POWER GAME

Will MMC Corporation, under the stewardship of Tan Sri Syed Mokhtar Albukhary, succeed in acquiring Malakoff and consolidate its power assets in the process?

By Gurmeet Kaur

WILL Malaysian tycoon Tan Sri Syed Mokhtar Albukhary succeed in convincing the shareholders of Malakoff Bhd to let go of the assets of their power company at RM10.35 per share? If they do so, this deal would pave the way for a consolidation of Syed Mokthar's power assets under his flagship company MMC Corporation Bhd.

To recap, MMC is proposing to acquire all of Malakoff's assets and undertakings for RM9.3 billion, less the cash balance in Malakoff. The deal is set to be Malaysia's biggest-ever corporate takeover to date, eclipsing Bumiputra-Commerce Holdings Bhd's RM6.7 billion purchase of Southern Bank Bhd in March.

Syed Mokhtar: Consolidating his power assets

If this deal goes through, Malakoff would have to pay out RM10.35 per share to its shareholders and be de-listed in 2007.

MMC is carrying out the acquisition via a special purpose vehicle (SPV), a wholly owned unit called Nucleus Avenue Sdn Bhd. It is understood that the usage of this SPV (and not MMC per se) is to ensure that borrowings largely remain without recourse to the holding company level.

The cleverness of the deal is not lost. By acquiring Malakoff's assets instead of its shares, MMC only needs a simple majority (ie, 50% plus one share) from Malakoff's minority shareholders to acquire Malakoff's business. If MMC had proposed a mandatory general offer for Malakoff shares at RM10.35 per share, MMC would have needed 90% approval from its minority shareholders to take Malakoff private, which analysts say is unlikely to be achieved.

To finance the deal, Nucleus plans to obtain loans using Malakoff's annual cash flow as collateral. Malakoff's cash flow is estimated to be between RM1.2 billion and RM1.7 billion.

MMC is the single largest shareholder in Malakoff with a 22% stake. So, MMC only needs approval from half of the 78% of stock it does not already own.

Malakoff's other major shareholders include United Kingdom-listed International Power Plc, with an 18.1% stake and the Employees' Provident Fund Board (EPF) with about 10.5%.

International Power has in principal

FACT FILE
MMC CORPORATION BHD

PAID-UP CAPITAL

RM1.52 billion

BOARD OF DIRECTORS

Datuk Syed Abdul Jabbar Syed Hassan (chairman)
Datuk Ismail Shahudin (group chief executive)
Tan Sri Thong Yaw Hong
Tan Sri Dr Abdul Khalid Sahan
Tan Sri Dr Wan Abdul Rahman Wan Yaacob
Datuk Hilmi Mohd Noor
Datuk Abdullah Mohd Yusof
Datuk Dr Ahmad Zaidee Laidin
Encik Halim Din
Encik Feizal Ali
Datuk Mohd Sidik Shaik Osman

HIGHEST-PAID DIRECTOR

RM700,000-RM750,000

SUBSTANTIAL SHAREHOLDERS

Seaport Terminal (Johor) Sdn Bhd	- 40.09%
Skim Amanah Saham Bumiputra	- 33.43%
EPF	- 6.44%

LATEST RESULTS

Net profit of RM380.9 million for the financial year ended Dec 31, 2005 given its support to the deal. But analysts say, this is not necessarily an indication of how other Malakoff shareholders are going to vote on the deal.

This is because International Power had bought into Malakoff in the 1990s for exposure into the then-expanding Malaysian power sector. But the power sector in Malaysia is a different story today. National power company Tenaga Nasional Bhd (TNB) has a 42% reserve margin of power generation, indicating an oversupply situation.

More importantly, players like Malakoff are bidding for projects on the international scene and in some cases are competing with International Power for the deals.

International Power will likely want to use the proceeds from exiting Malakoff for its (International Power's) other newer overseas investments.

But the story is different with the other funds such as EPF, which have invested in Malakoff for its dividend yield. Such funds are believed to have invested in Malakoff at a much lower cost than the RM10 level that it is trading at now. A year ago, Malakoff was around RM6 per share, and at that entry level, the stock offered an attractive dividend yield of around 5%.

But analysts reckon that there is a high likelihood that the EPF would also vote in favour of the MMC-Malakoff deal. 'Recall that the EPF has been largely supportive of Syed Mokhtar's proposals of late such as MMC's acquisition of Johor Port where they were also the second largest shareholder,' notes a head of research at a local stock-broking company.

