

Malaysia

Malaysian outlook looks solid with deal activity mainly driven by cross-border deals in financial services, energy and real estate

Current Environment

Despite global economic uncertainties, Malaysia continued to register healthy economic growth in the early half of 2008, at a faster-than-expected rate of 7.1% in the first quarter compared to 5.1% over the same quarter last year. The increase was fuelled by domestic demand and driven by double-digit expansion in private and public consumption spending of 11.8% and 10.5% respectively, as well as, from strong export growth, particularly commodities such as crude oil and crude palm oil. Growth in the first quarter of 2008 was more broad-based than 2007, led by the services sector which grew at 8.0% followed by manufacturing 6.9%, agriculture 6.3%, construction 5.3% and mining 3.7%.

The rise in private and public consumption and investment was on the back of higher civil service incomes, household and business borrowings and strong tourist arrivals. Total direct investment, both local and foreign, approved by the Government, up to April 2008, nearly doubled to US\$7.4 billion compared to US\$3.8 billion in the same period in 2007, with 69.1% or US\$5 billion (RM16.6 billion) from foreign sources.

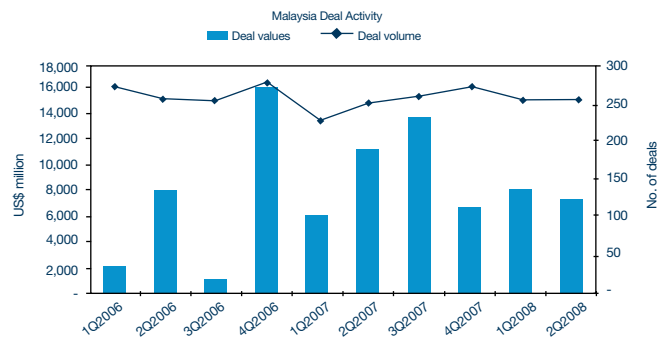
Inflation for the first four months of the year was under control, below 3%. However, with the double-digit increases in fuel prices, Malaysia's inflation rate is expected to rise to around 4% to 6% for 2008. In early June 2008, the Government revised upwards the price of petrol by 41% to RM2.70/litre, while the price of diesel was increased by 63% to RM2.58/litre. The central bank, Bank Negara Malaysia has kept the overnight policy rate unchanged at 3.5% since 2006 in an effort to steady economic growth and domestic demand in light of higher fuel and commodity prices. Nevertheless, the pressure to raise interest rates continues to mount, to curb rising inflation and to strengthen the local currency.

The Malaysian ringgit started the year strongly, appreciating against the US dollar to reach a 10-year high of 3.137 ringgit to the dollar. However, since the middle of April 2008, the dollar has strengthened on expectation that the US Federal Reserve will not cut interest rates further. In June 2008, the ringgit weakened further to 3.266 to the dollar with inflationary concerns, a lacklustre stock market and political uncertainties.

The unexpected outcome of Malaysia's 12th general election in March 2008, which saw the ruling party, Barisan Nasional winning by a slim margin, led to uncertainties in public policy direction. Post-general election, the local stock market, Bursa Malaysia, plunged amid weak local currency sentiment and negative news from the US sub-prime loans and higher global oil prices. This was despite starting the year with a bullish outlook. The benchmark KL Composite Index ("KLCI") reached a new high of 1,516 points in January 2008 due to strong corporate earnings and the performance of the plantations sector with higher crude palm oil prices. The KLCI, however, began to weaken in February in line with the rest of the regional equity markets, and was down to 1,183 at the end of June 2008.

The primary bond market had a good start in 2008, with US\$4.9 billion worth of bonds issued in the first four months of the year driven by investments in the services, construction, and infrastructure and utilities-related sectors. The IPO market performed poorly due to the stock market volatility, making companies rethink their listing plans. In the first four months of the year, only US\$130 million worth of IPOs took place.

Deal Activity



Source: Thomson Reuters, based on total domestic, inbound and outbound deals announced as of 30 June 2008

Over the first half of 2008, Malaysia's domestic M&A market value has declined sharply by 68% to US\$3.5 billion due to a sharp drop in volume and an absence of mega deals. However, cross-border M&A deals have picked up significantly, making up more than two-thirds of M&A deal value. During the same period, total outbound M&A reached US\$11.1 billion, an eight-fold or 816% increase over 2007's and triple of domestic deals of just US\$3.5 billion. The bulk of outbound deals centred on banking, oil and gas and telecommunications sectors.

