MERGERS AND VALUE CREATION
A CASE STUDY OF SIME DARBY BERHAD

Awasi Mohamad
Bachelor of Science (Hons) Estate Management
Birmingham Polytechnic, United Kingdom
1991

Vijay Baskar Tamarum Demudoo
Bachelor of Information Technology – Software Engineering (Hons)
University Tun Abdul Razak
2005

SUBMITTED TO THE GRADUATE SCHOOL OF BUSINESS
FACULTY OF BUSINESS AND ACCOUNTANCY
UNIVERSITY OF MALAYA, IN PARTIAL FULFILLMENT
OF THE REQUIREMENTS FOR THE DEGREE OF
MASTER OF BUSINESS ADMINISTRATION

AUGUST 2008
DECLARATION

We hereby declare that the work in this thesis/dissertation is our own except for quotations and summaries which have been duly acknowledged.

DATE: 22nd April 2009
Name: Awasi Mohamad
Matric No: CGA050169

Name: Vijay Baskar Tamarum Demudoo
Matric No: CGA060012
ACKNOWLEDGEMENT

It is obvious that the development of a project of this scope needs the support of many people. We are indeed grateful to the people who helped us during all these months of hard work. First of all, we would like to take this opportunity to the management of Sime Darby Group and the University as well for allowing us to carry out this thesis. We would like to express our gratitude to the staff of Sime Darby Group, who had helped us in providing the informations and data as per needed. Not forgetting, for the assistance, guidance and the time sacrifices by the employees in allowing us to gather the right and meaningful information and data which enable us to fit into our research.

Our hearties appreciation and thanks to Professor Madya Dr. Fazilah Abdul Samad for giving us the advice, guidance and chances to explore various type of financial methods which being very helpful in completing this thesis. In addition, her support and guidance all the time has being very helpful and mainly in keeping the ship afloat in our balance.

Besides that, we would also like extend our gratitude to our parents and family who supported and encouraged us all the time. We do take this opportunity to acknowledge our friends, course mates and seniors whom have shared their experience and ideas from development of their own thesis and provide invaluable amount of guidance for our research. Finally, we would like to thank the faculty as well, for being kind enough to donate the resources and being helpful all the time.
EXECUTIVE SUMMARY

Globalisation and the borderless world has brought with it heightened competition in the business circles. In not too distant a future, only very large multinational and multicultural management companies with economies of scale, globalised markets network, quality products meeting consumers’ expectations and taste but yet cost efficient would be able to survive. Smaller companies with specialised, differentiated and proprietary products would be the exception to this trend. There are many examples of industries impacted by globalisation which have taken the successful route of mergers and acquisitions (M&A). These included the airlines, banking, automotive and oil & gas industries.

Closer to home we have seen the successful M&A of the local banking industry. Synergy Drive Berhad (Synergy Drive) is a Special Purpose Vehicle (SPV) company set-up by CIMB Group’s private equity arm with the intends to merge all the assets and liabilities of Sime Darby Group, Kumpulan Guthrie Berhad, Golden Hope Plantations Berhad and six (6) of its listed subsidiaries. As such the merger of Sime Darby, Golden Hope and Kumpulan Guthrie is considered appropriate and timely to take advantage of economies of scale, synergies and greater productivity and efficiency. Synergy Drive’s plantation business would be able to emulate the three large multinationals in the USA which control the world’s edible oils markets like Cargill Incorporated, Archer Daniels Midland (ADM) Company and Bungee Corporation. Historically, the financial performance plantation business can be seen to be influence greatly by the prices of palm oil and hence
the palm oil industry is often referred to as cyclical in nature. In order to ensure that profits will not fluctuate greatly, the plantation business began their diversification all along the value chain or aptly termed as a fully integrated player.

A good example is PETRONAS, where the core business is petroleum. Building on the sound foundation anchored on integration, value-adding and globalisation, PETRONAS whose their initial involvement with multinational oil companies started with production sharing contract has since moved its upstream business overseas and downstream activities very successfully. Taking the cue from this, it would be strategic indeed for the plantation business to emulate the approach of PETRONAS by strengthening further both upstream and downstream sectors. Synergy Drive could move from just concentrating on the production of basic oleochemicals i.e. fatty acids which are derived from the splitting process, to the production of higher value-added products.

The creation of the largest plantation companies by merging Sime Darby, Golden Hope and Kumpulan Guthrie brings about significant prospects of cost and revenue synergies. The cost synergies among others include consolidation of contiguous estates, rationalisation of mill utilisation, unified procurement and logistic activities and consolidation of plantations management and administrative functions etc. The revenue synergies would include leveraging on global strategic presence of the three companies and wider customer spectrum for growing market share. The sharing of best practices and management expertise could also further enhanced both cost and revenue synergies. In addition to that, Synergy Drive able to move forward with sustainable profits gains,
productivity, capabilities, skills and expertise in its business operations and core competencies building. As an enlarged entity, Synergy Drive would have the capability and capacity to grow further the plantation and property business.

On 27 November 2006, Synergy Drive announced simultaneous offers to each of the participating companies through Voluntary General Offer (VGO) and Mandatory General Offer (MGO). Synergy Drive had offered eight (8) companies to acquire all their assets and liabilities under VGO namely Sime Darby Berhad, Sime UEP Properties Berhad, Sime Engineering Services Berhad, Kumpulan Guthrie Berhad, Mentakab Rubber Co. Berhad, Golden Hope Plantations Berhad, Guthrie Ropel Berhad and Highlands and Lowlands Berhad. At the same time, Synergy Drive also offered Negara Properties Berhad through MGO by issuing 11.6 million shares. By 1st October 2007, Synergy Drive and all participating companies have obtained all the requisite approvals to effect the merger. The major institutional shareholders of Synergy Drive are Permodalan National Berhad (17%), Amanah Saham Bumiputra (30.9%), Employees Provident Fund (11.7%) and other shareholding (40.4%).

The consolidation of all businesses of these three group of companies had formed five (5) strategic core businesses of plantations, property, motor, heavy equipment, and energy and utilities. From the merger, Synergy Drive’s had valued the target companies at a combined proforma market capitalization of RM 53.8 billion. The group is the world’s largest listed oil palm plantation group by planted land areas (520,000 ha), with significant presence in both upstream and downstream activities, i.e. they owned 65 mills
in Malaysia & Indonesia. They are one of Malaysia’s leading developers of quality residential and commercial communities.

Therefore, this study aims to investigate not only the issues faced by Synergy Drive in the pre-merger and post merger integration process, but also to evaluate the purchase consideration made for the merger, the types of financing used, achievement of the motivation for the merger and the value created via merger.

Accordingly, our study had identified that Synergy Drive does achieve their value creation via this merger exercise. A positive uptrend was shown upon the listing of the renamed Sime Darby on Bursa Malaysia and their shares remains as one of the top plantation shares for most foreign broking houses. The stock to date has surpassed the expectations of most broking houses, which had earlier capped the stock at the RM11-RM12 range for 2008. In addition to that, Synergy Drive did achieve its merger objectives in terms of business size, broader market penetration and wider market segments. The merger also allowed them to draw their focus on a set of core businesses within Asia Pacific and gain the benefits from population growth and economic development.
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Contents</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Declaration</td>
<td>II</td>
</tr>
<tr>
<td>Acknowledgement</td>
<td>III</td>
</tr>
<tr>
<td>Executive Summary</td>
<td>IV</td>
</tr>
<tr>
<td>List of Figures</td>
<td>XIV</td>
</tr>
<tr>
<td>List of Table</td>
<td>XVI</td>
</tr>
<tr>
<td>List of Abbreviations</td>
<td>XVII</td>
</tr>
<tr>
<td>List of Symbols</td>
<td>XXI</td>
</tr>
<tr>
<td>List of Appendix</td>
<td>XXII</td>
</tr>
</tbody>
</table>

## Chapter 1: Introduction

1.0 Introduction ............................................................................. 1
1.1 M&A in Malaysia ....................................................................... 2
1.2 Importance of Study .................................................................. 5
1.3 Purpose of Study ....................................................................... 8
1.4 Organization of Study ............................................................ 9

## Chapter 2: Literature Review

2.1 Definition of Mergers & Acquisitions ...................................... 13
2.2 Classification of M &A ............................................................. 16
2.3 Objective and Motive of M&A ................................................... 18
2.4 Due Diligence ............................................................................ 21
2.5 Post M&A .................................................................................. 23
2.6 The Integration Process ............................................................ 24
   2.6.1 The Merger & Acquisition Process ...................................... 26
   2.6.2 Post M&A Integration ......................................................... 29
   2.6.3 The Integration Process and Culture .................................... 31
   2.6.4 The Importance of Integration in Creating Synergy ............... 33
2.7 Synergy ..................................................................................... 36
2.7.1 Definition and Types.................................................................36
2.7.2 Problems with Creating Synergy...........................................38
2.7.3 Solutions to Problems with Synergy......................................39
2.7.4 The Management of Synergy................................................42
2.8 Theory Summary.......................................................................43

Chapter 3: Research Methodology..................................................45
3.1 Research Questions....................................................................45
3.2 Research Limitations.................................................................46
3.3 Research Methodology...............................................................47
    3.3.1 Data Collecting and Sampling...........................................47
    3.3.2 Methods of Valuation.......................................................48

Chapter 4: Background of Participating Companies.............................49
4.1 Sime Darby..................................................................................49
    4.1.1 Corporate Overview..........................................................49
    4.1.2 Board of Directors.............................................................50
    4.1.3 Sime Darby Group Business Activities................................52
        4.1.3.1 Plantations.................................................................52
        4.1.3.2 Property.................................................................53
        4.1.3.3 Motor...........................................................................57
        4.1.3.4 Heavy Equipments..................................................58
        4.1.3.5 Energy & Utilities.....................................................58
        4.1.3.6 General Trading.......................................................59
4.2 Kumpulan Guthrie Berhad..........................................................60
    4.2.1 Corporate Overview..........................................................60
    4.2.2 KGB Group Structure.......................................................63
    4.2.3 Major Business Groups....................................................63
        4.2.3.1 Plantations.................................................................63
        4.2.3.2 Property.................................................................67
    4.2.4 Board of Directors.............................................................68
Chapter 5: Industry Overview and Merger Initiations ................................................................. 80

5.1 Palm Oil Industry .................................................................................................................. 80
   5.1.1 Overview of Malaysian Palm Oil Industry ................................................................. 80
   5.1.2 Palm oil industry growth in Malaysia and Indonesia .................................................. 85
   5.1.3 Growth prospects ....................................................................................................... 88
   5.1.4 Industry players and competition .............................................................................. 91
5.2 Property Industry .................................................................................................................. 93
   5.2.1 Overview of the property industry in Malaysia ......................................................... 93
   5.2.2 Growth prospects ....................................................................................................... 97
   5.2.3 Industry players and competition .............................................................................. 98
5.3 Motor Industry ...................................................................................................................... 100
   5.3.1 Overview of the motor industry ................................................................................. 100
   5.3.2 Growth prospects ....................................................................................................... 104
   5.3.3 Industry players and competition .............................................................................. 106
5.4 Heavy Equipment Industry ................................................................................................. 108
   5.4.1 Overview of the heavy equipment industry in Australia ............................................ 109
   5.4.2 Growth prospects ....................................................................................................... 110
   5.4.3 Industry players and competition .............................................................................. 111
5.5 Energy and Utilities Industry .............................................................................................. 112
   5.5.1 Overview of Energy and Utilities Industry ................................................................. 112
   5.5.2 Growth prospects ....................................................................................................... 114
   5.5.3 Industry players and competition .............................................................................. 115
5.6 Challenges for the Merger Faced by Synergy Drive

5.6.1 Challenges to meet corporate and business strategy

5.6.2 Challenges to meet national agenda

5.6.3 Challenges to meet Globalisation and the Borderless World

5.7 Merger Rationalization

5.7.1 To Value-add and Become a Fully Integrated Plantation Company

5.7.2 To Optimise on Cost and Revenue Synergies

5.7.3 To Grow Further the Upstream and Downstream Sector

5.7.4 To Further Value-add the Palm Oil Business

5.7.5 To Focus on Quantum Leap R&D

Chapter 6: Merger Integration and Business Consolidation

6.1 Background

6.2 Background of Merger

6.3 Group Business Strategy

6.3.1 Strategy for the plantation business

6.3.2 Strategy for the property business

6.3.3 Strategy for other core business

6.4 Merger Synergies

6.4.1 Plantation

6.4.1.1 Cost Synergies

6.4.1.2 Revenue Synergies

6.4.2 Property business

6.4.2.1 Cost Synergies

6.4.2.2 Revenue Synergies

6.4.3 Corporate Services

6.5 Competitive Strengths

6.5.1 Scale-driven revenue and cost synergies for plantations

6.5.2 Focused set of core businesses within Asia Pacific

6.5.3 Experienced management team

6.6 Post Merger – Business Integration
Chapter 7: Research Analysis and Result

7.1 Pricing of the Merger Entities

7.1.1 Offer Prices Based On Indicative Valuation

7.1.2 Fair Valuation Based On DCF

7.2 Estimation of Target Companies Value’s

7.2.1 Sime Darby 5-Years Projection

7.2.1.1 Free Cash Flow and Terminal Value

7.2.2 Golden Hope 5-years Projection

7.2.2.1 Estimation of Cost of Equity and Cost of Capital

7.2.2.2 Determination of Firm Value

7.2.3 Kumpulan Guthrie Berhad’s 5-years projection

7.2.3.1 Free Cash Flows

7.2.3.2 Estimation of Cost of Equity and Capital

7.2.3.3 Determination of Firm Value
7.3 Measuring Value of Synergy Drive with Synergies.................................195
  7.3.1 Synergy Estimation..............................................................................195
  7.3.2 Calculating the Projected Income Statement.................................197
  7.3.3 Calculating the Projected Balance Sheet.......................................199
  7.3.4 Free Cash Flows..............................................................................199
  7.3.5 Determination of Firm Value..........................................................200
  7.3.6 Comparison of the Combined Companies Value with and Without
       Synergy...............................................................................................200
  7.4 Alternative Valuations.........................................................................201
  7.5 Price Determination.............................................................................202
  7.6 Weighted Average Valuation of Combined Firm............................206
  7.7 Value Creation Analysis.....................................................................206
  7.8 Share Price Valuation...........................................................................214

Chapter 8: Ideal Weighted Average Capital Structure..........................218

Chapter 9: Conclusion and Recommendations.......................................220
# LIST OF FIGURES

Figure 2.1: The definition of Mergers & Acquisitions.................................................................14  
Figure 2.2: Map of Mergers & Acquisitions Process.....................................................................27  
Figure 2.3: Watson Wyatt Deal Flow Model In Practice..............................................................28  
Figure 2.4: Three Focal Points of Post-Merger Integration..........................................................34  
Figure 2.5: The Process of Realizing Synergistic Gain.................................................................41  
Figure 4.0: Sime Darby Group’s Head Office..............................................................................50  
Figure 4.1: Sime Darby Berhad’s Board of Directors.................................................................51  
Figure 4.2: Sime Darby Group’s Business Activities.................................................................52  
Figure 4.3: Kumpulan Guthrie Berhad’s Structure.................................................................63  
Figure 4.4: Kumpulan Guthrie Berhad’s Board of Directors......................................................70  
Figure 4.5: Golden Hope’s Business Activities.........................................................................71  
Figure 4.6: Golden Hope’s Board of Directors.........................................................................79  
Figure 4.0: Synergy Drive Core Business....................................................................................125  
Figure 6.1: Synergy Drive Group Structure..............................................................................126  
Figure 6.2: Merger Integration Phases......................................................................................128  
Figure 6.3: Plantation’s Upstream and Downstream Activities..................................................145  
Figure 6.4: Plantations Production Process Flow.......................................................................146  
Figure 7.0: Sime Darby’s Free Cash Flow..................................................................................184  
Figure 7.1: Calculation of Cost of Equity and Capital (Sime Darby)........................................185  
Figure 7.2: Sime Darby’s Market Value......................................................................................186  
Figure 7.3: Calculation of Cost of Equity and Capital (Golden Hope)......................................190  
Figure 7.4: Golden Hope’s Free Cash Flow.............................................................................190  
Figure 7.5: Golden Hope’s Market Value...................................................................................191  
Figure 7.6: Kumpulan Guthrie Berhad’s Free Cash Flow.........................................................193  
Figure 7.7: Calculation of Cost of Equity and Capital (KGB)...................................................194  
Figure 7.8: KGB’s Market Value...............................................................................................195  
Figure 7.9: Calculation of the Estimated Cost and Revenue Synergies.....................................197  
Figure 7.10: Projected Income Statement....................................................................................198  
Figure 7.11: Estimated Cost and Revenue Synergies on the EBIT.............................................198
Figure 7.12: Projected Balance Sheet.................................................................199
Figure 7.13: Expected Cash Flow for the next 5 years.....................................199
Figure 7.14: Synergy Drive’s Group Value.........................................................200
Figure 7.15: Comparison of Synergy Value.......................................................201
Figure 7.16: Price/Net Asset & Price/Earning Valuation.................................202
Figure 7.17: Offer Price Data...........................................................................204
Figure 7.18: Firm’s Standalone Value...............................................................204
Figure 7.19: Consolidated Firm Value...............................................................204
Figure 7.20: Increase in Offer Price (Sime Darby) ...........................................205
Figure 7.21: Increase in Offer Price (Guthrie)...................................................205
Figure 7.22: Increase in Offer Price (Golden Hope) .........................................205
Figure 7.23: Weighted Average Calculation of the Combined Firm...............206
Figure 7.24: Sime Darby Share Price...............................................................214
Figure 7.25: Golden Hope Share Price.............................................................214
Figure 7.26: Kumpulan Guthrie Berhad Share Price.......................................215
Figure 8.1: Ideal WACC..............................................................................218
LIST OF TABLES

Table 2.1: Classification of Merger & Acquisition Transactions.................................7
Table 2.2: Merger & Acquisition Motives.......................................................................18
Table 5.0: Total Oil Palm Plantation Area in Malaysia................................................85
Table 5.1: Yield of FFB in Malaysia................................................................................85
Table 5.2: Production of CPO and PK in Malaysia.......................................................86
Table 5.3: Extraction Rate of Palm Oil in Malaysia.......................................................86
Table 5.4: Distribution of Oil Palm Plantations Areas...................................................86
Table 5.5: Major Palm Oil Producer.............................................................................91
Table 5.6: Major Palm Oil Plantation (Planted Area) in Malaysia...............................92
Table 5.7: Property Development Companies by Market Capitalisation..................99
Table 6.0: Mills owns by the Synergy Group...............................................................150
Table 6.1: Biodiesel Production Plants.........................................................................155
Table 6.2: R&D Centres and Activities.................................................................156
Table 6.3: R&D Expenditure.......................................................................................160
Table 6.4: Group Motor’s Operation............................................................................169
Table 7.1: Profitability Ratios......................................................................................207
Table 7.2: Efficiency Analysis......................................................................................210
Table 7.3: Altman’s Z-Score.......................................................................................213
LIST OF ABBREVIATIONS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>BCHB</td>
<td>Bumiputra-Commerce Holdings Berhad (50841-W)</td>
</tr>
<tr>
<td>BNM</td>
<td>Bank Negara Malaysia</td>
</tr>
<tr>
<td>Board</td>
<td>Board of Directors</td>
</tr>
<tr>
<td>Bursa Depository</td>
<td>Bursa Malaysia Depository Sdn Bhd (165570-W)</td>
</tr>
<tr>
<td>Bursa Securities</td>
<td>Bursa Malaysia Securities Berhad (635998-W)</td>
</tr>
<tr>
<td>Bursa Securities LR</td>
<td>Listing Requirements of Bursa Securities</td>
</tr>
<tr>
<td>CIMB</td>
<td>CIMB Investment Bank Berhad (18417-M)</td>
</tr>
<tr>
<td>CIMB Group</td>
<td>CIMB Group Sdn Bhd (706803-D)</td>
</tr>
<tr>
<td>CIMB PE</td>
<td>CIMB Private Equity Sdn Bhd (648424-H)</td>
</tr>
<tr>
<td>CKD</td>
<td>Complete Knocked Down</td>
</tr>
<tr>
<td>CMSA</td>
<td>Capital Markets and Services Act, 2007</td>
</tr>
<tr>
<td>Code</td>
<td>Malaysian Code on Take-Overs and Mergers, 1998</td>
</tr>
<tr>
<td>CPKO</td>
<td>Crude palm kernel oil</td>
</tr>
<tr>
<td>CPO</td>
<td>Crude palm oil</td>
</tr>
<tr>
<td>EBIT</td>
<td>Earnings before interest and taxation</td>
</tr>
<tr>
<td>EBITDA</td>
<td>Earnings before interest, taxation, depreciation and amortisation</td>
</tr>
<tr>
<td>EFB</td>
<td>Empty fruit bunches</td>
</tr>
<tr>
<td>EPF</td>
<td>Employees’ Provident Fund Board</td>
</tr>
<tr>
<td>EPS</td>
<td>Earnings per share/stock</td>
</tr>
<tr>
<td>ESOS</td>
<td>Employees’ share or share option scheme</td>
</tr>
<tr>
<td>FELDA</td>
<td>Federal Land Development Authority</td>
</tr>
</tbody>
</table>
FFB ........................................ Fresh fruit bunches
FIC ........................................ Foreign Investment Committee
Frost & Sullivan ...................... Frost & Sullivan (M) Sdn Bhd (522293-W)
GCE ........................................ Guthrie Corridor Expressway
GDP ........................................ Gross domestic product
GDV ........................................ Gross development value
GHope ..................................... Golden Hope Plantations Berhad (29992-U)
GHope Group ......................... GHope and its subsidiaries, collectively
GHope Shares ....................... Ordinary shares of RM1.00 each in GHope
GRopel .................................. Guthrie Ropel Berhad (6710-T)
GPDH ..................................... Guthrie Property Development Holding Bhd (15631-P)
Ha .......................................... Hectare
HLB .......................................... Highlands & Lowlands Berhad (24817-H)
HR .......................................... Human resource
IT .......................................... Information technology
JPPH ..................................... Jabatan Penilaian dan Perkhidmatan Harta (or the Valuation and Property Services Department)
KER ........................................ Kernel extraction rate
KGB .......................................... Kumpulan Guthrie Berhad (4001-P)
KGB Group ............................. KGB and its subsidiaries, collectively
KGB Shares ........................... Ordinary shares of RM1.00 each in KGB
Khazanah ............................. Khazanah Nasional Berhad (275505-K)
LPD .......................................... 31 August 2007, being the latest practicable date prior to the registration of this Prospectus
Mentakab................................. Mentakab Rubber Company (Malaya) Berhad (3325-W)

Merger ........................................... Merger of all the Participating Companies pursuant to their respective Sale of Business Agreements

MI ........................................... Minority interest

MIC ........................................... Merger Integration Committee

MITI ........................................... Ministry of International Trade and Industry

MOF ........................................... The Minister of Finance

MPOB ........................................... Malaysian Palm Oil Board

MT ........................................... Metric tonnes

MW ........................................... Megawatt

Negara ........................................... Negara Properties (M) Berhad (3432-P)

NTA ........................................... Net tangible assets

OER ........................................... Oil extraction rate

PAT ........................................... Profit after taxation

PATAMI ........................................... Profit after taxation and minority interests

PBT ........................................... Profit before taxation

PE Multiple ................................... Price earnings multiple

PK ........................................... Palm kernel

PKO ........................................... Palm kernel oil

PNB ........................................... Permodalan Nasional Berhad (38218-X)

PNB Unit Trust Funds ................. Unit trust funds managed by PNB and companies related to PNB

PVC ........................................... Polyvinyl chloride
R&D ........................................ Research and development
SASB ........................................ Skim Amanah Saham Bumiputera
SC ................................................ Securities Commission
Sime Darby ................................... Sime Darby Berhad (41759-M)
Sime Darby Group ......................... Sime Darby and its subsidiaries, collectively
Sime Darby Shares ....................... Ordinary shares of RM0.50 each in Sime Darby
Sime Engineering ......................... Sime Engineering Services Berhad (582750-H)
Sime UEP ..................................... Sime UEP Properties Berhad (5835-W)
Synergy Drive .............................. Synergy Drive Bhd (752404-U)
Synergy Drive Shares ................. Ordinary shares of RM0.50 each in our Company
YPB .......................................... Yayasan Pelaburan Bumiputra (37113-P)
LIST OF SYMBOLS

β .................................................. Beta
β_u ................................................ Unlevered Beta
β_L ................................................ Levered Beta
K_d ................................................ Cost of debt
K_e ................................................ Cost of equity
R_d ................................................ Rate of return on debt
R_f ................................................ Risk free rate
R_LT .............................................. Return on long term assets/debts
R_m ................................................ Return on market
R_p ................................................ Risk Premium
R_TB .............................................. Return on treasury bills
t ..................................................... Taxation rate
LIST OF APPENDICES

Appendix 1: Interview Questionnaires with the Management of Participating Companies - Set One (Semi Structured)
Appendix 2: Interview Questionnaires with the Management of Participating Companies – Email Questions
Appendix 3: Interview Questionnaires with the Management of Participating Companies - Set Two (Semi Structured)
Appendix 4: Credit Spread From Malaysian Corporate Bonds
Appendix 5: KLCI Return
Appendix 6: Regression Result for Beta Calculation – Sime Darby Bhd – Pre-Merger
Appendix 7: Regression Result for Beta Calculation – Golden Hope Plantation Bhd – Pre-Merger
Appendix 8: Regression Result for Beta Calculation – Kumpulan Guthrie Bhd – Pre-Merger
Appendix 9: Regression Result for Beta Calculation – Sime Darby Bhd – Post-Merger
CHAPTER 1: INTRODUCTION

A corporation has diverse options to choose from when it comes to growth strategies. Growth is an important aspect for any companies, either individual owned, listed companies or even multinational companies. On the various option for growth are to grow organically by increasing sales personnel, new product developments and by expanding into new geographical areas. Alternative options such as inorganic growth are external revenue growth which is for example strategic alliances, joint ventures and franchising. Another option is to merge and acquire (M&A) which is an inorganic example of how a company can grow (Sherman, 2005). According to Lees (2003) and Sudarsanam (1995), M&A’s are mainly about growth. Organic or internal growth is most often a sluggish process and M&A’s are one option that will increase the growth process. With an M&A deal the company can get instant access to new markets, technology and operations can be made more efficiently.

There are several possible motives or reasons why a company chooses to grow through an M&A. The most common motive is to create synergy and value creation. On the other hand, other motives are diversification of the business, improved management, market power or tax motives (DePhamphilis, 2005; Gaughan, 2002). According to Johnson and Scholes (1997), M&A is a fast way of entering new areas of markets or products. Besides that, it can also be a way to gain competence or resources that the company is lacking off. Market knowledge is also a major cause why companies choose M&A’s as way to
international development. Another reason when two companies freely engage in M&A are to search for benefits arising from synergies.

M&A’s have become increasingly international. This increase can perhaps be contributed to some major economic forces than has come into play in recent years, such as the European Union’s single market, the globalisation of the marketplace and the increasing global competition. Many companies have realized that they need to go global in order to maintain the competitive edge in current environment. On top of that, an important issue which had an impact to global business and venturing is that the barriers to trade have been reduced. Corporate mergers and acquisitions (M&A) have long received a lot of attention from the corporate world, the public as well as the academic world. Many corporations across the world have been considering M&A strategies to realize cost synergies against increased competition, pricing pressures, gaps in product mix and asset concentration.

1.1 M&A IN MALAYSIA

In Malaysia, the M&A’s exercises are growing widely. Looking at the first half of the year of 2007, the M&A deals was over US$23 billion. The figure was nearly to the US$27.4 billion deal, which was recorded for the whole year of 2006. M&A activity during the period mentioned above was dominated by the telecommunication and financial services. Other significant areas include industrial products, property, consumer products and media.
Malaysia, like the rest of the world, has been swept by the privatization trend. In the first half of the year of 2007 alone, around US$13.4 billion of market value has been wiped out from the Malaysian stock market, where at least 17 firms taken to be private. The present low interest rate and high liquidity in the credit market has encouraged owners to take their undervalued stocks private despite the fact that prices are now are more expensive compared to those days. Other key factors driving for the deals include corporate long-term strategic considerations and an increase in confidence in the present economic outlook. (PricewaterhouseCoopers, 2007)

Some of the major deals engaged in Malaysia for the half year of 2007, includes:

- Maxis Communications Bhd, Malaysia’s leading mobile operator, by Binariang GSM Sdn Bhd for US$4.8 billion.
- AmInvestment Group Bhd, the country’s second largest investment bank, by AMMB Holdings Bhd for US$698 million.
- Property and plantation companies, Island & Peninsular Bhd and Petaling Garden Bhd by state fund manager, Permodalan Nasional Berhad for US$339 million.
- Employee Provision Fund acquiring and taking private Malaysia’s fourth largest banking group, Rashid Hussain Bhd and its subsidiaries for US$4.5 billion.

Besides the listed deals above, there were a notable numbers of cross-borders deals, mainly involving foreign acquisitions of Malaysia’s assets. These acquisitions are mainly on the sector such as telecommunications, financial services, industrial products, property and media and publishing. Some of the cross border mergers and take over’s a below:
- Saudi Telecom Co taking over a 25 percentage stake in Binariang, the parent company of Maxis, worth US$3 billion.
- Bank of Tokyo-Mitsubishi acquiring a stake in Malaysia’s second largest banking group, Bumiputra-Commerce Holdings Bhd (CIMB), for US$382 million.
- Singapore’s State investment arm Temasek Holdings selling its stakes in Telekom Malaysia Bhd for an amount of US$360 million.
- Sale of three up market shopping malls in Penang for over US$290 million to a US insurance group.
- Local timber-cum Chinese press tycoon Tan Sri Tiong Hiew King merging its Hong Kong and Malaysia media arm, with Ming Pao Enterprise Corp Ltd of Hong Kong acquiring Sin Chiew Media Corp and Nanyang Press Holdings Bhd of Malaysia for US$269 million.

There are still a number of companies that have ideal underlying ingredients for going private and merging exercises. These companies are aiming to achieve a strong free cash flow, good quality assets and robust earning potential relative to their market value via the deals. Looking at emerging M&A, among the sectors are financial services and property. Deals in financial services are expected to be driven by cross border and industry consolidation factors. Malayan Banking Bhd, Malaysia largest bank, for instance is on the hunt for banks within the region while two local banking groups, RHB Capital Bhd and EON Capital Bhd are seeking foreign strategic partners, with plans to sell 10 to 35 percentage stakes. There are also possibilities of further consolidation within local banking industry.
Meanwhile in property, the attractiveness of undervalued Malaysian property investment relative to regional markets is anticipated to come from overseas investors’ interest with the broad focus on the Iskandar Development Region. In addition, companies such as Lion Group (a diversified industrial and retail group) and Genting Group (involved in gaming and leisure among others), are also rationalising their portfolio strategy, which could draw further divestment and acquisition deals. On the other hand, government-linked companies like Proton Holdings Bhd, Malaysia Airport Holdings Bhd and Silterra Malaysia Bhd do also feature strongly in M&A scene. Synergy Drive, one of the largest companies listed in Malaysia’s Stock Exchange, born from the merger of three plantations oriented groups, Sime Darby Berhad, Golden Hope and Kumpulan Guthrie.

1.2 IMPORTANCE OF STUDY

First of all there is a need to define the concept of M&A. In a merger the two companies shareholders remain as joint owners and the two companies combine their resources to achieve common goals (Sudarsanam, 2003). The two companies become a new legal entity while in an acquisition one of the companies take control of the other firm’s assets (Buckley & Ghauri, 2002). According to a publication by UNCTAD (2000) the phrase “mergers and acquisitions” essentially mean acquisitions because even M&A deals that are supposed to be mergers are in reality acquisitions where one company controls the other one. In 2000 only 3% of mergers and acquisitions were actually mergers (cited in Buckley & Ghauri, 2002). Sudarsanam (2003) defines M&A as when two companies are combined to achieve certain strategic and business objectives and in this thesis M&A will
be defined as such. We have chosen this definition because it covers many forms of both mergers and acquisitions.

The most important aspect for firms lies within the frames of the synergetic effects which is the end result of any M&A. Synergy represents the additional value that is created by merging two firms together (Lees, 2003; Gaughan, 2002). One way of creating synergy is when decreases in per-unit costs results from an increase in the size or scale of a company, so called economies of scale (Gaughan, 2002). This is normally practiced as a tool for raising capital to any M&A. According to Seth (1990) synergy and value creation is synonymous. Synergy can be an unclear word which some might use as a synonym for cost cutting but it also include positive aspects of the merger which is the growth aspects and knowledge sharing (Haberg, et al. 2000). A synergy can be achieved by merging or acquiring a company that has access to a new geographic market or access to a new customer segment. This allows the acquiring company to reach those new markets and segments at a faster pace and at a lower cost (Ficery, Herd & Pursche, 2007). In this thesis, we defined synergy as the extra and additional value and positive aspects created by the M&A which cannot be contributed by the two separate companies or individual companies. We have chosen this because it covers several definitions from others researches and this definition will be the base for comparison with the results from our case study.

Synergy might be one of the reasons for an M&A deal but in a survey by A.T.Kearney in 1998/99 it was found that half of the companies failed to attain this value creation and
instead the value was destroyed (cited in Habeck, Kröger & Träm, (2000). Lees (2003) points out that, value destruction is an unanswered question when it comes to M&A. Some blame it on paying too much for an M&A deal or overvaluing the synergy effects while most blame it on the integration process. The grass root cause and fact is that those who are responsible for the implementation are often not involved in the previous stages before the deal is made. According to Shill, Mann, Ficery & Pursche (2005) M&A have been practiced since a long time ago. Having to say that, most companies today should and already have pre-M&A and post-M&A experience. However, the companies are still having problems in capturing value and realizing synergy.

Many researchers have pointed out how crucial the integration process especially when focusing in creating synergy (Shaver, 2006). The integration process of the post-M&A phase can be the riskiest in M&A deal but it is also most often the key to success (Habeck, et al. 2000). According to Hitt, Harrison and Ireland (2001) integration is a necessity if synergy is going to be created. These are practical issues experienced by the management of companies after the M&A deal. This mainly when they have to create and realize the synergies that they had in mind when they went through M&A. We focus on the synergy creation and realization because synergy does not just happen when two companies M&A. It takes managerial action to actually make the expected synergies happen.
1.3 PURPOSE OF STUDY

The purpose of this thesis is to analyze how the management of a company create and realize synergies in the M&A process. In addition, we do intent to explore the other factors that had contributed to the value creation and the M&A integration process.

It is very essential for the management of the participating companies to realize the effects and importance of the takeover to their organization. On top of that, it is even important for the participating companies to ensure that the objective and purpose of the deal is achieved as per proposed.

In addition, we will provide a concrete and comprehensive knowledge background mainly to investigate and elaborate our understanding about the value creation and synergy realization from M&A projects and integrations. We aim to provide fruitful insights that will assist any organizations or companies in achieving success in their M&A projects.

Apart from looking into how the above process was done, we would also touch on why the merger needed to be initiated by a third party and discuss the issue of related party transactions which involved in the merger process. We would discuss on the motivation of the merger, challenges and how this could possibly be achieved by Synergy Drive.
Lastly, we would estimate in our valuation chapter on how the target prices for the merger entities and the synergy value were calculated by using Discounted Cash Flow Method.

Our study will contribute to the body of knowledge regarding the synergy realization, synergy management, critical success factors for M&A projects, business operation integration from a specific perspective, concerning on the plantation, property, and other business division of the participating companies.

1.4 ORGANIZATION OF THE STUDY

Chapter Two underlines of the Literature Review that we did for this study. The literature review focuses on the need for firms in seeking benefits and value creation through M&A as part of their corporate strategy. This section also examines the rationales behind any M&A and out of numerous motivations cited before, common motives that drive any company to join the M&A bandwagon mainly imputable to growth and expansion, synergistic factor and value creation from the M&A exercises.

Chapter Three underlines the research methodology applied in this study and Chapter Four explains in details on the pre-merger background of the participating company in the merger. We did study and examine on the similarity of the business among the company which drives to the merger integration. Chapter four also explicates in details of the background of all the three companies, Sime Darby Berhad, Kumpulan Guthrie
Berhad and Golden Hope and the business model adopted by the company and their product lines.

Chapter Five explains on the overview of industry involved by the participating companies. Among the industry are plantations, property, motor, heavy equipments and energy and utilities business. We did a compressive study on the performance of the industry prior to merger, the growth and prospects of the industry during the period. In addition to that, we did look at the competitors and the industry players, and the competitions in the industry.

Chapter Six focuses on the merger process of Sime Darby Berhad, Kumpulan Guthrie Berhad and Golden Hope by Synergy Drive. This chapter explains about merger initiation, background and explains the motivations that drive Synergy Drive to initiate the merger on the three companies. The ultimate reason underpinning the merger initiative of Synergy Drive is to grow in market capitalization, operations revenues, profitability, productivity, capabilities, skills and expertise in its business operations and core competencies building. This section examines in details the advantages of the merger in terms of business expansion factor, economies of scale and scope, product design and offer, market penetration and distribution channels factor. The analysis also focuses on the merger synergies and post merger business integration on each of the participating companies.
Chapter Seven outlines the valuation of the merger price based on Indicative Valuation Method and Discounted Cash Flow Valuation Method. This section measures the creation of value consequential from the merger exercise, of whether it brings synergy to Synergy Drive. We did also estimate and compared the value of this merger exercise. The key performance ratios are referred to in the reflection of performance of Synergy Drive (Sime Darby) after the merger. The calculations also focus on measuring the post-merger economies of scale achieved by Synergy Drive.

