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A tale of two choices

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AFTER months of mulling it over, the board of Cahya Mata Sarawak Bhd (CMSB) was finally confronted with a stark situation - merge its subsidiary Utama Banking Group Bhd (UBG) with the RHB Group or risk losing its banking licence.

The seemingly plain and simple alternatives belie the deep repercussions the group could face - both financially and stature-wise - should it choose either.

Contrary to reports that the CMSB board was split on the merger proposal, a source says the directors were unanimous in opposing it.

'A vote was taken a few months ago and all directors were against the deal. If it was less than RM4 per share, the deal would have been inked a long time ago,' says the source. 'Also, it is not a straightforward marriage of two parties. In this case, we have to court the grandmother, then the mother, before marrying the daughter.'

The source was referring to the complex structure of the RHB Group. Its ultimate holding company is RHB Bhd which holds 51 per cent of RHB Capital Bhd, its financial arm. RHB Capital in turn owns 70 per cent of RHB Bank, with the remainder held by Khazanah Nasional Bhd. RHB Capital also owns 51 per cent of RHB Merchant Bankers Bhd.

The deal between the Sarawak-based bank and RHB has been on the cards since May last year. However, both parties could not agree on a price and negotiations were aborted. It is learnt RHB had even notified the authorities of the stalemate and was looking at a merger with Bumiputra-Commerce Bank (BCB).

The turning point was the statement by Prime Minister Datuk Seri Dr Mahathir Mohamad, who is also Finance Minister, that UBG could lose its banking licence if it failed to merge by end-June. Within days, UBG and RHB were back at the negotiating table.

'There wasn't much of a choice,' says a source close to the CMSB board. 'The CMSB board would rather go ahead with the merger, even at RM6 per share, than risk losing its banking licence.'

At time of writing, there was no news from either UBG or RHB on the status of their renewed talks. It is learnt that an announcement will be made after a due diligence audit. The CMSB board, say sources, has appointed a few directors to look into the due diligence of some critical operations of the RHB Group.

CMSB may be a reluctant predator. Some feel its reason for going ahead with the acquisition of RHB is to keep the Sarawak flag flying in the domestic banking sector. But at what cost?

The deal is speculated to be a two-step procedure. In the first phase, UBG would buy Malaysian Resources Corporation Bhd's 22.6 per cent in RHB Bhd at RM4.50 per share. The cost is estimated at RM520 million. The second phase would involve UBG acquiring the stakes of RHB founder Tan Sri Rashid Hussain in RHB Bhd and RHB Merchant Bankers. Sources do not discount the possibility of RHB Capital subsequently being delisted.

The deal with Rashid for RHB Bhd could involve cash or a share swap. However, the RHB Merchant Bankers acquisition would likely be a cash deal. The price being bandied about is RM4 per share, but sources say this would be subject to due diligence. At RM4, it would cost UBG about RM380 million. In total, UBG and its parent company are staring at raising some RM900 million in cash.

At 51 per cent, RHB Capital is the biggest shareholder in RHB Merchant Bankers. Rashid is next with 20 per cent via Panduan Cekal Sdn Bhd.

However, say sources, Rashid is not likely to walk from the deal a wealthy man. 'But he should have enough to settle his personal liabilities, with some leftover,' they say.

As for RHB Bank, it has firmly entrenched itself as the third largest in the country. But whether it will have strong shareholders in the new entity is another question.

UBG is 51.8 per cent-owned by CMSB, a company linked to the family of Sarawak Chief Minister Tan Sri Taib Mahmud. Its biggest shareholder is Taib's brother Datuk Onn Mahmud. Taib's two sons own more than nine per cent each and they sit on the CMSB board.

Last December, CMSB redeemed a RM350 million bond issue via borrowings - RM175 million from financial institutions and RM175 million from wholly-owned subsidiary CMS Cement Sdn Bhd.

'Financially, CMSB is not in a strong position,' says an analyst. 'Raising money for the RHB deal may not be a problem for CMSB considering its strong position in Sarawak, but the larger issue is whether it would be worth the effort. Can CMSB recoup its investments?'

CMSB also has to convince Khazanah Nasional of its future plans. Khazanah is said to be not keen on a share swap; it wants cash, an option that may force UBG to dig deeper into its pockets.

Sources say one of the main fears of the CMSB board is that returns from investments in the bank may not be enough to repay borrowings.

Rashid established the RHB Group when banking licences fetched a huge premium. He paid more than three times book value for Kwong Yik Bank that was later merged with Development & Commercial Bank to form RHB Bank. He later managed to average down his cost in Kwong Yik Bank by paying a much smaller price for Sime Bank. But the burden of expanding at a high cost was telling.

UBG and CMSB are looking at expanding through borrowings. The fear is that if the risk and returns are not properly managed, the result may prove to be far more expensive than the present cost of becoming an anchor bank.

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