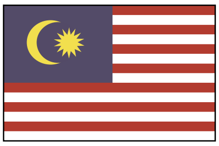


Malaysia

Domestic consolidation and overseas expansion make for a very strong year in Malaysian M&A

Current Environment

Malaysia's economy is expected to remain moderately strong in 2006. GDP grew by 5.4% during the first half of 2006, which is roughly the same for the full year of 2005, on the back of high private demand and private investments and strong contributions from the manufacturing, services and agriculture sectors.

The country's consumer price index continued to rise in 2006, reaching a peak of 4.8% year-on-year in March before stabilising to 4.1% for the half year as a result of the increase in the prices of goods following the sharp fuel price hike.

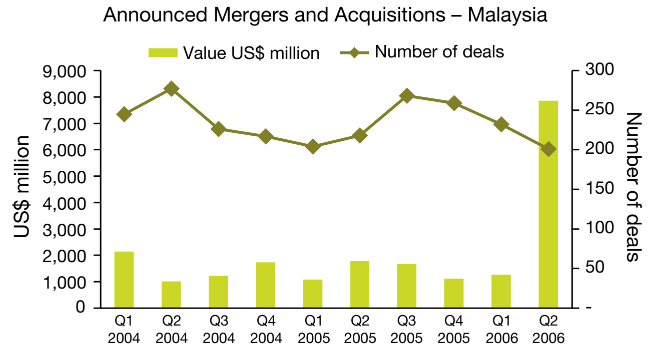
In an effort to control inflation, the central bank, Bank Negara Malaysia, has tightened monetary policy by raising the overnight policy rate (OPR) from 2.7% in November 2005 to 3.5% in April 2006. Consequently, the average bank's base lending rate has also increased to 6.6% from 6.0%, over the same period.

Similar to other regional stock markets, the local bourse has not been spared from the bearish sentiment over concerns on the impact of rising US interest rates and inflation on its economy. The Kuala Lumpur Composite Index started off the year on a high note on the back of strong US growth and semiconductor demand and a strengthening Ringgit against the US dollar. It climbed from 893 points at the start of 2006 to a peak of 967 points in May before sliding back to year start levels by June 2006.

The primary IPO market has eased in the first half of 2006, with only 22 IPOs compared to 39 over a similar period in 2005. In addition, new funds raised from the IPO market dropped to RM540.6 million (US$147.7 million) for the first four months of 2006 compared to RM2.9 billion (US$789.5 million) over a similar period in 2005.

In contrast, the bond market saw a surge in new issues of private debt securities (PDS), which nearly doubled to RM13.3 billion (US$3.6 billion) in the first four months of 2006 compared to RM7.0 billion (US$1.9 billion) over the same period in 2005. The Islamic bonds which took up more than half of the total issuance in 2005 are likely to be sustained in 2006. Meanwhile, outstanding corporate debt securities in the market edged up to RM189.3 billion (US$51 billion) as at end-April 2006.

Deal Activity



Source: Thomson Financial

Malaysia experienced a robust M&A market in the first half of 2006, with transactions worth US$9.1 billion, compared with only US$5.7 billion for the whole of 2005. More than half of the deals involved multi-billion Ringgit transactions (transactions valued around US$270 million or more) such as:

- MMC Corporation proposed acquiring the assets of Malaysia's largest Independent Power Producer, Malakoff, for around US$2.5 billion
- Bumiputra-Commerce Holdings, which controls Malaysia's second largest banking group, acquiring Southern Bank for US$1.8 billion

In terms of geographical direction of Malaysia's M&A, domestic deals (Malaysian firms acquiring Malaysian targets) continued to dominate. An emerging feature of recent deals in Malaysia is privatisations and delistings as reflected by the largest corporate takeover of 2006 - i.e. the MMC Corporation / Malakoff deal. Amongst the factors cited for delistings is major shareholders being able to unlock value not reflected in market pricing.

Further, there is continued growth in "outbound" deals. Significant outbound activity was noted in the telecommunications and financial services sectors. The key macro drivers for outbound growth are the more limited domestic market opportunities and rapid globalisation, which has opened up wider market opportunities.