Chapter Eight on summary and conclusion summarize the findings in this study and propose some suggestions in which Synergy Drive should take large steps in improving some of their business operation and initiatives, human capital and technology in order to meet the expectations of their stakeholders and unit holders.
CHAPTER 2: LITERATURE REVIEW

A merger happens when two companies combined together into one entity (Sherman, 2005). Generally, in a merger, the involved companies’ shareholders will be remains as joint owners. Nevertheless, the involved companies will combine their resources in order to achieve common goals. The involved companies will become into a new legal entity (Buckley & Ghauri, 2002) while in an acquisition one of the companies will take control of the other firm’s assets. The shareholders of the acquired firm cease to be the owners and the acquired firm becomes a subsidiary of the acquiring firm (Sudarsanam, 2003). An acquisition is not only the purchase of a company but can also be the purchase of a specific plant or division or any another asset (Sherman, 2005). Normally, the acquiring firms will hold its money, assets and identity while the acquired firm will loses all its assets and liabilities. This is due to engagement with various operations as a different business entity. The concept is also related to the idea of consolidation (Ross, Westerfield & Jaffe, 2005). An example of this is when Proctor & Gamble acquired The Gillette Company in 2005 reason being they wanted to extend into the consumer product industry (Sherman, 2005). Ross et al. (2005) further stresses that the acquisitions normally have two main objectives; it is acquisition of stock or assets. The main reason and objective behind buying the stocks is to purchase the firm’s voting paying cash, shares of stocks, or other securities.

Generally, it has been practiced widely by people, who tend to use the terms mergers and acquisitions interchangeably. Having to say that, this does not pose a problem because it
is not makes sense to separate them. There is no wide distinction between a merger and an acquisition because the results are generally being considered as the same. Two separate companies with different owners that are afterwards seen as one or operating as one with shared visions (Sherman, 2005). For this thesis, we are focusing deeply on how the companies create and realize synergy. Having to say that, and as what we had stated in the problem discussion, we will use Sudarsanam’s (2003) definition; Mergers & acquisitions is when two companies are combined to achieve certain strategic and business objectives.

2.1 DEFINITION OF MERGERS & ACQUISITIONS

Mergers & acquisitions (M&A), in the broad sense, may imply a number of different transactions ranging from the purchase and sales of undertakings, concentration between undertakings, alliances, cooperation and joint ventures to the formation of companies, corporate succession/ ensuring the independence of businesses, management buy-out and buy-in, change of legal form, initial public offerings and even restructuring (Picot, 2002, p.15). However, Nakamura (2005) explains that using a broad definition of M&A could lead to confusion and misunderstanding as it entails everything from pure mergers to strategic alliance. Therefore, for this thesis, we adopt the definition of M&A in a narrower sense, as clarified below:

- Merger is the combination of two or more companies in creation of a new entity or formation of a holding company (European Central Bank, 2000, Gaughan, 2002, Jagersma, 2005).
Acquisition is the purchase of shares or assets on another company to achieve a managerial influence (European Central Bank, 2000, Chunlai Chen and Findlay, 2003), not necessarily by mutual agreement (Jagersma, 2005).

On the other hand, we do refer to the model which has been developed by Nakamura (2005) to provide clear understanding in a narrow concept about the definition of M&A. The model mentioned are as per in figure 2.1.

Figure 2.1: The definition of mergers & acquisitions Source: Adapted from Nakamura (2005, p.18)

Mergers are commonly referred to, either as ‘merger by absorption’ or ‘merger by establishment’ (Chunlai Chen and Findlay, 2003, Nakamura, 2005). Merger by absorption happens when a company buys all stocks of one or more companies (i.e.,
absorbing). The absorbed companies cease to exist whereas merger by establishment refers to the case where two or more firms are merged into a newly created entity and the combining firms in the merger are dissolved (Chunlai Chen and Findlay, 2003). According to Nakamura (2005) merger by absorption could be considered as a de facto acquisition. In addition, the term ‘consolidation’ could also be used to imply a merger by establishment (Gaughan, 2002).

However in acquisitions, the acquiring company may hunt for to acquire a significant share of stocks or assets of the target company. Consequently, there are two forms of acquisitions, which are assets acquisitions and share acquisitions (Chunlai Chen and Findlay, 2003). An asset acquisition occurs when a company purchases all or part of the target company’s assets and the target remains as a legal entity after the transaction. However, in a share acquisition, a company buys a certain share of stocks in the target company in order to influence the management of the target company. Depending on the significance of the share of stocks acquired by the acquiring company, acquisitions are then classified into three types:

- complete take over (100% of target’s issued shares),
- majority (50-99%), and
- minority (less than 50%) (Chunlai Chen and Findlay, 2003, Nakamura, 2005).

Merger and acquisition are two different types of transactions with different consequences with regards to the legal obligations, acquisition procedures, and tax liabilities (Marren, 1993). However, taking into consideration of the general view of
M&A transactions, the final outcome of the activity is to achieve synergies and value generation, which is achieved by combining their business efforts into a single entity.

2.2 CLASSIFICATION OF MERGERS & ACQUISITIONS

In the view of M&A transactions from the perspective of the value chain, M&A can be classified as horizontal, vertical or conglomerate (Gaughan, 2002, Chunlai Chen and Findlay, 2003). The horizontal M&A happens when, the acquiring and the target companies are competing firms in the same industry. According to Chunlai Chen and Findlay (2003), horizontal M&A has grown rapidly over recent years due to global restructuring of many industries in response to technological change and liberalization. This trend is observed in such industries as pharmaceuticals, automobile and petroleum. The merger of US$76 billion transaction value between the two giant pharmaceutical companies, Glaxo and SmithKline Beecham, is a good example for M&A under this category (MANDA, 2007). As Jan Leschly, the former CEO of SmithKline Beecham, said, the aim of the two parties was R&D synergies to drive revenues since in this particular industry new technologies result in enormous opportunities for revenue creation (Carey, 2000 in Harvard Business Review, 2001).

The vertical M&A are combinations of firms in client-supplier or buyer-seller relationships. The firms involved seek to reduce uncertainty and transaction costs by upstream and downstream linkages in the value chain and to benefit from economies of scope (Chunlai Chen and Findlay, 2003).
Lastly, a company may attempt to diversify risks and attain economies of scope by engaging in conglomerate M&A transactions, which involving companies operate in unrelated businesses. An example of conglomerate M&A is Philip Morris, a tobacco company, which acquired General Foods in 1985 for US$5.6 billion (Gaughan, 2002).

On top of that, M&A could also be classified as ‘friendly’ or ‘hostile’ (Chunlai Chen and Findlay, 2003). When an M&A transaction is undertaken in a friendly manner, the board of the target company agrees to the transaction. On the contrary, a hostile deal is one that pits the offer against the wishes of the target, since the board of the target refuses the offer.

Last but not least, M&A transactions could be either domestic or cross-border with regards to where the companies involved base and operate. A cross-border M&A transaction involves two firms located in different economies, or two firms operating within one economy but belonging to two different countries (Chunlai Chen and Findlay, 2003). Accordingly, in domestic M&A transactions, the firms involved originate from one country and operate in that economy-country.

The classification of M&A could then be summarized in the table below:

<table>
<thead>
<tr>
<th>Value Chain</th>
<th>Relationship</th>
<th>Economic Area</th>
</tr>
</thead>
<tbody>
<tr>
<td>Horizontal M&amp;A</td>
<td>Friendly M&amp;A</td>
<td>Domestic M&amp;A</td>
</tr>
<tr>
<td>Vertical M&amp;A</td>
<td>Hostile M&amp;A</td>
<td>Cross-border M&amp;A</td>
</tr>
<tr>
<td>Conglomerate M&amp;A</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Table 2.1: Classification of merger & acquisition transactions**
2.3 OBJECTIVES AND MOTIVES OF M&A

There are two perspectives in understanding on the objectives that companies have in order to pursue for an M&A. The objectives are to the maximization perspective of shareholders’ wealth and the managerial perspective. The first one, which is to the shareholders’ wealth maximization perspective, the firm’s decision to M&A with another company is based on the fact that companies look for the maximization of the wealth of the shareholders. The maximization of the value of the shareholder takes place when the net present value of the investment is positive. The second perspective is the managerial perspective for conducting an M&A. These can be varied such as growth reasons, to use previous underemployed abilities and skills, risk diversification and to evade being the ones being taken over (Sudarsanam, 1995).

The literature on M&A has placed a significant amount of efforts on exploring the motivation of firms engaging in M&A transactions. On the other hand, Trautwein (1990) and later Cox (2006) had provided a systematic summary of the motives, which underlay the different theories (refer to Table 2.2: M&A Motives). On the motives suggested under various theories, Trautwein (1990) noted that, M&A makers frequently refer to synergy and value creation (the deal having a positive Net Present Value) objectives to justify their actions. Unsurprisingly, there are neither claims that the motive is to achieve monopoly power nor instances where managers refer their own benefits to justify an M&A deal. Trautwein (1990) also noted that there is little evidence in both practice and research on the motives implied by the process and the raider theories. He discusses
disturbance theory as well but it is not considered in this section since M&A is then considered at the macro-economic level rather than the micro-economic (i.e., firm) level. On the other hand, Gaughan (2002) takes more practical view to identify M&A motives by referring back to theories and heavily supporting with multiple empirical case studies.

According to Gaugham, four main motives are:

- M&A is considered as a means for firms to grow quickly;
- M&A firms hope to experience economic gains as a result of economies of scale or scope;
- a larger firm as a result of M&A may have a better access to capital market, which later leads to a lower cost of capital, i.e., financial benefits; and
- M&A is aimed at anticipated gains which a firm may experience when applying its superior management skills to the target’s business.

Thus, we can conclude so as to all the three authors had harmonized that M&A is driven by many complex motives, which can vary from deal to deal and cannot be fully justified by any single theory/approach.
<table>
<thead>
<tr>
<th>Motive</th>
<th>Theory</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>M&amp;A as rational choice</td>
<td></td>
<td><strong>M&amp;A benefits</strong>&lt;br&gt;bidders' shareholders&lt;br&gt;Net gains through synergy**&lt;br&gt;Efficiency Theory**&lt;br&gt;M&amp;A is planned and executed to achieve synergies of three types: financial, operational and managerial.</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Wealth transfers from customers</strong>&lt;br&gt;Monopoly Theory**&lt;br&gt;M&amp;A is planned and executed to achieve market power. Horizontal and conglomerate M&amp;A may allow firms to cross-subsidize products, simultaneously limit competition in more than one market, and deter potential entrants from the markets, all of which result in higher market power.</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Wealth transfers from target's shareholders</strong>&lt;br&gt;Raider theory**&lt;br&gt;A raider is a person who causes wealth transfers from the stockholders of the companies he bids for in the form of greenmail or excessive compensation after a successful takeover.</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Net gains through private information</strong>&lt;br&gt;Valuation theory/Investment Theory**&lt;br&gt;M&amp;A is planned and executed by managers who have better information about the target's value than the stock market.</td>
</tr>
<tr>
<td>M&amp;A benefit managers</td>
<td></td>
<td><strong>Empire building theory/ Agency theory</strong>&lt;br&gt;M&amp;A is planned and executed by managers who thereby maximize their own utility instead of shareholders' value.</td>
</tr>
<tr>
<td>M&amp;A as process outcome</td>
<td>Process theory</td>
<td>M&amp;A decisions are outcomes of processes governed by one or more of the following influences: organizational routines, political games played between an organization's sub-units and outsiders, and individuals' limited information processing capabilities</td>
</tr>
<tr>
<td>M&amp;A as macroeconomic Phenomenon</td>
<td>Disturbance theory</td>
<td>M&amp;A waves are caused by economic disturbances: Economic disturbances cause changes in individual expectations and increase the general level of uncertainty, thereby changing the ordering of individual expectations. Previous non-owners of assets now place a higher value on these assets than their owners and vice versa. The result is an M&amp;A wave.</td>
</tr>
</tbody>
</table>

Table 2.2: Merger & acquisition motives (adapted from Trautwein, 1990 and Cox, 2006)
2.4 DUE DILIGENCE

Due diligence has throughout the recent years developed into a very familiar term and important countenance in an M&A process. During the due diligence element, the acquiring company or the advisers have the responsibility to show forward every aspect of the target company’s strengths and weaknesses. This is to verify, or in other word to ensure them that nothing is missing and enabling a deep and unbiased analysis. Having to say that, it does enlighten different problems and other obstacles that could potentially yield an unsuccessful M&A so that the acquiring company does not only find negative synergies.

The areas to acknowledge are unique and different for each M&A. Nevertheless, some are usually more likely common and more importance like confirming that the object has superior title to its materials, acknowledge intangible and tangible assets rights, ensure that the change of ownership will not have a counter effect on the business. These also confirm that all the licenses, contracts and applicable laws so that no negative surprises will occur later in the post-M&A process (Whalley & Semler, 2000).

According to Whalley and Semler (2000) there are three common risks when acquiring another business. The first one is that, companies simplify the process and only focusing on making a profit-making M&A. An M&A is usually much broader and results in gaining access to new markets, acquisition of otherwise unavailable technology, or strengthening of a competitive position etc. The focus which mainly on the making
profit-making M&A would retaliate back and consequently the buyer would fall short compare to the initial objectives of the acquisition.

Secondly, the great importance is that the acquired company will be able to continue as a strong company after the acquisition. This risk is most present when the M&A is focused on acquiring assets. If the legal entity will be alter consequently, the assignments, business contracts, and other factors that relates to business operations will also change. However it also present in other types of M&A where suppliers or customer have the right to terminate contracts or regulatory authorities can withhold business licenses and consequently harm the new organization (Whalley & Semler, 2000).

Thirdly, the acquiring companies need to adopt with strong leaders who able to control and integrate the other companies within the new organization. On the other hand, it is also important to protect the target company’s goodwill, in order to satisfy employees. Otherwise there will be always a risk that they will not get the whole organization harmonized, who supports the deal. This is because certain people who might not agree upon the new ways of working or management styles are a risk to the company. Hence in the long run, the employees who do not support the deal can infect the organization, which will spread bad morale among the work force. Even, the external parties, such as suppliers and other stakeholders might also be reluctant to support the company when new owners have arrived (Whalley & Semler, 2000).
2.5 POST M&A

In the middle of 1980s, researcher had discovered that it is relevant to understand the organizational consequences of the M&A’s. There are researchers, who had pointed out the consequence of the period following the initial M&A much earlier. However, the acceptances of the period consequences are inadequate. Lately, more strategically oriented studies have been carried out. These studies mainly concentrate on issues as how the management can bring about the anticipated or other potential synergistic benefits, create value, transfer knowledge or capabilities from one organization to another or enhance learning (Vaara, 2003).

Merging two firms into a single unit is the most important and difficulty in the M&A process (Shrivastava, 1986). It can be argued that changes and issues in the post-M&A process differ from case to case, where its deeply depend on the merging entities. What can be seen as a problem for one firm might even be an added opportunity for another firm. However, the post-M&A process do involve in taking care of earlier experiences of the two companies which is a complicated procedure (Haspeslagh & Jemison, 1991). It is complex since it involves several procedures such as creating synergy through growth or diversification, taking care of tax motives and at the same time keeping a good economic result (Gaughan, 2002). M&A’s entails that the organizational structure will be changed in different ways. The distribution of work and the tasks change, and might lead to difficulties for the employees to relate them to the new situation (Vaara, 2003).
As discovered by Larsson and Finkelstein (1999), synergy realization or expectation in a large extent very much dependent on organizational integration. In most cases, the acquiring firm is in possession of the post-M&A decisions and the learning processes that takes place (Zollo & Singh, 2004). Zollo and Singh (2004) stated that economic benefits will be offered when two organizations integrate. However, the integration does not have to be in total, though it has to be carried through to some extent.

### 2.6 THE INTEGRATION PROCESS

Value is not created until and after the integration (Haspeslagh et al., 1991). Commonly, capabilities are transferred via-versa and people from both organisations will collaborate to create the expected benefits or to discover any new business opportunities. The following part describes the integration process through what different researcher has stated within in this area.

Considering in integrating fully the new company into the large organisation, it is expected that there will be conflict arise in area of financial and human factors. However, the higher level integration achieved (assuming on stability and success of financial), the higher the chance that synergy can be aimed or developed. At the same time, a higher degree of change is expected to lead to more concern and discomfort among the employees, threatening financial goal realization. The key for management to succeed after the M&A is to minimize changes for people, apart from the changes in the systems necessary for administrative and financial control (Bijlsma-Frankema, 2004).

It a natural, where there will be always a conflict between the newly acquired company and the parent corporation. Any changes in existing policies and procedures must be handled extra carefully. It is important for the management to explain the changes clearly for the employees before they are implemented. On top of that, a sufficient time must then be allowed for a reaction and feedback from employee. Besides that, in order to minimise the worries about changes in the existing policies and procedures, managers must discuss clearly and fully the reasons behind the corporation’s policies and procedures. It is not necessary that all of the newly acquired employees agree with the policies, but they should understand what the policies about (Huang & Kleiner, 2004).

M&A’s make the communication channels grow longer and wider. This is due to the increasing employee and more people who being involved in the exercise. Moreover, due to the larger size, some employees may unintentionally get left out of the loop. Therefore, trying to maintain closer-than-usual contact is very important (Huang et al., 2004). Any M&A transaction is scenery for great uncertainty, frequent rumours, and constant decisions that change the scene gradually. Communications played as one of the key important role in ensuring the successful of integration. Clear, brief and constant communication throughout the integration process can provide decisive answers and dispel rumours. Open communication is essential, because it clarifies expectations and reduces ambiguity (Purnam & Srikanth., 2007). Unstructured communication, like frequent face-to-face interactions, avoids the disruptive consequences of administrative and cultural integration, while on the other hand enables high levels of coordination (Purnam et al., 2007).
2.6.1 The Merger & Acquisition Process

In literature, we found that the M&A process have been described slightly differently by different authors. According to Picot (2002), a typical M&A transaction goes through three phases, which starts with planning, continuous with implementation and finally integration. In the planning phase, the overall plan for the transaction is developed “in the most interdisciplinary and comprehensive manner possible” (Picot, 2002, p.16). The planning phase covers the operational, managerial and legal techniques and optimization with special regards to the two following phases. The next phase, implementation phase covers a range of activities starting from the issuance of confidentiality or non-disclosure agreements, followed with letter of intent and ends with the conclusion of the M&A contract and deal closure. The last phase is more concerned on the post-deal integration.

Picot’s explanation is relatively similar to the Watson Wyatt Deal Flow Model, which was introduced by Galpin and Herndon (2000), the two practitioners at Watson Wyatt Worldwide. However, the Watson Wyatt Deal Flow Model break down the M&A process into five smaller stages namely Formulate, Locate, Investigate, Negotiate and Integrate. They do explain that the most significant milestone is when the two transacting firms sign the agreement, finishing the deal and entering the integration stage. The first three stages mentioned above, belongs to the pre-deal phase. The ‘Negotiate’ stage represents the deal phase which ends when the above milestone is achieved. The post-deal phase only contains the last stage named as ‘Integrate’. The Watson Wyatt model includes ‘Formulate’ in the first stage which is mainly for the setting of business strategy as well
as growth strategy. However, when comparing to Picot’s model, the ‘Formulate’ step is missing in the planning phase. This is an addition in Watson Wyatt Deal Flow model, which could be considered as an attempt to give a more strategic insight into the M&A deal.

Moreover, Aiello and Watkins (2000, in Harvard Business Review 2001) suggested another model which describes the M&A process. However, their model only outlines phases within the negotiation process of the M&A deal. These phases however have been covered by the activities under the pre-deal and deal stages in the Watson Wyatt Deal Flow Model. In view of our opinion, in comparing the three representative models, the Watson Wyatt Deal Flow Model is deemed to capture the most comprehensive picture of how any M&A process are organized. Furthermore, the Watson Wyatt Deal Flow model also explained in detail on the pre-acquisition analysis of strategic fit and organizational fit, which is very crucial to the M&A process itself. Drawing from the above discussion, we had selected the Watson Wyatt Deal Flow Model the illustration of the M&A process. The model is presented in Figure 2.2 below.

![Figure 2.2: Map of merger & acquisition process](source: Adapted from Galpin and Herndon (2000, p.9))
The above model presents the stages in a linear order. However in reality, as explained and suggested by Galpin and Herndon (2000), a firm normally starts a stage when the previous one has not been completed. All the five stages are interdependent and “concurrently engineered to provide the right input and the right decision at the right time” (Galpin and Herndon, 2000, p.18). Refer to Figure 2.3 below:

![Figure 2.3: Watson Wyatt Deal Flow Model in practice](image)

**Source:** Adapted from Galpin and Herndon (2000, p.18)

M&A process are commonly being viewed as a decision making activities by most of the firms. Sudarsanam (1995) has highlighted that firms need to manage carefully and strategically on the decision making activity. This is because the decision making activity is a very complex process and even more broad in relation to M&A. Sudarsanam (1995) describe decision making process as four potentially debilitating inter-related factors, namely:

- Fragmented perspective on the acquisition held by different manager,
- Escalating momentum in decision making,
Ambiguous expectations of different managers about the benefits of the acquisition, and

Diversity of motive among managers in lending support to the acquisition (Sudarsanam, 1995, p.45).

Jemison and Sitkin (1986) had described M&A as a discontinuous and fragmented process. However, Sudarsanam’s view eventually had explain further the research done by Jemison and Sitkin(1986).

2.6.2 Post-M&A Integration

Basically, the major problem in any M&A is to integrate the participating companies into a single unit. This integration can be carried out in several different stages. The most common stage is to begin with the accounting systems. The financial system and accounting systems of the participating firms need to be combined. Besides the financial and accounting systems, a common legal platform within the participating firms needs to be developed.

Subsequent to that, the next step is the integration of physical assets, product lines, production systems and technologies. Upon integration of business assets, the process follows with human behavioral. Managing cultural differences and diverse managerial viewpoints are often considered to be the most critical part. It is not always, that all these types of integration are successfully achieved (Shrisvastava, 2006).
Generally, a common problem in M&A integration is due to the organization structure, where there are various departments in an organization. Each organization operates through various departments, and these departments are specialized in different areas. For an instance, there are departments such as production, marketing, accounting and finance. There are three main procedures of integration concerning on the various department in an organization. The main or first battle is to coordinate activities. Activities or functions of each department should be consolidated in a comfort method. This is followed with monitoring and controlling activities which enable the organization, in order to attain high quality. Lastly, the third action is to create common goals for all the departments (Shrisvastava, 2006).

The organizational integration is influenced by numerous factors which in a way makes the M&A process as a complex activity. Basically, a change in the market and organizational technological environments will eventually create uncertainties in the M&A. However, these uncertainties can be overcome accordingly by assigning specific tasks to functional groups, such as sales, purchasing, production, accounting and R&D. These groups apparently need to be integrated among each other, to reform a single business unit. It is also important to focus deeply on the nature of the technology that the participating firms use for its production. This is because, different production technologies generally requires special types of human skills and abilities. Organizational size also mediates the success of integration. A larger organization has a greater need for integration. This is because, larger firms involves in diverse units of business which need to be coordinated (Shrisvastava, 2006).
Shrisvastava (2006) had cited three different types of procedures which is important for organizations in achieving a successful integration after any M&A. The highlighted procedures are procedural integration, physical integration and managerial; and socio-cultural integration. The first procedures, procedural integration refers to actions such as combining operating activities, management control and strategic planning levels. The ultimate goal of this process is to standardize procedures which in a way help to improve communication between the merging companies. On the other hand, physical integration refers to the consolidation of product lines, production technologies, R&D projects, plant and equipment; and real estate assets. At this stage, the firm’s assets are combined and integrated accordingly to create synergist affects. The socio-cultural integration explains about the integration of decision making at various levels in an organizations. This is based on the fact that managers tend to hold their organization and its environments.

2.6.3 The Integration Process and Culture

In the context of most M&A, integration means the successful imposition of the existing culture of the acquirer or dominant merger partner on the other rather than the fusion or blending of the two (Gertsen, Söderberg & Torp, 1998). Hence, corporate culture plays an important role in any M&A. Culture is the biggest sticking point besides being the major reason for many M&A failures in creating expected value for shareholders. Success in M&A is more achievable if the target businesses fit those of the buyers as to business concepts, markets principle and culturally in terms of assignment of responsibilities and motivation of its people (Huang et al., 2004).
The culture of an organization defines the appropriate behavior, bonds and motivates individuals. The corporate culture is the culture applied inside the organization. It is the way a company processes information, its internal relations and values (Hampden-Turner, 1990). There are several different factors involved in the concept of culture, such as in which industry the company operates, its geographic location, historical events, the employee’s personalities and their patterns of interaction (Sadir & Lees, 2001). The culture also covers emotional, behavioral and cognitive elements of total psychological functioning of the members of the group (Schein, 2004).

Culture is complex area and it’s very hard to control. This makes an organization impossible to manage the process of cultural integration compared to managing integration in manufacturing and distribution processes. Thus, undergoing an M&A of two companies is a complicated task. Many organizations fail to give enough attention in culture integration aspects which in a way being the reason to integration problems and M&A failure. Managing the culture integration process effectively ensures that the merger is in the right direction. In addition, members in culture integration process adapts to each other’s different way of thinking and acting. This will result in a new culture characterized by the interaction of the two separate cultures and the desired degree of synchronization (Pribilla, 2002 cited in Picot, 2002).

Pribilla (2002) further stresses that there are four different things that cultural integration is dependent upon. Among the things are dominating behavior of the stronger company, attitudes of employees and managers toward the M&A, desired degree of synchronization
and degree of cultural freedom conferred upon the M&A. Basically, a successful cultural integration gives assurance that, the stronger the culture becomes or forms, less efforts and control is needed from the management in the future. Furthermore, if the integration has preceded well among the employees at various levels, it allows the employees to deliver more to the organizations. This is because, the employees know what is expected from them in the majority of the situations as they share the same core values, goals and directions (cited in Picot, 2002).

When companies from different countries are involved in an M&A, there is a great chance that they will experience cultural conflicts and clashes. Culture also can be defined not only at the national but also at the organizational level (Hampden-Turner, 1990). The relative weight that is placed on the issue of national versus organizational cultures as a barrier to integration will depend upon the degree to which national culture, governments and ideologies are considered to influence and shape organizational behaviour and their members’ lives (Gertsen et al., 1998).

2.6.4 The Importance of Integration in Creating Synergy

Since M&A becomes more common in order for companies to differentiate themselves from competitors the success of the deal becomes more dependent on the post-M&A stages; especially the integration process where the search for value creation is underappreciated (Chanmungam, Shill, Mann, Ficery & Pursche, 2005). Habeck et al. (2000) agreed that integration process of the post-M&A phase is most important to
success. He had described three areas (see figure 2.4) which is essential during the post-M&A process integration. The first area mentioned is that all levels of the participating organization need to buy-in to the deal, where all the levels need to be align with the direction. Secondly, for the people to support the vision there must be a sense of orientation and people must be well-informed with the organization’s directions and updates concerning to the merging activity. Lastly, all expectations need to be managed directly and communicated throughout the process.

![Figure 2.4: Three focal points of post-merger integration (Habeck et al., 2000, p.12)](image)

Habeck, et al. (2000) has developed “seven rules for success in M&A”. The seven rules basically meant for successful post-M&A integration. The rules are more like guidelines and reference in assisting firms in increase the chances for an effective integration which leads to value creation. The first rule is vision, where a combined vision is essential for the buy-in and to manage expectations. Generally, many companies look at the shaping between the companies before having a clear vision on and of what they want to achieve. The second rule is leadership, which is very important to apply consecutively to execute the vision accurately. Failure in appointing a good management team as soon as possible will lead to uncertainty. The third rule is growth, where synergies are not just cost
savings but should be prominence on market-oriented upside-opportunities. The fourth rule is early-wins, which is to beat people’s uncertainties about the M&A in achieving some early results. These early results are often used to gain reassurance, which helps to buy-in and as a motivation for working towards the long-term goals. The fifth rule is cultural differences. This is important to consider the differences cultures and how best to deal and overcome them. The sixth rule is communication, where without adequate communication it is hard to get employees committed to the M&A. Communication is important because it shows how well managers get the whole team and others to believe in their vision and mission. The seventh rule, which is also the last rule, is risk management. M&A are risky but it is important to proactively face risk. Risk management is one way of assuring and managing uncertainties which benefits for long-term growth.

According to Hitt et al. (2001), any M&A activity need to be properly integrated to create synergies that will result in competitive advantage and an increase in shareholder value. In the integration process, if there are any potential problems has been noted, essential actions need to be taken in order to prevent integration difficulties. The earlier where noted problems being solved or mitigated, the more likely the integration will be a success. In a post-M&A integration, focus should be put on creating value. Therefore the activities in the integration process are very important and should be dealt first. If the company believes the greatest value from the M&A comes from sharing customer information then the activity of integrating the customer information systems should be dealt with first of all (Chanmungam et al., 2005). When integrating two businesses to
create synergy values, they become interdependent and an adverse effect on one business will have a greater effect to the associate. This is called the contagion effect. Besides that, another effect when integrating two companies is the capacity effect. This happens because when realizing synergy, the capacity utilization is often increased which leads to a decrease in underused resources. This can be negative because the capacity constraint can make it more difficult to take advantage of positive shocks in the business environment compared to when the two companies were separate. The contagion and capacity effects indicate that even if the M&A is well implemented and creating synergy, the outcomes will not always be higher, according to Shaver (2006) the paradox of synergy.

2.7 SYNERGY

2.7.1 Definition and Types

According to Seth (1990) and Gaughan (2002), synergy and value creation is synonymous and synergy arises when the value of an M&A exceeds the combined value of the two participating firms. Lees (2003) explained, synergy represents the additional value that is created by merging two firms together. Synergy is normally used for raising capital to an M&A (Lees, 2003). When paying a premium for synergy, the company is paying for an opportunity and companies normally have a hard time identifying and capturing some synergies. According to Habeck, et al. (2000) many organizations use synergy as a synonym for cost cutting. He believes that company which has this
definition of synergy needs to be redefined. The companies should include other positive aspects of the M&A such as growth aspects and knowledge sharing. A synergy can be achieved by engaging M&A with a company that has access to a new geographic market. In addition, access to a new customer segment allowing the acquiring company to reach those new markets and segments at a faster pace and at a lower cost (Ficery, Herd & Pursche, 2007). It is very important to capture growth synergies as quickly as possible and prioritize area where cost efficiencies can be gained, and in this way synergy is an important part in the successful merger (Habeck et al., 2000). Lees (2003) believes that when two companies do an M&A, the balance is disturbed and it becomes disorganized, the energy used on markets and competition is needed to bring order back which will affect the performance of the companies.

Hitt et al. (2001) has divided synergy into three types; financial, operational and managerial synergy. The first type, financial synergy is the present value of the future profits that derives from the M&A. Meanwhile, operational synergy is the ability to create more value from the two companies via working together rather than two companies working separately. Managerial synergy refers to additional value which is created from the decision makers’ ability to integrate the two companies and create a competitive advantage. Hitt’s (2001) synergy types can be compared to Larsson’s (1990) four synergy typologies, which are market power, operational, management and financial synergy. Market power synergy happens when a company has merged into a monopoly sized company. This helps the company to increase their bargaining power, ability to charge customers more or even force suppliers to charge less. Operational synergy is
when the company due to increased scale and experience which can lower production and marketing costs. Management synergy is when the company benefits from the sharing of the two separate companies complementary or supplementary management techniques, professionalism, knowledge and talents. The last topology, which is financial synergy, is about reducing risk and lowering the cost of obtaining capital.

2.7.2 Problems with Creating Synergy

Value creation is a management’s ultimate goal in any organizations. However, it has been noted that value creation is not realized and in some cases value might even be destroyed. A.T.Kearney performed a global survey of 115 M&A transactions in 1998/1999. The result shows that 58 percent failed to attain the value goals set by the management and more than half of the M&A value were destroyed (A.T.Kearney cited in Habeck et al. 2000). M&A’s have been around for quite some time now. However, companies and managers who have experience in dealing with M&A are still failing to create synergies. According to Chanmugam et al. (2005) the reason is because M&A’s has become a mature utility. Companies find it is difficult to differentiate themselves with their bids because most of them calculate synergies similarly. Therefore they start to overestimate synergies to ensure a winning bid. Ficery, et al. (2007) points out that many synergies go unrealized because of paying too much for the M&A deal and cost. This is mainly because of a lack of understanding on what synergy is and how they can be attained. Ficery, et al. (2007) has identified six problems regarding synergies that a merging organization should avoid. The problem are defining synergies too narrowly or
too badly, missing the window of opportunity, incorrect or insufficient use of incentives, not having the right people involved in synergy capture, mismatch between culture and systems; and using the wrong processes. On the other hand, another reason why value might be destroyed is due to the organizations who want to integrate the two companies as quickly as possible. Having to say that, the integration of all the business functions are carried out with no regard on which will bring the most value, instead of focusing on value creating activities first (Chanmungam, et al. 2005). Hitt et al. (2001) point out that value can be destroyed when organization trying to create synergy because of the hidden costs which is cultural problems and inefficient integration processes. Creating synergy also comes with opportunity costs. This is because when trying to capture synergies, managers may divert the focus on the core business and neglect initiatives that might create real benefits.

### 2.7.3 Solutions to Problems with Synergy

Hitt et al. (2001) stated that there are four foundations in the creation of synergy which is strategic fit, organizational fit, managerial actions and value creation. When all the four foundations exist, the likelihood of creating synergy is substantially better. Strategic fit is the match between the two companies’ organisational capabilities. When two companies with similar capabilities, similar strength and weaknesses merge, the prospect of creating synergy is reduced. Organizational fit happens when the companies are highly compatible, meaning that they have similar management processes, cultures, systems and structure. This makes the companies easier in sharing resources, transfer or sharing
knowledge, skills and develops an effective communication. Companies without organizational fit possibly will stumble and the integration process will be stifled or prevented. Managerial actions refer to what managers do in order to realize the difference in synergies and the benefits that they convey. Creating synergy requires an active management involvement in recognizing the international issues and all other problems which associated to the M&A process. The last mentioned foundation is value creation. This is based on the basic fact that the benefits from the synergy must exceed the cost of creating and capturing synergy. Costs which are very important are the premium paid for the M&A deal, the financing of the M&A deal and the actions needed to integrate the two companies in order to create synergy. Synergy will not create value if the costs of creating it outweigh the value of the synergy.

Chanmugam et al. (2005) has through their work found an explicit value-capture strategy named lifecycle approach which managers have tried to achieve through four key drivers. The first key driver is to treat M&A as a holistic process, as a whole with interdependent parts instead of separate parts. This leads to a more successful integration process compared to the pre-deal which is treated as something separate to the post acquisition phase. The second key driver is to focus on value creation and not only integration. This explains that companies should not just integrate the two companies as quickly as possible but they should prioritize the integration activities according to the value benefits and creation. The third key driver is to accelerate the M&A planning and execution by developing an approach called the intelligent clean room. This is a concept which allows a third party to analyze the deal and integration planning is started even
before a deal is made. The fourth key driver is to use culture as a value creation tool. It is found that even managers that identify cultural issues beforehand have a hard time incorporating these issues into the integration process. Successful acquirers should perceive culture as a tool by assessing the impact of cultural differences on the M&A process, avoiding the common pitfalls and proactively use culture to create value.

Gaughan (2002) has compiled a model (see figure 2.5) of the process of realizing synergistic gains. As a start, management should carefully deal with the strategic planning because the more appropriate planning were carried out; there is a better chance to success in any M&A deals. Secondly the management needs to integrate the two companies into one. In the end synergy can be separated into revenue enhancing synergies or cost cutting synergies. During the overall process, the management team needs to be aware and ahead of what competitors might respond in different ways to the M&A deal.

![Figure 2.5: The process of realizing synergistic gain (Gaughan, 2002, p. 120)](image-url)
2.7.4 The Management of Synergy

Creating synergy could require activities such as combining similar processes, coordinating business units using common resources, centralizing support activities and solving business unit conflict. Mostly, the synergy creation is considered to be the managers’ job. Managers often underestimate these problems which connected to the integration. They do often overlook the problem of peoples acceptance in regards to the actions needed in the integration.

In the past, synergy creating has been more likely when managers have spent time and energy helping other members creating synergy, setting aside a team responsible for the actions in connection with creating synergy, forming a vision and direction in order to communicate to everyone how transactions will create synergy and form the behavior of the organisational members that are expected in order to create synergy (Hitt, et al. 2001).

Generally, managers need to recognize the synergy which is needed for the success of M&A. There might be occurring events in an industry which directly or indirectly affect the M&A success and managers should accept this and take in to count of this influence. Creating synergy to increase firm value should be evaluated relative to other opportunities and alternatives. Before the management decides on an M&A strategy, other strategies which could lead to the same business goals need to be evaluated then. Synergy creation and the actions required to realize synergy need to be talked about before the transaction takes place so that everyone knows what is expected and required.
Research has proven that the most successful M&A have happened when all four foundations (strategic fit, organisational fit, managerial actions and value creation) of synergy creation have been present. The management team needs to be committed and actively manage processes in order to create synergy because the term synergy is vague and does not happen by chance. Synergy can be created by redundancies but the management team needs to carefully consider this since knowledge is a new way of competitive advantages and redundancies might not be good for the long term.

