INVEST KL
MALAYSIA

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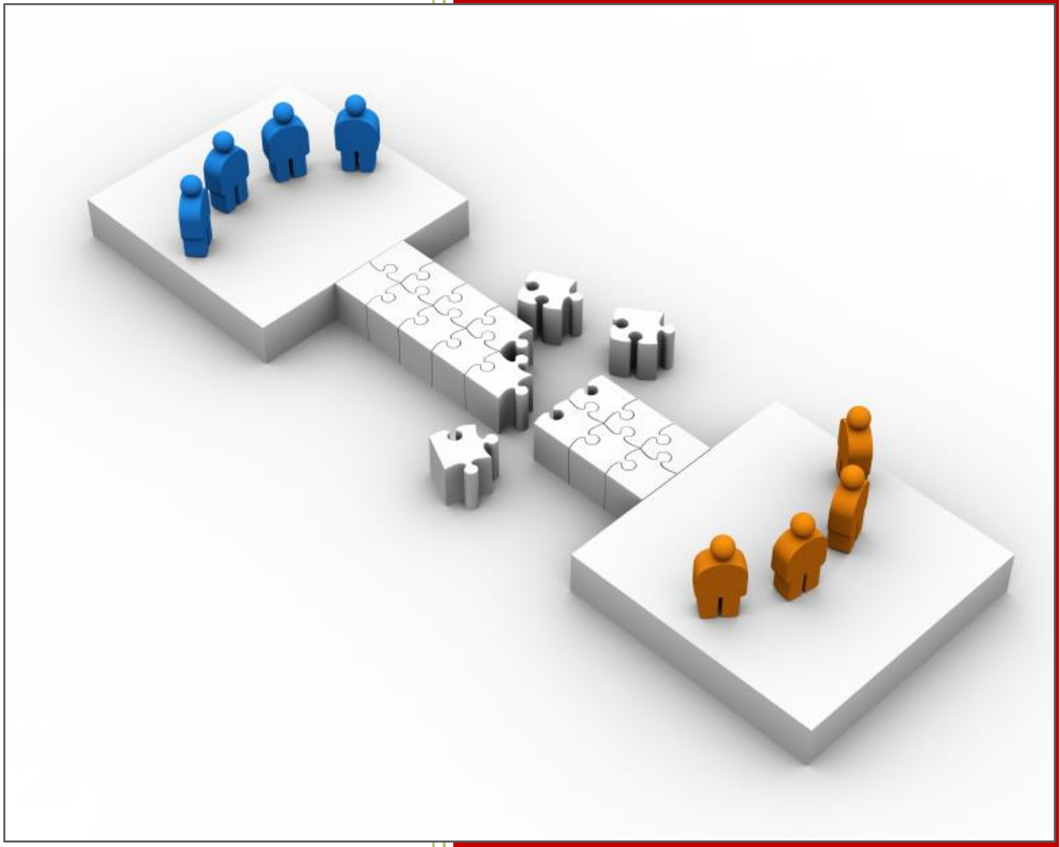
Value Creation through Mergers and Acquisitions



PREFACE

The globalisation of businesses has induced a search for competitive advantage that is worldwide in scale. In a rapidly consolidating global economy, the pressure of globalisation has spurred an increase in cross-border M&A activities. This has become a fundamental characteristic of the business landscape now, with Malaysia proving no exception.

FINANCING THE ASIA PACIFIC'S GROWTH

Merger and acquisition (M&A) is one avenue toward restructuring success, stimulated by a range of strategic factors. These include domestic competition, growing pressure on operational and capital efficiency, and delivering bottom line growth – especially growth in value for shareholders. Since organic growth is hard to come by when the rates of projected economic expansion are low in most markets and sectors, many firms, both large and small, have undergone M&A exercises in order to remain competitive against the onslaught of global conglomerates.

