CORPORATE

Will low valuations lead to more privatisation?

Price offered by major shareholders must ideally be fair and reasonable

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TALK in the market is that the bearish market conditions could lead to more privatisations or buyouts of public listed companies.

This is premised largely on the fact that many listed companies are trading at gaping discounts to their underlying values, reflected by ratios such as their net tangible assets. **(See table)**

Bursa Malaysia now trades at a forward price-earnings (PE) multiple of 14.3 times for 2022, well below its historic average of above 16 times. The PE multiple has been on a downtrend since 2018 as the political risk premium rose for the local market, according to analysts.

Net sales by institutional investors looking to diversify portfolios geographically and meet withdrawals has also contributed to the issue which has had an impact on the pipeline of new listings, especially big-ticket names.

Companies like Weststar Aviation Services Bhd, Kulim Malaysia Bhd and QSR Brands (M) Holdings Bhd are speculated to be holding back on their listings due to the weak market conditions.

Valuation, however, is a subjective matter. While existing shareholders may see valuation of their company and the market as low, others believe there is room and reason to go lower.

"I think the markets, which have come off a bit, are not cheap. However, should markets correct at some point, it's possible that companies may trade below their intrinsic value and become candidates for privatisation.

"We have in the past and on a continuous process looked at such opportunities," Brahmal Vasudevan, founder and CEO of private equity firm Creador Capital Group, tells *StarBizWeek*.

He adds that Creador has typically looked for growth companies that have the capacity to grow earnings by 20% or more per annum.

"We do review companies which are trading below their intrinsic value such as below book value or low PE multiples. What is key is to ensure there is sustainable earnings and to ensure prospects for such companies remain intact.

"We are always open to partnering with passionate entrepreneurs. What we look for is integrity and capability to build their business," Brahmal adds.

The FBM KLCI appears to have come under fresh selling pressure last week as investor sentiment turned poor as foreign markets fell on bearish inflation data and weaker growth projections.

Local equity market trajectory appears to disconnect from the progress of the local economy, which is on track to grow strong this year.

"We believe that the current low valuation of our market is driven by the aggressive US Federal Reserve in terms of its rate hikes, which are not only affecting our market but globally as well.

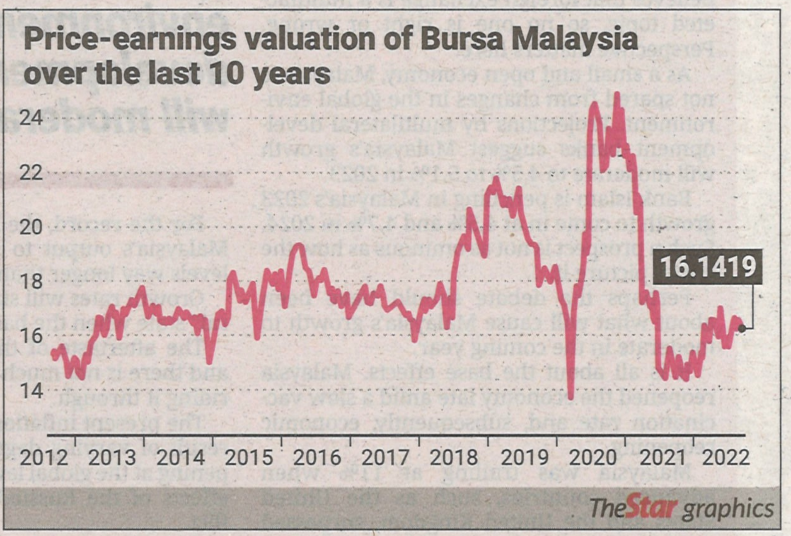
"Therefore, there may not be any action that can be done to address this for now. Nevertheless, in our view, this situation will not persist and valuation will recover," says MIDF Research director and head Imran Yusof.

Speculation of buyouts

Nevertheless, cheaper valuations on Bursa Malaysia have helped fuel speculation of possible buyouts of asset-rich companies trading at low prices.

As an example, a recent media report pointed out that tycoon Tan Sri Syed Mokhtar Al-Bukhary could be mulling a privatisation of DRB-Hicom Bhd, which trades way below its true value.

In the spotlight: People walk past the bull and bear statue at Bursa headquarters. Cheaper valuations on Bursa have helped fuel speculation of possible buyouts of asset-rich companies trading at low prices.