2.8 THEORY SUMMARY

The theories have been chosen in order to enable us to answer the purpose on how the management can create and realize synergy in the post-phase of an M&A. There are theories to give an overview and necessary background data to the research such as definition of M&A, the objectives, the post-M&A phase and cultural issues. These are all important theories but in order to answer the research questions and ultimately the purpose mainly the theories on synergy and integration will be put to practice.

Gaughan (2002) has created a model that gives us as an overview of the process of realizing synergistic gains. Another model is the model by Habeck et al. (2000), on the three important areas of post-M&A integration, as it identifies that everyone in the companies need to buy-in to the deal, they need to feel that there is a sense of and that people’s expectations need to be managed. Then there are their seven rules for a
successful M&A. These seven rules emphasize on common problem areas in M&A and recommend actions to be taken in order to be more successful.

Further theories enlightened are Hitt’s, et al. (2001) four foundations of synergy creation. Forstbrook’s (2007) four key drivers and Chanmugam’s et al. (2005) value-capture strategy are more theories on how to be more successful in creating synergy. Finally there is Hitt’s et al. (2001) managerial guideline that explained the issue on the importance of good management when it comes to M&A and the creation of synergy. These theories are all relevant when it comes to analyzing our study and they will be essential for reaching an answer to our research questions on the creation and realization of synergy.
CHAPTER 3: RESEARCH METHODOLOGY

3.1 RESEARCH QUESTIONS

The merger of Sime Darby Berhad, Golden Hope Plantations Berhad and Kumpulan Guthrie Berhad was considered a unique merger exercise as it was initiated by a merchant bank, CIMB Investment Bank Berhad which via its special purpose vehicle, Synergy Drive Sdn Bhd, has proposed to acquire all the businesses including assets and liabilities of the eight listed companies in which Permodalan Nasional Berhad (PNB) and unit trust funds under its management and Employees Provident Fund (EPF) are the major shareholders. PNB and EPF are owned by the Malaysian Government which involves in direct and indirect investments home and abroad. As they are owned by the government and profit is not only the main objectives, other issues such as guarding the national interest and fulfilling the Bumiputra’s participation have been discussed/commented especially in issues of related parties’ transaction that they involved in this merger exercise.

Besides, there are issues related to each stage of the merger integration which involved nine companies namely, Sime Darby Berhad, Sime Engineering Services Berhad, Sime UEP Properties Berhad, Golden Hope Plantations Berhad, Mentakab Rubber Company (Malaya) Berhad, Kumpulan Guthrie Berhad, Guthrie Ropel Berhad, Highlands & Lowlands Berhad and Negara Properties Berhad, with different backgrounds, cultures and systems into a working unit was deemed to be time consuming and difficult to be
achieved. The process of integration requires a tedious process and plan the right framework and implementation program in order to achieve its objectives in a target time frame.

In view of factors above, we propose that this study would address the following research questions:-

- Determine the merger options, issues and why the merger via SPV’s proposal was chosen.
- Identify the main motivation of the merger.
- Examine what actually happened during the whole merger process.
- Determine how synergistic value is created through the merger.
- Investigate the impact of the integration strategies on the outcomes of the merger.
- Identify the relationship between the synergistic value and pre and post-merger performances of the merger entities.
- Explore how the merger can lead to value creation.

### 3.2 RESEARCH LIMITATIONS

The research may touch upon several issues sensitive to the decision makers within the parties involved. As the study faced limitations in terms of assessing into information sensitive to the government, PNB and the companies, the respondents were not willing to share and disclose such information.
This study is confined to the comparisons of valuations based on best practices with the offer price by Synergy Drive to the respective companies. The comparison of premium or discount price against the actual amount offered by Synergy Drive depicts the value of the merger.

The confidence level of the existing shareholders and potential investors of the merger entities were not examined in detail in this study apart from the share market response.

3.3 RESEARCH METHODOLOGY

3.3.1 Data Collection and Sampling

The collection of data is done through the interviews with the management and the relevant employees of Sime Darby (Synergy Drive), as well as a few merchant bankers. The interview with the management of Sime Darby aims at gaining insight of the merger exercise, its rationale and motivation while the purpose of interviews with the employees from their finance and research departments is obtain information of the flow of the process, in-depth analysis directing towards the decision making and the implementation process after the takeover across all relevant functional departments in the organization.

In order to obtain third party’s (independent’s) perspectives, interviews were also conducted with the participating merchant bankers namely CIMB and Public Investment
Bank Berhad, as well as analysts from KN Kenanga and CITI Bank by using another set of questionnaires.

A respective set of interviews questionnaires is as illustrated in the Appendix 1. Apart from that we also referred to the statement of income, balance sheet and statement of cash flow as our main secondary sources of financial data to support this research.

3.3.2 Methods of Valuation

Some literatures cited that to measure a merger performance, a researcher should look into two types of performance measurement, by using accounting data and market-based. Since all the pre-merger entities were de-listed, historical accounting data are used as the bases to project five years forward into the future using DCF valuation in the assessment of the companies values as against the offer price paid.

Determination of the creation of value post-merger is based on the interpretation of the key performance ratios as reflected in the financial statements of the combined entity.
CHAPTER 4: PRE-MERGER: BACKGROUND OF PARTICIPATING COMPANIES

4.1 SIME DARBY BERHAD

4.1.1 Corporate Overview

The Sime Darby Group is Malaysia's leading multinational and one of Southeast Asia's largest conglomerates. Founded in 1910, the Group has grown from a single company offering a single product and service in one country into a strong and dynamic international Group with a comprehensive range of business activities carried out by more than 28,000 employees in over 300 companies in more than 20 countries. Known for its financial and management capabilities, Sime Darby is listed on the Main Board of Bursa Malaysia Securities Berhad with a market capitalisation in excess of US$3.68 billion as at 30th June 2006.

Today, in addition to its original plantations core business activity, Sime Darby is also a major player in the motor vehicle, heavy equipment, property, and energy & utilities industries. While the core businesses are located in Malaysia, the Group has extensive trading and manufacturing interests in the People' Republic of China (including Hong Kong SAR and Macau SAR), Singapore and Australia. The Group also operates in Negara Brunei Darussalam, Indonesia, Thailand, Vietnam, the Philippines, United Kingdom, New Zealand, the Solomon Islands, Papua New Guinea and New Caledonia.
Sime Darby's Group Head Office, a 21-storey glass-fronted building, is located at the junction of two of the busiest roads in Kuala Lumpur - Jalan Raja Laut and Jalan Sultan Ismail.

![Figure 4.0: Sime Darby's Group Head Office](image)

4.1.2 Board of Directors

Led by former Chief Secretary to the Government Tan Sri Dato' Seri Dr. Ahmad Sarji bin Abdul Hamid, Sime Darby's Board of Directors comprises mainly Malaysians complemented by representatives from Singapore and Hong Kong to reflect its multi-national status.
Figure 4.1: Sime Darby Berhad’s Board of Directors
4.1.3 Sime Darby Group Business Activities

Figure 4.2: Sime Darby Group Business Activities

4.1.3.1 Plantations

The Group’s first business activity and a leading palm oil producer in Malaysia, with related activities in oils and fats and agri-foods.

i. Plantations Management

The management of approximately 80,000 hectares of prime oil palm plantation land in Peninsular Malaysia, Sabah and Kalimantan in Indonesia, as well as the production and sale of crude palm oil (CPO). The Division's activities are structured under 10 Business Units comprising estate and mill operations. A total of 8 palm oil mills are in operations to process harvested crop from the estates. Sime Darby is acknowledged as one of Peninsular Malaysia’s lowest cost palm oil producers.
ii. Oil & Fats

Kempas Edible Oil in Pasir Gudang, Johor, with a total refining capacity of 300,000 metric tonnes annually is a premier manufacturer of vegetable oil including palm and palm kernel oil and specialty fats.

Sime Darby Edible Products Ltd is an internationally reputable and reliable company operating in Singapore and supplying vegetable oil and specialty fats under various well-known brand names with over 50 years of experience in packing and international marketing. SDEPL products remain the customers' preferred choice in many domestic and overseas markets.

Morakot, Thailand’s leading manufacturer of cooking oil has a refining facility near Bangkok with a capacity of 150,000 tons per year. Its strong brand name and quality product image is a result of its modern manufacturing process and careful selection of raw materials. In addition, the "Morakot" brand is the first palm-based cooking oil in Thailand to be awarded the 'Halal' certification.

4.1.3.2 Property

Since venturing into the property business with the purchase of United Estate Projects in 1985, later renamed Sime UEP Properties Berhad, the Sime Darby Property Group has expanded its activities to include both property development, and hospitality and property project management, which are carried out in six countries in the Asia-Pacific region.
i. **Property Development**

In Malaysia, Sime UEP Properties Berhad, best known for developing the world class award-winning townships of Subang Jaya and UEP Subang Jaya (USJ), continues to be a leader in its industry with the launch of Putra Heights, its third blue-chip township in the Klang Valley.

Bandar Bukit Raja, another mega township in Klang developed under a joint venture with Consolidated Plantations Berhad, was launched in August 2002. Besides township and property development, Sime UEP is also the Project Manager for the Ara Damansara Township in Petaling Jaya, Selangor Darul Ehsan and Bandar Bukit Raja in Klang, Selangor Darul Ehsan.


In Singapore, the Property Group is currently involved in:

- **The Orion** - Standing tall at 27 storeys, Orion offers 46 exclusively designed homes comprising 3 bedroom and 4 bedroom suites, with only two units on each floor and 2 luxurious penthouses. Its stunning
architecture incorporates unique curves into its design and offers its privileged residents panoramic, unobstructed views of the pulsating heart of Orchard Road on the one hand and the lush greenery of Nassim Hill on the other.

- **10/12 Jalan Kilang**, an 8-storey private leasehold development comprising 46 strata titled units ranging from 689 sq. ft. to 2,208 sq. ft. and basement car parks, offers its occupants maximum comfort and convenience within an exclusive and conducive ambience.

ii. **Property Management**

- **Wisma Sime Darby**: Owned by the Sabah Government, the office building is leased to and managed by Wisma Sime Darby Sdn Bhd. The 22-storey office building is with a total gross built-up area (including car park) of 777,200 sq.ft and a net lettable area of 478,858 sq.ft.

- **The Kompleks Sime Darby**, located in UEP Subang Jaya, Selangor covers a total area of 24.169 acres. This commercial cum industrial complex comprises the Malaysia Region Centre, Customer Service Centre and three warehouses.

- **Sime Darby Centre** is a four-storey building located in the prime residential district of Bukit Timah.

- **Performance Centre** is strategically located along Alexandra Road, which is near to the Central Business District and has easy access to the highway.
- **PT Bhumyamca Sekawan**, in which the Group has a 49% stake, owns a leasehold Cilandak commercial estate in Jakarta and offers customised building for offices, warehousing and light manufacturing.

### iii. Hospitality

The Group is involved in the management of modern premier service apartment complexes and executive suites, most with resort style amenities, as well as a convention centre. The new **Sime Darby Convention Centre**, located in the resort setting of the Kuala Lumpur Golf & Country Club vicinity, houses the Sime Darby Human Resource Training Centre, function rooms for up to 300 persons and a convention hall for 1,200 persons.

**Darby Park Executive Suites**, Singapore, is executive luxury in the heart of the city. With only 75 suites, Darby Park Executive Suites offer personalized services to each guest.

**Rangdong Orange Court** is the only luxurious service apartment available in the scenic coastal city of Vung Tau, Vietnam. Designed and furnished for maximum comfort, the apartments provide a luxurious retreat from a hectic expatriate lifestyle.
**Quest Subiaco** offers fully equipped 1, 2 & 3 bedroom apartments in a safe relaxed environment. Ideally suited for families and executives who enjoy peaceful outer city living, whilst only 10 minutes from the CBD.

**Karri Valley Resort** is nestled in the heart of the Karri forest are secluded 2 and 3 bedroom chalets, perfect for couples, groups and families offering all the comforts of home, a fully equipped kitchen and private balcony with outdoor dining.

Bordered by the tranquil state forest, **Quest Margaret River** is situated on the entrance to this beautiful town in the heart of the Cape to Cape wine region.

**PNB Darby Park Executive Suites**, combine the practicalities of day-to-day living with the comforts of home as well as a convenient access to the prime shopping and entertainment areas of Kuala Lumpur.

### 4.1.3.3 Motor

The Sime Darby Group’s motor vehicle sales operations, previously managed according to geographical lines, have now been brought under the umbrella management of a centralised Motor Group, which will enable the operations to be carried out more efficiently in the face of AFTA. The motor companies under the Group are franchise holders for some of the world's best known marques in their respective countries. This includes moving forward with more strategic joint ventures and focusing on fostering
effective collaborative partnerships to provide superior value. In the area of joint ventures, the Group’s proven track record includes well-established partnerships with such global companies as BMW, Caterpillar, Ford, Land Rover, Mitsubishi, Hyundai and Peugeot, as well as holding one of the largest Caterpillar dealerships and BMW dealer groups in the world.

4.1.3.4 Heavy Equipment

The Sime Darby Heavy Equipment Group comprises activities carried out in Malaysia, Singapore, People's Republic of China (including Hong Kong SAR), Australia and the Philippines. The Group has exclusive Caterpillar distribution rights in the sale and rental of Caterpillar heavy equipment, parts and service support in Malaysia, Singapore, Hong Kong SAR, Brunei, The People's Republic of China (7 provinces), the states of Queensland and Northern Territory of Australia, as well as in Papua New Guinea, New Caledonia, the Solomon Islands, Nauru, Republic of Maldives and Christmas Island (Indian Ocean).

4.1.3.5 Energy & Utilities

The Sime Darby Energy Group's Engineering Services Division is headed by Sime Engineering Services Berhad, comprising companies with businesses in the oil and gas, electrical and electronics, information technology, industrial, mechanical and engineering industries. Sime Darby Engineering Sdn Bhd (SDE), the primary fabrication arm of the Division, specializes in fabrication of all types of offshore and onshore structures and complexes. SDE operates an approved Quality Management System that meets the
requirements of ISO 9001, independently audited by Lloyd's Register Quality Assurance (LRQA). SDE has proven capability and competency to deliver complete work packages, having fabricated more than 100 structures for local and international clients since its inception. Sime Engineering Sdn Bhd, an ISO 9001 certified engineering design company, is involved in the provision of project management services to upstream sectors, and engineering, procurement, construction and commissioning (EPCC) for downstream sectors of the petroleum, petrochemical and power industries. Sime Engineering is leading a consortium of companies responsible for the construction of the RM1.78 billion CW2 Package (Main Civil Works) for the Bakun Hydroelectric Project in Sarawak which started in 2002 and expected to be completed by 2007.

4.1.3.6 General Trading

A diverse range of other businesses not classified under the first five groups such as:

- **Manufacturing**

The Group's main manufacturing focus is in tyres. It has a 49% interest in Continental Sime Tyre Sdn Bhd, a joint-venture with Continental AG of Germany, which is principally involved in the marketing and local manufacturing of a wide range of tyres. Continental Sime Tyres is the holding company with its tyre manufacturing business activity carried out by its two tyre manufacturing companies - DMIB Berhad with its factory located in Petaling Jaya, and Sime Tyres International Sdn Bhd located in Alor Setar - while marketing and sales is carried out through Continental Sime Tyre Marketing Sdn Bhd. The company’s strength is best reflected in its multi-brands comprising
Continental, Dunlop, Barum, Sime Tyres and Simex. This multi-brand portfolio has comprehensive range of tyres for passenger cars, 4-wheel drive, truck, bus, motorcycle, forklift, and earthmover, agricultural, industrial and military vehicles. Continental Sime Tyre also has the largest tyre dealer network totaling over 1,000 outlets within Malaysia.

- **Travel & Tourism**

Sime Darby Travel, a leading travel agent in Malaysia and a wholly-owned subsidiary of the Sime Darby Group, has over 40 years’ experience in the business of servicing the sophisticated and discerning needs of the international travellers. In 1994, Sime Darby Travel joined Business Travel International (BTI) in recognition of the the globalisation of travel and the need to better service multinational clients on a global and regional basis. Owing to the affiliation with BTI, Sime Darby Travel is now known as BTI Malaysia - Sime Darby Travel. Products & Services include Corporate Travel, Management Information, Hotel Reservations, Global Assistance, Visa Documentation, Account Management, Conference & Incentive Leisure Travel, Car Rental Transfer, Insurance, and Miscellaneous.

### 4.2 KUMPULAN GUTHRIE BERHAD

#### 4.2.1 Corporate Overview

Kumpulan Guthrie Berhad lays claim to a distinguished history spanning 185 years and has played a major role in making the Malaysian palm oil industry the multibillion dollar business it is today. The origin of the Guthrie Group can be traced back to 1821 when
Alexander Guthrie set up an agency in Singapore, making it the first British trading enterprise in South East Asia. Incorporated on 25 November 1960, Kumpulan Guthrie Sendirian Berhad (KGSB) was initially formed to serve as the local agent for Guthrie Estate Agency Limited (GEAL). In 1965, the Guthrie Corporation Limited (GCL) was formed by the merger of plantation companies which were previously under the management of GEAL. In the same year, GCL obtained a listing on the International Stock Exchange of London and embarked on a diversification programme into the trading and manufacturing sectors in the United Kingdom, Europe and United States of America.

In 1981, Malaysian parties acquired GCL on the London Stock Exchange. In 1982, GCL’s plantation and related interests were transferred to KGSB. In 1987, KGSB was converted to a public company and renamed Kumpulan Guthrie Berhad (Guthrie). Guthrie was first listed on the Kuala Lumpur Stock Exchange which is now known as Bursa Malaysia Securities Berhad (Bursa Malaysia) in 1989, in what was then the largest public issue of shares in Malaysia. Two subsidiary companies of Guthrie, Highlands & Lowlands Berhad (54.53% was held by KGB) and Guthrie Ropel Berhad (57.85% was held by KGB), are also listed on Bursa Malaysia.

Today, Guthrie is a leading producer of palm oil. The Group plantation operations span Southeast Asia, from Kedah to Sabah in Malaysia, and from Sumatera to Sulawesi in Indonesia. The Group plantation operations consist of two divisions, Plantation Malaysia and Plantation Indonesia, which manage operations in the respective countries. Plantation
Malaysia comprises 45 estates on a total land area of 101,603 hectares with a total planted area of 98,725 hectares.

Meanwhile, Plantation Indonesia comprises 55 plantation estates on a total land area of 220,201 hectares with a total planted area of 164,124 hectares, spread over Sumatera, Kalimantan and Sulawesi. With a total plantation land bank of about 320,000 hectares in both Malaysia and Indonesia, the Guthrie Group today is one of the largest plantation conglomerates in the region.

Other than plantations, the Group has also established itself as a distinguished property developer in the country with award winning property development projects. The property operation is managed primarily through Guthrie Property Development Holding Berhad (GPDH), a 54.77% owned subsidiary of Kumpulan Guthrie Berhad. The property division has more than 16,000 acres of land bank in the Klang Valley, of which the Guthrie Corridor Visionary Communities (Bukit Jelutong, Bukit Subang, Elmina and Bukit Lagong), account for over 11,500 acres.

Its other businesses include manufacturing of medium density fibreboard, production and sale of planting materials, agricultural consultancy, resort development and ICT services. The Group also has rubber processing and trading operations in Thailand.
4.2.2 KGB Group Structure

![Kumpulan Guthrie Berhad's Structure](image)

Figure 4.3: Kumpulan Guthrie Berhad’s Structure

4.2.3 Major Business Groups

4.2.3.1 Plantations

- Plantations Malaysia

With the improving age profile of Group plantations and strengthening of operational efficiency firmly in place, Plantation Malaysia expects to achieve higher performance through higher yield and FFB production in 2007 and in the years ahead. Higher palm oil prices which so far have averaged more than RM1900 per tonne will further contribute to positive results for the Group. Realizing that technology and innovation will play a crucial role in maximizing yield, the Group has taken the initiative to accelerate the planting of clonal oil palms in the Group annual replanting programme. More Group estates will be planted with the AAB1 clonal oil palms in 2007. The first batch of clonal oil
palms planted in Bukit Cheraka Estate, Selangor in 2006 is making significant progress. The Group’s integrated ICT project, GEMAS was successfully completed at its pilot project site in Labu Mill, Negeri Sembilan. Group-wide implementation is scheduled to be completed within the first half of 2007 to further enhance efficiency in operations.

The total crude palm oil (CPO) produced in 2006 was 431,152. Initiative undertaken within the PNB Group to optimize operational efficiency resulted in the sales and purchase of FFB between the Group and Golden Hope Plantations Berhad. This arrangement benefited both parties in reducing transportation and mill processing costs. Oil yield was 4.2 tonnes per hectare in 2006 compared with only 3.6 tonnes in 2005 with a total of seven estates achieving more than 5.0 tonnes of oil per hectare.

The group was continuing in strengthening of the implementation of the five strategic thrusts, which focused on the enhancement of key areas of operations, had resulted in higher operational performance. The five strategic thrusts implemented for operational excellence are Yield Maximization, Cost Optimisation, Quality and Sustainable Practices Enhancement, Agricultural and Milling Practices Enhancement, and the Strengthening of Human Capital Development.
Plantation Indonesia

The Group titled area is 220,428 hectares spread over 56 estates. The planted area increased to 174,564 hectares in 2006 compared to 169,111 hectares in 2005. The Group operates 17 mills with a total milling capacity of 775 tonnes per hour. The total crude palm oil (CPO) produced in 2006 was 641,355 tonnes. The 2006-2010 Operations Blueprints provides the roadmap and the action plans to maximize yields, improve work efficiency, and improve quality of palm products, and reduce costs of production with emphasis on strengthening human capital capability. Yield enhancement initiatives such as soil and water conservation, better management of manuring, pests and diseases control, canopy management and other agro-techno practices have improved FFB yield and increased FFB production in the estates. In mature areas, fronds, empty fruit bunch and palm oil waste are applied in the inter-rows to provide a good source of nutrients to the palm. Through water conservation methods such as conservation pits, terraces in inland soils, a system of water-gates and flood pumps in the peat areas, optimal water levels are maintained, supplying the water requirement for the palms. Biological controls such as barn owls, beneficial plants and judicious spraying have minimized damage to the palms caused by pests and diseases.

The focus on mill cleanliness and preventive maintenance has enhanced mill processing efficiency. Potential sources of contamination and losses are eliminated by implementing good management practices throughout the processing stages. Good housekeeping practices are advocated in all the mills to
ensure mill sanitation and workers’ safety. Development of the support services and infrastructure including new mills, jetties, bulking facilities and roads to further enhance the performance of the Indonesian operations are being focused heavily. In 2006, two new mills in Kalimantan and one new mill in Sumatera have commenced construction. The construction of another new mill in Sumatera will be completed in 2008. On completion, the milling capacity in Indonesia will reach 920 tonnes per hour. The additional capacity is to meet the expected surge in crop production when most of the young matured palms move into the prime age group in the next few years. The construction of a jetty at Sungai Durian, South Kalimantan commenced in 2006 and has been completed. Various projects to upgrade field roads to all-weather roads and bridges will improve crop quality and reduce the cost of transport for both the estates and mills.

The Group will further maximize yields, improve quality and reduce costs through new initiatives adopted from its Malaysian operations such as Structured Block Supervision (SBS) and Huka-bin mechanization system for FFB transport. The SBS advocates a systematic check for all levels of management to enhance control and supervision of key field operations such as maturing, spraying and harvesting. With the on-going implementation of performance enhancement initiatives, Plantation Indonesia is in position to show better prospects in the years to come.
4.2.3.2 Property

Looking at business performance for the year 2006, the Group property operations remained focused on the development of Bukit Jelutong and Denai Alam. In a move to strengthen its position as the premium property brand, Guthrie Property Development Holdings (GPDH) unveiled the new brand name ‘Guthrie Properties’ in January 2006. This rebranding exercise coupled with an aggressive promotion and marketing drive are aimed at expanding the Group property business and market base, and essentially, to reposition Guthrie Properties as a leading and visionary property player.

The performance of the Group property business generally mirrored the modest economic conditions during the period under review. Amidst the moderation of the general property market coupled with the expectation of increase in interest rates, fluctuations in crude petroleum prices and the hike in power tariff, the property development of the Group’s associated company, GPDH continued to contribute significantly to the Group in 2006. At the operating level, Guthrie Properties registered an operating profit of RM168.05 million (2005: RM176.2 million) on a back of a turnover of RM567.8 million (2005: RM395.1 million). The sale of developed areas at Sungai Kapar Indah and Bukit Jelutong Parcel J Commercial Centre valued at RM152.8 million and RM30.6 million respectively, boosted the earnings from the property development segment of the Group.

During the year, Guthrie Properties achieved another major milestone in its mission to further strengthen the quality culture in its operations. Guthrie Properties was awarded
the Environmental Management System, EMS 14001 certification and Occupational Health & Safety Accreditation System, OHSAS 18001 certification by SIRIM Berhad for its commitment and compliance to total quality management pertaining to environmental management, occupational health and safety requirements.

The general property market outlook is expected to be positive in 2007 with property development in strategic and prime locations expected to continue to perform favorably. The township and community development in Bukit Jelutong and Denai Alam will continue to be a major source of revenue and earnings for Group Property. With the positive market outlook, Guthrie Properties is preparing for a series of new property launches in 2007 which includes high-end bungalows and Semi-Ds in Bukit Jelutong and highend products in Denai Alam. Moving forward, Guthrie Properties’ immediate to medium term growth strategies will hinge upon large and visionary development projects, development of niche and unique highend products, and other developments outside the vicinity of Guthrie Corridor Expressway. With the achievement of the three Quality certifications from SIRIM, Guthrie Properties targets to implement the Integrated Management System (IMS) by mid 2007 that will integrate the ISO 9001, EMS 14001 and OSHAS 18001 into a single system and enable projects to be implemented more effectively.

4.2.4 Board of Directors

Led by former Deputy Prime Minister, Tan Sri Dato Musa Hitam, Kumpulan Guthrie Berhad’s Board of Directors comprises mainly Malaysians.
Tan Sri Dato Musa Hitam
Chairman

Dato' Abd Wahab Maskan
Non-Independent Executive Director

Raja Tan Sri Muhammad Alias Raja Muhammad Ali
Non-Independent Non-Executive Director

Tan Sri Dato' Dr. Wan Mohd. Zahid Mohd. Noordin
Non-Independent Non-Executive Director

Datuk Nik Mohamed Affandi Nik Yusoff
Non-Independent Non-Executive Director

Datuk Mohamed Adnan Ali
Non-Independent Non-Executive Director

Datuk Alladin Hashim
Non-Independent Non-Executive Director
4.3 GOLDEN HOPE

4.3.1 Corporate Overview

Golden Hope Plantations Berhad is a company steeped in history with significant highlights that have helped chart its course on the local and global arena. From being a part of the Harrisons & Crosfield empire which had its beginnings in 1844, to the present day, the company has grown from strength to strength be more than just a plantation player. The history of Golden Hope Plantations Berhad dates back to 1844, the year where brothers Daniel and Smith Harrison and Joseph Crosfield formed a tea and coffee trading partnership called Harrisons & Crosfield, in Liverpool, England.
Golden Hope's solid 161-year foundation is reinforced by the key strategies and corporate values. Golden Hope is one of Bursa Malaysia's top 30 companies based on market capitalization and was named as one of the Top 200 companies in Asia Pacific by Forbes Asia. The group owns a plantations landbank of 190,000 ha and deals mostly in oil palm and palm oil products. Golden Hope is the first Malaysian public-listed plantations company with downstream refineries and activities in oils & fats industry in Europe and South Africa. A founder member of the Roundtable on Sustainable Palm Oil (RSPO), the global environmental awards include the Forest Stewardship Council Certification (FSC), ISO 9001, ISO 14001, OHSAS 18001, Chain-of-Custody (COC) and HACCP. They are also the first plantation company in Malaysia to receive the Global 500 Award by the United Nations Environment Programme (UNEP) for their “Zero Burning” practices.

Golden Hope has now transcended boundaries and transformed into a global integrated oil palm company with the downstream refineries and activities in the oil & fats industry. Golden Hope currently operates in numerous countries around the globe, namely Bangladesh, China, Germany, Indonesia, the Netherlands, South Africa and Vietnam. Its oleochemicals business had taken the company into various continents like Americas and Europe.

Figure 4.5: Golden Hope’s Business
4.3.2 Main Business Group

4.3.2.1 Plantations

It was a dawning of a new era for the Plantations Division with the relocation of the office to Carey Island on November 14, 2005. All six departments – Estates Operations, Mill Operations, Human Resources and Administration, Total Quality and Environment Management, Engineering Services and Security made the shift from Menara PNB, Kuala Lumpur. The new office, a single storey building on stilts, is located about seven kilometers from the island’s bridge. Erected on a 11.32 ha land, the Istana Jugra-inspired building was designed to conform with the existing island’s heritage. The relocation is in line with Golden Hope’s business strategy to enhance operational efficiency by grouping all divisional departments and units under one roof. Closer proximity to the estates and oil mills will also promote greater interaction and speedier decision making. This historic move will see a reduction in the Company’s overhead cost especially on office rental and utilities. A total of 60 executives and 52 non-executives were involved in this relocation exercise.

In a bid to further enhance efficiency in managing estates and mills, the Group revamped the organizational structure of Estates Operations Department. Under the new structure effective January 1, 2006, operations of both estates and mills in the Peninsular were regionalized into three regions – Northern, Central and Southern, each headed by its own General Manager. Both the Southern and Central regional offices have already been set-up in Linsum and West Estates respectively whilst the Northern regional office will soon
be located in Sungai Wangi Estate. Regionalization will reduce the number of tiers in the management hierarchy and allow for greater focus on individual estates and mill operations. The move is designed to empower those who are dealing directly with day-today operational matters to make quick decisions on the ground. Implementation of recommendations can also be closely monitored.

The Group's relentless march towards achieving Vision 30: 25:30-tonne fresh fruit bunch (FFB) per hectare and 25% oil extraction rate (OER) by the year 2010 remains on track. Upgrading works in the AEB estates is near completion and the group expects a significant boost in yields in the coming years. The yield from the GH400 Series has been particularly encouraging and with the large scale planting of the latest GH 500 series, future FFB production can be expected to climb steadily to meet the vision 30:25, 35:25 and 40:25 by the year 2010, 2015 and 2020 respectively.

4.3.2.2 Oil & Fats

The Oils & Fats Division offers the customers the best in kind. The group is offering more than just products; in fact they are offering business solutions worldwide for products such as bakery fats, low saturated fats, trans-free fats, animal fats replacer (healthier alternative) and other ingredients. As an ongoing and healthy striving business, the group currently has production facilities in numerous countries across the globe. These include in Malaysia (Golden Jomalina, Austral Edible Oils), Vietnam (Golden Hope-Nha Be), the Netherlands (Unimills), and South Africa (Hudson &Knight). The division has also formed joint venture partnerships with business related companies in
Bangladesh (Bangladesh Edible Oils), Morocco [Afia Edible Oils (formerly known as Savola Edible Oils)] as well as Cognis Malaysia for the oils & fats businesses that focus on market needs on differentiated specialty products. In view of the high economic growth rates and potential markets from regions such as China and India, the division is currently exploring alternative business opportunities in the said regions by establishing new strategic alliances and partnerships in all facets of the Division’s business activities, i.e. manufacturing, marketing,

The continued growth of the oleochemicals market offered opportunities for the Oils & Fats Division to further realize its strategy to add value to its palm products, together with Cognis, joint venture partner of over 20 years. In line with the group’s key strategic focus towards increasing their global presence and strengthening the oleochemicals business, in February 2006, the division marked yet another milestone in its global expansion plan. This was the finalization of the acquisition of Cognis Deutschland GmbH & Co KG’s (Cognis) global oleochemicals and derivatives businesses. The new acquisition has resulted in expanding interest in the Cognis global operation with presence in Europe, USA, Canada, the Far East and Latin America through the Group’s 50% equity in Cognis Oleochemicals Malaysia Sdn. Bhd. The group also has extended their market presence in North Africa with the equity acquisition of a new start-up company in Morocco through strategic alliance with Afia Edible Oils (formerly known as Savola Edible Oils) of Saudi Arabia. The conglomerate has vast experience in the marketing and distribution of the oils and fats consumer products especially in the Middle East.
4.3.2.3 Property

Golden Hope’s property division had completed three main projects for last year, 2006. Among the project are the Kuala Langat District Office at Sg Sedu, Banting, TESCO Hypermarket at Saujana Impian, Kajang and Puteri Nursing College at Kota Seriemas, Nilai, Negeri Sembilan. Another major accomplishment is the recently completed international standard Indoor Bowls Stadium at Kota Bayuemas, in Klang, Selangor. As an ongoing effort to develop potential land bank value, the group are now in negotiation stages for the construction of Kolej Kemahiran Tinggi MARA on a 70-acre site at the New Lunderston Estate in Banting, Selangor.

The Group’s Landbank Management Unit, will continue to enhance estate value by tapping its property development potential. Though no longer an active physical participant, it remains involved in numerous business arrangements, such as sales of development land plots and joint ventures in order to create Group land value enhancement. A positive example was a joint agreement to develop 133-acres of Mostyn Estate in Kunak, Sabah by Golden Hope Properties Sdn. Bhd. The Land bank Management Unit also played a pivotal role in the Conservation Planning of Carey Island. The island is one of the first islands developed for agriculture in the late 1800s. In view of this, Golden Hope’s property division is currently undertaking restoration works on numerous Badan Warisan Malaysia recognized historical buildings. On top of that, the Facility Development and Management Unit manages the Group’s sports and resort facilities. Among the facilities and resorts are the Impian Golf and Country Club, Impian Court Condominiums and the Bayuemas Oval, an internationally accredited cricket pitch.
The Impian Golf and Country Club was proclaimed the golf course of choice for the PGA Tour for the year 2004 by the Malaysian Professional Golfers’ Association. With the additional landscaping features, Impian Golf and Country Club course is rated the best in the country recently. In addition, to complement the golf course, a new driving range has been developed at Saujana Impian. The Carey Island Golf Club is one of the oldest golf clubs managed by the Group.

The Group’s international standard cricket pitch known as Bayuemas Oval and the Akademi Kriket Melayu Tuanku Jaafar celebrated its first anniversary on 21 February 2005. The Group’s contribution to the development of sports in the country did not end with the construction of the Bayuemas Oval. The group has embarked on another project which is the in-door lawn bowls stadium.

4.3.2.4 Other Business

- Harvik Rubber Industries

Harvik has re-energized the business by making the switch from non-safety rubber boots to safety boots manufacturing. The group’s safety boots include fire fighting boots, chainsaw cut-resistance and mining boots and industry boots. Today, the group has established as one of the top manufacturers of the fire fighting and chainsaw boots in the world. Rubber division sales volume has increased to RM25.5 million from RM23.7 million recorded recently. Contribution from the PVC division is approximately RM10 million, mainly from Harvik’s production of 500,000 pairs of
PVC footwear for BATA UK during the year. Currently, Harvik’s boots are exported to countries such as Russia, South America, South Africa, Middle East, Canada, United States of America and Europe. The group’s reputation as one of the top manufacturers of safety boots is further sealed with several new tenders won for the fire fighting boots supply to new markets such as Taiwan, Turkey, Lebanon, Egypt and etc.

- **Kapar Coconut Industries**

  Kapar Coconut Industries (KCI)'s maintained productions of Coconut Milk Powder (CMP) and Low Fat Desiccated Coconut (LFDC). Due to stiff competition in both local and global markets, the unit are now focused on minimising the impact of falling prices and increased costs by implementing resolute business strategies. Based on these plans to improve margins, KCI will soon embark on various diversification programmes which is producing coconut beverages, frozen pasteurised coconut milk, low fat desiccated coconut biscuits and coffee creamer. KCI products are currently exported to Europe, United States, Taiwan, Hong Kong, Japan, Saudi Arabia, Australia, Canada, Pakistan, Caribbean Islands and Singapore.

- **Golden Hope Food & Beverages**

  Formerly known as Centrifugal Process Sdn. Bhd., and name was officially changed to Golden Hope Food & Beverages Sdn. Bhd. (GHF&B). The rebranding of the name was made due to the streamlining of plantations, processing and trading operations. GHF&B sold 4,140 tonnes of puree during the first 11 months compared to 1,926
tonnes for the whole of last year, a remarkable 114% sales increase. The turnover recent year was higher, RM10.9 million (4,140 tonnes) compared to RM3.8 million in 2004/2005. The hectare was increased from 130 hectares to 506 hectares. Good agricultural practices have resulted in higher guava fruit yield. The group also recorded a yield of 53 tonnes per ha. With Europe as the main market, the business units are now exploring new areas of growth, either direct or through agents, to countries such as New Zealand, Philippines, Indonesia and Bangladesh. The group are anticipating that pink guava puree production to rise to 12,000 tonnes in 2007/08. With this increase, it will set to capture approximately 30% of the world's pink guava puree export market.