The worldwide M&A transactions have reached unprecedented levels over the past few years, powered by a triple-digit percentage increase in the number of deals over US$10 billion, totalling US$4.7 trillion during 2015. As domestic competition heats up and globalisation opens new doors, some firms go further with acquisitions by carrying them out across national borders. Cross border M&A activity totalled US$1.6 trillion in 2015; accounting for one-third of overall M&A volume and a 27% increase over 2014 levels (see figure 1).

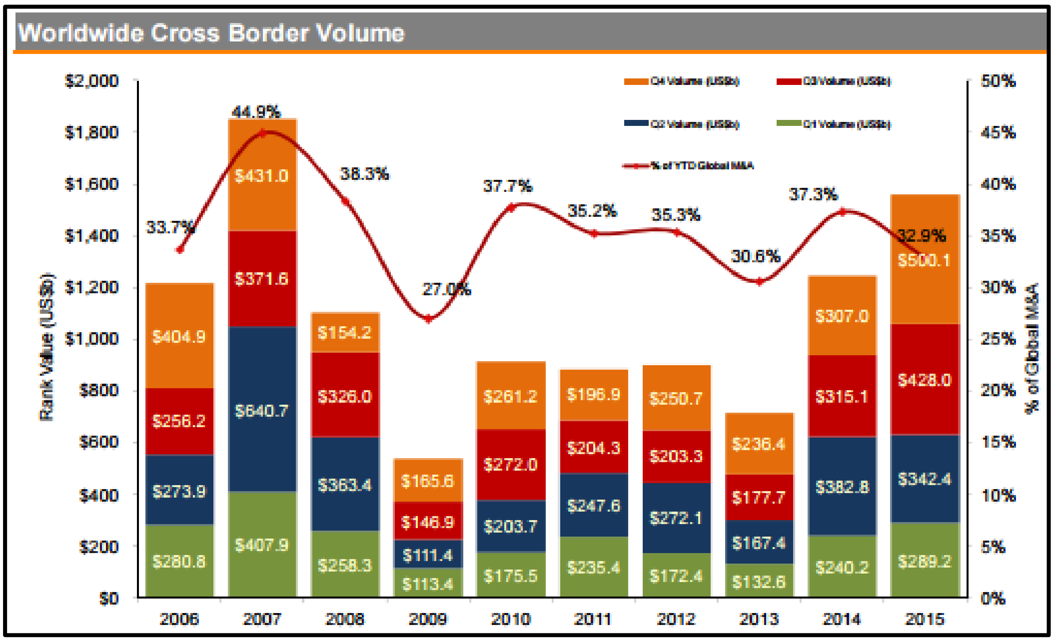


Figure 1: Worldwide Cross Border Volume
Source: Thomson Reuters

M&A activity involving Asia Pacific companies has been particularly robust. The competitive landscape in Asia - rapid economic growth, technological change, enormous rise in consumption demand - allows companies to leverage on Asia Pacific region as a growth driver. In 2015, M&A activity in Asia Pacific (ex-Japan) hit the trillion dollar mark for the first time in history, with US$1.143 trillion, a 63% increase over the US$702.4 billion recorded last year (see Figure 2).

The increase in deal making is broad-based across sectors and industries, propelled by three global trends: hot high-tech markets, companies seeking to adapt to a new normal in their sector or industry, and consolidation along with the hunt for innovation. The majority of activities involving Asian companies targeted the Industrials sector, followed by High Technology and Financials (see Figure 3).