Price-earnings valuation of Bursa Malaysia over the last 10 years

CGS-CIMB Research pegs DRB-Hicom's asset value at a whopping RM8.3bil, compared with its market capitalisation that stood at a mere RM3.13bil as of market close on Thursday.

June saw DRB-Hicom's share price fall to March 2020 Covid-19 period lows of RM1.11 a share after the diversified group posted a net loss of RM25.7mil for its first quarter ended March 31, 2022.

The market price was well below its RM3.73 net asset per share value as at the end last year.

With such a large discount to the intrinsic value, it is possible that the speculative talk of a buyout led its share price to rebound to hit a high of RM1.66 per share this week.

Like other diversified groups, DRB-Hicom's lower valuation by the market is often associated with its conglomerate structure and inter-company deals.

It has interests in auto manufacturing, property development, aerospace and defence, Islamic banking and postal services.

There has been no offer yet from DRB-Hicom's controlling shareholder Etika Strategy Sdn Bhd (owning 55.92%), which is controlled by Syed Mokhtar. Interestingly, DRB Hicom has yet to issue any statement on the matter since the article appeared on Sept 5.

The association to buyouts is nothing new for Syed Mokhtar, who took undervalued MMC Corp Bhd private via a selective capital reduction (SCR) exercise in December last year.

Seaport Terminal (Johore) Sdn Bhd, the controlling shareholder, in June last year, proposed a SCR at RM2 a share or RM2.94bil in total. MMC shares were trading at about 80 sen in February 2021, well below its net asset per share value of RM3.12 or at a price-to-book ratio of 0.375 times as at end-2020.

When the offer was tabled on June 3, MMC was trading at RM1.30 a share. Despite the SCR price being at a premium over the share price, the independent adviser Alliance Investment Bank Bhd stated that the offer was not fair because it was below its fair value of RM3.32 to RM3.41 but was reasonable, given the historic share value.

MMC shareholders nevertheless accepted the SCR and the logistics and engineering group was delisted on Dec 16.

While property counters like SP Setia Bhd, IOI Properties Group Bhd and UEM Sunrise Bhd trade at deep discounts to their asset values, analysts think the discount is partly justified as the asset value includes land banks that do not generate cash flows unless developed.

Pricing issue

While buyouts are part and parcel of a well functioning capital market, the issue of value of offers is often controversial for minority investors.

"The main and only issue is the price offered by the major shareholders – it must ideally be fair and reasonable.

"On occasions, minority shareholders will be prepared to accept an offer that is deemed as not fair, but reasonable if the reasons given for such pronouncement by appointed independent advisers are convincing," says Devanesan Evanson, CEO of the Minority Shareholders Watchdog Group.

That aside, he said a fair marketplace must provide both an entry and exit opportunity for companies and their promoters.

Timing of investment appears to be key when dealing with buyout offers.

Buyout offers can be rewarding for minority shareholders if they are at a premium to the underlying share price like the MMC SCR and vice versa if the offer price is lower than the transacted price.

When buyout offers don't meet minority shareholders' expectations, the exercises can turn out to be drawn out and messy.

"Low valuations should serve as an impetus for public-listed company owners to buy out minority shareholders. However privatisation can be a long and drawn out affair as in the recent Cycle & Carriage Bintang Bhd (CCB) or FGV Holdings exercises show.

"This is due to the regulatory requirements which are designed to protect the minority. It can be challenging to touch the minimum 90% level required to carry out a compulsory acquisition," says Thinkat Advisory Sdn Bhd managing director Karl Fredericks.

He adds that funding can also be an issue as not many banks are willing to do large-scale equity financing unless there is a clear take out source.

The privatisation of CCB by controlling shareholder Jardine Cycle & Carriage Ltd (Jardine CCL), spanning some three years, was a case of minority shareholders standing their ground and demanding a higher price, quite successfully.

Jardine took three attempts to successfully delist (on Sept 19) CCB and in the process had to raise the SCR offer price from RM2.20 in November 2019 to RM2.40 in March 2021 and then to RM2.70 a share in July 2022.

Investment banker turned investor Ian Yoong Kah Yin believes CCB minority shareholders got a RM2.70-per-share offer from Jardine CCL mainly due to the resistance of shareholders like Muar Ban Lee Group Bhd (MBL).

"I think if not for the actions of MBL to hold out for a higher price, the discount Jardine CCL would have enjoyed on the CCB buyout would have been more attractive," he says.