4.3.3 Board of Directors

Led by former Chief Secretary to the Government Tan Sri Dato' Seri Dr. Ahmad Sarji bin Abdul Hamid, Golden Hope's Board of Directors comprises mainly Malaysians.
Figure 4.6: Golden Hope’s Board of Directors
CHAPTER 5: INDUSTRY OVERVIEW AND MERGER INITIATIONS

5.1 PALM OIL INDUSTRY

Since all the participating companies involved mainly in plantations business in Malaysia and Indonesia, we focus our review on the palm oil industry in Malaysia and Indonesia.

5.1.1 Overview of the Malaysian palm oil industry

a) Performance for the year 2006

The Malaysian oil palm industry recorded an impressive performance in 2006. Export earnings of oil palm products rose to a record RM31.8 billion, while palm oil stocks declined and prices firmed up sharply especially during the last quarter of the year. The industry also saw exciting developments shaping up in the local biofuel industry with the Honourable Prime Minister of Malaysia launching the Envo Diesel (palm olein blend with diesel) and the first integrated palm oil biodiesel plant using MPOB technology in March and August 2006 respectively.

The production of CPO increased further by 6.1% to 15.9 million tonnes in 2006 from 15.0 million tonnes the previous year. The increase was mainly attributed to the expansion in matured areas by 2.0% and rise in the average FFB yield per Ha by 3.8% to 19.6 tonnes due to better management and agricultural inputs. The oil yield per Ha saw a 3.4% year-on-year increase to 3.9 tonnes, despite the OER declining marginally by 0.5% to 20.04%. CPKO production rose by 6.1% to 1.96 million tonnes in tandem with a 4.1% growth in PK production.
The total exports of oil palm products, constituting of palm oil, PKO, PK cake, oleochemicals and finished products increased by 8.1% or 1.51 million tonnes to 20.13 million tonnes in 2006 from 18.62 million tonnes recorded in 2005. The total export earnings also increased by 11.2% or RM3.23 billion to RM31.81 billion compared to RM28.60 billion in 2005. All the oil palm products registered export volume increases in 2006 compared to the previous year, led by oleochemicals with an increase of 17.7%, followed by PKO, finished products, palm oil and PK cake. The higher export demand for oleochemical products in 2006 was boosted by the lower price oleochemical-based products vis-à-vis petroleum-based products. The increased of exports of CPO by 46.7% to 2.36 million tonnes also helped increase exports of palm oil. The lower PKO prices as a consequence of lower lauric oil prices helped boost export demand for the product.

Exports of palm oil increased by 7.1% to 14.40 million tonnes compared to 13.45 million tonnes in 2005. China maintained its position as the biggest export market for Malaysian palm oil for the fifth consecutive year with off takes totalling 3.58 million tonnes or 24.9% of total palm oil exports, followed by the EU 2.58 million tonnes (17.9%), Pakistan 0.96 million tonnes (6.7%), USA 0.68 million tonnes (4.8%), India 0.56 million tonnes (3.9%), Japan 0.52 million tonnes (3.6%) and Bangladesh 0.44 million tonnes (3.1%). All the countries, accounted for 9.32 million tonnes or 64.7% of total Malaysian palm oil exports in 2006. The increase in palm oil exports was mainly to China which registered an increase of 0.62 million tonnes or 21.0%, followed by the EU (+0.31 million tonnes or 13.5%), Vietnam (+0.13 million tonnes
or 88.4%), USA (+0.13 million tonnes or 22.4%) and Jordan (+0.10 million tonnes or 204.4%).

The abolishment of the Tariff Rate Quota effective 1 January 2006 for vegetable oils coupled with the price competitiveness of palm oil against soya bean oil had a very significant impact on Malaysian palm oil exports into China. Higher demand for palm oil in the EU came from both the edible and non-edible sectors. The lower import duty on processed palm oil in line with Asean Free Trade Area (“AFTA”) Commitment was the contributing factor for increased exports to Vietnam. The higher import volume to the USA was driven by the new trans-fat labelling law which came into effect on 1 January 2006, while exports to Jordan increased mainly due to re-exports to the Iraqi market.

Exports of PKO increased by 9.7% from 0.85 million tonnes in 2005 to 0.93 million tonnes in 2006. The USA was the major market for PKO in 2006 with 0.23 million tonnes, followed by EU (0.13 million tonnes), China (0.09 million tonnes) and Japan (0.06 million tonnes).

Exports of PK cake increased by 4.5% to 2.12 million tonnes from 2.03 million tonnes in 2005. The major PK cake markets were the EU (1.55 million tonnes or 72.8% of total PK cake exports), South Korea (0.25 million tonnes or 11.7% of total PK cake exports) and New Zealand (0.17 million tonnes or 7.8% of total PK cake exports).
The major markets for oleochemicals were the EU, China, USA and Japan. The major oleochemical products exported are fatty acids, followed by soap noodles and fatty alcohol.

Exports of finished products increased by 7.4% to 420,319 tonnes from 391,389 tonnes in 2005. The major markets for palm oil finished products in 2006 were Kuwait, Pakistan, Saudi Arabia, UAE and Russia. The major products exported under this group were shortening.

Palm oil stocks closed at 1.51 million tonnes, a drop of 0.1 million tonnes or 6.1% compared to the previous year’s closing level of 1.6 million tonnes. The main factor for the decline was the sharp fall in CPO production by 26.3% or 407,605 tonnes in December against the previous month because of the massive floods that disrupted harvesting in some of the major oil palm growing areas. However, PKO closing stocks rose by 54.6% to 0.36 million tonnes due to larger availability of supplies.

The average prices of oil palm products in the domestic market recovered in 2006. Positive market sentiments arising from the anticipated demand from the biodiesel industry coupled with higher soya bean oil prices were the contributing factors for the upward trend in palm oil prices. In addition, the rise in world crude oil prices also spurred local palm oil market sentiments.

The average CPO price increased by 8.4% or RM116.50 to RM1,510.50 in 2006
against RM1,394.00 the previous year. Prices which traded in a narrow range during the first 9 months of 2006 subsequently traded higher during the last quarter of the year. The lowest and highest monthly average price recorded was in June and December at RM1,397.00 and RM1,865.00 respectively. In line with the firmness of local CPO prices, the average export price for processed palm oil products also increased, namely, Refined, Bleached & Deodorized (“RBD”) palm oil by RM80.00 or 5.5% to RM1,534.00; RBD palm olein by RM124.50 or 8.3% to RM1,621.50; and RBD palm stearin by RM198.00 or 15.3% to RM1,496.00.

The average price of PK in 2006 declined by 12.3% or RM125.00 to RM892.00 from RM1,017.00 the previous year. Prices softened during the year due to the strong growth in production, higher stock levels and lower CPKO prices in the domestic market. The average price of CPKO declined in 2006 owing to increasing domestic supplies and lower lauric oil prices in the world market as a consequence of a recovery in world coconut oil production. The average price fell 12.6% or RM275.50 to RM1,907.50 in 2006 from RM2,183.00 the previous year. In the case of FFB, the average price at 1% OER rose in tandem with the higher CPO price by 5.8% to RM15.40 from RM14.55 the previous year.

(Source: MPOB website at www.mpob.gov.my)

b) Performance of 1st half of 2007

CPO production decreased by 8.0% during the first 6 months of 2007 (January-June 2006: 1.3%) due to lower FFB yields on account of “tree stress” peak production in
late 2006 and lower output from flood-affected areas in early 2007. FFB yields declined 9.7% to 8.2 tonnes per Ha (January-June 2006: 9.1 tonnes per Ha) in the first 6 months of 2007. However, the OER for the same period improved to 20%.

The average CPO price for the first 7 months of 2007 registered an increase of 60.4% to RM2,266 per tonne as against RM1,413 per tonne in the corresponding period of 2006. The local delivered CPO price soared to an all-time high of RM2,886 per tonne in June 2007. The surge in the price of CPO was largely due to tight supply and increasing global demand for edible oils and biodiesel as well as increased prices of substitutes, particularly soya bean and rapeseed oils.


5.1.2 Palm oil industry growth in Malaysia and Indonesia

a) Malaysia

The growth of the palm oil industry in Malaysia for the past 3 years from 2004 to 2006 is set out below in the following tables:

<table>
<thead>
<tr>
<th>Plantation Area (000 Ha)</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mature</td>
<td>3,451</td>
<td>3,631</td>
<td>3,703</td>
</tr>
<tr>
<td>Immature</td>
<td>424</td>
<td>420</td>
<td>462</td>
</tr>
<tr>
<td>Total planted</td>
<td>3,875</td>
<td>4,051</td>
<td>4,165</td>
</tr>
</tbody>
</table>

Table 5.0: Total oil palm plantation area in Malaysia

<table>
<thead>
<tr>
<th>Yield (MT/Ha)</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>FFB</td>
<td>18.60</td>
<td>18.88</td>
<td>19.60</td>
</tr>
</tbody>
</table>

Table 5.1: Yield of FFB in Malaysia
### Table 5.2: Production of CPO and PK in Malaysia

<table>
<thead>
<tr>
<th>Production (000 MT)</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPO</td>
<td>13,976</td>
<td>14,962</td>
<td>15,881</td>
</tr>
<tr>
<td>PK</td>
<td>3,661</td>
<td>3,964</td>
<td>4,125</td>
</tr>
</tbody>
</table>

### Table 5.3: Extraction rate of palm oil in Malaysia

<table>
<thead>
<tr>
<th>Extraction Rate</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>OER (%)</td>
<td>20.03</td>
<td>20.15</td>
<td>20.04</td>
</tr>
<tr>
<td>KER (%)</td>
<td>5.25</td>
<td>5.34</td>
<td>5.20</td>
</tr>
</tbody>
</table>


A summary of the distribution of oil palm plantation areas in Malaysia over the past 3 years from 2004 to 2006 is set out below:

### Table 5.4: Distribution of Oil Palm Plantation Areas

| Distribution of oil palm plantation area in Malaysia (As a % of total planted area in Malaysia) |
|---------------------------------------------------------------|-----------------------------------------------|
| Area \ Years                                                  | 2004  | 2005  | 2006  |
| Peninsular Malaysia                                           | 57%   | 57%   | 56%   |
| Sabah                                                        | 30%   | 30%   | 30%   |
| Sarawak                                                      | 13%   | 13%   | 14%   |
| Total                                                        | 100%  | 100%  | 100%  |

(Source: Malaysian Oil Palm Statistics 2006 (26th Edition))

### b) Indonesia

The palm oil industry in Indonesia is driven by the rising global demand for vegetable oils for food and other industrial applications. The palm oil industry in Indonesia grew significantly during the 1990s, becoming a major influential factor not only in the Indonesian economy but also in the global oils and fats market.
Oil palm is grown in 17 provinces in Indonesia, directly employing approximately 2 million workers and farmers. In 2006, Indonesia’s CPO production was estimated at 14.7 million tonnes (valued at USD6.1 billion), an 8% increase over the 13.6 million tonnes produced in 2005.

In recent years, palm oil production in Indonesia has increased rapidly, partly driven by increases in planted area, but more by improvements in oil yield per hectare. However, the average annual CPO yield in Indonesia is still currently only 2.86 tonnes per Ha. This is mainly due to the relatively larger area of younger and immature planted area in Indonesia. As this area matures, oil yield is expected to increase, and this will be a significant driver for increased production going forward.

The total planted area of oil palm has been steadily growing in Indonesia. Starting from around 600,000 Ha in 1985, the total area reached around 2.8 million Ha in 1998 and over 5.5 million Ha in 2006. Mature plantations accounted for more than 80% of the total planted area. The development of the oil palm sector in Indonesia is mainly export-driven, with key export markets being India, the Netherlands, China, Pakistan, Bangladesh, UK and Malaysia. In 2005, total export of palm oil was estimated to be over 10 million tonnes. In 2006, exports increased by 9.3% reaching 11.3 million tonnes and valued at USD4.7 billion. This includes CPO and processed products such as RBD palm oil, RBD palm olein and RBD stearin. Demand from Indonesia’s rising oleochemical and soap industries have also been on the rise recently. There has been an increase in long term agreements and joint ventures
between multi-national specialty chemical companies and Indonesia’s plantation companies. The main driver for this market trend has been the shift to vegetable-based raw materials within the oleochemical industry, with total domestic demand in 2005 and 2006 over 3.5 million tonnes and 3.7 million tonnes respectively. CPO consumption is also expected to be driven by demand from the biodiesel industry.

(Source: Industry Overview Report for Oil Palm Upstream Market in Indonesia, Frost & Sullivan 2007)

5.1.3 Growth prospects

a) Malaysia

Production of CPO in 2007 is projected to record lower output of 15.7 million tonnes (2006:15.9 million tonnes). Output of palm oil is expected to increase by 2.0% following improved yields and expansion in matured areas. In addition, measures taken to achieve vision 35:25, a target of 35 tonnes per hectare of FFB and 25.0% OER through the wide use of high quality seedlings and latest technology as well as knowledge-based production systems will result in higher output of palm oil. The new matured areas coming onstream, better estate management and higher quality agricultural inputs are expected to partially offset the negative impact of unfavorable weather. Higher oil palm prices are expected to encourage better efficiency in oil palm harvesting.

The global stock of palm oil is expected to decrease in 2007 due to lower supply and increased demand from major markets in particular China, coupled with higher
demand from the biodiesel industry.


It is forecasted that there will be stronger than expected demand for edible oils from India and China in 2007, which has not been accounted for by major oil palm producers. On 23 July 2007, the Indian government announced further reductions on import duties for all vegetable oils. With this exercise, the import duties on crude and refined palm oil came down to 46.35% and 54.08% respectively. The reduction was anticipated in view of the global supply of palm oil is expected to decline by between 2.5 to 3.0 million MT. This is positive for palm oil as it enhances palm oil’s competitiveness against soybean oil in India.

(Source: Malaysian Palm Oil Council website at www.mpoc.org.my)

Malaysia remains the leading palm oil producer and exporter, and efforts were taken to enhance value added activities in the industry. In this regard, the Biofuel Bill was passed in 2007 to kick-start the biodiesel industry. In addition, a RM500 million Biodiesel Fund was established to promote the production and use of biodiesel. As of 28 March 2007, approval was granted to 9 companies and the projects are currently at various stages of implementation.


Projection of higher world demand for vegetable oil and fats and palm-based biofuel industry as well as tight supply are expected to push CPO prices to higher levels.
In addition, Indonesia, the world’s second largest producer of CPO after Malaysia, restricted exports of CPO by imposing higher export duty to meet local demand of cooking oil. India, one of the world’s largest edible oil importers, slashed import duties on crude and refined palm oil as part of the efforts to contain rising inflation. In the USA, more food producers and fast-food chains are switching to trans-fatty acid-free oil such as palm oil. Following the ban by New York City on the use of trans-fatty acids in eateries effective 1 July 2007, other cities in the USA are expected to take similar action. These developments will have positive impact on the price of CPO which is estimated to remain high at RM2,400 per tonne in 2007 (2006: RM1,503 per tonne).


b) Indonesia

Palm oil production is rising in Indonesia at a rate of 5% to 8% per annum. Frost & Sullivan estimates that CPO production in Indonesia will exceed 19 million tonnes per annum by 2010. There are 11 million Ha of palm oil plantations worldwide. Of these, 5 million Ha are found in Indonesia and 4 million Ha in Malaysia alone. Future plans for palm oil plantations in Indonesia include planted areas of up to 20 million Ha. Indonesia is ideal for palm oil cultivation in terms of soil and climate conditions, with the added advantage of competitive labour costs in the country. All these factors have contributed to the excellent growth of the industry during the past 3 decades. The future prospect of the industry is highly promising, with demand driven by the food and industrial sectors in Indonesia, as well as growing demand for CPO products.
worldwide. The growth in the industry is also expected to be further accelerated by
demand from the emerging biodiesel industry.

(Source: Industry Overview Report for Oil Palm Upstream Market in Indonesia,
Frost & Sullivan 2007)

5.1.4 Industry players and competition

At the global level, the major palm oil producers and their respective CPO production
output (in MT ’000) over the past three 3 years are presented in the following table:

<table>
<thead>
<tr>
<th>Year</th>
<th>Malaysia</th>
<th>Indonesia</th>
<th>Others</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>13,976</td>
<td>12,350</td>
<td>4,583</td>
<td>30,909</td>
</tr>
<tr>
<td>2005</td>
<td>14,962</td>
<td>14,070</td>
<td>4,700</td>
<td>33,732</td>
</tr>
<tr>
<td>2006</td>
<td>15,881</td>
<td>15,900</td>
<td>4,952</td>
<td>36,733</td>
</tr>
</tbody>
</table>

Table 5.5: Major Palm Oil Producer

(Source: Malaysian Oil Palm Statistics 2006 (26th Edition))

As increasingly more oil palm estates are developed, lands for new developments are
increasingly more difficult to procure, resulting in higher land prices and increases in the
cost of development of land. The availability of labour is another concern in the
Malaysian palm oil industry. Both these factors have caused an increase in the
production cost per tonne of palm oil.

a) Malaysia

We did a comparison against the major oil palm plantation industry players by
planted area in Malaysia. Refer to table below:
No. | Name                          | Planted area (Ha) |
---|-------------------------------|------------------|
1. | FELDA                         | 690,054          |
2. | Synergy Drive                 | 520,067          |
3. | IOI Corporation Berhad        | 144,055          |
4. | Kuala Lumpur Kepong Berhad    | 123,462          |

Table 5.6: Major Palm Oil Plantation (Planted Area) in Malaysia

(Sources: FELDA website at www.felda.net.my, Respective annual reports 2006 of GHope Group, KGB Group and Sime Darby Group.)

In addition, palm oil faces competition from other edible oils, in particular, soya bean oil, rapeseed oil and sunflower oil. Currently, the production costs per tonne for these substitutes are comparatively much higher than that of palm oil although the former may be reduced in line with advances in research including genetic modification technologies. Amongst all the oil bearing plants, the oil palm provides the highest yield and at a lower cost of production. However, whilst other countries are more likely to subsidize their oil seed crops, palm oil is heavily taxed in Malaysia. Nonetheless, the palm oil industry is expected to continue to remain competitive.

b) Indonesia

Up until March 2006, Indonesia had nearly 300 oil palm plantations spread over some 16 provinces. About 240 of these are located in the northern parts of Sumatra and nearly 40 in Kalimantan.

The larger plantations normally incorporate their own CPO milling facilities, while
the smaller plantations sell the palm oil bunches to neighboring plantations or millers. There are a number of large players in the CPO business, who collectively command more than 50% of planted areas in Indonesia, namely PT Smart, Raja Garuda Mas, Astra Agro Lestari, Minamas Plantation, Indofood Agri Resources, Agro Indomas, PP London Sumatra, Pacific Rim Palm Oil Pty Ltd, PT Bakrie, SIPEF Group, Socfin Group, Wilmar International Limited, Musim Mas, Asian Agri, and Perkebunan Nusantara. The Perkebunan Nusantara plantation is a government plantation arm constituting the largest majority of planted palm oil area, with an estimated 600,000 Ha. The next largest planted areas of approximately 320,000 Ha and 280,000 Ha are owned by Raja Garuda Mas and PT Smart respectively.

(Source: Industry Overview Report for Oil Palm Upstream Market in Indonesia, Frost & Sullivan 2007)

5.2 PROPERTY INDUSTRY

As a result of the concentration of the operations of the Property division in Malaysia, the industry review below is focused on the property market in Malaysia.

5.2.1 Overview of the property industry in Malaysia

Activity in the residential segment grew at a moderate pace (in 2006) as demand eased following the strong performance in previous years. This was reflected in the moderation in loan applications during the year. Housing developers also responded to changing
market conditions by reducing launches of new properties and adapting to the changing requirements of consumers. Despite these efforts, the overhang of residential properties increased to 28,827 units by end-September 2006. In line with the overall market conditions, the Malaysia House Price Index rose at a more moderate pace of 2% in the first half of 2006. Despite the overall cautious attitude of the consumers, demand for residential properties near the city area remained strong.

During the year (2006), the Government undertook a number of important measures to facilitate the growth of the residential segment. The Strata Title Act and related bills were amended in December 2006, to enable a faster and more transparent approval process for strata titles, as well as to provide clearer oversight of property managers on the management of funds collected and disbursed. Amendments were also made to the Housing Development Act, whereby the Certificate of Fitness for Occupation, previously given by the local authorities, will be replaced with the Certificate of Completion and Compliance (“CCC”). The CCC will be issued by private architects and engineers, thus facilitating early occupation of buildings. The Government also liberalized rulings on foreign ownership of residential properties. Foreigners no longer need to obtain prior approval from the FIC to purchase houses above RM250,000. Through these initiatives, property transactions are expected to increase.

(Source: BNM Annual Report 2006)

The market recorded 269,000 transactions worth RM58.58 billion in the year 2006. The transactions volume registered 2.5% reduction from the year 2005 (276,508). On the
other hand, the transactions values rose by 4.9% against 2005 (RM56.78 billion). Notwithstanding this, the rate of decrease in the transaction volume was lower than negative 5.7% recorded in 2005 whereas the value improved from negative 5.3% in 2005 to positive 4.9% in 2006.

The residential property sub-sector continued as the market driver contributing 65.4% and 48.2% to the volume and value of transactions respectively. The year 2006 recorded 176,277 transactions worth RM28.70 billion against 181,762 transactions worth RM28.41 billion recorded last year. This accounted for 3.0% decrease of the volume whilst the value increased marginally by 1.0%.

(Source: Property Market Report 2006 issued by JPPH)

During the Ninth Malaysia Plan (“9MP”) period, requirement for new houses is expected to be about 709,400 units, of which 19.2% will be in Selangor followed by Johor at 12.9%, Sarawak 9.4% and Perak 8.2%. Of the total requirement, 92.8% will be for new houses while 7.2% for replacement. The private sector is expected to supply 72.1% of the total requirement. In terms of the housing category, 38.2% will be a combination of low- and low-medium-cost houses as well as houses for the poor while 61.8% in the category of medium- and high-cost houses.

(Source: 9MP 2006-2010 available at www.bnm.gov.my)

The volume of property transactions increased 3.0% to reach 135,189 transactions in the first half of 2007 (January-June 2006: -4.1%; 131,313 transactions). However, value of
transactions increased 12.4% to RM32.3 billion (January-June 2006: 0.9%; RM28.8 billion) reflecting the general improvement in buying sentiment of the property sector, in particular, the high-end residential segment. Residential transactions accounted for 63.6% of the total transactions during the period, followed by agricultural, commercial, development and industrial.

With stable interest rate and lower inflation, purchasing sentiment picked up in second quarter of 2007 as reflected by the take-up rate of newly launched residential units which improved to 30.8% (April-June 2006: 11.0%). The high-end property market (more than RM250,000) performed better, as seen in the newly launched detached houses and high-end condominium segments which registered higher take-up rates of 57.1% and 42.8% respectively (April-June 2006: 3.6%; 33.6%). Government proactive measures such as the exemption of RPGT, the removal of the limitation on the number of loans given to non-residents and the lifting of FIC approval on foreign ownership of residential properties above RM250,000 are expected to support the sub-sector.

On the supply side, developers’ optimism was boosted by the establishment of the one-stop- centre to expedite approvals for development of housing projects and incentives offered to developers who undertake the build-then-sell concept. In tandem with these developments, new sales and advertising permits for construction of residential units and shophouses as well as renewals of such permits increased to 490 and 874 (January-June 2006: 488 permits; 790 permits) respectively. Loans by the banking system for residential property also rose by 7.4% to RM167,549 million (end-June 2006: RM156,044 million).
Reflecting the improvement in demand and consumer sentiment, the Malaysian All House Price Index trended upwards by 3.6% during the first half of 2007 (January-June 2006: 1.9%), with higher-than-average prices recorded in Klang Valley and Penang.


5.2.2 Growth prospects

In April 2007, the Housing and Local Government Ministry launched a 4-pronged strategy to reduce bureaucracy in real estate and construction sectors and boost the country’s competitiveness. The four initiatives include:

- the creation of a “one stop centre” to reduce the time for property projects approvals from 2 years previously to between 4 and 6 months;
- replace the Certificate of Fitness for Occupation with the CCC, which will be issued by professionals i.e. architects or engineers, appointed by the developers;
- creation of the position of Building Commissioner, which would be empowered to resolve problems regarding strata titles and dispute between developers and purchasers; and
- the “build then sell” concept, whereby incentives will be introduced to encourage adoption of this concept by developers.

(Source: Housing and Local Government Minister's Speech dated 13 April 2007)

In considering easing the burden of loan repayment, the Government will allow EPF contributors to make monthly withdrawals from the balance in Account 2. The scheme will be effective 1 January 2008 and is for the financing of one house. This is a major
move, which will benefit 5 million active EPF contributors. This scheme will enable contributors to own better houses than they could otherwise afford as well as lessen their monthly financial obligations. This scheme will make available up to RM9.6 billion annually for the purchase of houses.

To further stimulate the property sector in particular housing, the Government proposes that a 50% stamp duty exemption on documents of transfer be given for the purchase of one house of not more than RM250,000 per unit. This measure will reduce the cost of purchasing a house by up to RM2,000.

(Source: 2008 Budget Speech by the Prime Minister)

5.2.3 Industry players and competition

Whilst there are currently 88 property development companies listed on the Main Board of Bursa Securities, there are also many other property development companies in Malaysia that are not listed. There are no official statistics and reports on the number of players in the property development business in Malaysia.

We set out below the top 10 largest property development companies by market capitalisation as at 30 August 2007 that are listed on the Main Board and their respective annual revenue.
<table>
<thead>
<tr>
<th>Company</th>
<th>Revenue (RM million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>S P Setia Bhd</td>
<td>1,154.6</td>
</tr>
<tr>
<td>Sunway City Bhd</td>
<td>1,574.4</td>
</tr>
<tr>
<td>E&amp;O Property Development Bhd</td>
<td>490.5</td>
</tr>
<tr>
<td>KLCC Properties Bhd</td>
<td>780.7</td>
</tr>
<tr>
<td>IGB Corporation Bhd</td>
<td>719.0</td>
</tr>
<tr>
<td>IOI Properties Berhad</td>
<td>609.2</td>
</tr>
<tr>
<td>Bandar Raya Developments Bhd</td>
<td>561.5</td>
</tr>
<tr>
<td>Sime UEP</td>
<td>489.3</td>
</tr>
<tr>
<td>Sunrise Bhd</td>
<td>359.2</td>
</tr>
<tr>
<td>Guocoland Malaysia Bhd</td>
<td>131.0</td>
</tr>
</tbody>
</table>

Table 5.7: Property Development Companies by Market Capitalisation

(Source: Annual reports for the latest financial year ended 2006 of the respective companies).

The residential sub-sector remained as the driver of the property market, registering RM28.7 billion worth of transactions in 2006. The sub-sector dominated 65.4% of the total volume and 48.3% of the value of transactions respectively. However, demand for residential property in the primary market softened due to a slower take-up rate despite a prevailing accommodative financial market. On the supply side, construction activity of residential properties was slow-moving with reductions in completion, starts and new building plan approvals. The number of completed units had reduced by 5.3% in 2006 compared to 2005.

Further, the average prices of all property sub-sectors recorded increases except for the commercial sub-sector, which experienced a 4.1% decrease. Prices of residential property grew but at a lower margin. The Malaysian Annual All House Price Index in 2006 was 117.8 points, up by 1.9% from 115.6 points in 2005. In line with this, the price
of the “average” all house increased marginally by 2.1% from RM161,500 in Q4 2005 to RM164,861 per unit in Q4 2006. Concerning on the location and states, Kuala Lumpur had the highest priced house in the nation at RM352,335, followed by Selangor (RM242,512) and Sabah (RM214,264).

(Source: Property Market Report 2006 issued by JPPH)

5.3 MOTOR INDUSTRY

Since the group involve and concentration in motor operations across countries such as Australia, China, Malaysia and Singapore, we focus on the passenger car industry in the said countries.

5.3.1 Overview of the motor industry

a) Australia

For the last 6 years, the Australian market has enjoyed good automotive sales. The total sales volume of automobiles in Australia in 2006 was 962,666 units which was the second highest annual sales in history. A total of 62.2% is attributed to the passenger cars segment i.e. 598,778 of passengers cars were sold in 2006. Although the fuel prices fluctuated and there was interest rate speculation, sales volume was still maintained at a healthy level. A total of 1,004,097 units were sold in the 2006-2007 financial year as compared to 981,791 units in 2004-2005.
The Australian automotive vehicle market is classified into 4 segments, namely, passenger cars, sports utility vehicles (“SUV”), light commercial vehicles, and medium and heavy commercial vehicles.

Light car sales rose by 20,196 units or 21.1% while small car sales remained much the same, up 1,345 units or 0.6%. Light cars are more fuel-efficient, more practical and carry good features for their price range. The large car segment and the medium SUV segment both suffered a significant slowdown in sales which fell by 30,775 units and 10,632 units respectively. In contrast was the strength of the luxury SUV segment, which grew 1,739 units or 10.5%. The large cars segment is still favoured as consumers look for as much space, power and performance as they can afford. The four-wheel vehicles (which includes jeeps with off-road capabilities) (“4X4”) Pick-up/Cab Chassis segment grew by 4,911 vehicles or 7.8%, depicting a trend towards private use from trading. The light truck sales, on the other hand, declined slightly by 6,087 vehicles or 3.6%.

(Source: Industry Overview Report for Passenger Cars Market in Australia, Frost & Sullivan 2007)

b) China

The total sales of automobiles in China increased from 2.36 million units in 2001 to over 7.21 million units in 2006. The automotive sales in 2006 increased by 25.2% compared with that in 2005. The market share of passenger cars stood at 72% in 2006.
The total sales of passenger cars were 4.26 million units (exclusive of mini buses) in 2006. The sedan cars claimed the biggest market share, followed by the mini buses, SUVs and multi-purpose vehicles. Their market share were 74.0%, 17.7%, 4.5% and 3.6% respectively.


c) Malaysia

The total sales of automobiles in Malaysia jumped from about 396,400 units in 2001 to 490,800 units in 2006. The automotive sales in 2006 decreased by 10.9% compared with that in 2005. Malaysia remains the third largest automotive consumer in South East Asia. The market share of passenger cars was maintained at 93% in 2006, demonstrating the largest passenger vehicle market in South East Asia.

The total sales of passenger cars was 367,000 units in 2006. Passenger cars claimed the biggest market share at 75%, followed by commercial vehicles (18%) and 4x4 (7%). Most of the top 10 best-selling models are of low cylinder volume (1.0 litre to 1.6 litre). 56% of passenger vehicle sales in Malaysia consist of cars below 1.4 litre. Fuel efficiency is highly valued.

(Source: Industry Overview Report for Passenger Cars Market in Malaysia, Frost & Sullivan 2007)

The Malaysian Automotive Association (“MAA”) announced that the total motor
vehicle sales in the first 6 months of 2007 was 12% lower than the motor vehicle sales in the corresponding period in year 2006. The decrease was due to lack of consumers’ confidence, difficulty in obtaining hire purchase loans and poor resale value of used cars. The MAA announced that motor vehicle sales improved by 6% for August 2007 over July 2007 and expects the sales volume in September 2007 to be maintained.

(Source: MAA press releases for July and August 2007 available at www.maa.org.my)

d) Singapore

The total sales of automobiles in Singapore jumped from about 85,861 units in 2003 to 110,464 units in 2006. Passenger car sales in Singapore grew by a compound annual growth rate ("CAGR") of 11% from 2003 to 2006. Singapore’s strong economic performance and relatively lower Certificate of Entitlement ("COE") prices kept passenger car sales at around the 100,000 mark from year 2005 to 2006. Nonetheless, Singapore’s passenger car sales declined marginally by approximately 3% from year 2005 to 2006, due to slightly tighter COE quota restrictions in 2006. The total sales number of passenger cars was about 98,700 units in 2006. Passenger cars claimed the biggest market share of 89%, followed by commercial vehicles at 11%.

5.3.2 Growth prospects

a) Australia

For the first 6 months of 2007, motor vehicle sales totaled 524,376 units, up 8.5% compared to the corresponding period of 2006. In June 2007, the strong performance was largely generated by the light, small and medium passenger car segments which combined to sales of 5,244 units. The large car segment improved its sales by 3.7% and the upper large segment saw a significant increase by 28.3%. The light truck market increased slightly by a modest 2.0% and the SUV market was up by 4.9%. The Australian market’s sales volume is forecasted to grow marginally in 2007 with a steady increase moving the total motor vehicles sales to close to 1 million units. Low interest rates, strong consumer spending, continuing healthy employment rate and rising incomes are favourable to stimulate further growth of passenger car sales and the growth rate is expected to be sustainable throughout upcoming years.

During the period 2005 to 2011, the total automotive vehicle market in Australia is expected to grow at a CAGR of 4.0%. This is partly driven by the reduction of the automotive tariffs levied as a form of protectionism from 15.0% to 10.0% effective from 1 January 2005. This is likely to present new challenges to the industry participants. Product differentiation and innovation, investment in R&D, and efficient management of resources are the key industry challenges. In addition, the industry also needs to focus on developing and utilising cost efficient and environmentally-friendly fuels such as bio-diesel, liquefied petroleum gas and lightweight materials for components and parts.
b) China

The growth of the passenger cars market in China is growing at a faster rate than the growth rate of the total automotive market and also the country’s GDP. In year 2006, it has grown by 30.2% while the growth rate of the total automotive market was 25.1% and growth rate of GDP was 10.7%. The Chinese passenger cars market is expected to reach 6.3 million in 2007, up approximately 22% from 5.2 million in 2006. In the near future, more hybrid cars are also expected to be sold in the Chinese market. Administrative Regulations for the Approval of Alternative Energy Vehicle Manufacturing was recently issued as a draft document by National Development and Reform Commission (“NDRC”) of China to encourage the development of alternative fuel vehicles.


c) Malaysia

In 2006, the passenger vehicles market and automotive market dropped by 9.0% and 11.0% respectively while the country’s GDP grew by 5.7%. The Malaysian automotive market is expected to reach 506,200 units in 2007 at a growth rate of 3.8%.

(Source: Industry Overview Report for Passenger Cars Market in Malaysia, Frost & Sullivan 2007)
d) Singapore

The passenger car growth rate and vehicles growth rate in Singapore have outpaced that of the GDP growth rate for the period of 2003 to 2006. In 2006, the passenger car market grew at 35.2% and the vehicles market grew at 28.7% while the country’s GDP grew by 33.6%. The overall car population would continue to grow at approximately 3% annually until 2008. The Singapore government is promoting car ownership in order to meet the rising demand from its increasingly affluent population and also to drive its automotive industry forward. However, it maintains its policy of reducing traffic congestion through its various schemes and measures because its city-state condition does not allow a large influx of vehicles on the road. Although the measures to reduce road usage are still in place, it is expected that the number of weekend cars will increase due to the increased number of vehicles purchased. The Land Transport Authority (“LTA”) car population policy (3% annual growth rate) is due for revision after 2008. With expectations that the government’s policy of promoting car ownership remain the same, the Singapore market offers steady growth prospects for automotive Original Equipment Manufacturers (“OEM”), particularly in the mid-sized car segment.


5.3.3 Industry players and competition

a) Australia

The market leader for the fourth year in a row with 22.2% share of the total market
was Toyota, followed by Holden (15.2%), Ford (11.9%), and Mazda (6.6%).

(Source: Industry Overview Report for Passenger Cars Market in Australia, Frost & Sullivan 2007)

b) China

Foreign OEM dominates the Chinese market. In 2006, 22 foreign OEM held 69.6% market share with sales of 4.2 million passenger cars (excluding mini buses) out of which 13 OEM have captured 64.8% market share. The largest foreign OEM (under joint ventures) are Shanghai General Motors (9.5%), Shanghai Volkswagen (8.2%), FAW VW (8.1%), Beijing Hyundai (6.8%) and Guangzhou Honda (6.1%). There are a large number of domestic carmakers, approximately 33 in 2006. However, they only contributed to approximately 30.4% market share in 2006. The trend however points to a growing market share captured by domestic carmakers i.e. Chery and Geely in the last 3 years (2004 to 2006). Shanghai Volkswagen, FAW VW, FAW Toyota, Dongfeng Peugeot Citroen Automobiles and Chang’an Ford won more market shares in 2006 whereas Japanese OEM like Guangzhou Honda, Dongfeng Nissan, Chang’an Suzuki and FAW Hainan Mazda saw market share drop in 2006.


c) Malaysia

The consolidated market share of Proton and Perodua dropped to 55.3% in 2006 compared to 59.6% in 2004. Perodua gained 6.3% market share in 2006. The launch
of the new Camry, Civic, and Accord helped to sustain growth for Toyota and Honda.
There are no significant new model launches in the compact and mid-size sedan segment. Local assembly of Spectra, Carnival, Carens, Sorento and Picanto drives Naza Kia’s growth.

(Source: Industry Overview Report for Passenger Cars Market in Malaysia, Frost & Sullivan 2007)

d) Singapore

The Singapore market is largely dominated by Asian OEM. In 2006, the dominance of the top 10 foreign OEM has been slightly eroded, falling from 91% to 89%. The largest foreign OEM are Toyota/Lexus (25%), Nissan (15%), Honda (11%), Hyundai (10%) and Mitsubishi (9%).


