return to back with pre-tax profit of RM476,985 in FY19.
30.07.20 (Thur) 10.30 am	JKG Land Bhd (AGM)	The Group's unbilled sales as at end-FY2020 stood at RM401.8 million and the strong demand for ERA property project in KL can help the Group to ride through the sluggish property market.

One of the points of interest to be raised:	
Company	**Points/Issues to Be Raised**
Pegasus Heights Bhd (AGM)	The Trading segment recorded a higher revenue of RM8.31 million with a loss after tax of RM0.04 million in FY 2019 as compared to a lower revenue of RM6.85 million with a profit of RM 0.049 million in FY 2018. (pages 121 and 123 of Annual Report) a) Why is the profit margin from the Trading segment so low for both FYs? b) What are the measures taken by the Company to improve the Trading segment profitability? c) As disclosed on page 125 of the Annual Report, the Trading segment has two big customers who constituted 62.1% of the total revenue in FY 2019. Please explain how the Company mitigates the concentration risk arising from these two customers
Sapura Resources Bhd (AGM)	The Aviation business segment reported a higher loss of RM15.2 million in FY 2020 as compared to a loss of RM10.7 million in FY 2019. The MRO business segment also reported a loss of RM12.1 million in FY 2020, its first year of operation. (pages 181 & 182 of Annual Report) a) Please explain the reasons that contributed to the higher losses in the Aviation and MRO business segments in FY 2020? b) What measures has the Company taken to reduce the losses of the Aviation and MRO business segments moving forward? c) The air travel industry has been badly affected by the COVID-19 pandemic that has restricted air travel. What are the measures the Company has taken to overcome this challenging time and operate in the "New Normal" environment? d) When is the Company expected to provide MRO services for Boeing 737 series and Airbus A320 family aircraft at Senai Airport? What is the expected revenue for its first year of operation?
Affin Bank Bhd (AGM)	Remuneration paid to directors of subsidiaries increased by 60.38% y-o-y to RM2.57 million in FY19 from RM1.6 million the year before. What is the rationale for the sharp increase in remuneration paid to directors of subsidiaries?

<table>
<tr><td>Teck Guan Perdana Bhd (AGM)</td><td>The Group's estates produced a total of 18,563MT (2019: 23,849MT) of FFB which was about 22.16% lower than the previous year mainly due to lower yield (page 18 of Annual Report 2020 ("AR2020")).

a) The Group's FFB production and yield per mature hectare have been on a declining trend since FY2018, what are the reasons for the decline in yield?

b) What are the Group's plans to improve the FFB production and yield per mature hectare?</td></tr>
<tr><td>Quality Concrete Holdings Bhd (AGM)</td><td>In 2019, MSWG questioned the Company on the chances of recovering the impaired trade receivables. The Company, in its reply letter, among others, stated that it was pursuing legal action on debts of about RM4.1 million.

What portion of the RM4.1 million has been recovered to-date? What is the current status of the legal action?</td></tr>
<tr><td>Kumpulan H&L High-Tech Bhd (AGM)</td><td>Other Investments recorded a fair value loss of RM203,867 in FY 2019 as compared to RM76,142 in FY 2018. The loss was due to the write-down in values of golf club membership (RM48,000) and unquoted shares (RM47,236). (page 41 of the Annual Report)

a) Please provide a breakdown of the balance of the fair value loss of Other Investments amounting RM108,631 in FY 2019.

b) Please explain the reason for the investment in unquoted shares that resulted in the high fair value loss of RM47,236 from the initial cost of RM50,000?</td></tr>
<tr><td>Axiata Group Bhd (AGM)</td><td>1. In regard to operating revenue, sales of devices has declined significantly from RM1,273.5 million in FY 2018 to RM664.4 million in FY 2019. (Page 84 of Governance and Audited Financial Statements 2019 – GAFS).

What were the main reasons for the sharp decline in the sales? What are the measures taken to address the decline? What is the outlook for FY2020?

2. Outstanding provision for impairment for the following items increased significantly from FY 2018 to FY 2019:

FY 2019 (RM mil) FY 2018 (RM mil)
(i) Contract assets 51.9 33.5</td></tr>
</table>

	(ii) Trade receivables 702.8 568.1 (iii) Other receivables 183.6 115.5 What were the reasons for the significant increases? What is the nature of contract assets and other receivables? How much of the impaired amounts have been recovered to-date? What is the probability of recovering the remaining impaired amounts?
George Kent (Malaysia) Bhd (AGM)	What are the reasons for the significant decline in the share of results of the joint venture from RM13,407,000 in FY2019 to RM274,000 in FY2020 (Page 77 of the Annual Report 2020)?
Inix Technologies Holdings Bhd (AGM)	1. Accumulated impairment losses on trade receivables amount to approximately RM5.0 million for FP2020 (2018: RM5.2 million) (Note 10, page 91 of AR2020). a) What is the aging of these accumulated impairment losses on trade receivables in the following categories: 1 to 3 years and over 3 years, respectively? b) To-date, how much of the accumulated impairment losses on trade receivables have been recovered? c) Given that the Group expects the said amount to be recovered through the debt recovery process (Note 10, page 93 of AR2020), what is the probability of recovering the said trade receivables and are there any foreseeable write-offs for financial year ending 2021? 2. Other receivables increased significantly to RM5.2 million (2018: RM0.5 million), while accumulated impairment losses on other receivables was RM1.7 million (2018: RM1.5 million) (Note 11, page 93 of AR2020) a) What are the reasons for the significant increase in other receivables? b) What are the major items comprising other receivables? c) What actions have been taken to recover the accumulated impairment losses on other receivables? d) To-date, how much of the accumulated impairment losses on other receivables have been recovered