Scorecard: Worldwide Announced M&A — Jan 1 - Dec 31

Target Region/Nation	1/1/2015 - 12/31/2015 Rank Val US$m	1/1/2015 - 12/31/2015 No. Deals	1/1/2014 - 12/31/2014 Rank Val US$m	1/1/2014 - 12/31/2014 No. Deals	% Change in Rank Value
Worldwide	**4,747,567.3**	**42,313**	**3,338,146.8**	**42,220**	**42.2 ▲**
Americas	2,517,835.6	12,753	1,666,870.9	13,187	51.1 ▲
Caribbean	18,752.5	121	18,748.6	131	0.0 -
Central America	21,762.8	229	16,528.4	257	31.7 ▲
Mexico	19,791.9	181	14,416.9	203	37.3 ▲
North America	2,425,775.4	11,437	1,538,281.5	11,821	57.7 ▲
United States	2,344,405.8	9,962	1,426,675.9	10,129	64.3 ▲
Canada	81,369.7	1,475	111,605.7	1,692	-27.1 ▼
South America	51,544.9	966	93,312.4	978	-44.8 ▼
Brazil	40,471.9	573	48,958.6	530	-17.3 ▼
Chile	5,993.2	119	18,806.4	126	-68.1 ▼
Africa/Middle East	80,107.2	1,253	65,124.1	1,317	23.0 ▲
Middle East	21,958.2	428	22,313.0	453	-1.6 ▼
North Africa	3,618.4	163	6,108.1	145	-40.8 ▼
Sub-Saharan Africa	53,015.9	613	28,274.4	652	87.5 ▲
Europe	907,480.4	14,786	842,946.8	14,374	7.7 ▲
Eastern Europe	55,729.3	3,235	49,729.4	3,322	12.1 ▲
Western Europe	851,751.1	11,551	793,217.3	11,052	7.4 ▲
United Kingdom	423,539.5	2,547	178,313.4	2,538	137.5 ▲
Germany	83,818.5	1,487	75,329.3	1,604	11.3 ▲
France	81,784.6	2,589	149,657.0	2,140	-45.4 ▼
Asia-Pacific	1,142,542.3	11,250	702,449.3	11,201	62.7 ▲
Australasia	120,842.6	1,357	88,131.2	1,499	37.1 ▲
Australia	111,574.6	1,138	78,087.4	1,258	42.9 ▲
New Zealand	8,396.9	190	5,153.1	211	62.9 ▲
South East Asia	53,186.0	1,798	69,408.2	1,858	-23.4 ▼
Singapore	28,541.5	375	34,567.5	460	-17.4 ▼
Malaysia	10,228.1	446	14,948.3	514	-31.6 ▼
North Asia	940,606.2	6,964	514,245.3	6,752	82.9 ▲
China	684,289.2	5,137	394,061.8	4,650	73.7 ▲
Hong Kong	153,831.6	625	45,896.0	595	235.2 ▲
South Asia	27,907.5	1,131	30,664.6	1,092	-9.0 ▼
Central Asia	1,514.7	49	8,428.7	67	-82.0 ▼
Japan	99,601.9	2,271	60,755.7	2,141	63.9 ▲

Figure 2: Worldwide Announced M&A Scorecard

Source: Thomson Reuters

Any Asian (ex-Japan) Involvement Announced M&A by Target Industry ($bil)

