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Sentimental ties

TAN Sri Frank Tsao Wen King has a strong streak of sentiment when it comes to shipping. His affection is especially pronounced in the case of Malaysian International Shipping Corporation (MISC).

Currently, Tsao owns 2.3 per cent in MISC, a bloc acquired in1968. The passion for shipping that runs in his blood means that he has little intention of surrendering his MISC stake, although fellow MISC compatriot Robert Kuok - Malaysia's very own sugar king - sold out a long time ago.

Muses Tsao, `I'm a shipping man. Today, I own 23 million shares. At today's (Oct 12, 1997) price, it's worth roughly RM150 million. To an individual, it's an astronomical sum. But to a shipowner, it's not that significant.'

Exactly how did Tsao get into MISC? For the answer, dredge up ancient history. As Tsao recalls, the Japanese government awarded a sizeable sum of money to its Malaysian counterpart. The moolah was a goodwill gesture. In return, Malaysia would abandon its compensation claims for Japanese brutality during World War Two.

Malaysia decided to use the money to buy ships. But there was a problem. There was excessive Japanese cash for one ship but far too little for two ships.

Tsao's solution? 'After negotiating with the shipbuilders, we got two ships by paying cash outright instead of paying on an instalment basis,' says the genial, gracious Tsao who is now chairman of IMC Group of Companies, a Hong Kong-based mega shipping empire.

His coup was rewarded with a stake in MISC. Today, Tsao is one of the 20 largest shareholders in MISC.

By virtue of his privately-held stake, Tsao has remained deputy chairman of MISC since the shipping firm's inception. He's seen - and done - a lot. For instance, Tsao and Tan Sri Rama Iyer actually researched different international maritime laws to create Malaysia's own set of maritime laws. The headache: everything had to be translated into Bahasa Malaysia. `That alone took two years,' sighs Tsao.

Throughout Tsao's tenure at MISC, there have been various changes at board level. Former chairman Raja Tan Sri Muhammad Alias Raja Muhammad Ali and managing director Ariffin Alias were the latest to leave when Petronas recently bought out Kumpulan Wang Amanah Pencen's 29.4 per cent stake in MISC at an undisclosed price. Today, Petronas president and chief executive officer Tan Sri Mohamad Hassan Marican is ensconced as chairman of the national flagbearer while Petronas vice-president for marketing Datuk Mohamed Ali Yasin is managing director.

Will the infusion of new oil-based brains revive MISC? The national shipping company has often been labelled a government company labouring under stifling layers of bureaucracy. Says an observer, `It's top-heavy.' Thus, the Petronas invasion may inject a more fluid and relaxed corporate style. But detractors point out that Petronas itself is a statutory body. On top of that, being oilmen, the new directors may have little expertise in shipping.

Of course, the Petronas conundrum may not exist in future if the heavily-rumoured purchase of Petronas' MISC bloc or certain of its businesses by Konsortium Perkapalan Bhd (KPB) actually materialises. Says an analyst, `That option is still open. Many believe Petronas may be holding the MISC stake for a third party.' Alternatively, the appointment of Petronas' Hassan Merican and Ali Yasin indicates that Petronas isn't letting go of MISC.

Nevertheless, some quarters would have preferred KPB's Mirzan Mahathir at MISC's helm because it would have been `quite refreshing'. `KPB people are quite young, they would have brought in corporate experience,' says the analyst. But despite the prevailing `government mindset' at MISC, there's no escaping the fact that the company is still basically in good shape. Nevertheless, earnings growth has been slow, bogged down by two years of weak industry freight rates in a very competitive industry.

MISC's saving grace is actually its liquefied natural gas (LNG) division, which currently contributes 75 per cent of earnings. This substantial fixed income stream is sourced from a long-term contract with Petronas to ferry the latter's LNG until the year 2005. Whether MISC will retain the Petronas contract or not remains open to speculation. Says an analyst, `The uncertainty about the renewal of the contract means that I'm not willing to call a buy on MISC at this point.' In addition, any renewal may not feature rates as favourable as in the existing contract, since MISC's five LNG tankers are old.

But there shouldn't be a drastic change in MISC's earnings even if the new charter contracts aren't as lucrative as before. For the year ended Dec 31, 1996, the LNG division contributed RM379.9 million to pre-tax profits of RM506.5 million. LNG should bring in about RM400 million of 1997's estimated pre-tax of RM551.7 million.

Since its LNG tankers are old and fully depreciated, MISC's depreciation expenses are minimal. But can the tankers be used for a long time more? The residual life of the tankers is unpredictable because it depends on how the company treats its ships. MISC apparently has a programme where it refurbishes and drydocks its ships for repair.

Notably, Petronas has also attempted to control its own freight costs by purchasing its own LNG tankers. As of May 1997, Petronas had five LNG tankers. Technically, says an analyst, `Petronas doesn't have to renew the LNG contract with MISC.' And it would be easy for Petronas to become entirely self-sufficient in LNG freight. Being very cash-rich, Petronas could just buy another five tankers - the last French-built tanker that was delivered in May 1997 cost RM800 million - and depreciate them very fast.

But there are also other more palatable alternatives for MISC versus complete independence in LNG freighting on Petronas' part. For instance, Petronas could hive off its LNG freight division and merge it with MISC's LNG subsidiary. Says the analyst, `In such a scenario, MISC would look very strong.'

But in Tsao's opinion, exactly what kind of shape is MISC actually in? Says Tsao, `MISC is quite healthy financially. It has lots of assets.' Says an analyst, `In fact, MISC would be an attractive addition to any stable of companies. Any company that takes in MISC will improve its balance sheet.' Although it's not exactly cash-rich - as at December 1996, it had RM220.7 million cash in hand - gearing is pretty minimal for a shipping company. But bear in mind, says the analyst, that `MISC will be using its cash for a programme of buying and selling ships'. Long-term loans were RM103.5 million as at Dec 31, 1996. Cashflow is okay with debt collection within 35 days while creditors are paid after a three-month cycle.

MISC is also attractive in the sense that it's undervalued. Most of MISC's assets haven't been marked to market value, says Tsao. For instance, the MISC land and building is still believed to be booked at cost.

Theoretically, a possible asset revaluation exercise at MISC would make the company very attractive to potential highly-geared raiders. Asset revaluations would enable potential gearing at MISC to be pumped up. In the event of a takeover, the raider's assets could be transferred to MISC. MISC would then pay cash for the new assets, either from existing reserves or via a new gearing exercise.

And MISC is quite cheap, in tune with the downdraft in the rest of the market. Based on its Nov 6 price of RM6.10, MISC is currently trading at a historic price earnings multiple of 12.8 times FY1996 earnings and a prospective 11.75 times FY1997 earnings. At market price, Petronas' MISC bloc would sell for less than RM2 billion.

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