Another reason why EPF and other funds which are shareholders of Malakoff could vote in favour of the deal is that MMC may invite financial investors to acquire part of the SPV. This way, it will realise some cash and also not burden the books of MMC with Malakoff's debts of RM10 billion.

The acquisition is likely to make MMC a more interesting stock for institutional investors. At the moment, MMC is off the radar screens of investors, despite efforts by management to transform it from a sleepy mining company into a thriving infrastructure play in the last five years. Investors prefer stocks such as Malakoff for its direct exposure to the power generation business.

'By closing the direct route to Malakoff, MMC could emerge as the close substitute. The proposal is a clever way for MMC to increase its exposure in Malakoff without additional strain on its already debt-laden balance sheet,' points out an analyst with a foreign-based research house. As a subsidiary, Malakoff's cash flow will go straight back to the MMC group.

The purchase of Malakoff's assets is also expected to boost MMC's earnings in the long run by giving it complete ownership of the source of about 41% of its pre-tax profit.

Malakoff is Malaysia's 17th biggest company by market capitalisation with a market value of RM8.8 billion, and is the country's largest independent power producer (IPP). It expects the first phase of its Tanjong Bin 2,100-megawatt coal-fired power plant – the largest in the country — to begin output in August.

The power utility also owns stakes in five power plants, located along the West Coast of Peninsular Malaysia. They include Kapar Power Station in Selangor. Analysts note that Malakoff's generation capacity will jump 64% to more than 5,000 megawatts next year after the completion of the Tanjung Bin plant, accounting for a quarter of the country's total capacity.

Interestingly though, the MMC-Malakoff deal comes at a time when the Malaysian government is asking IPPs, such as Malakoff, to renegotiate power-purchase agreements with the heavily indebted TNB. Power plants in the country sell their electricity to TNB.

This in turn has led some observers to question the timing of the MMC-Malakoff deal. Why not wait until the details of the re-negotiation with TNB are finalised? But as other market players point out, these are issues which Syed Mokhtar has already factored in before making this bid.

Hence, is it not surprising that some analysts think that the RM10.35/share offer, which is at a 5.7% premium to its market price, is unattractive. 'Malakoff's intrinsic value is worth much more than the RM10.35/share offer price. We value the stock at RM10.90/share based on an RNAV valuation,' notes Kuala Lumpur City Securities in a report.

However, this has to be offset with the uncertainty surrounding the renegotiation of power-purchase agreements between IPPs like Malakoff and TNB, points out another analyst.

Like Tanjong Plc's privatisation of Powertek in 2004, Malakoff's IPP assets will ultimately form a core energy division within MMC forming a third leg to the existing transportation/logistics and engineering/construction divisions.

Other assets held by MMC include Tronoh Consolidated Bhd, which helps build power stations, and Pelabuhan Tanjong Pelepas, a container port set up to rival Singapore's PSA Corp.

And to bring its debt at the holding company level to a more manageable level, MMC intends to dispose of some of its non-core assets. Assets that have been earmarked for sale include 41 million shares in Sime Darby, 22.5 million shares in Malaysian Smelting Corporation and shares in listed Kramat Tin and Integrated Rubber Corporation Bhd. These shares have a combined market value of RM400 million.

For the immediate term though, not unlike Tanjong and its Tropical Island project, issues elsewhere within the MMC group such as concerns of the ongoing asset restructuring of Syed Mokhtar's companies may undermine the defensive value of the power assets, analysts say. mb

FACT FILE

MALAKOFF BHD

PAID-UP CAPITAL

RM878 million

BOARD OF DIRECTORS

Tan Sri Abdul Halim Ali (chairman)
Ahmad Jauhari Yahya (managing director)
Tan Sri Nuraizah Abdul Hamid
Datuk Abdul Aziz Abdul Rahim
Datuk Ismail Shahudin
Abdul Jabbar Abdul Majid
Azizan Mohd Noor
Vincent Richard Harris
Georgina Seeley

HIGHEST-PAID DIRECTOR

RM1,150,001-RM1,200,000

SUBSTANTIAL SHAREHOLDERS

MMC Corp	- 22.11%
International Power Holdings Limited	- 18.06%
EPF	- 10.5%

LATEST RESULTS

Net profit of RM126.67 million for the first quarter ended Nov 30, 2005