He also notes the SCR of Selangor Properties Bhd saw the promoters revise the SCR offer price two times from RM5.70 a share to RM6 and then finally RM6.30 a share before minority shareholders, who held some 31.77% of shares outstanding, agreed to support the exercise.

The SCR offer price was nevertheless below its revalued asset value of RM8.28 per share.

Yoong believes the promoters of Selangor Properties would have undertaken the buyout as access to financing post delisting was not an issue for the company.

He adds that buyouts should not be perceived negatively as it makes complete sense for major shareholders to try to take companies at discount values while the exercise offers an opportunity to shareholders to exit at a single price, especially for thinly traded counters with a "status quo" management approach, which can act like a bear trap as well.

Apart from CCB, year-to-date, Bursa Malaysia has seen five other takeover offers for Zenworld Holdings Bhd, Computer Forms (M)

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>
> Brahmal Vasudevan

Companies trading at big discounts to their NTAs

Companies with market capitalisation of above RM1bil

Name	Share price as of Sept 14	NTA per share (RM)	Discount to NTA		Market cap (RM mil)	Net cash or (net debt) (RM mil)
			Current %	One year ago %		
SP Setia Bhd	0.68	3.83	82.26	68.95	2,771.33	(10,926.20)
UEM Sunrise Bhd	0.29	1.22	76.65	68.46	1,441.67	(3,355.94)
Boustead Holdings Bhd	0.62	2.53	75.49	77.07	1,256.73	(6,589.70)
IOI Properties Group Bhd	1.00	3.74	73.40	66.05	5,478.61	(14,468.71)
Lotte Chemical Titan Holding Bhd	1.69	5.85	71.12	56.42	3,849.07	4,558.49
Berjaya Corp Bhd	0.24	0.73	67.16	64.42	1,330.06	(5,648.90)
OSK Holdings Bhd	0.91	2.69	66.11	66.86	1,876.51	(1,933.67)
Sime Darby Property Bhd	0.47	1.37	65.70	52.93	3,196.39	(2,988.68)
Malaysian Resources Corp Bhd	0.34	0.97	65.39	58.16	1,496.62	(1,290.93)
Genting Bhd	4.50	12.50	64.00	60.48	17,327.59	(17,896.20)
Mah Sing Group Bhd	0.62	1.70	63.87	52.71	1,493.03	(489.68)
Tropicana Corp Bhd	1.16	3.04	61.82	66.10	2,282.13	(3,119.33)
MPHB Capital Bhd	1.40	3.51	60.16	57.60	1,001.00	289.07
DRB-Hicom Bhd	1.58	3.93	59.77	59.01	3,054.51	(3,675.90)
Supermax Corp Bhd	0.76	1.88	59.66	-35.62	2,019.13	2,799.18
Eco World Development Group Bhd	0.68	1.62	58.29	50.88	1,987.45	(2,107.97)
Capitaland Malaysia Trust	0.55	1.11	50.88	43.67	1,174.59	(1,341.02)
Affin Bank Bhd	2.11	4.09	48.35	58.39	4,668.02	757.69
Malaysia Building Society Bhd	0.61	1.17	48.23	46.94	4,338.75	(10,754.17)
IJM Corp Bhd	1.70	3.22	47.28	42.01	5,992.65	(2,031.29)