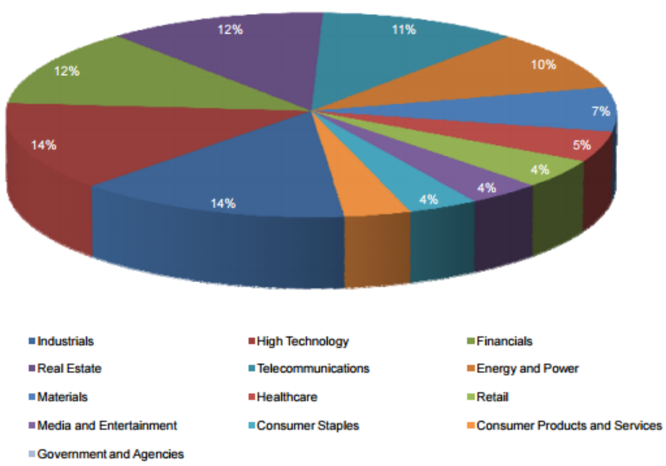


Figure 3: M&A by Target Industry

GENERATING VALUE VIA PURCHASE OF GROWTH IN MALAYSIA

Mergers with, or acquisitions of, domestic firms by international firms, have increased as part of a worldwide trend in corporate structuring. Apart from globalisation pressure, there are many other reasons that prompt M&A activities. Among them are to achieve a bigger market share, generating synergistic gains and cost savings opportunities. M&A deals in Malaysia came up to a total of 446 in 2015, 40% more than the 322 deals done in 2014, despite the slump in oil prices, weakening currency and the 1MDB debacle that dragged down the local market (refer to Figure 4).

Malaysia is ranked among Asia Pacific's top 10 foreign direct investment (FDI) hotspots, according to a study by US-based global information company IHS Inc. Recent FDI based on mergers and acquisitions reflects a rapid increase in M&As rather than the traditional foreign investment in "greenfield" projects (those designed to build new means of production). Strategic growth industries in the services sector include financial services, healthcare, education, commercial aviation, tourism and the IT-Business Process Outsourcing industry, as Malaysia becomes an increasingly important services and services-exporting economy for Southeast Asia.

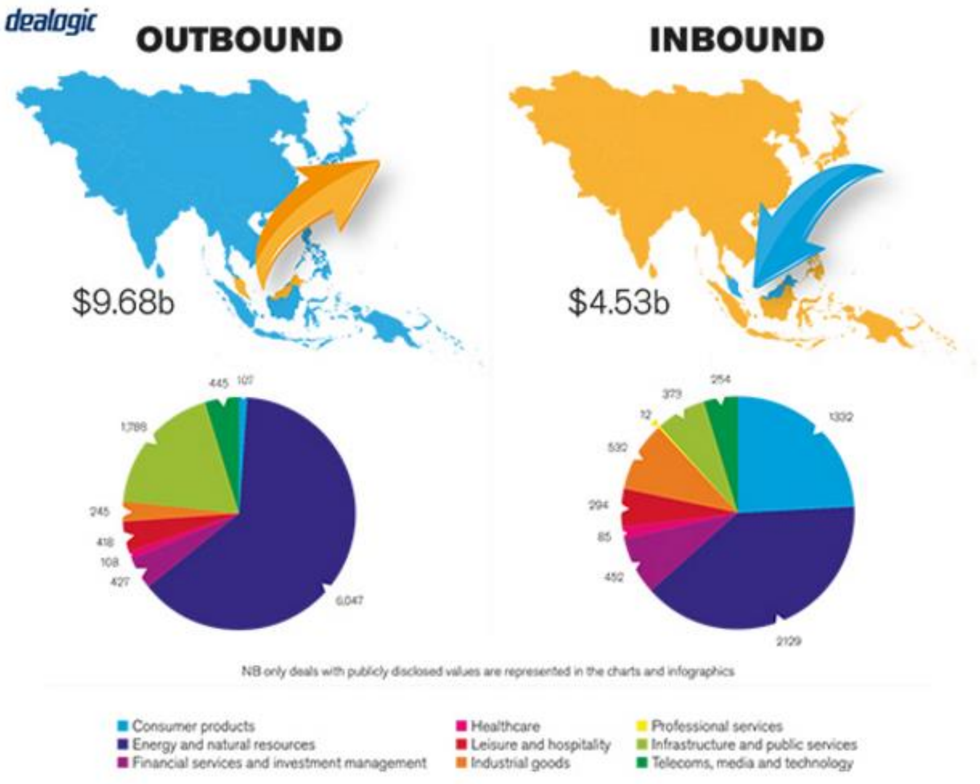


Figure 4
Source: International Financial Law Review

In the oil and gas sector, companies are using M&As to adapt to changing environments. The large and sudden fall in oil prices—driven by big increases in world supply and the battle between Persian Gulf producers and nimble new North American shale and fracking companies—has caused a sea change in the industry. Many exploration and production (E&P) companies in the oil and gas sector are undergoing portfolio management exercises – divesting non-core assets and reducing exploration and development budgets. In contrast, Special Purpose Acquisition Companies (SPACs), listed under a new framework of the Malaysian stock exchange (Bursa Malaysia), are cash rich and actively seeking investment opportunities.