Outbound activity

Nearly half of outbound M&A was attributed to the banking sector with two of Malaysia's largest banks, Maybank and CIMB, acquiring a total of US\$3.7 billion in foreign banking assets. CIMB plans to acquire 42% of BankThai, Thailand's ninth largest lender, for US\$179 billion. Maybank was particularly active, purchasing the following stakes:

- Bank Internasional Indonesia for US\$2.7 billion, by making a mandatory general offer
- Pakistan's MCB Bank Ltd for US\$673 million
- Vietnam's An Binh Rural Joint-Stock Common Bank for US\$134 million

The oil and gas sector was the second most active outbound M&A sector, dominated by the national oil and gas company Petronas, who acquired stakes in two oil and gas exploration and production companies:

- Gladstone Liquefied Natural Gas Project in Australia for US\$2.5 billion; and



- Cairn India Ltd for US\$628 million, in a joint venture deal with Orient Global Tamarind Fund Pte Ltd

Outbound deals in telecoms were notable too and included:

- TM International acquiring an additional 15% stake in India's Idea Cellular Ltd for US\$1.7 billion; and
- Usaha Tegas purchasing a 35% interest in Sri Lanka Telecom plc for US\$299 million

Other significant outbound M&A deals included:

- KMN Group, a process equipment maker, acquiring 100% of Borsig Bbetv for US\$532 million. Borsig is a leading industrial company in Germany which manufactures boilers, steam turbines and engines
- State investment firm, Khazanah Nasional buying an additional 16% stake in Singapore's healthcare company Parkway Holdings for US\$392 million
- Tasek Corporation acquiring Singapore-based Hong Leong Asia Ltd's building materials business, Island Concrete Pte Ltd for US\$273 million
- Pelikan International Corp acquiring a China-based stationery firm for US\$200 million

Inbound activity

There were also a significant number of announced inbound deals, particularly in financial services and real estate. Major deals in the financial services sector included:

- Abu Dhabi Commercial Bank, the second largest bank in the United Arab Emirates, acquiring a 25% stake in RHB Capital for US\$1.2 billion, the latter controls the fourth largest bank in Malaysia, RHB Bank; and
- OCBC Bank of Singapore made a conditional offer for the remaining shares in insurer PacificMas it does not own, for US\$228 million

In real estate, the significant inbound M&A transactions included:

- Kuwait Finance House planning to acquire Menara YNH, an office tower block in Kuala Lumpur, for US\$281 million
- Singapore-based CapitaLand has bought 62% of the retail area at Sungei Wang Plaza, a major retail centre in Kuala Lumpur, for US\$185 million
- Abu Dhabi-Kuwait-Malaysia Investment Corp taking a 37% stake in UBG Bhd, a property holding company, for US\$141 million
- Germany-based Union Investment Real Estate AG to purchase Capital Square Office Tower 2 for US\$136 million

Domestic M&A and Others

The domestic M&A scene during the first half of 2008 was relatively quiet, with few major deals. Among the notable deals are the restructuring of government linked companies ("GLC") and government investment linked companies' ("GILC") foreign assets. Among them:

- Khazanah Nasional and Bumiputra-Commerce Holdings Bhd announced plans to merge the two Indonesian banks that they own (PT Bank Niaga Tbk and PT Bank Lippo Tbk) worth US\$2.7 billion
- Khazanah Nasional selling its telecommunication stake in Indonesia-based PT Excelcomindo Pratama and Singapore's MobileOne Ltd to TM International for more than US\$800 million

Another key domestic deal involves the national shipping company MISC's reverse takeover of Ramunia Holdings, an oil and gas services company, by selling its manufacturing business, Malaysia Marine and Heavy Engineering. The deal is estimated at US\$1 billion.

Outlook

The Malaysian economy in the second half of 2008 is expected to remain resilient despite the mixed global economic outlook and higher oil prices. Growth is expected to be supported by sustained domestic demand reinforced by expanding intra-regional trade, with forecast economic growth of 5-6% for the whole of 2008.

Going forward, in the second half of 2008, market conditions remain favourable for M&A. Stable economic fundamentals with reasonable growth especially from the domestic sector, coupled with higher but controlled inflation, will provide impetus not only for local but foreign companies to continue to invest in Malaysia. In addition, current low market valuations, liquidity and low interest rates will provide opportunities for takeovers or transactions taking companies private. Outbound deals will feature more among investment companies like Hong Leong Group, Usaha Tegas and Khazanah Nasional, as well as other GLCs looking for potential opportunities to invest overseas.

M&A will remain strong in the financial services, oil and gas and related services, real estate and industrial sectors. In financial services, for example, RHB Capital is looking both for potential strategic investors and acquisition targets. In the oil and gas sector, the potential for oil prices to continue their upward climb will continue to fuel investment in oil and gas by Petronas and other upstream services companies. Within the real estate sector, Malaysia's well-developed infrastructure and its relatively cheaper pricing versus other cities in the region provide attractive investment opportunities for foreign investors, particularly for quality high-end properties.