Companies with market capitalisation below RM1bil

Name	Share price as of Sept 14	NTA per share (RM)	Discount to NTA		Market cap (RM mil)	Net cash or (net debt) (RM mil)
			Current %	One year ago %		
Xidelang Holdings Ltd	0.02	0.62	96.79	92.79	42.32	741.46
Serba Dinamik Holdings Bhd	0.03	0.51	95.05	28.73	92.74	(3,722.88)
Landmarks Bhd	0.19	2.78	93.15	85.77	127.59	(126.70)
Puncak Niaga Holdings Bhd	0.26	2.99	91.30	84.94	116.28	(895.30)
Anzo Holdings Bhd	0.01	0.11	91.24	60.58	11.16	16.71
Parkson Holdings Bhd	0.14	1.34	89.93	83.96	155.10	(3,291.92)
Lion Industries Corp Bhd	0.30	2.80	89.30	78.95	204.24	524.71
Reach Energy Bhd	0.04	0.37	89.08	78.16	43.86	3.42
Kanger International Bhd	0.04	0.36	88.80	-54.03	24.12	(3.17)
Sanichi Technology Bhd	0.03	0.21	88.12	83.37	35.08	113.66
AirAsia X Bhd	0.46	3.70	87.69	78.35	188.74	22.15
Fitters Diversified Bhd	0.08	0.61	87.61	39.72	45.60	(16.01)
Meridian Bhd	0.02	0.15	86.83	-8.67	18.08	(1.88)
Lion Posim Bhd	0.44	3.25	86.45	80.13	100.24	131.58
Eversendai Corp Bhd	0.11	0.78	85.98	71.96	85.91	(1,139.22)
Sealink International Bhd	0.07	0.45	85.70	60.40	32.50	(71.39)
CSH Alliance Bhd	0.04	0.28	85.56	51.28	55.26	112.63
Country Heights Holdings Bhd	0.40	2.72	85.47	55.87	115.93	(200.12)
MK Land Holdings Bhd	0.15	0.99	85.37	78.82	174.67	47.64
Seacera Group Bhd	0.17	1.12	85.33	82.66	102.61	1.56

Source: Bloomberg TheStar graphics

Bhd, ECM Libra Group Bhd, Olympia Industries Bhd and Hock Seng Lee Bhd (HSL).

Why do it?

Buyouts can be a corporate restructuring tool regardless of the company's position of strength or weakness.

When reshaping corporate goals and strategies in dealing with organisational issues and opportunities, controlling shareholders sometimes consider privatisation as a route to embark on a total organisational revamp, restructuring of its capital base, take on mergers and acquisitions or respond to industry restructuring or regulatory compliance, says Kevin Chew, senior executive director at Strategy and Transactions, Ernst & Young PLT.

Billionaire T. Ananda Krishnan did so with Maxis Communications Bhd in 2007 and Astro All Asia Networks Bhd in 2010. Both companies were then relisted in 2009 and 2017, respectively.

"Before the Covid-19 pandemic, controlling shareholders of public companies who took their companies private often cited multiple factors such as poor market valuations as a result of low investor sentiment, particularly with corporate stakeholder management issues and market challenges.

"The promoters also did so because there was easy access to financing from banks and other funding options that did not require corporate placement exercises such as rights and bonus issuances," Chew says.

He adds that concerns of higher operational costs and increasing transparency requirements from corporate reporting led to buyouts as did increasing stakeholder activism that demand a higher communication budget and management efforts across stakeholder segments.

Buyouts are also driven by the need to restructure businesses without the complexity of stakeholder and regulator scrutiny. Cases in point include the privatisations of DXN Holdings Bhd and MMC's SCR. The latter was speculated to have been done ahead of a possible relisting of port assets at a later date.

"I think MMC could relist its port operations if it can successfully take over the port operations of Suria Capital Holdings Bhd. The Sabah ports will give it access to the South China Sea and will be an asset and complement its existing ports in the peninsula," points out Yoong.

Some companies embark on a delisting route to proceed with strategic plans before a potential relisting of an entirely new entity as is the case with the proposed relisting of DXN.

The company was delisted in December 2011 from the Main Board following a takeover offer of RM1.75 per share from its promoters, which gave it a market capitalisation of RM393.7mil.

The offer price was at a premium of RM1.12 or 277.8% to its IPO price of 63 sen and a premium of 32 sen or 22.4% over its last traded price.

DXN, in its draft prospectus for a relisting on Bursa Malaysia, said the delisting was done to address business challenges the company faced by undertaking the necessary restructuring, reorganisation and rationalisation that needed to be done.

Since its delisting, it has transformed into a different entity. The company has concentrated its resources on the sales of health and wellness products as well as raised its production capacities. Revenue has ballooned from about RM255mil in 2011 to RM1.15bil in 2021 while net profit has risen from RM41.46mil to RM191.6mil over the period.

Buyouts on the horizon could also be triggered by issues like environmental, social and governance (ESG) and climate change, say analysts. Institutional investors, under pressure from activist investors, could exit companies that don't address ESG concerns or have a significant carbon footprint.

"Share prices will tend to fall when you have ESG and climate change issues – a form of market discipline.

"The share price fall is more pronounced if you have institutional investors, as they tend to dispose off shares of companies if you are recalcitrant when it comes to adopting best practices in ESG and climate change. This will drive share prices down and this may offer an opportunity to privatise the company," says Devanesan.