In 2011, Hibiscus Petroleum Bhd (Hibiscus) became the first SPAC in Malaysia and South East Asia, raising US$78m. In 2013, Cliq Energy Bhd (Cliq Energy) and Sona Petroleum Bhd (SONA) raised US$188m and US$172.12m in their respective IPOs, and last year Reach Energy Bhd (Reach Energy), who secured investment from CIMB, Hong Leong Asset Management Bhd and Norway's sovereign wealth fund Norges (among others) became Malaysia's largest SPAC, raising US$245.29m.

Companies	Listing Year	Funds Raised	Upstream Acquisitions
Hibiscus Petroleum Bhd	2011	US$78.0m	Australia – VIC/P57; Australia – Timor Leste JPDA – Kitan oil field; Oman – Block 50; UAE – 3 blocks; Norway – 13 blocks
CLIQ Energy Bhd	2013	US$188.0m	Shortlisted 2 assets in Asia Pacific
Sona Petroleum Bhd	2013	US$172.19m	Agreed to buy 40% stake in Thailand's B8/38 & G4/50 Concessions
Reach Energy Bhd	2014	US$245.29m	–

Source: RigZone

In the energy sector, the Blackstone Group made $800 million line of equity commitment to Tamarind Energy, a Malaysian exploration and production company focused on South East Asia oil and gas exploration and development. Government-supported private equity firm Ekuiti Nasional Bhd bought out Orkim Sdn Bhd (largest clean petroleum product (CPP) transportation provider in Malaysia) for US$114.92 million as part of its strategy to create a leading regional downstream petroleum transportation and logistics group.

In real estate, materials and healthcare sectors, many companies are seeking to scale and enhance their market positions. Notable deals were IOI Properties Group Bhd's acquisition of Mayang Development Sdn Bhd for US$277.5 million, Pandawa Sakti Sdn Bhd buying 98.1% in Sabah Forest Industries Sdn Bhd for US$500 million and IHH Healthcare Bhd picking up a 73.4% stake in India's Global Hospitals Pvt Ltd for US$194 million, respectively.

In the mature and competitive consumer and retail sector, acquirers such as Aeon Co. Malaysia Berhad (which acquired Tesco Malaysia Retail at US$1.4 billion) clearly believe that buying established brands is both less expensive and more certain than trying to build them, both at home and internationally.

The technology sector continues to see a wave of deals. Technology companies are on the lookout for portfolio add-ons to expand their capabilities and customer base, and some non-tech companies are seeking diversification in order to participate in the high-tech growth story. The most recent example in February 2016, was the REA Group (an Australian-based digital advertising media company), which completed the acquisition of iProperty Group (Malaysian company touted as Asia's #1 online property group).

Seek Limited (Australia's biggest online job ads company) purchased JobStreet Corporation Berhad's online employment business valued at RM1.73 billion. The JobsDB online website operates in seven countries across Southeast Asia. This combination of the JobStreet business with JobsDB allows for the company to unlock large growth opportunities in this region.

Japan possess the power of original content, sophisticated technology and infrastructure, and the availability of funds for strategic investment in the creative content industries. Investors in search of international joint productions utilising the respective strengths of difference countries and regions, such as combining Japan's scenario, Malaysia's creative talent pool and finance functions, and the consumer access to ASEAN, China, Middle East markets, will find that Malaysia presents a valuable synergistic environment in which Asian creators and consumers develop shared value base and interaction refer to Case Study).