Since the beginning of 2006, there have been over 60 announced "outbound" deals with a total deal value of around US$2.7 billion. Major foreign acquisitions by Malaysian companies include:

- A joint venture between Indonesia's Lippo Group and Malaysia's Usaha Tegas to acquire a Singaporean property company, Overseas Union Enterprise, for US$1.1 billion
- Public Bank's acquisition of Hong Kong's Asia Commercial Bank for US$589 million

- Telekom Malaysia's acquisition of India's cellular operator Spice Communications for US$180 million
- Genting's acquisition of three Chinese power plants for US$155 million

It is also heartening to note that even small players are going outbound, for example Mesdaq-listed, Green Packet has partnered with one of China's largest telco's, Sichuan Telecom to implement "wireless e-communication" ; and also with notebook makers, BenQ and Lenovo to launch a notebook bundling program in China.

The M&A landscape continues to be dominated by utilities, industrial, real estate and financial services. These sectors alone contributed more than three quarters of the M&A value during the first half of 2006. In fact, each of these sectors are represented in the top five deals of the first half, highlighted above.

Meanwhile, companies such as Petronas will continue to seek market opportunities with the objective of securing new sources of energy and raw materials abroad.

The first half of 2006 saw a significant jump in foreign interest in Malaysian companies, including:

- Daikin Industries' takeover of air-conditioner manufacturer, OYL Industries, for US$2.1 billion
- India's Ballappur Industries and JP Morgan Securities' (Asia-Pacific) joint-acquisition of paper mill, Sabah Forest Industries for US$258 million

In order to boost competitiveness, Malaysian corporates are also seeking technology transfer opportunities, such as Golden Hope's joint-venture unit, Cognis Oleochemical's acquisition of Cognis Deutschland for RM688 million (US$188 million), one of the world's largest producers of fatty acids and more recently its joint venture with Austrian-based biodiesel company, Godiver Handels.

Outlook

The Government anticipates full year growth for 2006 to reach 6.0%, compared to 5.3% in 2005, especially amid strong domestic and external demand in the second half of the year. Economists, however, have projected slightly more conservative growth of 5.0% to 5.5% in 2006, due to the impact of higher petrol and electricity prices, a rise in inflation and interest rates, softening of US economic growth with possible US interest rate hikes, along with sector specific factors such as a weakening in semiconductor demand.

There are prospects of the central bank raising the OPR by 50 basis points over the short term to 4.0% in an effort to combat inflation, which is forecast to be between 3.5% and 4.0% for the whole of 2006. The corporate bond market (PDS) is expected to grow by up to 29% in 2006 on strong funding requirements from the infrastructure sector. Total bond issuances are projected to range between RM35 billion (US$9.6 billion) and RM40 billion (US$10.9 billion). The bulk, or 70%, of issuances are expected to arise from new financings, with 30% from refinancings.

Going forward, there are a number of key factors driving Malaysian M&A. The limited domestic market opportunities and rapid globalisation has opened up wider market opportunities for overseas deals. Continued restructuring of corporate Malaysia, amongst Government-linked companies and PLC's opting for privatisation, with the need to enhance shareholder value in the long term, will also steer corporate M&A plans.

Both the overseas-led M&A and domestic consolidation trends are expected to continue into the next few years. In addition, the drop in the values of listed companies, as a result of current equity market weaknesses, and the gradual strengthening of the Ringgit, will open opportunities for value creation and influence M&A plans.

Sectors likely to dominate Malaysian M&A into the medium term are:

- Automotive and auto-parts
- Financial services
- Oil and gas
- Plantation, oleochemical and biodiesel
- Real estate
- Telecommunication
- Utilities (power)

Meanwhile, countries or regions where corporate Malaysia is looking at expanding into include China, Vietnam, Indonesia, the Indian subcontinent (India, Pakistan and Sri Lanka), and the Middle East. Local companies are attracted by the relatively untapped markets and large population bases of these countries, as well as potential for infrastructure development.

In summary, a combination of domestic consolidation and overseas expansion should make for a very strong year in Malaysian M&A.