5.4 HEAVY EQUIPMENT INDUSTRY

As a result of the concentration of the Heavy Equipment division’s operations in Australia, the review below is focused on the heavy equipment industry in Australia based on an industry overview report prepared by Frost & Sullivan for the heavy equipment market (referred to as construction equipment in the report) in Australia.
5.4.1 Overview of the heavy equipment industry in Australia

At a broad level, construction equipment or machinery refers to the heavy equipment used largely for material handling functions. Such heavy equipment largely focuses on the movement, handling and storage of materials that are used in a variety of end user sectors including, among others, mining, physical infrastructure development (such as roads, ports, railways, airports), large heavy engineering sectors (such as steel, automotive, petrochemicals, fertilisers) and logging.

The Heavy Equipment industry is the fourth largest in Australia and is one of the most significant contributors to the Australian economy which is growing at a robust 3.8% per annum. With strong infrastructure investment, the engineering construction sector is expected to rise continuously especially in the transport infrastructure like major road and rail projects, mining construction, water supply, power generation, and construction and upgrading of freight and port facilities.

The total imports of Heavy Equipment for Australia were valued at USD1.2 billion in 2006. Imports from the USA largely dominated the market, with imports valued at USD512.9 million and the leading import market share of 41.9% in 2006. This covers Heavy Equipment such as off-highway dumpers, graders and levelers, self-propelled track laying bulldozers and angle dozers, front-end shovel loaders, scrapers, and excavators. The Australian Heavy Equipment market is largely dominated by imports. The principal import country market share is led by the USA, followed by Japan (23.8%), Germany (8.0%), France (4.5%), South Korea (3.0%), UK (2.8%), and Sweden (2.4%).
The import duty on Heavy Equipment from the USA has been eliminated through the Free Trade Agreement between the USA and Australia. Imports from other countries remain at 5%. As pricing is also a major consideration for purchasers in the Heavy Equipment market besides technology advancement and efficiency, the elimination of import duty had greatly improved the competitive position of the USA. USA manufacturers have a strong establishment in the Australian market and mostly operate through wholly-owned subsidiaries or Australian agents.

(Source: Industry Overview Report for Heavy Equipment Market in Australia, Frost & Sullivan 2007)

5.4.2 Growth prospects

With strong infrastructure growth projected by the Australian government, the investment in Heavy Equipment is likely to continue in the next few years at a robust growth rate. The growth in engineering construction spending is anticipated to grow at 6.5% per annum during the period 2006 to 2012 in nominal terms according to the Construction Forecasting Council of Australia. The market trend points to higher demand for Heavy Equipment, such as public works machinery, off-highway dumpers, self-propelled track laying bulldozers and angle dozers, graders and levellers and mechanical shovels and excavators. It is anticipated that the growth in Heavy Equipment will be aligned to the trend in engineering construction spending.

There is also a market trend indicating increasing demand of these vehicles in Queensland and Western Australia due to a boom in mining and construction projects.
5.4.3 Industry players and competition

The heavy industrial equipment market in Australia is dominated by imports of equipment from the USA, Japan, Germany, France, South Korea, UK and Sweden. The largest share of imports of heavy industrial equipment is held by the USA suppliers valued at USD512.9 million for 2006. The major industry player from the USA comprises Caterpillar, Case New Holland, John Deere and Ingersoll-Rand Heavy Equipment. The principal machinery imported from major industry players in the USA are mechanical shovels, self-propelled forklift trucks, off-highway dumpers, self propelled track laying bulldozers and angle dozers, front-end shovel loaders, graders and levelers.

Imports of Heavy Equipment from Japan in 2006 were valued at USD291.8 million. The major industry players from Japan are Komatsu, Hitachi, Kobelco, Kawasaki, Kubota, Sumitomo and Kato. The principal machinery imported from Japan are similar to that imported from the USA. From Germany, major industry players include Liebherr, Dernag, Bornag, and Tadano. The principal machinery imported from Germany comprise mobile cranes, mechanical shovels, front-end shovel loaders, forklift parts, public works machinery, selfpropelled fork-lift trucks and other work trucks with lifts, front-end shovel loaders, and track-laying tractors. Imports from France in 2006 were valued at USD55.3 million. The major industry players from France are Manitou and Haulotte, and the
principal machinery imported are mechanical shovels, forklift trucks, elevated work platforms. Major industry players from South Korea are Samsung, Doosan Daewoo, and Hyundai, with imports from Korea valued at USD36.7 million in 2006. JCB, MF Industrial and RMD Kwikform are the major industry players from the UK. The major industry players from Sweden are Atlas Copco, Volvo, Dynapac, and Sandvik.

(Source: Industry Overview Report for Heavy Equipment Market in Australia, Frost & Sullivan 2007)

5.5 ENERGY AND UTILITIES INDUSTRY

The group’s involvement in the energy and utilities industry is mainly in the power, oil and gas, and engineering segment. We set out below an overview of the energy and utilities industry in respect of the segments in where Sime Darby Group is mainly involved.

5.5.1 Overview of the energy and utilities industry

a) Power

The energy sector performed favourably in improving energy supply security to meet the increased demand. The long-term sustainability of the energy sector was enhanced with the implementation of measures on efficient utilisation of resources and the adoption of demand-side management initiatives.

(Source: 9MP 2006-2010 available at www.bnm.gov.my)
Entities that wish to operate as an Independent Power Producer (“IPP”) in Malaysia are required to obtain the necessary licenses from the Energy Commission. This license allows the IPP producing electricity for use in Malaysia to generate a stated amount of electricity, which is to be sold to TNB. Coupled with the need for a huge capital outlay, the license serves as a high barrier to entry for a new operator.

b) Oil and Gas and Engineering Services

The performance of this segment hinges on the performance of the oil and gas industry in Malaysia as well as in overseas countries. The growth of the oil and gas industry would expand the market for the offshore and onshore fabrication and engineering services industry.

The mining sector registered a mild contraction of 0.2% in 2006 due to lower production of crude oil and natural gas. The shutdown of a number of oil fields for maintenance, as well as the phased upgrading to expand capacity at the Malaysia Liquefied Natural Gas 2 (“MLNG 2”) plant, led to lower activity in the mining sector during the year. Nevertheless, the sector’s contribution to the overall economy was significant in terms of foreign exchange earnings from exports, revenue to the Government and investments in exploration and downstream activities.

In 2006, crude oil production (including condensates) averaged 699,796 barrels per day, representing a decline of 0.5%. The lower production of crude oil (excluding condensates: -3.5% to 548,487 barrels per day) was a result of the shutdown of
several oil installations during the year for repairs and maintenance. This was mitigated to some extent by the rising contribution of condensates to overall oil production.

(Source: BNM Annual Report 2006)

The demand and supply of the services offered by the Energy and Utilities division is related to the performance of the oil, gas and petrochemical industry. The current surge in oil prices along with high consumption from emerging developing countries have provided a positive outlook for the global oil and gas industry. Capitalising on the activities within the oil and gas industry and the anticipated increase in consumption of energy, the demand for the products and services offered by the Energy and Utilities division remains positive.

The engineering services offered by this sector are industry-specific and they require different level of skills, expertise and capabilities. As a result, new operators who wish to venture into this segment are required to equip themselves with this set of skills.

5.5.2 Growth prospects

a) Power

The overall demand is expected to increase at an average rate of 6.3% per annum during the 9MP period to 2,218 petajoules in 2010, due to the higher GDP growth expected for the period. The energy intensity of the economy is projected to increase
to 6.3 gigajoules (“GJ”) in 2010. With the expected improvement in the quality of life of the population, there will be an increase in energy consumption due to, among others, the increased use of electrical appliances and more frequent travels. In this regard, per capita consumption of energy is expected to increase from 62.2 GJ in 2005 to 76.5 GJ in 2010.

(Source: 9MP 2006-2010 available at www.bnm.gov.my)

b) Oil and Gas and Engineering Services

The mining sector is expected to expand by 2.8%, supported by higher output of crude oil and natural gas. Crude oil production (including condensates) is expected to average 722,500 barrels per day, supported by the commencement of operations at the new Kikeh oil field located offshore from Sabah in the final quarter of the year.

(Source: BNM Annual Report 2006)

5.5.3 Industry players and competition

Energy and Utilities division is one of the fabricators who holds a major fabrication license granted by Petronas to undertake major fabrication work for the offshore oil and gas structures. The division provides a wide range of fabrication and engineering services for the local and international markets and has completed a broad variety of projects for the oil and gas industry. Other fabricators in Malaysia include Brooke Dockyard & Engineering Works Corporation, Kencana HL Sdn Bhd, Oilfab Sdn Bhd, Malaysian Marine and Heavy Engineering Sdn Bhd and Ramunia Fabricators Sdn Bhd.
5.6 CHALLENGES FOR THE MERGER FACED BY SYNERGY DRIVE

5.6.1 Challenges to meet corporate and business strategy

As a result of synergies achieved from the proposed Synergy Drive (SD) merger, SD can be expected to deliver the following:

- Achievement of headline key performance indicators (KPIs) – improvements can be expected of headline KPIs such as return on equity (ROE), earnings and oil extraction rate (for plantation) over and above what has been targeted by the companies individually (20% increase can be set as a targeted benchmark);
- Improvement in corporate ratings – a larger entity in the form of SD can be expected to get better ratings from agencies and secure funding at lower rates; and
- Growth story – on a short to medium term basis, SD represents a growth story, and is poised to expand overseas to fuel its growth, in both plantation and property.

5.6.2 Challenges to meet national agenda

The creation of SD’s is to a large extent towards fulfilling national objectives, which includes the following:

- Largest listed oil palm plantation company – SD will be the largest listed oil palm plantation company in the world, which will have plantation operations in Malaysia and Indonesia, as well as involved in global property development projects, and listed on the Malaysian capital market;
- Substantial shareholding by GLIC in strategic global industry – SD ensures that a GLIC retains a substantial shareholding in a strategic global industry, as well as a strategic global player;
- Creation of Global Leader – SD is poised to be a global leader in the palm oil industry, particularly in the downstream industry and trading of palm oil; and
- Bigger Global Opportunities for BCIC2 – SD will enable BCIC2 opportunities to enter global markets, with a better competitive edge.

5.6.3 Challenges to meet Globalisation and the Borderless World

Globalisation and the borderless world has brought with it heightened competition in the business circles. In not too distant a future, only very large multinational and multicultural management companies with economies of scale, globalised markets network, quality products meeting consumers’ expectations and taste but yet cost efficient would be able to survive. Smaller companies with specialised, differentiated and proprietary products would be the exception to this trend. There are many examples of industries impacted by globalisation which have taken the successful route of mergers and acquisitions (M&A). These included the airlines, banking, automotive and oil & gas industries.

Closer to home we have seen the successful M&A of the local banking industry. As such the merger of Sime Darby, Golden Hope and Kumpulan Guthrie is considered appropriate and timely to take advantage of economies of scale, synergies and greater productivity and efficiency. Synergy Drive’s plantation business would be able to
emulate the three large multinationals in the USA which control the world’s edible oils markets like Cargill Incorporated, Archer Daniels Midland (ADM) Company and Bungee Corporation.

Latest in the picture is the merger of the Kuok Group. They are in the process of merging both of their upstream and downstream companies, namely Wilmar International Ltd., PBB Oil Palms Pte. Ltd., Kuok Oils & Grains Pte. Ltd. and PGEO Group Sdn. Bhd.

5.7 MERGER RATIONALIZATION

5.7.1 To Value-add and Become a Fully Integrated Plantation Company

Historically, the financial performance plantation business can be seen to be influence greatly by the prices of palm oil and hence the palm oil industry is often referred to as cyclical in nature. In order to ensure that profits will not fluctuate greatly, the plantation business began their diversification all along the value chain or aptly termed as a fully integrated player. A good example is PETRONAS, where the core business is petroleum. Building on the sound foundation anchored on integration, value-adding and globalisation, PETRONAS whose her initial involvement with multinational oil companies started with production sharing contract has since moved its upstream business overseas and downstream activities very successfully.

Taking the cue from this, it would be strategic indeed for the plantation business to emulate the approach of PETRONAS by strengthening further both upstream and
downstream sectors. The four sectors are plantations, oils & fats and specialty products, oleochemicals and biodiesel.

The oleochemical sector could be propelled to greater height in view of the continuing demand for eco-friendly products. Synergy Drive could move from just concentrating on the production of basic oleochemicals i.e. fatty acids which are derived from the splitting process, to the production of higher value-added products.

These are higher value-added products used in various industries such as textile, cosmetic, pharmaceutical, plastic and other applications. Although fatty alcohols find limited use, their derivatives: fatty sulphates, fatty alcohol ethoxylates and fatty alcohol ether sulphates can be extensively used in production of washing and cleaning products. Fatty amines are mainly used in the detergent industry as softening agents, in the mining industry as anti-caking agents, as biocides and in road building and other applications.

The biodiesel sector is indeed a strategic opportunity. It is a safety net for the country to stabilise the palm oil prices. In this connection, Government support through tax incentives should be obtained for companies in biofuel production much like the assistance in Europe and the USA. After all, oil palm leads many other crops in term of energy balance. The high energy balance reflects that oil palm is the best candidate crop for biofuel production that could reduce reliance on fossil fuels. From an input energy of 19.2 GJ/ha/year, oil palm gives products with a total energy of 182 GJ/ha/year. This high
input: output ratio of 9.5 times is commendable as compared to soyabean and rapeseed with 2.5 and 3.0 times respectively.

5.7.2 To Optimise on Cost and Revenue Synergies

The creation of the largest plantation companies by merging Sime Darby, Golden Hope and Kumpulan Guthrie brings about significant prospects of cost and revenue synergies. The cost synergies among others include consolidation of contiguous estates, rationalisation of mill utilisation, unified procurement and logistic activities and consolidation of plantations management and administrative functions etc. The revenue synergies would include leveraging on global strategic presence of the three companies and wider customer spectrum for growing market share. The sharing of best practices and management expertise could also further enhanced both cost and revenue synergies.

5.7.3 To Grow Further the Upstream and Downstream Sectors

As an enlarged entity, Synergy Drive would have the capability and capacity to grow further the plantation business. There will be opportunities to establish and acquire oil palm plantations and related downstream businesses such as oils & fats and specialty products, oleochemicals and biodiesel facilities.

Rubber plantations and downstream business is also an opportunity. At current prices, rubber is much more profitable than oil palm. The huge land bank of Synergy Drive would necessitate the planting crops based on agro-climatic and terrain suitability. Expansion of the rubber business overseas like Cambodia should be considered.
Integration with livestock and crop integration are possible. There are currently successful projects to integrate the plantation through livestock and crop integration. While oil palm will continue to be the anchor crop, livestock and crop integration will provide further opportunity for the industry to practice diversification. Another is the potential use of the large tract of land under TNB rentices for growing high value crops which otherwise would be left idle.

5.7.4 To Further Value-add the Palm Oil Business

Oil palm biomass is the answer to growing concern over environmental issues affecting natural forest conservation. Each year, the oil palm industry generates more than 30 million tonnes of biomass in the form of empty fruit bunches, oil palm trunks and oil palm fronds. These may be used for commercial products e.g. pulp and paper, MDF, automotive components etc. Effective utilisation of palm biomass into value-added products has the potential to generate another revenue stream estimated to be in the region of RM20 billion in the next 10-15 years.

5.7.5 To Focus on Quantum Leap R&D

There is potential of enhancing R&D within Synergy Drive. Although, oil palm R&D is carried out by the Malaysian Palm Oil Board (MPOB), the success of the industry has also been attributed by private research houses of large plantation companies. Going by the example of developed world, a strong emphasis on R&D is essential to make the group sustainable. Oftentimes, R&D is done for the future whilst the business is doing
well. All that the group oversees today are fruits of years of R&D where full commercialization occurred well after discovery many years down the road.

Areas of particular interest for oil palm R&D include:

- Bioethanol production from biomass to compliment biodiesel from palm oil. Bioethanol may be mixed with petrol much like biodiesel with petroleum diesel.
- Biopolymers from palm oil. Palm oil has been successfully used to produce polyols, which in turn, is used for making of polyurethane with a multitude of industrial plastic applications.
- Genetic engineering of the oil palm tree for increased yields, improved palm oil quality, pest and disease tolerant, salinity and drought tolerant.
- Exploiting the minor components in palm oil such as sterols, squalene, co-enzyme Q10, etc. These may be marketed as neutraceutical, pharmaceutical and food supplements. Currently only the carotene and vitamin E (tocotrienols and tocopherols) are commercially produced.
CHAPTER 6: MERGER INTEGRATION AND BUSINESS CONSOLIDATION

6.1 BACKGROUND

Synergy Drive Berhad was set up as a special purpose company to facilitate the merger of the Golden Hope Group, Kumpulan Guthrie Berhad and Sime Darby Group. The merger of these three companies are on-going gradually, and as for to the date, the business operations both in local and international have been consolidated successfully. Along with the completion of the business operations, the Golden Hope Group, Kumpulan Guthrie Berhad and Sime Darby Group which initial was merged under Synergy Drive has been re-branded to be remained as Sime Darby Group.

The rationale for this merger is mainly to extract arising synergies from combining the complementary strengths of the three groups particularly in the plantations and property businesses. By incorporating the businesses, Sime Darby Group can leverage on the economies of scale arising from the merger, owning a large pool of industry experience and management talent from the merging companies, and able to strongly establish in key growth sectors and business. This will enable the group to become an enlarged group and a multinational group of businesses in key complementary growth sectors with established market positions, strong brands and vast experience.

Synergy Drive Berhad was incorporated in Malaysia on 7 November 2006 under the act as a private limited company. The company has commenced business on 7 November
2006 and was converted into a public limited company on 5 April 2007. Synergy Drive has been re-branded to be remained as Sime Darby Berhad on 28th November 2007 and subsequent to that, the company was listed into Kuala Lumpur Stock Exchange on 30th November 2007.

6.2 BACKGROUND OF MERGER

The merger has enable Sime Darby Group to be the world’s largest and listed oil palm plantations group. This has been derived through the planted land area, together with significant presence in both upstream and downstream palm oil activities. Sime Darby Group are now one of the global leaders in palm oil origination i.e. plantation and palm oil extraction, which is presently the most profitable part of the palm oil value chain. Sime Darby’s Plantations division, which significantly presence in the upstream palm oil activities provides an opportunity for the group to be a strong counter-weight to the growing power of traders and other large plantations players.

The merger also provides an opportunity for Sime Darby Group to be Malaysia’s leading developer of quality residential and commercial communities. Sime Darby Group will continue in participating selectively in and grow their existing complementary property businesses such as asset management and enter into strategic partnerships to strengthen their businesses in locally and internationally.
As a result of the merger of the Golden Hope Group, Kumpulan Guthrie Berhad and Sime Darby Group, the newly branded Sime Darby are now a conglomerate that involved in five main and core businesses namely, plantations, property, motor, heavy equipment, and energy and utilities.

![Figure 6.0: Synergy Drive Core Business](image)

In addition to the above, Sime Darby Group also involves in various non-core businesses such as healthcare, insurance broking, bedding and others.
The proposed pre-merger group structure of Synergy Drive is as figure 6.1 below. The names of the holding companies have been changed accordingly upon completion of the merger.

**Figure 6.1: Synergy Drive Group Structure**
Leading to an announcement of the merger in November 2006, Synergy Drive Berhad has been established and a committee has also been formed. The committee named as Merger Integration Committee (MIC) are represented by Tan Sri Dato’ Md Nor Md Yusof, Tan Sri Hadenan A. Jalil, Raja Datuk Arshad bin Raja Tun Uda, Dato’ Mohamed bin Sulaiman, Azmi Mohd Ali, Dato’ Seri Ahmad Zubair @ Ahmad Zubir bin Haji Murshid, Dato’ Sabri Ahmad, and Dato’ Abd Wahab Maskan. In addition, a Merger Integration Office has been formed and 7 sub-committees comprising representatives from each of the Participating Companies (“Merger Team”) has been created. An assortment of consultants has been appointed to advise the committee in integration matters mainly in areas of financial, strategic alliances, information technology, business consolidations, communication and others.

The Merger Team’s charter was to develop a master plan for the integration and to identify the potential synergies that can be extracted from the integration of the Participating Companies. The master plan for the integration firstly involves the identification of synergies and key initiatives to extract the synergies. At the same time, the Merger Team with the assistance of the consultants also glance into the integration and strategy development for the combined group. Among the strategies are mainly to focus in areas such as the business transformation and positioning of the group as an industry leader.

The Merger Team, together with assistance from the consultants, had identified key synergy areas, along with a plan to capture the synergies. This mainly focuses in the
plantations business, property development business, and corporate services such as IT, HR, finance, overheads and administrative support. These areas are subject to further refinement in the subsequent phases in line with the transformation plans that are also being developed. Due to the scale of the merging companies, the Merger Team views the integration as an impetus for repositioning and transforming the enlarged plantations and property development businesses as an industry leader.

6.3 GROUP’s BUSINESS STRATEGIES

Sime Darby Group is planning to focus in set of businesses that are in key complementary growth sectors. As an enlarged entity, Sime Darby Group had planned to embark on a 3-phased road map over the near to medium term as stated below:

|-----------------------------------|-----------------------------------------------|--------------------------------|
| • New organisation, management team and key performance indicators in place | • Full value capture from plantations and property integration
• Plantations and property businesses integrated
• Other core businesses developed to full potential | • Fully integrated and positioned to embark on growth
• Complementary growth opportunities across all businesses |

Figure 6.2: Merger Integration Phases

Sime Darby Group had developed its own planned directions and strategies for its core
business. Among the developed and strategies arising from the merger integration are as per below:

6.3.1 Strategies for the plantations business

Sime Darby Group intends to continue to focus on the upstream activities which are presently the most profitable part of the palm oil value chain. For the upstream activities, the group are aiming to achieve the lowest industry cost, high asset efficiency and strong growth by:

- increasing the proportion of upstream activities which are involved in low-cost origination in selective regions;
- enhancing yield per hectare of palm products;
- migrating high cost land to alternative uses by capitalising on the symbiotic relationship between the plantations and property development businesses; and
- creating opportunities for non-asset intensive growth through integrated plantations services and originating palm oil from third parties.

Sime Darby Group will continue to participate selectively in mid/downstream activities to realise the highest value by, amongst others, participating selectively in downstream activities through strategic partnerships or on the group’s presence. In addition to that, the enlarged plantations business allows Sime Darby Group to be a strong counter-weight to the growing power of traders and other large plantations players.
6.3.2 Strategies for the property business

Sime Darby Group is aiming to be Malaysia's leading developer of quality residential and commercial communities. The group intends to achieve this by:

- proactively managing land banks to enhance portfolio quality and increase asset turnover;
- strengthening brand value and building a reputation for customer-centric product innovation and quality to command premium pricing; and
- achieving best-in-class cost management through leading edge operational practices and execution excellence.

In addition, Sime Darby Group will continue to participate selectively in and grow their existing complementary businesses such as asset management and enter into strategic partnerships to strengthen their businesses.

6.3.3 Strategies for other core businesses

Looking at other core businesses, namely motor, heavy equipment and energy and utilities, Sime Darby Group will continue to implement the existing growth strategies and build on their respective established positions. The Motor business will continue to build on the existing extensive network while expanding the representation of the luxury marques that the group currently represent.
The Heavy Equipment division will continue to pursue growth by capitalising on the continuing demand for infrastructure, mining, timber, and oil and gas industries across the Asia Pacific region and in particular, from China.

The Energy and Utilities business will continue to pursue growth strategies to take advantage of the strong demand for oil and gas, energy and utilities in tandem with the economic growth in the Asia Pacific region. The group will carry out reviews of all core businesses and opportunities available to further develop their core businesses on an ongoing basis.

6.4 MERGER SYNERGIES

In addition to the business strategies above, Sime Darby Group had intend to extract synergies inherent in their enlarged group of businesses, particularly in the plantations and property development businesses and area of corporate services. The Merger Team, assisted by the consultants, has estimated the potential synergies which can be derived from the merger.

The synergies are estimated by excluding the expected natural improvement and present planned improvements of each of the participating companies. In addition to that, the synergies estimations have also not taken into consideration of the effects of the harmonization of accounting policies, the new accounting standards and any future changes to the accounting standards and policies within the group.
The key assumptions upon which the revenue and cost synergies have been derived are as follows:

- There will be no significant changes in the prevailing political, legislative, economic, market, taxation, foreign exchange and interest rates, inflation conditions both within and outside of Malaysia that will affect the businesses of the group.

- There will be no unfavorable weather conditions, natural disasters or major disasters, breakout of diseases, pests or major disruption in the planting, harvesting and other estate works, arising from industrial disputes, labour shortage, or any abnormal circumstances that will adversely affect the production, yield, oil and kernel extraction of the plantations, and there will be no major breakdown of equipment and facilities of the group.

- There will be no significant increases in wages, overheads and operating expenses and the increase is expected to be in line with inflation and industry expectations.

- The average selling prices for crude palm oil (CPO) and palm kernel (PK) are assumed to be at the prevailing average RM-prices for the past 1 year up to July 2007.

- Capital expenditure, and planned planting and replanting expenditure programmes will be implemented as scheduled, and there will be no material acquisitions or disposals of property, plant and equipment.

- There will be no material changes in infrastructure, construction and other related costs that will be incurred by the group, including steel and concrete.
that may affect the costs of the property development projects undertaken by the group.

- The launch date, commencement and completion of all identified property development projects will take place as scheduled. The expected number of sales units will be achieved as planned and sales units will be sold at the anticipated selling prices. There will be no significant deviation or delay from the expected physical completion and handover date for all phases under development.

- There will be no acute shortages of labour and materials in the industry. There will be no major disruption to the services provided by contractors. The contract sums/prices will be maintained at the level computed. The cost of contractors will not be affected to a material extent by variation orders, disputes with contracts (if any) and/or unfavourable conditions.

- There will be no significant delays in obtaining the relevant approvals for the project development activities. All planned development activities will also be approved by the relevant authorities. There will be no significant changes in authorities’ approval policies.

- Sime Darby Group designated key management and team members remain relatively unchanged.

Based on the above assumptions, the preliminary estimation of the synergies is expected by the ending of financial year 2009. On top of that, the group are expecting that the earnings before interest and taxation (EBIT) will improvement in range from RM400
million to RM500 million per annum. The EBIT improvements are expected to arise from both revenue and cost synergies.

Among the key areas from which the above synergies are expected to be derived are briefly explained below.

### 6.4.1 Plantations

Amongst the areas of operations identified above, the plantations business provides the most significant potential for synergies, aligned with the enlarged scale of the plantations business of Sime Darby Group. The potential synergies arising from the merger of the plantations business of the participating companies comprise both cost and revenue synergy, with the key areas is as follows.

#### 6.4.1.1 Cost synergies

The key potential areas of cost synergies are as per highlighted below:

**a) Optimizing mill routing and capacity utilization**

There are two potential areas of synergies in terms of optimizing mill routing and capacity which has been identified. Prior to the merger, each of the company Golden Hope, KGB Group and Sime Darby Group has their respective mills. Some of the mills are located within close proximity of each other. Therefore, from the perspective of an integrated entity, not all fresh fruit bunches (FFB) are currently processed at the closest mill belonging to the group.
With the integration of the plantations business, the group can better optimize the use of the mills, by consolidating milling activities in the most cost efficient manner. In addition to optimizing the capacity utilization of each of the mills, the consolidation of milling activities is also expected to reduce estate-to-mill FFB transportation costs. As part of the mills routing optimization, the overall distance in terms of FFB transportation is expected to be reduced.

b) Fertiliser optimization

Fertiliser cost is the largest component of non-labour costs that contributes significantly to all estate costs. Historically, each of the companies has been paying different price for their fertilisers. All the companies also have different fertilisers’ application policies. Upon benchmarking the prices paid for fertiliser, the group able to improve in their overall costs management.

The group can save in realizing the additional cost synergies through the sharing of knowledge and expertise of the companies and also by developing and adopting the best practices in fertiliser application policies by aligning the volume, type and technique of each of the company.

In addition to the above, the group able to save other potential cost synergies which includes the rationalizing the transport and logistics network, consolidating estate and
mill management and leveraging on scale to reduce procurement costs in other areas such as herbicides and transportation, in addition to fertilisers.

6.4.1.2 Revenue synergies

There are a significant portion of the revenue synergies which has been expected to be harnessed from the sharing of expertise which resulting from the adoption of best practices among the experienced plantations management teams of the respective companies. The group can further tap into the enlarged pool of human resource. In addition, the group able to select the most appropriate personnel to manage the two key sectors of the plantations value chain, which is estate management and mill management.

a) Adoption of best practices in estate management

The key areas in revenue synergy extraction for estate management are in the respect of potential improvement of yields and FFB recovery. In the short term plan, the enlarged plantations business group is focusing into enhancing yields and FFB recovery through sharing of best practices in areas of loose fruit collection, nursery management, replanting standards and fertiliser applications. In order to improve harvesting efficiency, ways of collecting loose fruits and mechanising the harvesting process have been embarked in. In long run, through the sharing of experience, the group is looking into sharing best practices in terms of replanting, which will cover areas such as the design of the layout of estates and the type of seedlings to be used. The result of these longer term initiatives are only expected to materialize over a
longer period, as opposed to the earlier mentioned immediate enhancements through better harvesting and collection practices.

**b) Adoption of best practices in mill management**

The key area in revenue synergy extraction for mill management is in respect of potential milling efficiency. The plantations sub-committee members had compared the oil losses between mills to determine the range of mill performance. They have further discussed the reasons for the differences in extraction efficiency between the mills and have decided that there remains potential for improvement among the mills, both in terms of CPO and PK extraction. The integration of the plantations businesses provides a platform for the management of the mills to re-examine their practices and to improve processes through the sharing of best practices. In addition, in line with the mill optimization, there will be upgrades carried out within certain mills to improve on the efficiency of the machinery.

In addition to both the cost and revenue synergies highlighted above, the group is planning to look across the plantations value chain to target specific areas for margin optimization. For instance, with the increased CPO production, the refinery business will have to improve its access to better quality of CPO to reduce refining cost and increase the proportion of higher margin products in certain refineries.
6.4.2 Property Development

In relation to the property business, a significant portion of the synergies is expected to be harnessed from scale advantage, the sharing of expertise which will result in adoption of best practices among the experienced property management teams of the Property division. The potential synergies arising from the merger of the property development businesses of the companies comprise both cost and revenue synergy, with the key areas as follows.

6.4.2.1 Cost synergies

The key potential areas which can be achieved in the course of cost synergies are as highlighted below:

a) Leveraging scale for price optimization from contractors and consultants

The group’s property development business can benefit from the combined scale of the Property division. The increased pool of contractors bidding for similar tenders by the group could lead to a potential reduction in construction costs as contractors offer competitive pricing to win the tenders.

On top of that, the property sub-committee are also exploring in awarding of contracts on a larger amount which able to allow the contractors/consultants in achieving economies of scale. This could result in lower construction costs for the property development projects. The group able to offer scale benefits/savings (i.e. spreading overheads across larger contracts and increase in procurement scale) to such contractors and thus may be able to share in the resultant scale benefits.
b) Sharing costing data to achieve “best practice” contractor prices

With the enlarged scale of the property development business, the Property division would be able to share internal costing methods to obtain the best contractor prices. In addition to the above key areas, other areas that provide potential cost synergies include sharing “best practice” project management experience within the Property division.

6.4.2.2 Revenue synergies

a) Optimizing pricing with better market pricing information

Internal benchmarking of products of comparable quality will enable a better understanding of product pricing, leading to potential realization of higher selling prices. By close alignment and standardization of similar products with similar specifications and quality, the Property division could strategize to realign the selling prices and project launch dates to achieve revenue upside.

6.4.3 Corporate Services

The corporate services category of costs cover areas comprising Information Technology (IT), Human Resource (HR), finance and other corporate functions, centralized at and carried out by the respective management of the participating companies. The group had explored areas in which improvements can take place as a result of the integration of the participating companies. Amongst the initiatives for cost savings identified include:

- consolidation of HR operations into a single shared service model to be deployed across the group;
- consolidation of finance operations, covering areas such as reporting, accounting, budgeting, treasury and cash management;
- optimization of treasury functions through redeployment of excess cash and minimization of borrowings/negative carry; and
- reduction of cost in terms of other corporate functions such as insurance, corporate legal and secretarial fees, annual report preparation and shareholders’ meeting costs, directors’ fees and relocation of offices to maximize space utilization.

The Sime Darby Group expects that there will be huge costs involvement in merging and integrating the businesses operations of all the companies. This is one-time integration cost which comprises costs in relation to branding initiatives, initiatives for the realization of synergies in the areas of plantations, property development and corporate services, as well as fees in relation to the merger.

6.5 COMPETITIVE STRENGTHS

There a few competitive strengths which arise from the merger and subsequently relates to the group’s business. Among the competitive strengths noted are as follows:

6.5.1 Scale-driven revenue and cost synergies for plantations

Merger has enabled the group to have the enlarged palm oil business which will allow the group to achieve better in cost and revenue efficiencies. Looking at the location of palm estates, most of the group’s oil palm plantations are adjacent or close to each other. The
consolidation of such estates will generate revenue and cost synergies through lower overheads, mill optimisation and the sharing of best estate management practices, research and development (R&D) findings to further raise FFB yields. There will be savings from the elimination of duplicate R&D projects. The sheer size of the group’s planted area will also enable Sime Darby Group to implement cost-centric procurement and planting policies, which will lead towards achieving economies of scale.

### 6.5.2 Focused set of core businesses within Asia Pacific

Considering on the group’s core business, currently the business are focused within Asia Pacific. This merger, on the other hand will poised to benefit from population growth and economic development throughout the Asia Pacific region. Furthermore, both economic and population growth in the Asia Pacific region has outpaced comparing to Europe and North America in recent years and this trend is expected to continue within the next year.

(i) **Plantations**

Sime Darby Group will be the largest listed global palm oil originator with selective downstream participation. On top of that, demand for palm oil has been driven by consumer consumption of edible oils which will continue to be sustained by population growth throughout Asia Pacific. In line with growing biofuel usage in developed markets such as Europe also has driven to the demand for palm oil. This in a way has embarked Asian governments in looking at biofuel-friendly policies and which has anticipated in creating another source of demand in the longer term.
(ii) **Property**

Sime Darby Group has a great opportunity which arises from their diversifiable industry. This is because; there is a symbiotic relationship between property development and plantations. The group has prospects for migrations of prime land currently utilised as plantations to property development. Property prices in Kuala Lumpur are currently lower compared to those in other key Asian countries such as Singapore, Hong Kong and Japan. The rental yields are higher, which implies that there is further room for price appreciation.

(iii) **Heavy equipment**

This division will have exclusive Caterpillar dealer rights in several countries and territories across the Asia Pacific region. Heavy equipment dealers are expected to benefit from continued demand in the construction, mining, timber, and oil and gas industries on the back of economic development throughout the region, particularly in China.

(iv) **Motor**

Looking at motor business industry, the group will have BMW dealerships in various countries and territories in the Asia Pacific region, distributorship and dealership rights for other renowned marques, such as Hyundai, Land Rover and Ford. On the other hand, the rising prosperity and a number of growing
upper middle class are expected to sustain demand for automobiles, in particular for luxury marquee.

(v) **Energy and utilities**

Energy and utilities division will be a major oil and gas platform fabricator in Malaysia and will heavily involve in power generation. The current high oil and gas prices are driven by rapid regional economic development, particularly in China, which has consequently increased oil exploration, development and production activities. This will have a positive impact on the fabrication business. Demand for power generation will also increase in line with economic activity. The group currently have investments in port and water projects in China. Growing numbers of business volume with the opening of new industrial areas in China will increase port utilisation and water consumption.

### 6.5.3 Experienced management team

The Sime Darby Group will have an experienced management team with a good track record of successfully managing and expanding a set of diverse businesses throughout Asia Pacific. Sime Darby believes that the ability of the management team to adapt to various cultures and operating environments is essentials for their future success. This has been cultivated among all the employees with the slogan of “Ahead as One”.
6.6 POST MERGER - BUSINESS INTEGRATION

The merger has enabled Sime Darby Group to comprise the businesses of all the subsidiary and participating companies. The group currently owns 5 core businesses, namely, plantations, property, motor, heavy equipment, and energy and utilities.

6.6.1 Plantations business

With the completion of the Merger, the Plantations division will have a significant presence in both upstream and downstream palm oil activities. The Sime Darby Group becomes one of the global leaders in palm oil origination and industry. The principal operations of the Plantations division can be categorised into 3 categories:

i. FFB production for the estates;

ii. FFB milling which produce CPO and PK; and

iii. Downstream refinery of CPO and palm kernel oil (PKO) into value added products.

The Plantations division’s main production chain is illustrated in the diagram below:
Figure 6.3: Plantation’s Upstream and Downstream Activities

The division’s plantation activities are summarised as follows:

a. Develop, cultivate and manage oil palm plantation estates.

b. Other related upstream palm oil activities such as the production and/or sales of oil palm seeds and seedlings, research and cloning of oil palm for sale, and research and breeding programme of oil palm seeds for sale.
c. Milling of FFB into CPO and PK.

d. Production and sales of oils and fats (which includes specialty and end user fats).

e. Production and sales of biodiesel.

The production process is illustrated in the flow chart below and accompanied by a brief description of the process flow.

---

### Figure 6.4: Plantations production process flow

---

**a) Plantation process**

(i) The process begins with the careful selection of seeds which are then germinated and subsequently planted in polybags where the seedlings are tended in nurseries
for an approximate 11 to 12 months period before being planted in the field. The necessary land preparation and legume establishment is done before the seedlings are field planted in a triangular pattern.

