

Decision time for Proton

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A decision on Proton Holdings Bhd's future partner will most likely be announced towards the end of this month, sources say. Although the market was rife with rumour last Friday that German automaker Volkswagen AG had inked a deal to acquire a substantial stake in Proton's manufacturing division, sources close to the national car-maker have denied this.

Instead, it is believed that VW may actually not be the partner of choice for Proton, as far as policy-makers are concerned, sources add.

In any case, what has become painfully apparent is that Proton is

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VW keen on various Proton divisions

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in rather dire need of assistance — not so much because of its dismal results in the first quarter (1Q) of financial year 2006 but because of its obvious operational challenges.

For instance, in 1QFY2006, unit sales were 36,959, which shows a 6.5% decline quarter-on-quarter. This is of particular interest because previously it has often been pointed out that Proton's actual unit sales were increasing even though its market share was decreasing.

Meanwhile, Proton's latest offering, the 1.2-litre Savvy, has since its April launch, received bookings of just 5,500 units, when this was the model touted to help boost flagging market share. Which brings us to the national car's steadily declining market share. In June, Proton had a 36.6% market share when five years ago it was 63.4%.

What is most worrying about the whole saga has to be the fact that there is simply no easy way out of Proton's dilemma — discounting, of course, the obvious answer of selling out to a foreigner.

This brings us to a statement issued by Proton late last Friday entitled "Proton is committed to do better".

Reference was made in this statement to the difficult operating environment and plans were outlined to improve efficiencies at various levels. More interestingly, it said: "... It is also recognised that where advances to group companies were perhaps necessary in the past periods, their recovery may be arduous given their current financial state."

This was no doubt an oblique reference to

provisions of some RM136.5 million, RM91 million of which was for "doubtful debts" and RM45.5 million was for "allowances for doubtful debts for amount due from/advances to a jointly controlled entity".

What would be of interest to shareholders would be the names of the "group companies" the advances were made to and just what their "current financial states" are. What would also be of interest would be a comprehensive and more transparent explanation.

In the meantime, expectations are that Proton's 1QFY2006 net loss of RM12.3 million should not be repeated, unless the "current financial states" of "group companies" deteriorate further of course. Having said that, neither does any analyst contacted by *The Edge* expect a strong showing from Proton any time soon — barring a complete overhaul of its model plan, cost structures, product quality assessment and perception issues.

But Proton does not have the luxury of time on its side to implement the "various initiatives" announced last Friday to "mitigate the current difficult market environment".

"As far as the initiatives are concerned, they are no different from what there was before," notes Steven Tan of CIMB Research. Other analysts agree.

"Let's hope there is more than just this. Or we are looking at a company which could fail," adds a foreign analyst.

The VW situation

Meanwhile, the situation between Proton and VW remains somewhat murky, with sources on both sides of the divide saying they are uncertain of the status of discussions.

A source in Germany says there was an "end August" deadline for a final decision on whether or not the national carmaker intends to forge a strategic relationship with VW.

However, it is understood that VW is still waiting for an official response from Khazanah Nasional Bhd or Proton, neither of which has been forthcoming as at press time. Khazanah holds a 42.7% stake in Proton. The Edge had also reported earlier that conglomerate Sime Darby Bhd may be eyeing a stake in Proton, which of course raises new questions as to any role VW could play.

"We hear rumours but have yet to get anything official," the source says. "This is not really positive," he adds. "But now things are a bit mixed up with the CEO leaving."

With the exit of Tengku Tan Sri Mahaleel Ariff from Proton, the day-to-day operations have come under the auspices of joint chief operating officers Datuk Kamarulzaman Darus and Datuk Kisai Rahmat. The two COOs are also members of a management committee headed by Proton chairman Datuk Azlan Hashim. Azlan himself has taken on a more active role in the running of the company.

According to the source, VW will remain firm on certain conditions which it has laid down, such as management control and substantial equity participation, no surprise really considering its past track record.

"VW is in the automotive business and we want access to the Asean market. We want a production facility and would like an additional brand to add to our stable. Proton would fit this requirement," the source says.

For Proton of course, this could translate to an almost instant export market.

VW is keen on Proton's manufacturing, marketing and engineering divisions. It is believed that Proton's UK subsidiary Lotus would also be of interest because of its development capacity and competency.

Meanwhile, unlike existing business models in the local auto industry, the source says VW will not churn out cars rebadged as Protons. Instead, "We intend to jointly produce cars with Proton, which would have its own design and identity. There may be one or two models that will be rebadged but that is not our overall strategy. We will use our global scale so platforms and components may be the same, but otherwise Proton will still be Proton", the source adds.

This would not be dissimilar to how VW worked with Czech carmaker Skoda.

"We invested in Skoda in 1990 and it had three products in one segment. It produced 170,000 cars and exported 35% of its volume. In 2005, it has eight products, with the ninth in preparation for launch, it produces in several other countries besides Czechoslovakia, and it produces 490,000 cars a year and exports 85% of volume," the source says.

"The Skoda brand is getting stronger. We would treat Proton the same way."

As for Proton's vendors, the source says VW intends to "try and develop the vendors" to international standards and also to try to get them into its global sourcing systems.

"But we will not directly invest into the industry," he clarifies. ■