

03/09/1997

Economies of scale a major factor in Petronas move

Francis C. Nantha

PETRONAS, which is seldom seen as a major corporate player, now has the local corporate scene abuzz with its surprise move in buying the 29.3 per cent stake in Malaysia International Shipping Corporation Bhd.

Most of the discussions revolve around three key issues:

Why did the Government-owned oil giant buy into the privatised strategic national shipping firm?

What can it do to improve MISC's global expansion plans?

And where does this deal leave Konsortium Perkapalan Bhd, which initiated the original proposals to buy the MISC stake?

To the first question, the answer is simple - Petronas wanted more control of shipping operations involving its petroleum products, since MISC was one of its main contractors.

MISC's LNG tankers were on charter to its subsidiary, Malaysia LNG Sdn Bhd, to transport LNG to customers in Japan.

Petronas, through its wholly-owned subsidiary, Petronas Tankers Sdn Bhd, is also the owner and operator of LNG tankers - thus the purchase of the MISC stake would allow for rationalisation of this business activity.

In getting the largest share block in MISC, Petronas now effectively controls how its products are shipped around the world and will also be able to conduct rationalisation activities so as to achieve economies of scale.

This now brings us to the next issue - what can Petronas do to beef up MISC's operations?

Given its history, and the successful management principles that has built up Petronas to its present form, it is only natural that the company should apply its successful formula to another national strategic interest.

And this move to beef up MISC's operations has become even more imperative today in view of the recent currency turmoil and its possible impact on the economy.

At a glance, one should note that the ringgit is now at its lowest value since 1973, falling to a low of RM2.96 against the US dollar last Friday before closing at RM2.88.

This represents a drop of over 15 per cent since June this year, and the impact on exports is significant as most of the shipping costs is still calculated in US dollars.

Despite the lower ringgit expecting to boost Malaysian exports, Prime Minister Datuk Seri Dr Mahathir Mohamad has admitted that the currency's lower value will have an impact on our overall economy.

He said over the weekend that the economic growth will still be achieved at the eight per cent target, but only in ringgit terms.

In terms of other currencies, our economic growth may be seen to be lower.

On another front, shipping and related costs like insurance also make up a significant portion of fund outflow which has resulted in a services account deficit contributing to overall trade deficit.

While other efforts are being undertaken on the insurance industry angle, MISC represents the flagship of the nation's efforts to reduce outflow of funds to pay for shipping charges.

The key aspect that has to be looked into by MISC is to increase the number of vessels it operates - which now numbers 65 vessels with a total

dead weight of 2.42 million tonnes.

This costs money, and Petronas is undoubtedly in a very good position to assist in terms of capital infusion.

And, as a firm familiar with capital intensive-ventures with long gestation periods, it is not going to demand immediate results from MISC.

Also, Petronas is very much a firm with a global outlook, seeking out potential new oil-rich areas to ensure its petroleum reserves can be maintained as long as possible.

The shipping business is very much similar, as are some of the main players - namely the port authorities and freight forwarders.

As such, it is easy for Petronas to leverage off its partnerships and experiences to persuade more customers around the world to use MISC's services.

Even so, Petronas has to acknowledge that there is only so much it can achieve by itself and its existing partners.

And this brings us to the third issue of why Petronas has agreed to work with Konsortium Perkapalan - which is otherwise seen as a competitor who had previously tried to gain control of the 29.3 per cent stake in MISC.

In a global environment where everyone is both a competitor and a partner, there are obvious synergies that can be gained from Petronas working with Konsortium Perkapalan both locally and abroad.

Konsortium Perkapalan is essentially in the same business as MISC, although it has less ships than the latter.

Many are widely expecting Petronas to eventually dispose of its MISC stake in Konsortium Perkapalan, which in turn is expected to merge MISC with its shipping arm Diperdana Corporation Bhd.

While this is a logical conclusion to draw, a more likely scenario is that of strategic partnerships being forged so that both firms can effectively pool resources while still being separate to handle their individual strategies.

After all, Petronas still has its LNG and petroleum products shipments to consider and it is unlikely to give up control of this strategic interest.

Perhaps what may need to be done is to hive off this LNG business from MISC and sell the rest to Konsortium Perkapalan.

In so doing, both firms stand to gain.

Petronas gets to realise value for its MISC stake buy and yet keep its strategic LNG shipping business.

Konsortium Perkapalan gets to merge MISC with Diperdana Corporation and gain economies of scale, even if it has to pay the same sum for slightly lesser assets.

And the originally MISC stakeholder, Kumpulan Wang Amanah Pencen, should be able to stand quietly at the sidelines and realise the full potential of its investment by possibly getting blue-chip Petronas Gas shares - with a higher dividend receipt and a huge potential for capital gain.

After all, despite no announcements of the price KWAP paid for the MISC shares three years ago, there is no doubt that the share prices had dropped from 9.35 then to less than RM6 since.

Such a scenario is not likely to happen to Petronas Gas, which has so far been able to weather the recent downfall in the stock market.

(END)