Sapura Industrial Bhd (AGM)	In the business segments reporting, Others segment reported a lower revenue of RM1.1 million in FY 2020 as compared to RM2.12 million in FY 2019.However, this segment reported a higher loss of RM3.4 million in FY 2020 as compared to a loss of RM2.1 million in FY 2019.(pages 137 & 138 of Annual Report). a) Which business unit in the Others business segment contributed to the higher loss? b) What are the reasons for the higher loss in the Others business segment?
G3 Global Bhd (fka Yen Global Bhd) (AGM)	1. Administrative expenses and other expenses increased substantially from RM7.819 million (FY2018) to RM11.659 million (FY2019) and RM1,106.3 million (FY2018) to RM4,502.0 million (FY2019) respectively. (Page 57 of AR). What were the major reasons for the increase and what measures have been taken to contain the significant rise in these expenses? Staff costs rose sharply from RM3.656 million in FY2018 to RM6,870.0 million in FY2019. (Page 109 of AR). What were the reasons for the sharp increase? 2. 2 customers, in total, contributed substantially (87.2%) to the Group's revenue of RM14,213.6 million in FY2019 (RM9,341.2 million and RM3,046.6 million). (Page 120 of AR). There is a concern on concentration of customers risk. a) What measures have been taken to mitigate the concentration risk? What is the latest percentage contribution by these two major customers (as at May or June 2020)? b) Are the two customers related parties and if so, are the transactions on an 'arm's length' basis?
Astro Malaysia Holdings Bhd (AGM)	Go Shop, ASTRO's 24/7 multilanguage, multiplatform home shopping proposition has over 2.2 million registered customers. (Page 14 of Integrated Annual Report - IAR). Registered members totaled 1.8 million in FY 2019. However, home shopping registered lower revenue of RM368 million in

	FY2020 (FY2019: RM374 million) and continued to show losses before tax increasing from RM7 million in FY2019 to RM16 million in FY2020. (Pages 30 and 32 of IAR). a) Why does the segment continue to show losses and when is it expected to turn around? b) What are the strategies to improve its performance?
Minda Global Bhd (AGM)	1. As at end FY2019, allowance for impairment losses in respect of trade receivables stood at RM53.7 million constituting a significant 82.7% of total outstanding trade receivables of RM64.9 million. (Page 122 of AR) a) How did the allowance increase to such a massive amount? How much of these impaired receivables have been recovered to-date? What is the status of the remaining impaired receivables and what is the probability of their recoverability? b) Has the company reviewed its credit risk management policies and instituted further enhancements? 2. Included in other receivables of the Group is contingent consideration receivable amounting to RM11,139,485 (2018: RM8,048,444) pursuant to a profit guarantee arrangement with the vendors of the acquired subsidiary. (Page 122 of AR) a) Is the receivable amount due to the shortfall in profit guarantee in respect of the acquiree's profit for FY2019 and/or other financial years? b) When was the amount due? Has this amount been paid to-date, and if not, why? c) Was the amount due from related parties? And if so, how are they related?
Sapura Energy Bhd (AGM)	The Group has impairment on goodwill amounting RM3,043.4 million in FY 2020. (page164 of Annual Report) Please provide a breakdown on goodwill impairment according to the respective business segments like Engineering & Construction, Drilling Business and Exploration/Production for FY 2020 and 2019. What are the reasons for the impairment?

CYL Corporation Bhd (AGM)	Revenue of CYL has been declining over the past five years with declining pre-tax profit, save for FY20 (page 7 of Annual Report 2020). Revenue declined from RM70.04 million in FY16 to RM41.44 million in FY20. Profit-before tax decreased from RM7.18 million in FY16, to pre-tax loss of RM1.5 million in FY19, and then improved to RM476,985 in FY20. Pre-tax profit margin of the Company also declined year-on-year from 10.26% in FY16 to -2.81% in FY19 before bouncing back to 1.15% in FY20. a) Apart from cyclical resin price, which is beyond CYL's control, what are the other factors that caused the declining profit margin over the years? How successful and effective are the current strategies to improve business profitability? What are the strategies that are going to be implemented to revive performance? b) CYL achieved better bottom-line performance in FY20 due to lower resin price and a more favourable product mix. In view of the current economic environment, will the same product mix be maintained for FY21?
JKG Land Bhd (AGM)	The rental income from investment properties have increased marginally from RM1.18 million in FY 2019 to RM1.22 million in FY 2020. (page 102 of Annual Report) a) What are the gross and net rental yields of the investment properties for FY 2019 and FY 2020? b) What is the average occupancy of the investment properties in FY2020 and FY2019? c) 'Working from home' has become a norm due to the Covid-19 pandemic. Please explain how this 'working from home' has affected the Group's investment properties' occupancy as there is less demand for office space. d) Please provide the Group's investment property outlook in FY 2020 and the financial impact due to the "new normal" environment.

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•With regard to the companies mentioned, MSWG holds a minimum number of shares in all these companies covered in this newsletter.

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