(ii) Field upkeep and maintenance operations include fertiliser application, weed control, pest and disease control and maintenance of infrastructure such as roads and bridges.

(iii) Upon reaching maturity, which is about 3 years after field planting, harvesting will be carried out at intervals of 10 to 12 days throughout the oil palm’s economic life of 25 to 30 years.

(iv) The harvested FFB are collected and transported to the mills.

b) Milling process

(i) The FFB received must be processed soon after harvesting in order to ensure the production of high quality palm oil, particularly oil with low free fatty acids level.

All the incoming FFB will be weighed and recorded.

(ii) Thereafter, the FFB will go through various processes such as sterilisation, bunch stripping, oil extraction, oil clarification and purification as well as depericarping which will produce CPO and PK.

(iii) CPO and PK will then be delivered to our refineries or sold to third parties.

c) Refining process

(i) In the refinery, CPO and crude palm kernel oil (CPKO) are cleansed of impurities, gums, odour and fatty acids by various processes such as degumming,
bleaching, refining and deodorization.

(ii) In the fractionation process, the refined products are split into olein and stearin. Through multiple fractionation processes, various fractions such as palm mid-fractions, hard stearin of various qualities are produced for different applications.

(iii) With further treatment in the hydrogenation process and etherification process, the products are modified to meet specific quality and applications.

(iv) Products from the refinery include straight refined oils, olein, stearin, shortening, various fats blends and specialty fats which are dispatched in bulk and in various packages and containers.

d) **Oleochemical process**

(i) Basic oleochemicals; fatty acid, fatty alcohols, esters and glycerol are produced by the hydrolysis process where oils react with water to produce fatty acids and glycerol and transesterification process.

(ii) Fatty acids and fatty esters are further transformed through hydrogenation and reduction processes into fatty alcohols.

(iii) Derivatives of oleochemicals such as lubricants and methyl ester sulphonates are produced from esterification and sulphonation processes.

e) **Biodiesel process**

(i) Biodiesel is produced using inter-esterification process where refined oil is reacted with methanol using a catalyst. In the process, glycerine is also produced as a by-product.
(ii) The biodiesel from the reactor is cleansed of impurities by washing with water after which it goes through the drying process where the water is removed.

(iii) The by-product, glycerine, goes through the pre-treatment process prior to storage.

(iv) The biodiesel and glycerine are then delivered in bulk.

f) Consumer

In the consumer segment, the Plantations division produces products such as cooking oil, vegetable ghee, and frying fats under various packages and markets them under its own brands.

6.6.1.1 Plantations Business Operation & Activities

The Plantations division also involved in developing, cultivating and managing rubber plantations and other related downstream plantation activities such as manufacturing of latex concentrate, standard Malaysian rubber and epoxidised natural rubber, production and sales of rubber footwear products, and production and marketing of aeroponic vegetables. In addition, the Plantations division is involved in the provision of plantation/agricultural consultancy services which are not expected to form a large portion of the group’s plantations business.

Palm oil, and oils and fats are expected to be the major contributor to the plantation division’s operating results. Hence the discussion of the plantation business is centred upon the palm oil upstream and downstream activities.
a) **Upstream activities**

(i) **Plantations**

With the completion of the merger, the group seize a total of 543,579 hectare (Ha) plantations land bank spanning across both Malaysia and Indonesia. Out of this total, 524,626 Ha or 96.5% is already planted with palm oil trees.

(ii) **Mills**

The Plantations division owns 65 mills, of which 42 mills are located in Malaysia and the remaining 23 mills in Indonesia as stated in table below. For the financial year ended 30 June 2007, the Plantations division produced a total of 2,110,146 matric tonnes (MT) of CPO and 492,753 MT of PK. As part of the strategy to harness synergies from the Merger, there are plans to optimise mill routing and capacity utilisation by reorganising milling activities in the most cost efficient manner.

<table>
<thead>
<tr>
<th>Malaysia:</th>
<th>Mills</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Malaysia (Kedah, Perak, Selangor, Pahang and Terengganu)</td>
<td>16</td>
</tr>
<tr>
<td>Southern Malaysia (Negeri Sembilan, Melaka and Johor)</td>
<td>14</td>
</tr>
<tr>
<td>East Malaysia</td>
<td>12</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Indonesia:</th>
<th>Mills</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kalimantan/Sulawesi</td>
<td>14</td>
</tr>
<tr>
<td>Sumatera</td>
<td>9</td>
</tr>
</tbody>
</table>

**Total** 65

*Table 6.0: Mills owns by the Synergy Drive*
The yearly maximum capacity of the Plantations division is 14,961,000 MT of FFB (based on 20 hours per day, 300 days per year and the respective mill’s throughput capacity per hour). The average utilisation rate for the financial year ended 30 June 2007 is 66%, with 9,863,847 MT of total throughputs.

b) Downstream activities

The group’s activities comprise the oils and fats businesses which both are food and non food-based.

(i) Food-based operations

The Plantations division has edible oils and fats refineries in the Netherlands, Malaysia, Singapore, Thailand, Vietnam, South Africa, Morocco (associated company) and Bangladesh (associated company).

The refineries’ operations in the Netherlands are undertaken by Unimills B.V. (“Unimills”), one of the largest diversified oils and fats blend manufacturers in Europe, with products supplied mainly to manufacturers of margarine, dairy, confectionary and snack products. The major markets include Europe, North Africa and the Middle East.

The refineries’ operations in Malaysia are undertaken by Golden Jomalina Food Industries Sdn Bhd (“Golden Jomalina”), Austral Edible Oil Sdn Bhd (“Austral”) and Kempas Edible Oil Sendirian Berhad (“Kempas”).
Golden Jomalina produces a complete range of semi-refined and fully refined palm oil products and their fractions as well as refined PKO, supplied in bulk and various containers. In addition, it produces consumer products, ranging from vegetable ghee, shortening and dough fat to industrial margarine and cooking oil, packed in various materials and sizes.

Austral operates a refinery and a PK crushing plant in Bintulu, Sarawak. The company offers fully refined palm oil and its fractions, CPKO and PK cake. Its main markets are China, the Middle East and India. Kempas’s refinery is located in Pasir Gudang, Johor, and is one of the manufacturers of palm oil-based vegetable oil and specialty fats. The major markets are Thailand, Europe, Japan, Middle East, Russia, Ukraine, Mauritius and Algeria, where 90% of its produce is exported to and the remaining 10% is sold in the domestic market.

Sime Darby Edible Products Limited which is located in Jurong, Singapore, manufactures and markets soft oils i.e. sunflower oil, soya bean oil, ground nut oil, canola oil and dairy products. About 85% of its production is exported to the Middle East, African countries and other countries in Asia.
The refineries’ operations in Thailand are undertaken by Morakot Industries Public Company Limited (“Morakot”). Morakot is Thailand’s leading refiner and manufacturer of cooking oil under the “Morakot” brand. The company’s “Morakot” brand is the first palm-based cooking oil in Thailand to be awarded ‘Halal’ certification. Morakot’s production is mostly for domestic use and 20% of its production is exported to China, Cambodia, Laos, Vietnam and Myanmar.

In Vietnam, Golden Hope Nhabe Edible Oils Ltd’s refinery which is located in Ho Chi Minh City has its own brand of consumer packed cooking oils under the brand name “Marvela”. The company sells shortening and dough fat to industrial customers. About 80% of its production is for domestic sale and the rest are for export to Cambodia and Laos.

The operations in South Africa are undertaken by Hudson & Knight (Proprietary) Limited (“Hudson & Knight”), which operates a refinery and bakery fats business. Hudson & Knight also produces and sells cooking fats and frying oils through the “Holsum” and “Crispa” brands respectively. The primary market for its products is South Africa. Almost the entire produce is sold to the domestic market.
(ii) Non food-based operations

The Plantations division’s involvement in the non food-based operations, namely oleochemicals, is through Cognis Oleochemicals (M) Sdn Bhd ("Cognis"). Cognis is a producer of oleochemicals (fatty acids and glycerine) and oleochemical derivatives (oil field chemicals, ozone acids and lubricants). 80% of the oleochemicals are exported while the remaining 20% are for local market.

In February 2006, Cognis expanded its business beyond Malaysia by acquiring from Cognis Oleochemicals GmbH and its subsidiaries. The six companies are incorporated in the USA, Canada, Germany, Brazil, UK and Japan. The company also owns and operate oleochemical businesses with fatty acids, glycerine, hardened oils, triacetine, ozone acids, oilfield esters and chemicals, polyvinyl chloride lubricants and plasticisers.

In biodiesel, the Plantations division was one of the earliest to commercialise palm oil-based biodiesel production in Malaysia when it started its first dedicated biodiesel plant in mid-2006. Since then, the company has expanded its biodiesel business with commercial production of palm oil-based biodiesel at its second plant, which is in May 2007. The third plant is at Rotterdam, which was completed recently, 31 December 2007. Accordingly, the Plantations division have three biodiesel plants as
of 31 December 2007. The capacity and production of the biodiesel plants are as follows:

<table>
<thead>
<tr>
<th>Location of plant</th>
<th>Capacity (MT)</th>
<th>Current output (MT)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Teluk Panglima Garang, Selangor</td>
<td>30,000</td>
<td>15,800</td>
</tr>
<tr>
<td>Carey Island, Selangor</td>
<td>60,000</td>
<td>10,200</td>
</tr>
<tr>
<td>Rotterdam, Holland</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Table 6.1: Biodiesel Production Plants

c) Quality control

The Total Quality Management and Environmental Safety & Health unit (“TQM/ESH”) within the Plantations division are focussing on the growing challenges of stringent market requirements including product quality, certification, traceability and sustainable development. In order to achieve these objectives, the unit continuously implementing operating policies and guidelines that will govern and contribute positively to productivity, employees’ welfare, the community and the preservation of the environment.

The principle objective of TQM/ESH is to instil a culture of quality within the Plantations division. Having to say that, the group is aggressively undertaking the following measures:

- Introduce new processes that are safe, clean, cost effective and sustainable.
- Ensure compliance with all relevant laws, regulations and standards.
- Conduct regular monitoring and audits of all possible source of pollution that may deteriorate the environment.
- To make their employees and sub-contractors’ safety a priority.
d) Research & Development (R&D)

(i) Vision and strategies

The vision of the group’s R&D Centre is to be the premier private research institution for the business and technology driven for the benefit of the Plantations division of the group (“Vision”). The group have set out six key strategies to achieve their vision, which is as follows:

- Higher productivity and efficiency
- Waste to wealth
- Integration/value addition and creation
- Promotion of health and well being
- Product development and new uses
- Human capital development and retention

(ii) R&D team

The group’s R&D division consist a team of 153 scientists and officers. There are altogether three main R&D centres where research is carried out. The centres are as follows:

<table>
<thead>
<tr>
<th>Centre</th>
<th>Location</th>
<th>Activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guthrie Research Chemara</td>
<td>Seremban</td>
<td>plantation upstream</td>
</tr>
<tr>
<td>Golden Hope Research Centre</td>
<td>Carey Island, Banting</td>
<td>plantation upstream, downstream research</td>
</tr>
<tr>
<td>Sime Darby Technology Centre</td>
<td>Petaling Jaya, Selangor</td>
<td>specialises in biotechnology research</td>
</tr>
</tbody>
</table>

Table 6.2: R&D Centres and Activities
Moving forward, the group are in the midst of establishing a Seed Research Centre in Perlis to cater for the expanding food business of the group within the Northern Corridor Economic Region. The downstream research at Golden Hope Carey Island is currently involved in a smart partnership with the Food Valley Application Centre, Wageningen, Netherlands, in developing new and healthy oils and fats products. R&D will continue to play a significant role in the Group. Functionally, the R&D division can be summarised into the following six units as stated below:

- Quantum Leap
- Plantation
- Oils & Fats/Oleo
- Processing & Engineering
- Technology Transfer & Advisory
- Marketing (Agrotech)

The management of the R&D division are highly qualified and experienced in their respective areas.

(iii) R&D functions and activities

- Provision of technical and operational support services via the advancement of R&D to enable the group’s operations, in particular, the Plantations division, to achieve their current and future business plans.
- Leads investigations into scientific theories and applies existing and new theories and techniques to the design and development of new products and processes.

- Initiates and maintains extensive contacts with other significant contributors in the field of research, including government and private research institutions at both the national and international levels through mutually beneficial strategic alliances.

- Ensuring that all R&D works undertaken are in line with the group’s Quality, Environment and Biodiversity, Occupational Health & Safety and Food policies.

- Ensuring sustainability of R&D in the group by developing human capital through attraction of the best brains and adopting appropriate retention strategies.

- Transformation of the R&D Centre of the group into a premier private research institution that is business and technology driven in the plantations industry.

(iv) Future R&D plans

Over the next two years, 16 key initiatives will be vigorously worked on in preparation for launching. Going forward, the R&D team has identified 10 key areas for the group’s R&D which is as follows:

- Utilisation of biomass of oil palm as value-added products;

- Bioethanol from palm biomass;

- Biodiesel from palm oil through use of microbes;
- Biopolymers from palm oil;
- Oil palm breeding for special traits;
- Palm puree for phytonutrients and plant-based pharmaceuticals;
- Peat research;
- Mechanisation, automation and plant design;
- Novel oils & fats and oleochemical products; and
- Non-oil palm biotechnology products.

(v) **Key R&D achievements**

There are more than 30 significant technologies developed by the plantations industry that had made it as a golden industry and a Malaysian success story. Over the last 80 years, R&D under the group has contributed considerably in developing and pioneering best management practices and in many instances, assisted in commercialising them. The more notable best practices include:

- Making available superior planting materials for use by the industry;
- Introduction of the innovative zero burning technique;
- Stewardship in Integrated Pest Management;
- Water conservation and management practices for achieving high yields;
- Integrated FFB collection and evacuation system;
- Management of inoculums in the field for control of Ganoderma
disease;

- Utilisation of Palm Oil Mill Effluent, empty fruit bunches (EFB) and compost as organic manure;
- Environment friendly oils and fats products via enzymatic process; and
- Production of healthy oils and fats products.

(vi) R&D expenditure

Generally, the expenditure for R&D for the past 3 financial years ended 30 June 2005 to 2007 is as table 4.3 below:

<table>
<thead>
<tr>
<th>R&amp;D expenditure</th>
<th>For the financial year ended 30 June</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2005 (RM 000)</td>
</tr>
<tr>
<td></td>
<td>27,343</td>
</tr>
</tbody>
</table>

Table 6.3: R&D Expenditure

6.6.2 Property business

The Group’s property business comprises the existing property businesses of Golden Hope Group, KGB Group and Sime Darby Group. The Property division is positioned as an established integrated property player, presently focused on property development. The Property division’s current focus is on developing residential and commercial properties. In addition, the group does have other complementary operations such as property investment, property management and hospitality.
In the line to satisfy and cater for different consumer demands and preferences, the Property division has developed different types of residential and commercial properties in various locations in Malaysia, particularly focusing in the areas of Klang Valley and Selangor, as well as in Singapore. The properties range from low-cost to high-end, landed to high-rise, and freehold to leasehold units. In addition, the residential units have designs ranging from linked/semi-detached/bungalows/strata and design features/themes to cater for the discerning property purchasers.

As a property developer, the Property division assesses and determines the property type and mix of their respective developments based on the current and anticipated consumer demand and property market outlook. The Property division has land banks throughout various locations in the Klang Valley and Selangor.

6.6.2.1 Current ongoing/developed properties

As at 30 June 2007, the property development projects in Malaysia by the Property division has a total gross development value (GDV) in excess of RM18 billion while the total sales value since the launch of these properties are in excess of RM9 billion. The property developments in Singapore have a total GDV of SGD248.7 million while the sales value since the launch of these projects in Singapore amount to a total of SGD238.0 million. We set out below a brief description of the major properties that have been developed and currently being developed by the Property division in both Malaysia and Singapore.
a) **Major property developments in Malaysia**

(i) The Melawati Township is a 486 Ha township, of which 411 Ha have been developed as at 30 June 2007, located strategically near the Middle Ring Road II ("MRR2") comprising commercial and residential properties with a GDV of RM1988.8 million and a take-up rate of 100% as at 30 June 2007.

(ii) The Saujana Impian Township in Kajang is a 243 Ha resort-themed township, of which 174 Ha have been developed as at 30 June 2007, with a GDV of RM617.3 million and a take-up rate of 93% as at 30 June 2007. It is easily accessible via several major highways such as the Kuala Lumpur-Seremban Highway, Shah Alam Expressway, South Klang Valley Expressway and the MRR2.

(iii) Nilai Impian and Nilai Utama Enterprise Park ("NUEP") are modern and integrated mixed-developments comprising industrial, commercial and residential components with a GDV of RM1,180.2 million and a take-up rate of 75% as at 30 June 2007. Nilai Impian and NUEP cover an area of 522.4 Ha, of which 243 Ha have been developed as at 30 June 2007, and are located along the Kuala Lumpur-Seremban Highway.

(iv) Bukit Jelutong is located in Shah Alam. Launched in 1995, Bukit Jelutong is a low density township designed with wide open spaces and landscaped recreational parks. It is a mixed development of residential, commercial and industrial properties on 892 Ha of freehold land, of which 771 Ha have been developed as at
30 June 2007, with a GDV of RM4,317.5 million and a take-up rate of approximately 97% as at 30 June 2007. Bukit Jelutong is accessible via the Federal Highway, North Klang Valley Expressway (“NKVE”), North-South Expressway Central Link (“ELITE”) and Guthrie Corridor Expressway (GCE).

(v) Bukit Subang 1 is located approximately 7 km to the North of Bukit Jelutong and 13 km from the city centre of Shah Alam. Launched in 1998, Bukit Subang 1 comprises affordable low-cost to medium-cost residential and commercial properties on 101 Ha of freehold land, all of which have been developed as at 30 June 2007, with a GDV of RM368.3 million and a take-up rate of approximately 98% as at 30 June 2007.

(vi) Denai Alam (previously known as Bukit Subang 2) is located along the GCE and about 5 km North of Bukit Jelutong. The Denai Alam township is planned according to a unique “Denai” concept which is a 4.8 km continuous green space surrounding the development. Planned as a mixed development, Denai Alam comprises medium-cost to high-end double-storey linked houses and commercial properties on 372 Ha of freehold land, of which 125 Ha have been developed as at 30 June 2007, with a total GDV of RM1,950.6 million. The development was launched in November 2004 and recorded approximately RM153.5 million of sales and a take-up rate of approximately 71% as at 30 June 2007.

(vii) Sungai Kapar Indah is a self-contained mixed-development located in Klang. Sungai Kapar Indah comprises low-cost and medium-cost residential units and
commercial properties on 251 Ha of land, all of which has been developed as at 30 June 2007, with an estimated GDV of RM543.6 million and a take-up rate of 99% as at 30 June 2007.

(viii) Putra Heights is a 727 Ha township, of which 641.7 Ha has been developed as at 30 June 2007, situated in the Klang Valley, and comprises mixed development of landed residential properties and shop-office properties. Launched in 1999, the total GDV launched of Putra Heights is RM1,879.3 million whilst the average take-up rate is 93.7% as at 30 June 2007. Putra Heights is strategically situated along the North-South highway which leads to Putrajaya, Cyberjaya and the Kuala Lumpur International Airport, and can be accessed via the Lebuhraya Damansara Puchong.

(ix) Bandar Bukit Raja is an integrated and self-contained township in Klang, spanning 2,180 Ha, of which 527.8 Ha have been developed as at 30 June 2007. Launched in August 2002, Bandar Bukit Raja comprises residential properties such as low-cost apartments and linkhomes. In addition, the development in Bandar Bukit Raja comprises commercial, institutional and industrial properties. The total GDV launched of Bandar Bukit Raja is RM430.5 million whilst the average take-up rate is 76.1% as at 30 June 2007. Bandar Bukit Raja is accessible via various transportation networks such as the Federal Highway, NKVE and New North-Klang Straits Bypass.

(x) Ara Damansara is a 315.8 Ha development, of which 249.8 Ha has been developed as at 30 June 2007, located along the Sultan Aziz Shah International
Airport Road, between Saujana Golf and Country Club, and Tropicana Golf and Country Resort. Launched in 1999, Ara Damansara comprises residential and commercial properties. The residential properties in Ara Damansara include landed properties, medium-cost and low-cost apartments, and the newly-launched high-end luxury condominiums. Ara Damansara is accessible via the Federal Highway and NKVE. The total GDV launched of Ara Damansara is RM1319.7 million whilst the take-up rate is 88.1% as at 30 June 2007.

The properties developed in Pinggiran USJ and Taman Perindustrian USJ comprises double-storey linked homes and double-storey shop-offices. The total GDV launched is RM443.1 million whilst the average take-up rate is 93.7% as at 30 June 2007. The total GDV launched of Taman Perindustrian USJ is RM340.2 million whilst the average take-up rate is 96.4% as at 30 June 2007.

In addition, the Property division also has substantial land bank along the GCE which has immediate and medium term growth prospects. The land banks are strategically located at the various interchanges along the GCE at Bukit Subang 1, Denai Alam, Ladang Elmina and Ladang Lagong.

(b) Major property developments in Singapore

(i) The Orion is a 27-storey freehold residential development located at 6C Orange Grove Road, Singapore. As at 30 June 2007, the Orion has a GDV of SGD105.7 million with a take-up rate of 89.9%. The Orion is priced at an average of SGD1,470 per square foot.
(ii) Balmoral Hills is a residential development set on the high ground at Balmoral Park in prime district 10. Launched in the second half of 2005, the twin 12-storey blocks comprise 62 freehold apartments priced at an average of SGD1,233 per square foot. As at 30 June 2007, Balmoral Hills had a GDV of SGD143.0 million with a take-up rate of 100%.

6.6.2.2 Development land bank
The land bank available for immediate development over the next 5 years is approximately 8,700 acres, of which the bulk of 3,874 acres of undeveloped property land bank are strategically located in Klang Valley and Selangor.

6.6.2.3 Involvement in other types of property business
Apart from property development, the group is also involved in other types of property business such as asset management, hospitality and property investment. The range of business activities by the Property division includes service residences, resorts, golf courses, industrial parks and a convention centre. These businesses are located in Malaysia, Singapore, Australia, Indonesia, Vietnam, the Philippines, China and UK.

Besides that, the group also ventures into asset management services in Malaysia, Singapore, Indonesia, the Philippines, and UK. On top of that, property investment activities are carried out in Malaysia and China. In the area of hospitality, the Property division operates, PNB Darby Park, Sime Darby Convention Centre, Kuala Lumpur Golf & Country Club, Hotel Equatorial Melaka (Malaysia), Darby Park Executive Suites
(Singapore), Karri Valley Resort, Quest Subiaco and Quest Margaret River (Australia), and Rangdong Orange Court Service Residences (Vietnam).

6.6.2.4 Sales and marketing
The Property division markets its property launches through previews or soft launches, newspaper advertorials for the pre-launch and official launches, brochures, leaflets, signboards, billboards, model/show houses, and write-ups of projects in newspapers. In general, repeat buyers or interested buyers who have registered their details as well as residents living in the vicinity of the development are invited to the previews or soft launches at which discounts may be offered to buyers who place a deposit for a residential or commercial property during one of these events.

6.6.2.5 Contractors
As the Property division is principally involved in property development, the division relies on a pool of contractors with whom strong working relationships have been forged over the years to undertake the construction of the properties. The selection of contractors is based on a tendering process to ensure competitive pricing and takes into account their experience, track record and qualifications. In the context of larger projects, contracts may be awarded to more than one qualified and reputable contractor. The Property division does not foresee any significant challenges in sourcing or securing contractors for their various projects because the division has not been dependent on any one main contractor.
6.6.2.6 Quality control

The Property division places great emphasis on the quality of the developed properties. They maintain close monitoring and supervision of the works carried out by the awarded contractors. The strengths in quality control have been reflected in the timely delivery of projects and minimal building defects, as well as our subsidiaries garnering several quality certifications such as with ISO9001:2000 Certification of Quality Management System, OHSAS 18001:2006 for Health and Safety, and EMS 14001:2006 for Environmental Management System. In addition, the division also have institute a quality control unit.

6.6.2.7 Market research

The Property division undertakes continuous market research to ensure marketability of the products which is to be launched in the future. R&D and innovation have been emphasised in the operations. In addition, the division do practice in engaging best and independent property/market consultants for its development review.

6.6.3 Motor business

The Motor division has distributorships and/or dealerships for some of the well known marques in Malaysia, Singapore, Thailand, China including Hong Kong and Macau, Australia, and New Zealand. We had listed below in table 4.4 on the countries where the Motor division operates and the distributorships and/or dealerships that the division holds in the respective countries.
<table>
<thead>
<tr>
<th>Country</th>
<th>Marque</th>
</tr>
</thead>
<tbody>
<tr>
<td>Malaysia</td>
<td>BMW, MINI, Ford, Land Rover, Hyundai, Inokom and Alfa Romeo</td>
</tr>
<tr>
<td>Singapore</td>
<td>BMW, Ford, Land Rover and Peugeot</td>
</tr>
<tr>
<td>Thailand</td>
<td>BMW, Mazda, Chevrolet and Volvo</td>
</tr>
<tr>
<td>China</td>
<td>BMW, MINI, Suzuki, Mitsubishi, Ford, Land Rover, Rolls-Royce, Huanghai Bus and Peugeot</td>
</tr>
<tr>
<td>Australia</td>
<td>Peugeot</td>
</tr>
<tr>
<td>New Zealand</td>
<td>BMW, Alfa Romeo, Audi, Chrysler, Ferrari, Fiat, Jeep, Maserati, Peugeot, Porsche, Suzuki, Volkswagen, Kia and Nissan for cars, and Hino, Mack, Renault and Nissan for trucks</td>
</tr>
</tbody>
</table>

**Table 6.4: Group Motor’s Operation**

In the event of marques, whereby the division holds a distributorship license from the principal, the division is authorised to distribute the respective marque’s vehicles to the authorised dealers in the country. As a distributor, the division do also directly sell a marque’s vehicles to the end users. For marques whereby the division holds a dealership license from a marque’s distributorship in the country, the division is authorised to sell a particular marque’s vehicles to end users.

The Motor division obtains the supply of motor vehicles from its principals and/or distributors, depending on whether it holds a distributorship and/or dealership license for a particular marque. The division maintains a close and cordial relationship with these principals and/or distributors. As the division distributes and/or sells several marques across the region, the risk of over-reliance on a single marque for its operation is minimised.
The Motor division also operates two assembly plants in Malaysia where the complete knocked down (CKD) packs are imported from the respective principals from Thailand, Korea, India, USA and Germany and then locally-assembled for sale mainly in the Malaysian market. In ensuring high standard and quality products, the locally-assembled motor vehicles are subjected to a stringent pre-delivery inspection test. The outputs of the assembly plants are very much dependent on the demand for the vehicles.

6.6.4 Heavy equipment business

The group’s Heavy Equipment division holds exclusive Caterpillar dealer rights for the sale and rental of Caterpillar heavy equipment, parts and service support in Malaysia, Singapore, Hong Kong, Brunei, China (seven provinces), the states of Queensland and Northern Territory of Australia, Papua New Guinea, New Caledonia, the Solomon Islands, Republic of Maldives and Christmas Island (Indian Ocean). The Heavy Equipment division also carries other brands of heavy equipment including Case New Holland, Kubota, Terberg, Driltech, Kress and Mitsubishi Caterpillar Forklift. The division also provides product support services to its customers through long-term maintenance agreements.

The principal markets for the Heavy Equipment division are natural resource extraction, building and infrastructure construction, electrical power generation, and other capital goods manufacture, logging, construction, mining, oil and gas and agriculture. The heavy equipment business in Australia contributes to the bulk of income for the Heavy
Equipment division due to the rapid growth in the mining industry in Australia in recent years.

In Malaysia, the Heavy Equipment division is led by Tractors Malaysia Holdings Berhad (TMB). TMB primarily involved in the sale, rental, distribution and support of Caterpillar heavy equipment, Case New Holland agricultural machinery and other related equipment.

In Singapore, Tractors Singapore Ltd specialises in the design, supply, testing and commissioning of power system packages for the marine/petroleum sector, in addition to the sale and rental of heavy equipment to the construction sector.

In China, The China Engineers, Limited is the dealer of Caterpillar in Hong Kong, Macau and seven provinces in China.

In Australia, this business is handled through the Hastings Deering group which covers Queensland and Northern Territory in Australia, Papua New Guinea, New Caledonia and the Solomon Islands. These territories are rich in mineral resources, and the Heavy Equipment division in Australia provides parts and service support for heavy equipment and supplies equipment for the mining industry. The current global growth cycle has impacted commodity prices, particularly coal in Australia, which in turn has resulted in high demand for mining equipment. The mining cycle results in high demand for prime
products at mine start stage and then again at machine replacement stage either at the end of the machine life or at the end of the mine life.

The marketing activities for Caterpillar equipment are generally carried out by the division’s representatives in the countries in which it operates through displays, demonstrations, field shows, advertising and direct mail.

6.6.5 Energy and utilities business

The Energy and Utilities division comprises 3 segments as follows:

6.6.5.1 Power and utility

The operations of the power segment of the Energy and Utilities division are undertaken by Port Dickson Power Berhad (“PD Power”), JanaUrus PDP Sdn Bhd and Laem Chabang Power Co Ltd (“LCP”). There are two power plants as follows:

a) 440 MW open cycle power plant operated by PD Power, an independent power producer in Tanjong Gemuk, Port Dickson in Malaysia; and

b) 103.5 MW electricity and 50 tonne per hour steam co-generation power plant operated by LCP in Laem Chabang Industrial Estate, Chonburi in Thailand. Currently, there are capacity expansion plans underway to increase LCP’s plant capacity by 55 MW (electricity) and 25 tonne per hour (steam) by the year end of 2008.
PD Power’s power plant supplies its daily available capacity and electrical energy to Tenaga Nasional Berhad (“TNB”). As a result of the Power Purchase Agreement (“PPA”) entered into between PD Power and TNB, PD Power has a secured offtaker for the electrical energy output from its power plant. The PPA is for a period of 21 years commencing from 1993. PD Power’s plant uses gas that is supplied by Petronas Gas. Any volatility in the price of gas will be passed through to TNB. The operation and maintenance of PD Power’s plant is managed by JanaUrus PDP Sdn Bhd.

LCP’s power plant sells its electricity to the national utility company of Thailand, Electricity General Authority of Thailand (“EGAT”), as well as steam and electricity to industrial customers within the Laem Chabang Industrial Estate. Gas for the LCP power plant is supplied by Petroleum Authority of Thailand whereby any fluctuations in gas prices are passed through to EGAT. Industrial customers are charged prices at a slight discount to the published tariff which is adjusted on a quarterly basis in tandem with fuel price movements.

The net book values of the PD Power plant and LCP plant are RM264 million and RM253 million respectively as at 30 June 2007.

6.6.5.2 Oil and gas

The oil and gas segment of the Energy and Utilities division specialises in the fabrication of all types of offshore structures and complexes. It is capable of supporting full upstream value chain as a one stop solution centre for the oil and gas engineering needs such as
total solution from concept to design engineering, fabrication, procurement and hook-up, commissioning as well as installation.

The range of products and services offered are offshore platform topside modules; offshore platform jackets; module support frames; production, compression, water injection, process, power generation modules; integrated decks; helidecks; living quarters; hook up and commissioning; decommissioning; and the provision of fabrication, construction and support services for offshore engineering.

Its 100 acre fabrication yard is located at Pasir Gudang, Johor Bahru. The division owns one of the largest fabrication yards for offshore facilities, with a load out capacity of 15,000 MT and a fabrication capacity of 50,000 MT per year. Its local and international customers include Petronas Carigali, Shell, Exxon Mobil, Maersk, Qatar Petroleum and Murphy Oil Corporation.

The operating process involves the initial engineering of the structure, followed by the purchase of steel and equipment before the start of the construction. Testing and commissioning is carried out, after which the completed structure is loaded up and transported by barges to its final destination.

The key components, steel and equipment such as firewater pump generators, which are used in the fabrication process, are sourced from abroad. All bids have a fixed validity
period after which the contract value may be revised to accommodate steel price increases, thereby reducing volatility on margin.

Presently, the oil and gas segment leads the consortium of companies responsible for the construction of the main civil works for the Bakun Hydroelectric Project in Sarawak. In addition, it also provides the operation and maintenance services to the oil and gas and petrochemical industries. Given the division’s experience in providing fabrication and engineering construction services, it is continuously identifying opportunities to venture into new projects.

6.6.5.3 Engineering

The group’s engineering business is involved in amongst others; trading, design and fabrication, projects and system integration of a wide range of engineering solutions and products.

The division’s engineering activities are focused on four areas, which is:

(a) ventilation and environment control including industrial fans, boilers and filter presses;

(b) life science including the supply of scientific instruments and life science products for use at government institutions, hospitals, universities, pharmaceuticals, testing labs, petrochemicals and electronic industries;

(c) intelligent traffic management including car park systems, car park barrier systems, car park guidance systems; and
(d) SCADA, a supervisory and remote control system that allows automation control.

The division operates its engineering business from its offices in Singapore, Malaysia and Thailand. Its manufacturing facility is located in Singapore where its own proprietary products are designed and fabricated for specific orders. This segment designs and fabricates its own proprietary products for industrial ventilation fans, filter presses and intelligent car park management system. The group also involved in projects and systems integration of a wide range of engineering solutions and products. The engineering segment is migrating from traditional trading towards providing integrated one-stop solutions to meet customers’ needs. Its products and services are generally marketed through trade shows, exhibitions, advertisement and presentations to major customers.
CHAPTER 7: RESEARCH ANALYSIS AND RESULTS

7.1 PRICING OF THE MERGER ENTITIES

In any M&A or takeover deal, putting the right price to the target is a paramount process. In order to arrive at the right or fair price, knowing what an asset is worth and what determines that value is prerequisite for intelligent decision making (Damodaran, 2006). In determining the indicative price to be offered to the target companies, the share prices were estimated by comparing some successful M&A deals and compared with the company valuation with DCF valuation, a popularly used in investment evaluation technique to determine the fair price for a private company.

7.1.1 Offer Prices Based On Indicative Valuation

The whole merger exercise was completed mostly through share swaps, even though cash settlement was offered for Negara Properties shares holders who opted for the latter. This is done by issuance of RCPS by the Synergy Drive.

7.1.2 Fair Valuation Based On DCF

Being as an ongoing concern, the company was valued using the cost of capital approach by discounting the free cash flow to the firm (FCFF) at the weighted average cost of capital (WACC). The determination of firm’s value of the operating assets in this
Discounted Cash Flow (DCF) model would depend on assumptions made about its future growth. The value of firm derived from the value of operating assets of that company on a going concern assumption can be written as the present value of the expected cash flows to the firm as follows:

**Valuing firm operating assets:**

\[
\text{Value of firm} = \sum FCFF_t / (1+WACC)^t
\]

Where, \( FCFF_t \) = expected FCFF to firm in year \( t \)

\( WACC = \) weighted average cost of capital

In an assumption that the firm reaches steady state after \( n \) years and starts growing at a stable growth rate \( gn \) after that, the value of the firm can be written as follows:

**Value of operating assets of the firm**

\[
= \sum FCFF_t / (1+WACC)^t + [FCFF_{n+1}/(WACC-gn)] / [1+WACC]^n
\]

The formula for the calculation of WACC is as follows:

\[
WACC = [D/(D+E)] \times (Kd) + [E/(D+E)] \times (Ke)
\]

Where, \( Kd = \) cost of debt,

\( Ke = \) cost of equity

**Calculation of Cost of Debt, Kd:**

\[Kd = Rd(1-tax)\]

Where, \( Rd = \) rate of return on debt

\( Tax = \) taxation rate of the firm
Basis for calculation, $R_d$ is Base Lending Rate (BLR) + % of company’s credit risk. Whereby, the BLR is based on the average conventional financing and % of company’s credit risk is based on the basis points of risk premium of the company’s corporate bond rating.

**Calculation of Cost of Equity, $K_e$:**

$K_e$ based on Capital Asset Pricing Model (CAPM):

$$K_e = R_f + \beta (R_m - R_f)$$

Where, $R_f$ = risk free rate of return

$\beta$ = beta of the company

$R_m$ = return on market

The risk free rate of return, $R_f$, is based on the annual historical average rate of return on 5-year Malaysian Government Securities (MGS).

The return on market, $R_m$, is based on the 15 years historical average rate of return of the price index of the Kuala Lumpur Composite Index (KLCI).

The market risk premium is estimated by,

$$R_p = (R_m - R_f)$$
We did estimate Beta for the target companies, \( \beta \). The respective beta were determined by regression analysis on the earnings return of the respective companies (\( R_p \)) against the market return (\( R_m \)). The formula for beta estimation is as follows:

\[
R_p = \alpha + \beta (R_m)
\]

Where, \( \alpha = \) intercept from the regression
\( \beta = \) slope of the regression,
\( \beta = \text{Cov}[R_p,R_m] / \text{Var}[R_m] \)

The calculated \( \beta \) is an unlevered beta given that the company was debt free. For FCFF modelling, levered beta would be calculated based on an optimal capital structure, with an ideal composition of debt and equity in the firm valuation. The determination of the optimal structure of capital for the takeover financing based on the indication of the multiples of the equity premium so as to be in line with the industry practice.