KADOKAWA
GEMPAK STARZ
角川平方

Case Study: Japan Strengthening Linkages in the Asian Creative Content Industry

The Asian region has recently been making rapid progress in creating the conditions for content development and consumption. The diverse cultural, religious and historical backgrounds of the various Asian countries inevitably produce differences in the types of content to which they are receptive. At the same time, the many examples of content that have garnered international popularity and commercial success reveal possibilities for the broad-ranging prevalence of content grounded in universal values.

KADOKAWA began as a full-service publisher of books in 1945 and was listed in the Tokyo Stock Exchange in 1998. They have thrived over the years from the sale of books, comics and lights novels - now ranked Top-30 in the Global Publishing Leaders 2015 with consolidated revenue of US$1.3bn in 2014. For the past 10 years, KADOKAWA has embarked on a major M&A exercise and has since grown into a broad-based media company that produces animation, feature films, games, and other digital and multi-media content.

In 2015, in line with KADOKAWA's ambition to establish itself as a global entertainment enterprise, the company acquired Art Square Group (ASG), a leading publisher of comics and children's books in Malaysia. The restructured company, KADOKAWA Gempak Starz will be implementing an aggressive media-mix strategy in the creation of animation, creation of games and digitisation of IP content and merchandising, amongst other initiatives. The positioning of Malaysia as an important content IP development base for KADOKAWA Group will be a strategic gateway to neighbouring countries in Asia, Middle East as well as other Mandarin and English speaking markets.

With this potential game changer, Malaysia is poised to capture a bigger slice of the global creative content industry, valued at USD10.1 trillion up to 2019 (PWC Global Entertainment and Media Outlook 2015 -2019), with KADOKAWA positioning Kuala Lumpur as its export hub for Southeast Asia and the Middle East. Today, Malaysia's creative multimedia industry is worth an estimated RM18.7 billion.

Based on this MNC attraction by InvestKL, such synergistic acquisition creates a very favourable environment for Malaysian businesses. Not only is the willingness of Japan to engage in M&A activity driving up prices for Malaysian companies looking to sell, but the capital, experience and access to new markets that Japanese investors bring can be beneficial to Malaysian businesses.

LONG-TERM PROSPECTS

Cross-border M&A activity is still in an early phase in Asia's middle income economies and remains small, relative to their sizes and stages of development. For example, in 2015, M&A transactions accounted for 3% of GDP in Malaysia, compared with 14% of GDP in America.

However, M&A activity in Asia, specifically ASEAN, will continue to rise on the back of the region's strong economic fundamentals because business leaders realise they have to be strategically positioned to compete within ASEAN when it reaches its full potential. The economic and regulatory reforms, which a number of ASEAN countries such as Malaysia have undertaken, have helped bring about greater liberalisation of industries and attract more inbound investments. The cross-border deal flow is expected to be a key theme in the coming years, as major economies strike agreements and alliances to bolster trade. For instance the recently agreed Trans-Pacific Partnership between 12 Pacific-Rim countries, including the US, Japan, Canada, Australia and Malaysia, is the biggest global trade agreement in two decades.

Empirical analysis of specific acquisition strategies offers limited insights. Whether it is - for improving the performance of the target company, removing excess capacity from an industry, creating market access for products, acquiring skills or technologies more quickly or at lower cost than they could be built in-house, and picking winners early and helping them develop their businesses - the value creation opportunities are tremendous and have to be strategically pursued.

We are in a period of volatility, which has led corporates to streamline their capital allocation, define their focus clearly, and build scale across their core businesses. It will be opportunistic for buy-side M&As, especially for corporates with strong cash reserves and low reliance on external funding. In Malaysia, most M&A deals were undertaken either to acquire undervalued assets or to unlock the value of the underlying assets. With the Ringgit weaker against the US dollar, there is greater anticipation of foreign investments and more private equity deals. Though cautiously optimistic, we expect to see this momentum continue into 2016.

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