**Calculation of WACC:**

\[
\text{WACC} = \left( \frac{D}{D+E} \right) \times (K_d) + \left( \frac{E}{D+E} \right) \times (K_e)
\]

Whereby, \( D/ (D+E) \) is the ratio of the companies long term debt against the total capital whereas \( D/(D+E) \) refers to the ratio of the shareholders equity over the total capital.

**7.2 ESTIMATION OF TARGET COMPANIES VALUE’S**
Based on the above estimations, we manage to derive the valuation each of the individual target companies, which is as follows:

7.2.1 Sime Darby 5-Years Projection

This mega merger is to create the world’s largest palm oil plantation company. With its total combined land bank of 602,000ha and planted acreage of 522,200ha (including 8,380ha of rubber land), the plantation division would remain the key attraction for Synergy Drive. In analyzing the financial aspect of the merger, we’ll be looking on the income statement and balance sheet projection for the next 5 years with a focus on Sime Darby, Golden Hope and Guthrie.

On individual valuation, Sime Darby recorded a net profit of RM4.92b (EPS 1.95), RM5.90b (EPS: 2.34) and RM7.81b (ESP: 3.10) for FY08, FY09 and FY10 respectively based on the following conservative assumptions:

(i) Sime Darby's business plan refocuses the company to capitalize on its core strengths particularly in Plantations and Properties as these 2 sectors mainly contributed to the total revenue. Modest annual average market growth based on moving average method of 9%-11% is expected to start in two years time. Sime Darby's initiatives are expected to provide significant average market growth of around 8% over the following 3 years by gaining market share in the global markets when the three companies combined.
Cost of sales is affected by the merger activities. Restructuring of operations is expected to increase cost of sales in the initial two years, after which cost of sales will decline. On average the cost of sales based on moving average method is stated at average 63.2% of total revenue. Bringing down the Cost of Sales to 58% over the next five years will be achieved through the elimination of overlapping project in the combined companies and the improvement of supply chain performance and economics post-merger.

(ii) In terms of the Income Statement, Depreciation as percent of Gross Fixed Assets has been estimated at the average ratio over the historical period.

(iii) Employees Benefit is based on moving average method and expected to remain at 7.5% of sales for the next 5 years.

(iv) Other Operating Expenses are expected to remain at 15.6% for the next five years.

(v) With the combination of the three companies, the operating expenses is expected to be at constant rate and any increase in future will be compensated by the effective budget planning by the new combined entity.
Interest rates in general are expected to increase from all time historic lows by a conservative half percentage point per year due to natural economic forces.

The interest on Debt is constant based on conservative assumption at the maximum rate since 2006.

The tax rate shown includes deferred taxes, which is a significant factor in determining the effective tax rate. The effective tax rate was not constant historically. But it will be set at 27% in 2007 taking effect of the current tax.

Deferred acquisition costs has contributed to a significant portion of Other Assets, but is expected to decline as costs are paid off. Due to the combination of these factors, it is expected that Other Assets will decline the next few years.

With the combination of the land banks, factories and mills of the three companies, Sime Darby is expecting an average of 45.8% of PPE in the next five years.

To ensure sufficient liquidity a minimum cash balance of 11.7% is included in the forecast.
Current Liabilities are expected to increase 0.5% in the next five years as a result of severance pay and other costs occurring from its acquisitions initiatives. This percentage is expected to be reduced gradually over the forecast period as the current portion of long-term debt is expected to decrease over time as debt matures.

### 7.2.1.1 Free Cash Flow and Terminal Value

In the four years forecast period, explicit forecasts of free cash flow has been developed which has incorporated the economic costs and benefits of the transaction. The free cash flows for every year have been computed as figure 7.0 below:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>(+) Depreciation &amp; Amortization</td>
<td>376,700</td>
<td>677,400</td>
<td>722,491,029</td>
<td>767,829,605</td>
<td>817,964,484</td>
<td>871,026,457</td>
<td>927,038,732</td>
</tr>
<tr>
<td>(-) Change in Working Capital</td>
<td>100,200</td>
<td>84,900</td>
<td>1,077,399,436</td>
<td>256,797,313</td>
<td>331,501,470</td>
<td>330,512,163</td>
<td>670,300,499</td>
</tr>
<tr>
<td>(-) Capital Expenditure</td>
<td>738,700</td>
<td>990,500</td>
<td>1,101,859,969</td>
<td>1,234,083,166</td>
<td>1,382,173,145</td>
<td>1,534,212,191</td>
<td>1,702,975,532</td>
</tr>
<tr>
<td><strong>Free Cash Flow of Firm</strong></td>
<td>405,760,000</td>
<td>3,095,872,000</td>
<td>2,361,155,340</td>
<td>3,170,296,448</td>
<td>3,077,782,207</td>
<td>2,723,735,732</td>
<td>1,882,053,160</td>
</tr>
</tbody>
</table>

**Figure 7.0: Sime Darby’s Free Cash Flow**

The value of the company derived from free cash flows occurring after the forecast period was captured by a terminal value. Terminal value is estimated in the last year of
the forecast period and capitalizes the present value of all future cash flows beyond the forecast period.

To estimate the terminal value, cash flows are projected under a steady state assumption that the firm enjoys no opportunities for abnormal growth or that expected returns equal the required returns following the forecast period following the forecast period.

In determining the terminal value, the adjusted cost of capital of 8.36% was first calculated as below. The calculation for Cost of Equity and Capital are as figure 7.1 below.

![Calculation of Cost of Equity and Capital](#)

<table>
<thead>
<tr>
<th>Calculation of Cost of Equity and Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk-free Rate (Avg 5-yr MGS Bond)</td>
</tr>
<tr>
<td>SD's Unlevered Beta</td>
</tr>
<tr>
<td>SD's Target D/E Ratio</td>
</tr>
<tr>
<td>SD's Target Tax Rate</td>
</tr>
<tr>
<td>SD's Levered Beta</td>
</tr>
<tr>
<td>Market Risk Premium</td>
</tr>
<tr>
<td>SD's Cost of Debt</td>
</tr>
<tr>
<td>SD's Cost of Equity</td>
</tr>
<tr>
<td>SD's Weighted Cost of Capital</td>
</tr>
</tbody>
</table>

*Figure 7.1: Calculation of Cost of Equity and Capital (Sime Darby)*

The terminal value after the 5th year was calculated at RM 10.9 billion. The total net present value of Sime Darby cash flows for the five years, inclusive of the terminal value
of the project, and discounted back by its Cost of Capital to the present is RM 9.7 billion as illustrated below in figure 7.2. The calculation has resulted in a Market Value of Sime Darby at RM 30.6 billion and by taking into consideration the market value of long-term debt of RM 2.2 billion, the Net Equity Value was recorded at RM 31.1 billion and Equity Value per share of RM 12.40.

| RM, million |
|------------------|------------------|
| PV of Terminal Value | 10,913.3 |
| PV of FCFF         | 9,672.8          |
| Market Value of the Firm | 30,579.4 |
| (-) Market value of LT Debt | 2,285 |
| (+) Excess Cash (Investment) | 2,275 |
| Equity Value       | 30,569.4 |
| Equity Value per Share | 12.40          |

Figure 7.2: Sime Darby’s Market Value

7.2.2 Golden Hope 5-years Projection

The projection of income statement and balance sheet for the next five years from 2007 to 2011 is based on the following assumptions:

(i) Sales growth rate on average increases at 19.6% for the past 5 years. For the projection, Golden Hope is forecasted to increase its sales according to the moving average growth rate for the past historical 5 years. The increase in forecast is also due to the forecasted increase price for crude
palm oil (CPO) in 2007 and onwards. However, the company is embarking big on oleo-chemical business therefore the high cost of raw materials may affect the earning.

(ii) Cost of sales is projected to remain fairly high in the range of 78% of revenue according to moving average cost of sales for the past 5 years. It is forecasted to increase due to high cost of materials for its downstream businesses.

(iii) Depreciation as a percentage of fixed assets is forecasted constant to be constant at 2.1%. This is based on the average depreciation for the past 5 years.

(iv) Selling expenses is forecasted to increase based on the moving average expenses of the past 5 years, while general and administration expenses is forecasted to be constantly increasing at 6.5% based on the average of the last five historical ratios.

(v) Tax rate is kept constant at 27% for the next projected 5 years, based on the standard corporate tax rate.

(vi) Minority interest is kept constant for the projected 5 years.
(vii) Investment is forecasted to increase moderately as a percentage of fixed assets. This is assuming that Golden Hope does not taking new debts to fund its fixed assets.

(viii) Other assets are forecasted modestly as the moving average of the past 2 years’ percentage of sales. There is no significant increase in other assets despite the increase in sales.

(ix) Cash balance is kept constant at 6.5% starting 2007, since Golden Hope needs to fund its operation while having minimal debts.

(x) Other current operating assets are forecasted to be the moving average of past 2 years’ percentage of sales.

(xi) Gross fixed assets are forecasted to be decreasing due to the high percentage of fixed assets of sales. This is projected to improve the firm’s return on assets.

(xii) Current liabilities are kept low as a percentage of sales, at 25% of sales for the next 5 years. Other liabilities increase at the same growth rate as net sales.

(xiii) Minority interest in consolidated subsidiaries is increasing at the rate of 15% of previous year's minority interest.
7.2.2.1 Estimation of Cost of Equity and Cost of Capital

Golden Hope’s cost of equity and cost of debt is calculated to derive its weighted average cost of capital (WACC). To estimate Golden Hope’s cost of equity, risk-free rate is obtained from the average of 5 years of MGS. Golden Hope’s beta is 0.81. Based on Golden Hope’s beta, risk-free rate and market premium, the company’s cost of equity is calculated to be 9.52%.

Cost of debt for Golden Hope is derived by calculating the market value of Golden Hope’s long term debts. Based on the company’s existing debts as at end of 2006, the debt maturity schedule is prepared. It is assumed that the company does not issue new debts during the projected 5 years. By analyzing its existing debts, the total debts cash flow is discounted at the rate of 4.32%, as obtained from average of its interest bearing debts. The market value of debts is derived to be RM615 million, while Golden Hope’s cost of debts is 8.32%.

Based on the calculation of Golden Hope’s cost of equity and cost of debts, the firm’s weighted average cost of capital is calculated to be 8.68%. The calculation of cost of capital is illustrated in the following figure.
Calculation of Cost of Equity and Capital

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk-free Rate (Avg 5-yrs MGS Bond)</td>
<td>3.59%</td>
</tr>
<tr>
<td>Golden Hope’s Unlevered Beta</td>
<td>0.77</td>
</tr>
<tr>
<td>Golden Hope’s Target D/E Ratio</td>
<td>6%</td>
</tr>
<tr>
<td>Golden Hope’s Target Tax Rate</td>
<td>28%</td>
</tr>
<tr>
<td>Golden Hope’s Levered Beta</td>
<td>0.81</td>
</tr>
<tr>
<td>Market Risk Premium</td>
<td>7.32%</td>
</tr>
<tr>
<td>Golden Hope’s Cost of Debt</td>
<td>8.32%</td>
</tr>
<tr>
<td>Golden Hope’s Cost of Equity</td>
<td>9.52%</td>
</tr>
<tr>
<td>Golden Hope’s Weighted Average Cost of Capital</td>
<td>10.44%</td>
</tr>
</tbody>
</table>

Figure 7.3: Calculation of Cost of Equity and Capital (Golden Hope)

7.2.2.2 Determination of Firm Value

Based on the 5-year projected financial data, the free cash-flow is calculated as follows:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>EBIT (1-t)</td>
<td>208,779,120</td>
<td>207,965,028</td>
<td>172,999,497</td>
<td>130,781,213</td>
<td>126,728,674</td>
<td>60,885,435</td>
<td>(19,095,275)</td>
</tr>
<tr>
<td>(+) Depreciation &amp; Amortization</td>
<td>109,226,000</td>
<td>121,469,782</td>
<td>141,117,832</td>
<td>164,766,829</td>
<td>189,011,266</td>
<td>219,031,285</td>
<td>253,605,655</td>
</tr>
<tr>
<td>(-) Change in Working Capital</td>
<td>(110,593,000)</td>
<td>63,188,492</td>
<td>(72,312,477)</td>
<td>304,893,314</td>
<td>114,870,587</td>
<td>138,829,926</td>
<td>(1,484,955,001)</td>
</tr>
<tr>
<td>(-) Capital Expenditure</td>
<td>231,536,000</td>
<td>181,518,907</td>
<td>210,002,841</td>
<td>232,340,014</td>
<td>263,296,709</td>
<td>300,437,740</td>
<td>340,770,335</td>
</tr>
</tbody>
</table>

Figure 7.4: Golden Hope’s Free Cash Flow

The value of the firm is determined by discounting the free cash flow at the firm’s adjusted weighted average cost of capital, 12.5%. The terminal value is discounted at the
firm’s weighted average cost of capital, 11.02%. The present value of the firm’s free cash flow is calculated to be RM3.4 billion, while the present value of terminal value is RM8.2 billion. As such, the total market value of the firm is RM11.65 billion. To derive the equity value of the firm, the market value of its debts is deducted from the firm’s market value while excess cash for investment is added to the total market value. This results in the total equity value of the firm to be at RM9.68 billion, with value per share at RM8.18, as shown in the following figure.

<table>
<thead>
<tr>
<th>RM Million</th>
</tr>
</thead>
<tbody>
<tr>
<td>PV of Terminal Value</td>
</tr>
<tr>
<td>PV of FCFF</td>
</tr>
<tr>
<td>Value of the Firm</td>
</tr>
<tr>
<td>(-) Market value of LT Debt</td>
</tr>
<tr>
<td>(+) Excess Cash (Investment)</td>
</tr>
<tr>
<td>Equity Value</td>
</tr>
<tr>
<td>Value per Share</td>
</tr>
</tbody>
</table>

**Figure 7.5: Golden Hope’s Market Value**

### 7.2.3 Kumpulan Guthrie Berhad’s 5-years projection

Prior to valuing Kumpulan Guthrie Berhad (KGB), several factors and circumstances have to be taken into consideration in order to establish the assumptions in estimating the expected income for the upcoming years. Future performance was determined by adjusting KGB’s past performance to reflect what the management thought was possible.

The projection of the income statement was made based on the best estimate of future competitive dynamics and the current capabilities and internal resources of the Company.
Assumptions made are as follows:

(i) **Revenue:** Historically, for the past 5 years, KGB’s revenue has been experiencing a decrease of 13.6%, on average. Thus, it is projected that the future revenues of the Company to continue a decreasing trend until 2010. However, the Company is expected to register a positive year-on-year revenue growth in 2012.

(ii) **Cost of Sales:** Based on historical cost of sales to revenue, the Company’s costs of sales are expected to stabilise in the range of 65 - 75% of the total sales over the next 5 years.

(iii) **Selling, General and Administration (SGA) Expenses:** SGA expenses are expected to increase at 5% after 2006.

(iv) **Depreciation & Amortisation:** The rate is at 8% of the gross fixed assets.

(v) **Marginal Tax Rate:** The Company’s target tax rate is 28%.

(vi) **Assets:** The assets of the Company are expected to follow the forecasted revenue trend of the Company.

(vii) **Liabilities:** The liabilities of the Company are expected to follow the forecasted revenue trend of the Company.
7.2.3.1 Free Cash Flows

The projected cash flow analysis was for the next 5 years is shown below.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>EBIT(1-T)</td>
<td>384,486,480</td>
<td>472,783,896</td>
<td>560,332,259</td>
<td>640,418,927</td>
<td>621,361,245</td>
<td>616,624,798</td>
<td>617,891,726</td>
</tr>
<tr>
<td>(+) Depreciation &amp;</td>
<td>232,131,000</td>
<td>256,378,645</td>
<td>275,620,419</td>
<td>297,427,226</td>
<td>323,068,217</td>
<td>348,954,644</td>
<td>377,505,542</td>
</tr>
<tr>
<td>Amortization</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(-) Change in Working Capital</td>
<td>(39,849,000)</td>
<td>51,942,804</td>
<td>18,142,778</td>
<td>84,887,678</td>
<td>3,855,553</td>
<td>53,066,486</td>
<td>51,969,184</td>
</tr>
<tr>
<td>(-) Capital</td>
<td>276,966,000</td>
<td>143,495,000</td>
<td>150,766,500</td>
<td>166,579,375</td>
<td>173,094,219</td>
<td>158,483,773</td>
<td>162,230,967</td>
</tr>
<tr>
<td>Expenditure</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Free Cash Flow of</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm</td>
<td>379,500,480</td>
<td>533,724,736</td>
<td>667,043,400</td>
<td>666,379,100</td>
<td>767,479,690</td>
<td>754,029,183</td>
<td>781,197,117</td>
</tr>
</tbody>
</table>

Figure 7.6: Kumpulan Guthrie Berhad’s Free Cash Flow

7.2.3.2 Estimation of Cost of Equity and Capital

In discounting FCFF, the cost of capital was used, which is calculated using the market values of equity and debt. To calculate KGB’s cost of equity, we have gathered the following information: the company’s beta, risk-free rate, and market premium. The figure below shows our calculation in estimating the cost of equity and capital of KGB.
### Calculation of Cost of Equity and Capital

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk-free Rate (Avg 5-yrs MGS Bond)</td>
<td>3.59%</td>
</tr>
<tr>
<td>KGB's Unlevered Beta</td>
<td>0.67</td>
</tr>
<tr>
<td>KGB's D/E Ratio</td>
<td>81%</td>
</tr>
<tr>
<td>KGB's Target Tax Rate</td>
<td>28%</td>
</tr>
<tr>
<td>KGB's Levered Beta</td>
<td>1.07</td>
</tr>
<tr>
<td>Market Risk Premium</td>
<td>7.32%</td>
</tr>
<tr>
<td>KGB’s Cost of Debt</td>
<td>8.32%</td>
</tr>
<tr>
<td>KGB’s Cost of Equity</td>
<td>11.4%</td>
</tr>
<tr>
<td>KGB’s Weighted Average Cost of Capital</td>
<td>11.02%</td>
</tr>
</tbody>
</table>

**Figure 7.7: Calculation of Cost of Equity and Capital (KGB)**

In calculating the cost of capital of KGB, the following estimation was taken into consideration:

(i) **KGB’s Target D/E Ratio:** Historically, KGB is highly leveraged with the D/E ratio between a minimum of 67% and a maximum of 92% during the FYE 2002 – 2006. Thus, we believed that the target D/E ratio for the Company should be reduced to 50% in the future.
7.2.3.3 Determination of Firm Value

We then use the present value of the FCFF as our value for the firm and derive an estimated value for equity. The figure below shows our calculation in determining the Company’s value.

<table>
<thead>
<tr>
<th></th>
<th>RM million</th>
</tr>
</thead>
<tbody>
<tr>
<td>PV of Terminal Value</td>
<td>5,280.9</td>
</tr>
<tr>
<td>PV of FCFF</td>
<td>2,240.9</td>
</tr>
<tr>
<td><strong>Market Value of the Firm</strong></td>
<td>7,521.8</td>
</tr>
<tr>
<td>(-) Market Value of LT Debt</td>
<td>1,989.1</td>
</tr>
<tr>
<td>(+) Excess Cash</td>
<td>21</td>
</tr>
<tr>
<td><strong>Equity Value</strong></td>
<td>5,553.7</td>
</tr>
<tr>
<td><strong>Value per Share</strong></td>
<td>5.28</td>
</tr>
</tbody>
</table>

Figure 7.8: KGB’s Market Value

Based on estimated future income of KGB, KGB’s equity value was estimated to be about RM5.719 billion.

7.3 MEASURING VALUE OF SYNERGY DRIVE WITH SYNERGIES

7.3.1 Synergy Estimation

The management believes that the merged companies’ operations will be more efficient to reap the benefits of merger between the three groups of companies. Positive synergies are expected to be tapped in areas of shared resources, optimizing cost by reducing
'leakages' and enhancing operational and financial control of all operating units. Thus, in estimating the value of the combined companies, the revenue and cost synergy will have to be estimated in line with the management’s expectation.

We assume that all of the merger synergies will be realized immediately after the close of the deal that is, by the financial year 2008, and so fall well within the five-year forecast period.

Assumptions made are as follows:

(i) **Revenue Synergy:** Additional revenue contribution is expected to emerge from the merger as a result of improved product quality and a broader product offerings. Significant contribution is expected from the plantations division which is expected to contribute approximately 35% from the total additional revenue contribution. The additional total revenue contribution is expected to grow at an average of 13% year-on-year.

(ii) **Cost Synergy:** Cost savings is expected to result from economies of scale and scope and the elimination of duplicate jobs. Given the significant overlap of operations in the plantation division, cost synergies are most likely to be reaped in the plantation division rather than the other divisions.
Figure below shows the calculation of the estimated cost and revenue synergies. As a result of the estimated synergies, there will be an increase in the EBIT of the merged entity at a minimum of RM240.0 million and a maximum of RM380.0 million.

<table>
<thead>
<tr>
<th>Summary of Estimated Synergy</th>
</tr>
</thead>
<tbody>
<tr>
<td>The total increase in revenues will be:</td>
</tr>
<tr>
<td>- Plantations</td>
</tr>
<tr>
<td>- Property</td>
</tr>
<tr>
<td>- Motor</td>
</tr>
<tr>
<td>- Heavy Equipment</td>
</tr>
<tr>
<td>- Energy and Utilities</td>
</tr>
<tr>
<td>- Other business</td>
</tr>
<tr>
<td>2,249.97</td>
</tr>
</tbody>
</table>

The total annual savings from the merger:

| 2008 | 2009 | 2010 | 2011 |
| 724.80 | 797.28 | 877.01 | 964.71 |
| 77.09 | 97.36 | 121.70 | 152.13 |
| 491.34 | 526.19 | 567.81 | 610.39 |
| 420.96 | 526.20 | 657.75 | 822.19 |
| 120.68 | 132.78 | 146.02 | 160.52 |
| 166.54 | 174.67 | 183.61 | 192.79 |
| (2,062.22) | (2,256.65) | (2,553.91) | (2,902.94) |

The increase in EBIT:

| 2008 | 2009 | 2010 | 2011 |
| 114.36 | 125.79 | 130.37 | 152.21 |
| 37.65 | 47.07 | 58.65 | 73.54 |
| 7.61 | 8.19 | 8.80 | 9.46 |
| 44.99 | 56.24 | 70.29 | 87.37 |
| 45.76 | 50.33 | 55.37 | 60.90 |
| (3.21) | (3.37) | (3.84) | (3.72) |
| 247.16 | 284.24 | 328.12 | 380.26 |

Figure 7.9: Calculation of the Estimated Cost and Revenue Synergies

7.3.2 Calculating the Projected Income Statement

Figure below shows the projected income statement based on the best estimate of future competitive dynamics and the current capabilities and internal resources of the Company.

We incorporate the effects of the revenue and cost synergies into the cash flow model of the combined companies. Additional assumption were also made is on the integration expenses of RM1.2 million which is expected to be incurred in 2007.
Figure 7.10: Projected Income Statement

Figure below shows the effect of the estimated cost and revenue synergies on the EBIT of the combined companies. It is clear from figure 7.11 that the companies EBIT would be significantly better should the estimated synergy is realized.

<table>
<thead>
<tr>
<th>Combined Company's 5-Year Forecast</th>
<th>Projected Financials</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
</tr>
<tr>
<td><strong>Income Statement</strong></td>
<td></td>
</tr>
<tr>
<td>Net Sales</td>
<td>23,645</td>
</tr>
<tr>
<td>Net Sales Synergy</td>
<td>2,249</td>
</tr>
<tr>
<td>Less</td>
<td></td>
</tr>
<tr>
<td>Variable Cost of Sales</td>
<td>19,812</td>
</tr>
<tr>
<td>Depreciation</td>
<td>977</td>
</tr>
<tr>
<td><strong>Cost of Sales Synergy</strong></td>
<td></td>
</tr>
<tr>
<td>Total Cost of Sales</td>
<td>20,789</td>
</tr>
<tr>
<td>Gross Profit</td>
<td>7,851</td>
</tr>
<tr>
<td>Less</td>
<td></td>
</tr>
<tr>
<td>Sales Expense</td>
<td>2,010</td>
</tr>
<tr>
<td>G&amp;A Expense</td>
<td>4,104</td>
</tr>
<tr>
<td>Integration Expenses</td>
<td></td>
</tr>
<tr>
<td>Amortization of Intangibles</td>
<td></td>
</tr>
<tr>
<td>Other expense (income), net</td>
<td>3,628</td>
</tr>
<tr>
<td>Total Sales and G&amp;A Expense</td>
<td>9,799</td>
</tr>
<tr>
<td>Operating Profit (EBIT)</td>
<td>(1,542)</td>
</tr>
<tr>
<td>Net Profit Before Taxes</td>
<td>(1,542)</td>
</tr>
<tr>
<td>Less Interest Expense</td>
<td>38</td>
</tr>
<tr>
<td>Net Profit After Taxes</td>
<td>(1,504)</td>
</tr>
</tbody>
</table>
| **Figure 7.11: Estimated Cost and Revenue Synergies on the EBIT**

1) With revenue and cost synergy

<table>
<thead>
<tr>
<th>Projected Financials</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
</tr>
<tr>
<td>Operating Profit (EBIT)</td>
</tr>
</tbody>
</table>

2) Without revenue and cost synergy

<table>
<thead>
<tr>
<th>Projected Financials</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
</tr>
<tr>
<td>Operating Profit (EBIT)</td>
</tr>
</tbody>
</table>
7.3.3 Calculating the Projected Balance Sheet

Figure below then shows the corresponding projected balance sheet based on the management’s estimation.

<table>
<thead>
<tr>
<th>Combined Company's 5-Year Forecast</th>
<th>Projected Financials</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
</tr>
<tr>
<td><strong>Balance Sheet</strong></td>
<td></td>
</tr>
<tr>
<td>Current Assets</td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>6,008</td>
</tr>
<tr>
<td>Other Operating Assets</td>
<td>11,296</td>
</tr>
<tr>
<td>Total Current Assets</td>
<td>17,374</td>
</tr>
<tr>
<td>Investments</td>
<td>1,425</td>
</tr>
<tr>
<td>Gross Fixed Assets</td>
<td>19,998</td>
</tr>
<tr>
<td>Less: Accum. Depr. &amp; Amort.</td>
<td>5,510</td>
</tr>
<tr>
<td>Net Fixed Assets</td>
<td>14,482</td>
</tr>
<tr>
<td>Other Assets</td>
<td>2,597</td>
</tr>
<tr>
<td>Total Assets</td>
<td>35,919</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>8,796</td>
</tr>
<tr>
<td>Long-Term Debt</td>
<td></td>
</tr>
<tr>
<td>Existing Debt</td>
<td>3,555</td>
</tr>
<tr>
<td>New Debt</td>
<td>-</td>
</tr>
<tr>
<td>Other Liabilities</td>
<td>1,295</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>13,444</td>
</tr>
<tr>
<td>Minority Interests in Consolidated Subsidiaries</td>
<td>2,710</td>
</tr>
<tr>
<td>Common Stock</td>
<td>0,767</td>
</tr>
<tr>
<td>Retained Earnings</td>
<td>10,007</td>
</tr>
<tr>
<td>Shareholders' Equity</td>
<td>18,774</td>
</tr>
<tr>
<td>Total Liabilities &amp; Shareholders' Equity</td>
<td>35,131</td>
</tr>
</tbody>
</table>

**Figure 7.12: Projected Balance Sheet**

7.3.4 Free Cash Flows

Thus the expected cash flow for the next 5 years is projected as figure below:

<table>
<thead>
<tr>
<th>Free Cash Flow</th>
<th>Projected Financials</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2007</td>
</tr>
<tr>
<td>EBIT (1-2)</td>
<td>-1,418</td>
</tr>
<tr>
<td>Plus: Depreciation and Amort.</td>
<td>977</td>
</tr>
<tr>
<td>Less: Gross Capital Expenditures</td>
<td>1,025</td>
</tr>
<tr>
<td>Less: Change in Working Capital</td>
<td>1,486</td>
</tr>
<tr>
<td><strong>Free Cash Flow</strong></td>
<td><strong>-2,951</strong></td>
</tr>
</tbody>
</table>

**Figure 7.13: Expected Cash Flow for the next 5 years**
7.3.5 Determination of Firm Value

In determining the appropriate discount rate for the FCFF, the cost of capital for Synergy Drive was estimated, which is calculated by averaging each of the target’s companies cost of capital. Consequently, the estimated cost of capital for Synergy Drive is 7.57 percent.

As a result of the valuation of cost and revenue synergies together with the appropriate cost of capital, Synergy Drive’s market value was estimated to be about RM66.902 million. Consequently, the estimated equity value per share of Synergy Drive is RM11.56. Our calculation in determining Synergy Drive’s enterprise value is shown in figure below.

<table>
<thead>
<tr>
<th>Cost of Capital: 2002 - 2006 (%)</th>
<th>7.57%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of Capital: Terminal Period (%)</td>
<td>5.07%</td>
</tr>
<tr>
<td>Sustainable Cash Flow Growth Rate (%)</td>
<td>1.0%</td>
</tr>
<tr>
<td>PV: 2007 - 2011</td>
<td>$5,849</td>
</tr>
<tr>
<td>PV: Terminal Value</td>
<td>$64,347</td>
</tr>
<tr>
<td>Total PV (Market Value of the Firm)</td>
<td>$70,196</td>
</tr>
<tr>
<td>Less: Market Value of Long-Term Debt</td>
<td>$4,889</td>
</tr>
<tr>
<td>Plus: Excess Cash (Investments)</td>
<td>$1,595</td>
</tr>
<tr>
<td>Equity Value</td>
<td>$66,902</td>
</tr>
<tr>
<td>Equity Value per Share</td>
<td>$11.56</td>
</tr>
</tbody>
</table>

Figure 7.14: Synergy Drive’s Group Value

7.3.6 Comparison of the Combined Companies Value With and Without Synergy

The value of the combined companies with synergies, RM66.902 million, exceeds the value of the combined entity without synergy by RM12.211 million. This value provided
an estimate on the potential incremental value that could be created from the merger, which is greater than the summation of the three companies valued as standalone operations.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Discounted Cash Flow Valuations (M)</td>
<td>$54,690</td>
<td>$66,902</td>
<td>$12,211</td>
</tr>
</tbody>
</table>

**Figure 7.15: Comparison of Synergy Value**

### 7.4 ALTERNATIVE VALUATIONS

Given the importance attached to terminal value, additional estimate of the terminal value was conducted using market multiples derived from information based on publicly traded companies similar to the target companies. The benchmarks used for selecting the comparable companies as the basis of valuation are those companies with the same business interest, size and industry.

This process provides a multiple-based estimate of Synergy Drive’s terminal value of RM24.358 million in terms of price-to-net assets valuation and RM58.122 million in terms of price-to-earnings valuation.
### Price/Net Asset & Price/Earnings Valuation between Comparable Companies as at November 2006

<table>
<thead>
<tr>
<th>Companies</th>
<th>P/NA</th>
<th>P/E</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) Asiatic Development Bhd</td>
<td>1.6</td>
<td>18.5</td>
</tr>
<tr>
<td>b) IOI Corporation Bhd</td>
<td>3.2</td>
<td>21.2</td>
</tr>
<tr>
<td>c) Kuala Lumpur Kepong Bhd</td>
<td>1.9</td>
<td>19.2</td>
</tr>
<tr>
<td>d) PPB Group Bhd</td>
<td>1.2</td>
<td>14.1</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>7.9</td>
<td>73.0</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td>1.6</td>
<td>14.6</td>
</tr>
<tr>
<td><strong>Target Net Asset (2007)</strong></td>
<td>15,397.45</td>
<td>3,981.53</td>
</tr>
<tr>
<td><strong>Projected Value of Target</strong></td>
<td>24,358.77</td>
<td>58,122.40</td>
</tr>
</tbody>
</table>

**Figure 7.16: Price/Net Asset & Price/Earning Valuation**

### 7.5 PRICE DETERMINATION

To determine the initial offer price for each target company, Sime Darby, Golden Hope and Guthrie, the value of each firm is added to the synergy estimated from the projected synergy for the combined firm. The synergy from the combined firm is estimated as RM12,211 million. The total value of the combined firm inclusive of the synergy is calculated to be RM66,902 million. Out of the total synergy, the estimated percentage of synergy to be distributed to each firm is 15%.

Based on the existing share price for each company, the minimum offer price is derived by multiplying the existing stock price with the number of shares outstanding for each
The minimum offer price is RM14,485 million, RM4,416 million and RM11,618 million for Sime Darby, Guthrie and Golden Hope respectively.

The maximum offer price is determined by adding the amount of synergy estimated to the minimum offer price. The amount of synergy is first divided equally among the 3 firms and added to each firm’s minimum offer price to get the maximum offer price. This means that at most, 33% of synergy is distributed to each firm to derive the maximum offer price for each firm.

However, for the purpose of the estimation, the proposed synergy to be shared among the target firms is 15%. As such, for the estimation of initial offer price, only 15% of the synergy is added to the minimum offer price. Subsequently, the initial offer price per share for each firm is calculated by dividing the initial offer price by the number of outstanding shares for each firm.

The initial offer price per share is RM6.87, RM5.91 and RM5.96 for Sime Darby, Guthrie and Golden Hope respectively. Comparing the initial offer price calculated to each firm’s share price as at 31st December 2006, the purchase price premium per share is calculated to be 13%, 44% and 16% for Sime Darby, Guthrie and Golden Hope respectively.
Offer Price Supporting Data

<table>
<thead>
<tr>
<th></th>
<th>Sime Darby (SD) Share Price</th>
<th>Kumpulan Guthrie (KGB) Share Price</th>
<th>Golden Hope Share Price</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$6.10</td>
<td>$4.10</td>
<td>$5.15</td>
</tr>
</tbody>
</table>

Proposed % of Synergy 15.0%

<table>
<thead>
<tr>
<th>Shares Outstanding (Mil)</th>
<th>Sime Darby Shares Outstanding (Mil)</th>
<th>Kumpulan Guthrie Outstanding (Mil)</th>
<th>Golden Hope Shares Outstanding (Mil)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2,374.6</td>
<td>1,011.2</td>
<td>2,256.0</td>
</tr>
</tbody>
</table>

Figure 7.17: Offer Price Data

<table>
<thead>
<tr>
<th>Standalone Value</th>
<th>Sime Darby</th>
<th>Guthrie</th>
<th>Golden Hope</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discounted Cash Flow Valuations ($Mil)</td>
<td>$31,137</td>
<td>$5,161</td>
<td>$18,392</td>
</tr>
<tr>
<td>Minimum Offer Price (PV_{MIN}) ($Mil)</td>
<td>$14,485</td>
<td>$4,146</td>
<td>$11,618</td>
</tr>
<tr>
<td>Maximum Offer Price (PV_{MAX}) ($Mil)</td>
<td>$18,556</td>
<td>$8,216</td>
<td>$15,689</td>
</tr>
<tr>
<td>Initial Offer Price ($Mil)</td>
<td>$16,317</td>
<td>$5,978</td>
<td>$13,450</td>
</tr>
<tr>
<td>Initial Offer Price Per Share ($)</td>
<td>$6.87</td>
<td>$5.91</td>
<td>$5.96</td>
</tr>
<tr>
<td>Purchase Price Premium Per Share</td>
<td>13%</td>
<td>44%</td>
<td>16%</td>
</tr>
</tbody>
</table>

Figure 7.18: Firm’s Standalone Value

<table>
<thead>
<tr>
<th>Value of Synergy</th>
<th>Without Synergy (1)</th>
<th>With Synergy (2)</th>
<th>PV_{NS} (1) - (2)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$54,690</td>
<td>$66,902</td>
<td>$12,211</td>
</tr>
</tbody>
</table>

Figure 7.19: Consolidated Firm Value

While the initial offer price is assumed to include 15% of the synergy estimated, the price for each firm is further estimated for higher percentages of synergy to be distributed to each firm. The percentage is capped at 33% as that is the maximum synergy that can be distributed to each firm. As shown in the following figures, the results of the increase in the percentage of synergy indicate an increase in offer price for each firm.
### Sime Darby

<table>
<thead>
<tr>
<th>Offer Price Per Share</th>
<th>Offer Price $-millions</th>
<th>% Shared Synergy</th>
</tr>
</thead>
<tbody>
<tr>
<td>$6.87</td>
<td>16,317</td>
<td>15%</td>
</tr>
<tr>
<td>$7.13</td>
<td>16,927</td>
<td>20%</td>
</tr>
<tr>
<td>$7.39</td>
<td>17,538</td>
<td>25%</td>
</tr>
<tr>
<td>$7.64</td>
<td>18,148</td>
<td>30%</td>
</tr>
<tr>
<td>$7.80</td>
<td>18,515</td>
<td>33%</td>
</tr>
</tbody>
</table>

Figure 7.20: Increase in Offer Price (Sime Darby)

### Guthrie

<table>
<thead>
<tr>
<th>Offer Price Per Share</th>
<th>Offer Price $-millions</th>
<th>% Shared Synergy</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.91</td>
<td>5,978</td>
<td>15%</td>
</tr>
<tr>
<td>6.52</td>
<td>6,588</td>
<td>20%</td>
</tr>
<tr>
<td>7.12</td>
<td>7,199</td>
<td>25%</td>
</tr>
<tr>
<td>7.72</td>
<td>7,809</td>
<td>30%</td>
</tr>
<tr>
<td>8.09</td>
<td>8,176</td>
<td>33%</td>
</tr>
</tbody>
</table>

Figure 7.21: Increase in Offer Price (Guthrie)

### Golden Hope

<table>
<thead>
<tr>
<th>Offer Price Per Share</th>
<th>Offer Price $-millions</th>
<th>% Shared Synergy</th>
</tr>
</thead>
<tbody>
<tr>
<td>$5.96</td>
<td>13,450</td>
<td>15%</td>
</tr>
<tr>
<td>$6.23</td>
<td>14,061</td>
<td>20%</td>
</tr>
<tr>
<td>$6.50</td>
<td>14,671</td>
<td>25%</td>
</tr>
<tr>
<td>$6.77</td>
<td>15,282</td>
<td>30%</td>
</tr>
<tr>
<td>$6.94</td>
<td>15,648</td>
<td>33%</td>
</tr>
</tbody>
</table>

Figure 7.22: Increase in Offer Price (Golden Hope)
7.6 WEIGHTED AVERAGE VALUATION OF COMBINED FIRM

Based on the valuations calculated previously for the combined firm using the discounted cash flow method, earning and net assets comparable firm method, a weighted average valuation calculation is conducted. For each valuation method, a weighting factor is assigned where 50% is for the discounted cash flow method and 25% is assigned equally for both earnings and net assets comparable firm method. The result of the weighted average calculation estimates the value of the combined firm as RM47.966 billion.

<table>
<thead>
<tr>
<th>Valuation Calculation</th>
<th>Value</th>
<th>Weighting Factor</th>
<th>Weighted Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discounted Cash Flow Valuation</td>
<td>$54,690</td>
<td>50%</td>
<td>$27,345</td>
</tr>
<tr>
<td>Comparable Firms - Earnings Valuation</td>
<td>$58,122</td>
<td>25%</td>
<td>$14,831</td>
</tr>
<tr>
<td>Comparable Firms - Net Assets Valuation</td>
<td>$24,389</td>
<td>25%</td>
<td>$6,090</td>
</tr>
</tbody>
</table>

Figure 7.23: Weighted Average Calculation of the Combined Firm

7.7 VALUE CREATION ANALYSIS

As the main objective of a firm is to improve its shareholders’ wealth, value creation was used as the financial indicator for measuring and evaluating whether or not the objectives of the merger have been met. For that purpose, the following actual financial ratios of Sime Darby at the financial year at the pre-merger period (2006), during merger period (2007) and post merger period (2008) were analyzed. At the pre-merger and during merger periods consolidated financial results of the three merger entities were analyzed.
Profitability Ratios

In creating wealth to the shareholders, profitability ratios would provide the insight to the degree of success of achieving it.

The Return of Shareholders’ Funds (ROSF) compares the amount of profit for the period available to the ordinary shareholders and is formulated as:

\[
\text{ROSF} = \left( \frac{\text{Profit Before Interest & Tax}}{\text{Sales}} \right) \times \left( \frac{\text{Sales}}{\text{LT Capital employed}} \right)
\]

The Return on Capital Employed (ROCE) is a fundamental measure of firm’s business performance as it compares capital invested (Input) with profit (Output). The comparison is essential in assessing the effectiveness with which funds have been deployed. Based on this it is noted that ROCE calculates the Profit Margin Ratio and Asset Turnover Ratio which themselves are the measure of profitability and efficiency respectively. ROCE which express the relationship between net profit generated by a firm and its long term capital invested as follows:

\[
\text{ROCE} = \frac{\text{Profit Before Interest & Tax}}{\text{Ordinary Share Cap + Reserves}}
\]

The Net Profit Margin relates the net profit during a financial period to its sales (Revenue) and it is expressed as follows:

\[
\text{Net Profit Margin} = \frac{\text{Net Profit}}{\text{Revenue}}
\]
Net Profit Margin = Profit Before Interest & Tax / Sales

The Net Profit Before Interest and Tax is applied in the ratio as it represents the profit from operation which is not influenced by the way the business is financed.

The Gross Profit Margin Ratio measures the profitability in buying or producing and selling products before any other expense is taken into consideration. It is formulated as:-

Gross Profit Margin = Gross Profit / Sales

The results of the Profitability analysis are shown in Table 7.1 below:-

<table>
<thead>
<tr>
<th></th>
<th>Pre-Merger</th>
<th>During Merger</th>
<th>Post Merger</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROSF</td>
<td>11.07%</td>
<td>15.77%</td>
<td>17.32%</td>
</tr>
<tr>
<td>ROCE</td>
<td>12.40%</td>
<td>17.15%</td>
<td>20.09%</td>
</tr>
<tr>
<td>Net Profit Margin</td>
<td>10.65%</td>
<td>9.91%</td>
<td>15.42%</td>
</tr>
<tr>
<td>Gross Profit Margin</td>
<td>11.10%</td>
<td>4.66%</td>
<td>20.83%</td>
</tr>
</tbody>
</table>

Table 7.1: Profitability Ratios

It is noted that there was a rising trend in ROSF and ROCE throughout the pre-merger to the post merger periods which indicates healthy improvement in Sime Darby’s profitability with ROSF and ROCE has increased by 6.25% and 7.69% respectively. As
for the Net Profit and Gross Profit Margin improvement was evidenced during the post merger period with overall increase of 4.77% and 9.73% respectively even though there was a drop during the merger period.

**Efficiency Ratios**

The efficiency ratios examine the way in which the firm’s resources are managed. For the purpose of measuring Sime Darby’s efficiency during the periods, three measurements were computed.

The Average Turnover Period measures the average period the products are held meaning how long the funds are retained in production and cannot be used for other purpose. The Average Turnover Period is formulated as follows:-

\[
\text{Average Turnover Period} = \frac{\text{Average Turnover Held}}{\text{Cost of Sales}} \times 365 \text{ days}
\]

The Revenue to Capital Employed or the asset turnover ratio examines how effectively the firm’s assets are generating sales revenue and it is calculated as follows:-

\[
\text{Revenue to Capital Employed} = \frac{\text{Revenue}}{\text{Long Term Capital Employed}}
\]
The Revenue per Employee is the ratio which relates the sales revenue generated to a firm’s particular resource i.e. the employee (Labour) as it measures the productivity of labour. The Revenue per Employee is computed as:-

\[
\text{Revenue Per Employee} = \frac{\text{Revenue}}{\text{Average Employee}}
\]

The results of Sime Darby’s efficiency analysis are shown in Table 7.2 below:

<table>
<thead>
<tr>
<th></th>
<th>Pre-Merger</th>
<th>During Merger</th>
<th>Post Merger</th>
</tr>
</thead>
<tbody>
<tr>
<td>Average Turnover Period</td>
<td>62.92 days</td>
<td>62.54 days</td>
<td>84.78 days</td>
</tr>
<tr>
<td>Revenue To Capital Employed</td>
<td>1.16</td>
<td>1.73</td>
<td>1.30</td>
</tr>
<tr>
<td>Revenue Per Employee</td>
<td>RM258,095</td>
<td>RM691,167</td>
<td>RM340,447</td>
</tr>
</tbody>
</table>

Table 7.2: Efficiency Analysis

From the analysis, it is shown that there are consolidations in the Revenue to capital employed and Revenue per Employee which indicates that there are rooms for improvement and the merger is still far from its efficiency objectives. This is where the post merger Whereas, the Average Turnover Period has shown the increase of number of days funds trapped in production has jumped for about 36% from the average of 63 days. However, the result might not be accurate as the analysis was based on the average production of overall Sime Darby’s wide range of product in the five core businesses which includes services. Perhaps a more accurate analysis would be obtained if individual products are analyzed to obtain the individual average turnover period.
Liquidity Ratios

Liquidity Ratios are concerned with the ability of a firm to meet the short term financial obligations. For liquidity ratios, the ratios calculated are working capital, current ratio and quick ratio. Based on the calculation, it can be observed that the liquidity for the combined firm before the merger has decreased after the merger. For instance, the working capital is projected to decrease from RM8,577 to RM7,006 million. Similarly current ratio and quick ratio has decreased from 1.98 and 1.68, to 1.86 and 1.54 respectively. The decrease in liquidity can be attributed to the use of cash and sell-off of non-core assets after the merger.

Analyzing the debt ratios, it can be seen that the ratio of total liabilities to total assets has decreased from 37.99% to 33.45%. This is possibly due to the assumption that no new debt is issued after the merger. Similarly, this is reflected in the debt-to-equity ratio that has also decreased from 18.94% to 15.57%. The ratio of total assets per common stock equity has increased from 4.10 to 7.25 and times interest earned has also increased to 21.32 after the merger. This means that post merger, the combined firm has reduced its debts resulting to higher times of earnings over interest expenses. The combined firm also has increased its asset per equity, while reducing its debts.
Altman’s Z-Score

Another way of determining the health of the Sime Darby, we have also analyzed the firm’s credit worthiness. As one of the measures applied by the international rating agency, Standard & Poors, Sime Darby’s Z-scores are also analyzed.

Developed by Edward Altman, the original Z-score relied on multi discriminant analysis to identify variables providing information about the livelihood of bankruptcy. The larger the Z-score is, the lower the probability of default over the next 2 years.

The function was fitted as follows:-

\[
Z\text{-Score} = 1.2A + 1.4B + 3.3C + 0.6D + 1E
\]

Whereby, the above variables are determined by the followings:-

A = Net Working Capital/Total Assets

B = Retained Earnings/Total Assets

C = EBIT/Total Assets

D = Market Value of Common Equity & Preferred Stock/ Book Value of Debt

E = Sales/Total Assets
The results of the Z-Scores throughout the three periods are tabulated in Table 7.3 below:

<table>
<thead>
<tr>
<th></th>
<th>Pre-Merger</th>
<th>During Merger</th>
<th>Post Merger</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Working Capital/Total Assets</td>
<td>0.09</td>
<td>0.06</td>
<td>0.12</td>
</tr>
<tr>
<td>Retained Earnings/Total Assets</td>
<td>0.40</td>
<td>0.45</td>
<td>0.52</td>
</tr>
<tr>
<td>EBIT/Total Assets</td>
<td>0.09</td>
<td>0.11</td>
<td>0.15</td>
</tr>
<tr>
<td>Market Value of Common Equity &amp;</td>
<td>0.79</td>
<td>0.77</td>
<td>0.85</td>
</tr>
<tr>
<td>Preferred Stock/ Book Value of Debt</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales/Total Assets</td>
<td>0.80</td>
<td>1.06</td>
<td>0.95</td>
</tr>
<tr>
<td>Z-Score</td>
<td>2.22</td>
<td>2.52</td>
<td>2.81</td>
</tr>
</tbody>
</table>

Table 7.3: Altman’s Z-Score

Based on the results, it is noted that Sime Darby’s credit worthiness has improve by about 0.30 factor at each measured period which means that Sime Darby’s probability of default over the next 2 years has reduced by 0.3 factor yearly.
7.8 SHARE PRICE VALUATION

Figure 7.27: Sime Darby Share Price

---

Merger date
Synergy Drive, now renamed as Sime Darby Bhd (SDB) was listed on Bursa Malaysia on 30 November 2007 at RM 8.90, a reference price fixed by Bursa Malaysia. This is
equivalent to a market capitalization of RM 54.2b or US $16b and the listing of SDB was the final leg for the mega plantation merger and SDB made a strong debut on its first week of listing.

Driven by resurgent crude oil prices and a weak US dollar, Crude Palm Oil (CPO) prices have surged further ahead from RM 2,800/MT – RM 3,000/MT band to the RM 3,000/MT – RM 3,200/MT band from the last week of December. Bullish sentiments have continued to be underpinned by favorable demand-supply dynamics both for CPO and competing oils. The resurgent of crude oil prices in the early 2008 has driven the share price of SDB to jump at the highest peak of RM 13.40 on 14 Jan 2008. (Diagram 1).

Diagram 2 and Diagram 3 shows the share price movement of the other two listed companies involved in this merger, Golden Hope and Guthrie respectively. The share price of both companies reached its highest recorded peak upon the announcement of the merger in which Golden Hope recorded the highest price of RM 9.60 (on 11 October 2007) and Guthrie at RM 7.45 (on 16 October 2007). There was no trading post merger as both companies were de-listed from the Main Board of Bursa Malaysia.

On an interesting outlook, SDB share price had constantly recorded price above RM 8.90 of its listing price in November 2007, which was mainly due to the prices of major liquid plantation stocks have since risen by 13-21% with the plantation index up 8.7% in the past one month vs KLCI’s 0.7%. The out performance was driven by an unexpected
strong surge in CPO price to touch RM 3,000/tonne for 3-month forward contract on the back of rising crude oil price.

The volatility of SDB share movement was at a consistent pace until March 2008, with the collapse of a major US Investment Bank and investors are spooked that the development could be a harbinger for more US bank failures in the coming days as credit woes deepen in the States. The share price of SDB was further dropped in March and April due to uncertainties in US Market and domestic political concern. Due to some development on Wall Street Index and shocking fuel price hike in late May, the trading of SDB shares and other listed shares in general was slow with a relatively thin volume.
CHAPTER 8: IDEAL WEIGHTED AVERAGE CAPITAL STRUCTURE

Based on the present situation, we have computed the capital structure of Sime Darby Bhd and determined the ideal (Lowest) capital structure should be structured by them.

The post-merger beta is obtained by regressing the Sime Darby Bhd’s stock return against the KLCI return and we have noted that the beta has increased from 0.94 to 1.34. At the book value of debt/equity ratio of 14%, same risk free rate, market return, risk premium and tax rate we have computed the WACC for the firm as tabulated at in Table 8.1 below:-

<table>
<thead>
<tr>
<th>Unlevered Beta</th>
<th>Debt/Equity Ratio</th>
<th>Treasury Bond Rate</th>
<th>Tax Rate</th>
<th>Present Beta</th>
<th>Market Return</th>
<th>Country Risk</th>
<th>Risk Premium</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.3466097</td>
<td>0.14</td>
<td>3.59%</td>
<td>28%</td>
<td>1.3480</td>
<td>7.52%</td>
<td>1.00%</td>
<td>4.93%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Debt Percentage</th>
<th>Debt equity ratio</th>
<th>Beta</th>
<th>Cost of Equity</th>
<th>Interest</th>
<th>Cost of Debt</th>
<th>WACC</th>
</tr>
</thead>
<tbody>
<tr>
<td>0%</td>
<td>0%</td>
<td>1.3480</td>
<td>10.24%</td>
<td>6.00%</td>
<td>4.32%</td>
<td>10.24%</td>
</tr>
<tr>
<td>10%</td>
<td>11.11%</td>
<td>1.4558</td>
<td>10.77%</td>
<td>7.00%</td>
<td>5.04%</td>
<td>10.19%</td>
</tr>
<tr>
<td>20%</td>
<td>25.00%</td>
<td>1.5906</td>
<td>11.43%</td>
<td>8.00%</td>
<td>5.76%</td>
<td>10.30%</td>
</tr>
<tr>
<td>30%</td>
<td>42.86%</td>
<td>1.7640</td>
<td>12.29%</td>
<td>9.00%</td>
<td>6.48%</td>
<td>10.54%</td>
</tr>
<tr>
<td>40%</td>
<td>66.67%</td>
<td>1.9950</td>
<td>13.43%</td>
<td>10.00%</td>
<td>7.20%</td>
<td>10.94%</td>
</tr>
<tr>
<td>50%</td>
<td>100.00%</td>
<td>2.3186</td>
<td>15.02%</td>
<td>11.00%</td>
<td>7.92%</td>
<td>11.47%</td>
</tr>
<tr>
<td>60%</td>
<td>150.00%</td>
<td>2.8038</td>
<td>17.41%</td>
<td>12.00%</td>
<td>8.64%</td>
<td>12.15%</td>
</tr>
<tr>
<td>70%</td>
<td>233.33%</td>
<td>3.6126</td>
<td>21.40%</td>
<td>13.00%</td>
<td>9.36%</td>
<td>12.97%</td>
</tr>
<tr>
<td>80%</td>
<td>400.00%</td>
<td>5.2302</td>
<td>29.38%</td>
<td>14.00%</td>
<td>10.08%</td>
<td>13.94%</td>
</tr>
<tr>
<td>90%</td>
<td>900.00%</td>
<td>10.0831</td>
<td>53.30%</td>
<td>15.00%</td>
<td>10.80%</td>
<td>15.05%</td>
</tr>
</tbody>
</table>

Table 8.1: Ideal WACC
Based on the computation we have are of the opinion that the ideal WACC for Sime Darby Bhd should be at 10% debt ratio compared to the present ratio of 20%. With present cash strength Sime Darby Bhd should reduce its long term debt to the lowest WACC of 10%.
CHAPTER 9: CONCLUSION AND RECOMMENDATIONS

With operations across the Asia-Pacific, SDB is in all the right businesses now - Plantations riding on record CPO prices; high economic growth in driving demand and profits for the Property and Motor divisions; booming construction and mining activities boosting Heavy Equipment demand; and bulging fabrication orders on the back of record oil & gas activities boosting Energy profits.

The main motivations for this merger is create the world’s largest listed oil palm company and property giant in Malaysia with a focus to grow in its property division and increase its international businesses. A positive uptrend was shown upon the listing of the renamed Sime Darby on Bursa Malaysia and their shares remains as one of the top plantation shares for most foreign broking houses. The stock to date has surpassed the expectations of most broking houses, which had earlier capped the stock at the RM11-RM12 range for 2008. With the enlarged palm oil business upon the merger, Sime Darby is creating its own platform to achieve better cost and revenue efficiencies. The merger also allowed them to draw their focus on a set of core businesses within Asia Pacific and gain the benefits from population growth and economic development.

The consolidation of its core business functions are poised to give Sime Darby a significant presence in both upstream and downstream palm oil activities and leading the property segment in Malaysia as the top developer of quality residential and commercial communities.
The merger of Sime Darby Bhd, Golden Hope Plantation Bhd and Kumpulan Guthrie Bhd has no doubt not only met the original objectives to improve profitability and efficiency but also in improvement in the group credit worthiness.

Sime Darby Bhd’s market capitalization has propelled to RM60 billion from a mere RM16 billion prior to the merger. Sime Darby Bhd has leaped to become the company with the largest market capitalization in Malaysia and has been able to maintain the number one position since then. The giant presence in Bursa Malaysia, Sime Darby Bhd could be used as their advantage to gain confidence from the rating agencies, thus widening their credit options at a cheaper rate.

However there have been much of hypes and worries about the largest merger in Malaysia’s history. There were hypes over the potential value the conglomerate to project and which party would be benefiting from it.

The worries were generally emerged from political point of view especially from the opposition parties which are concerned over the future of this conglomerate. They opined that being one of GLC, Sime Darby Bhd should be preserved to protect public interest and should not be treated as a pure private company with profits as the main motivation. Apart from that previous acquisition failure in UMBC Bank may have haunted public over possible recurrence of same mistake.
However shareholders have responded well to the proposal with the majority of the shareholders of all the merger entities have accepted the offer made by Synergy Drive by agreeing to the share swap, indicating a friendly takeover. This was also supported by warm reception by market players in the Bursa. Sime Darby Bhd’s share price has shown tremendous improvement at the post merger period.

On the performance side, the initial year has shown that Sime Darby Bhd is in the right track and looked set to achieve the merger objective in less than 10 years.

However the pace of improvement has been slowed down by global economic slowdown due to credit crunch which has also affected the KLCI performance. This has been aggravated by the drop in CPO price and weakening of Ringgit against US Dollar.

The journey of SDB will not stop here as its share price performance would continue to be driven by its two key business divisions- oil palm plantations and property. And with promising factors such as the high price in CPO prices and future strategies planted for the company, Sime Darby is poised to achieve its main objective in leading the world’s oil palm company and property maestro in Malaysia in years to come.

Lastly, we submit three main recommendations to be undertaken by Sime Darby Bhd.

a) Improving the firm’s Weighted Average Capital Structure
Based on the study earlier we have noted that the firm’s WACC are presently not at its lowest. In order to increase the firm value the present debt ratio has to be lowered to 10% from the present 20%.

b) Taking the company private.

We would recommend the privatization of Sime Darby Bhd by its main shareholders i.e. PNB.

Due to dismal performance of capital market, Sime Darby Bhd’s share price has dropped tremendously due to weak capital market. The share price which has been floating between RM9-00 to RM9-50 does not reflect the true value and potentials of Sime Darby Bhd.

Furthermore, the company’s beta factor of 0.94 during pre-merger exercise has increased to 1.35 after merger. The increase in beta indicates the higher volatility of share price against the market price.

Sime Darby Bhd being the leading conglomerate in this country does not depend on capital market in order to raise fund as they may consider other better options. They may either use their high reserves not only to buy back their shares but may also fund their project or reduce their debt ratio.
They may also take the advantage of their good credit rating to issue islamic bond (Sukuk). While obtaining cheap borrowings, Sukuk would offer the tax incentives and rebates offered by the government such as income tax exemption be given on fees earned by institutions in arranging, underwriting and distributing of non-ringgit sukuk issued in Malaysia and distributed outside Malaysia and profits received from the trading of non-ringgit.

c) More focus on business with core competitive industries.

It is evidenced from the analysis that there are rooms for improvement by the firm especially in improving its efficiency. For that purpose, apart from restructuring the organization, concentration on core business could guide Sime Darby Bhd reduce redundancies and leverage the competencies in the core areas. None performing business such as insurance and medical services should be disposed of. With the failed acquisition of IJM recently it is timely that Sime Darby Medical Centre be sold to the potential buyers.
REFERENCES

A. Academics Writings and Paperwork


B. Books


10. Synergy Drive Berhad Prospectus (2007)

11. The Golden Hope Story (1844-2007)


C. Websites


2. Synergy Drive website - www.synergydrive.com.my


APPENDIX

Appendix 1

INTERVIEW WITH THE MANAGEMENT OF PARTICIPATING COMPANIES:

SEMI-STRUCTURED INTERVIEW QUESTIONNAIRES – SET ONE

1. Introduction
   - Are we allowed to disclose your name in the report or do you want to remain anonymous?
   - Are we allowed to record this interview?
   - What role did you have during the M&A?

2. M&A objective
   - Why did SDB/KGB/GHP decide to M&A?
   - What was the objective behind the deal?
   - Why did the participating companies choose to M&A with a plantation related company and why not with a company beyond plantations?
   - Did you see any potential benefits with a plantation M&A?
   - What do you consider the merger would be?

3. Integration
   - Do you have an integration process?
   - When did the integration process start? How and why?
   - When did the integration process stop? How and why?
   - To what degree has the three different companies been integrated? Why?
   - Which integration issues have you experienced during the M&A process?
   - How has the management dealt with the integration issues?
What has the three different corporate cultures meant to the integration process?

When starting the integration process, how was it decided in which order the different functions and activities would be integrated?

Do you feel that the integration process was an important regarding the creation of synergy effects?

What were the important issues in the integration process when creating synergy?

4. Synergy

What do you believe synergy is?

What synergy effects did you expect from the M&A?

Did these expect synergy effects become realized or not?

What did the management team do to create these synergies?

What do you see as the main source of synergy in the M&A?

Was there a strategic fit between each of participating companies?

What was the three company’s strength, weaknesses and capabilities? Different or similar?

Was there an organisational fit between each of the participating companies?

Did they have different or similar management processes, cultures, systems and structure?

What managerial actions were taken to realize synergy? How active were they in trying to recognize problems in the M&A process?

Has the benefits of the synergistic effects outweighed the costs?

Have the financing of the M&A deal and the cost of integration cost more than the benefits you have received from synergies?
• Did each of participating companies have an M&A strategy? What was that strategy?

• What had been done to understand the market and environment of the new company?

• How did each of participating companies manage the cultural issues?

• How did the management team deal with the strategic planning, integration and did they look at the response from competitors?

• Were there a special management team working with the M&A integration and synergy realization process?

• How was the employees informed about the M&A?

• Were potential synergies discussed before the deal?
Appendix 2

INTERVIEW WITH THE MANAGEMENT OF PARTICIPATING COMPANIES:

EMAIL QUESTIONS

- Describe how your participation in the Synergy Drive – merger?
- What were the main reasons for Synergy Drive – merger?
- How the combination was potential investigated before the Synergy Drive – merger?
- What were the objectives that were set up before the merger? Have these objectives been fulfilled?
- Please describe the merger initiation and the subsequent integration.
- What was the most successful integration techniques used for Synergy Drive – merger?
- What similarities and differences could be found in the three participating companies? (Ex-Sime Darby Berhad, ex-KGB and ex-GHP)
Appendix 3

INTERVIEW WITH THE MANAGEMENT OF PARTICIPATING COMPANIES:

SEMI-STRUCTURED INTERVIEW QUESTIONNAIRES – SET TWO

- What are the objectives of the merger? What role was of the merger is expected to perform? (Copy of BOD’s resolution on the decision)

- What are the motivations of the merger?

- Two of the main motivations of the merger are operational and financial synergies. How do you see that these can be realized in plantation, property and motor industry sectors? How the expected cost/yield be reduced/increased respectively?

- Upon merger, Synergy Drive was said to be cash rich. How do you judge this statement in view of unlocking any cash traps in the pre-merger organizational structure?

- What are the criteria made for the selection of merger partners? Why Sime Darby, Golden Hope and Guthrie were selected? What do you foresee over this decision?

- Do you have any value estimation (analysis) prior to the merger? Any due diligence procedure performed? Did you engage external consultant?
- How was the merger initiated? How long the bidding process went on? (Timeline). Which are the parties involved in the bidding process? What model was used?

- The merger exercise was done through the initiation of SPV by CIMB. How did you see that this is the best option in the context of PNB as the main shareholder of the merger entities? How is this done?

- Was there any other possible suitors/alternative to this merger?

- Any specific methods of approaching the target? (Direct/indirect/white knight/etc)

- Golden Hope shareholders had initially objected the merger. Why? How was this overcome?

- How was the acquisition pricing of the targets determined? What are the bases used? Any prior estimation made? Based on the final figures were there at a discount/premium?

- What were the settlements for the purchase consideration? (Share transfer/cash/etc.)

- How was this merger financed? (Internal/external financing, determination of financing instrument, post-merger capital structure determination)
- Was the acquisition costs apportioned overtime?

- Was there any tax advantage obtained?

- How do see the merger in meeting the group common strategic objectives, mission and vision?

- How about the merger objective itself to the corporate strategy objective?

- Based on the business model what are the challenges the merger entities would face in their integration?

- Was there any integration planning team established? What are they and their function?

- What are the direct/indirect benefits expected from the merger? Was there any cost/benefit analysis?

- What are the takeover implementation strategies for consolidation and target deadline? Was there any other implementation strategy?

- Do you foresee any value enhancement in the strategy in terms of market size, geographical presence, consolidation in the five core businesses?
- Was there any resources planning after the merger with regards to consolidation of operational functions, staffing (Retrenchment, HR benefit program etc.) and systems?

- So far, what are the feedbacks/responses from the markets, shareholders & employees? How about the responses from the competitors? What are actions taken for improvement as a result of the feedbacks?

- Lastly, how do you judge the performance of CIMB in pursuing the merger exercise?
## Appendix 4

### Credit Spread From Malaysian Corporate Bonds

<table>
<thead>
<tr>
<th>BOND YIELD (%)</th>
<th>CREDIT SPREAD (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>AAA</strong> 5Y</td>
<td><strong>AA1</strong> 5Y</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>Jan-05</td>
<td>3.750</td>
</tr>
<tr>
<td>Feb-05</td>
<td>3.740</td>
</tr>
<tr>
<td>Mar-05</td>
<td>3.771</td>
</tr>
<tr>
<td>Apr-05</td>
<td>3.797</td>
</tr>
<tr>
<td>May-05</td>
<td>3.705</td>
</tr>
<tr>
<td>Jun-05</td>
<td>3.710</td>
</tr>
<tr>
<td>Jul-05</td>
<td>3.719</td>
</tr>
<tr>
<td>Aug-05</td>
<td>3.705</td>
</tr>
<tr>
<td>Sep-05</td>
<td>3.711</td>
</tr>
<tr>
<td>Oct-05</td>
<td>3.767</td>
</tr>
<tr>
<td>Nov-05</td>
<td>3.872</td>
</tr>
<tr>
<td>Dec-05</td>
<td>3.705</td>
</tr>
<tr>
<td>Jan-06</td>
<td>4.078</td>
</tr>
<tr>
<td>Feb-06</td>
<td>4.232</td>
</tr>
<tr>
<td>Mar-06</td>
<td>4.244</td>
</tr>
<tr>
<td>Apr-06</td>
<td>4.562</td>
</tr>
<tr>
<td>May-06</td>
<td>4.780</td>
</tr>
<tr>
<td>Jun-06</td>
<td>4.835</td>
</tr>
<tr>
<td>Jul-06</td>
<td>4.732</td>
</tr>
<tr>
<td>Aug-06</td>
<td>4.497</td>
</tr>
<tr>
<td>Sep-06</td>
<td>4.357</td>
</tr>
<tr>
<td>Oct-06</td>
<td>4.144</td>
</tr>
<tr>
<td>Nov-06</td>
<td>4.065</td>
</tr>
<tr>
<td>Dec-06</td>
<td>4.011</td>
</tr>
<tr>
<td>Jan-07</td>
<td>4.046</td>
</tr>
<tr>
<td>Feb-07</td>
<td>4.027</td>
</tr>
<tr>
<td>Mar-07</td>
<td>3.898</td>
</tr>
<tr>
<td>Apr-07</td>
<td>3.814</td>
</tr>
<tr>
<td>May-07</td>
<td>3.834</td>
</tr>
<tr>
<td>Jun-07</td>
<td>3.900</td>
</tr>
<tr>
<td>Jul-07</td>
<td>3.958</td>
</tr>
<tr>
<td>Aug-07</td>
<td>3.992</td>
</tr>
<tr>
<td>Sep-07</td>
<td>3.949</td>
</tr>
<tr>
<td>Oct-07</td>
<td>3.988</td>
</tr>
<tr>
<td>Nov-07</td>
<td>4.045</td>
</tr>
<tr>
<td>Dec-07</td>
<td>4.067</td>
</tr>
</tbody>
</table>

Average differential between grades: 0.399 | 0.711 | 0.756 | 0.622

Source: Daintree, Rating Agency Malaysia Berhad (RAM)
Appendix 5

Average KLCI Market Return

<table>
<thead>
<tr>
<th>YEAR</th>
<th>KLCI</th>
<th>ANNUAL RETURN</th>
</tr>
</thead>
<tbody>
<tr>
<td>1989</td>
<td>562.28</td>
<td></td>
</tr>
<tr>
<td>1990</td>
<td>606.92</td>
<td>-10.02%</td>
</tr>
<tr>
<td>1991</td>
<td>556.22</td>
<td>9.94%</td>
</tr>
<tr>
<td>1992</td>
<td>643.96</td>
<td>15.77%</td>
</tr>
<tr>
<td>1993</td>
<td>1,275.32</td>
<td>96.04%</td>
</tr>
<tr>
<td>1994</td>
<td>971.21</td>
<td>-23.85%</td>
</tr>
<tr>
<td>1995</td>
<td>995.17</td>
<td>2.47%</td>
</tr>
<tr>
<td>1996</td>
<td>1,237.96</td>
<td>24.40%</td>
</tr>
<tr>
<td>1997</td>
<td>594.44</td>
<td>-51.98%</td>
</tr>
<tr>
<td>1998</td>
<td>586.13</td>
<td>-1.40%</td>
</tr>
<tr>
<td>1999</td>
<td>812.33</td>
<td>38.69%</td>
</tr>
<tr>
<td>2000</td>
<td>679.64</td>
<td>-16.33%</td>
</tr>
<tr>
<td>2001</td>
<td>696.09</td>
<td>2.42%</td>
</tr>
<tr>
<td>2002</td>
<td>646.32</td>
<td>-7.15%</td>
</tr>
<tr>
<td>2003</td>
<td>793.94</td>
<td>22.84%</td>
</tr>
<tr>
<td>2004</td>
<td>907.43</td>
<td>14.29%</td>
</tr>
<tr>
<td>2005</td>
<td>899.79</td>
<td>-0.84%</td>
</tr>
<tr>
<td>2006</td>
<td>1,096.24</td>
<td>21.83%</td>
</tr>
</tbody>
</table>

**Avg 15-yrs mkt return**  7.32%
**Avg 10-yrs mkt return**  2.48%
**Avg 5-yrs mkt return**  6.31%

Source: Datastream
Regression Result for Beta Calculation – Sime Darby Bhd – Pre-Merger

Dependent Variable: SD  
Method: Least Squares  
Date: 05/14/09  Time: 17:12
Sample (adjusted): 1/01/1993 10/12/2007  
Included observations: 772 after adjustments

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>KLCI</td>
<td>0.942290</td>
<td>0.033733</td>
<td>27.93407</td>
<td>0.0000</td>
</tr>
<tr>
<td>C</td>
<td>0.000867</td>
<td>0.001126</td>
<td>0.770356</td>
<td>0.4413</td>
</tr>
</tbody>
</table>

R-squared     | 0.503326 | Mean dependent var | 0.002307 |
Adjusted R-squared | 0.502681 | S.D. dependent var | 0.444303 |
S.E. of regression   | 0.031243 | Akaike info criterion | -4.091480 |
Sum squared resid    | 0.751598 | Schwarz criterion | -4.079436 |
Log likelihood       | 1581.311 | F-statistic | 780.3125 |
Durbin-Watson stat   | 2.441385 | Prob(F-statistic) | 0.000000 |

\[
SD = 0.9422895101 \times \text{KLCI} + 0.000867134507
\]

\[
\text{Beta} = 0.9422895101
\]
Regression Result for Beta Calculation – Golden Hope Plantation Bhd – Pre-Merger

Dependent Variable: GH  
Method: Least Squares
Date: 05/14/09   Time: 17:08
Sample (adjusted): 1/01/1993 10/12/2007
Included observations: 772 after adjustments

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>KLCI</td>
<td>0.774544</td>
<td>0.039475</td>
<td>19.62121</td>
<td>0.0000</td>
</tr>
<tr>
<td>C</td>
<td>0.001919</td>
<td>0.001317</td>
<td>1.457009</td>
<td>0.1455</td>
</tr>
</tbody>
</table>

<p>| | | | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>R-squared</td>
<td>0.333329</td>
<td>Mean dependent var</td>
<td>0.003103</td>
<td></td>
</tr>
<tr>
<td>Adjusted R-squared</td>
<td>0.332463</td>
<td>S.D. dependent var</td>
<td>0.044749</td>
<td></td>
</tr>
<tr>
<td>S.E. of regression</td>
<td>0.036561</td>
<td>Akaike info criterion</td>
<td>-3.777086</td>
<td></td>
</tr>
<tr>
<td>Sum squared resid</td>
<td>1.029261</td>
<td>Schwarz criterion</td>
<td>-3.765042</td>
<td></td>
</tr>
<tr>
<td>Log likelihood</td>
<td>1459.955</td>
<td>F-statistic</td>
<td>384.9920</td>
<td></td>
</tr>
<tr>
<td>Durbin-Watson stat</td>
<td>2.050485</td>
<td>Prob(F-statistic)</td>
<td>0.000000</td>
<td></td>
</tr>
</tbody>
</table>

GH = 0.77454364*KLCI + 0.001919230116

Beta = 0.77454364
Regression Result for Beta Calculation – Kumpulan Guthrie Bhd – Pre-Merger

Dependent Variable: KGH
Method: Least Squares
Date: 05/14/09   Time: 17:13
Sample (adjusted): 1/01/1993 10/12/2007
Included observations: 772 after adjustments

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>t</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>KLCI</td>
<td>0.673842</td>
<td></td>
<td>0.039280</td>
<td>17.15495</td>
<td>0.0000</td>
</tr>
<tr>
<td>C</td>
<td>0.001912</td>
<td></td>
<td>0.001311</td>
<td>1.458511</td>
<td>0.1451</td>
</tr>
</tbody>
</table>

R-squared 0.276514  Mean dependent var 0.002942
Adjusted R-squared 0.275575  S.D. dependent var 0.042743
S.E. of regression 0.036380  Akaike info criterion -3.786993
Sum squared resid 1.019114  Schwarz criterion -3.774949
Log likelihood 1463.779  F-statistic 294.2922
Durbin-Watson stat 2.188749  Prob(F-statistic) 0.000000

$\text{KGH} = 0.6738420087 \times \text{KLCI} + 0.001911714485$

$\text{Beta} = 0.6738420087$
### Regression Result for Beta Calculation – Sime Darby Bhd – Post Merger

Dependent Variable: SD  
Method: Least Squares  
Date: 05/14/09  Time: 17:02  
Included observations: 74

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>KLCI</td>
<td>1.346610</td>
<td>0.170005</td>
<td>7.920992</td>
<td>0.0000</td>
</tr>
<tr>
<td>C</td>
<td>0.002987</td>
<td>0.004650</td>
<td>0.642422</td>
<td>0.5226</td>
</tr>
</tbody>
</table>

R-squared: 0.465646, Mean dependent var: -0.005042  
Adjusted R-squared: 0.458224, S.D. dependent var: 0.053038  
S.E. of regression: 0.039039, Akaike info criterion: -3.621869  
Sum squared resid: 0.109730, Schwarz criterion: -3.559597  
Log likelihood: 136.0091, F-statistic: 62.74211  
Durbin-Watson stat: 1.756755, Prob(F-statistic): 0.000000

\[
SD = 1.346609683 \times KLCI + 0.002987260104
\]

**Beta** = 1.346609683