MINORITY SHAREHOLDERS WATCH GROUP
BADAN PENGAWAS PEMEGANG SAHAM MINORITI BERHAD
(Incorporated in Malaysia . Registration No. 200001022382 (524989-M))

The Observer

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❖ Diversification, pure play and conglomerates

They say that you should never put all your eggs in one basket. And that diversification is the answer to spread your risk. And there is truth in the saying. What is often not emphasized enough is the risk of over-diversification and the perils it brings – the risk of being 'a jack of all trades but a master of none'.

PLCs have a choice. Whether to diversify on remain focused on one business. And even when we talk about diversification, there is diversification in related areas e.g., downstream and upstream operations, and diversification into other unrelated sectors.

Vertical integration

An example of diversification in related areas is Farm Fresh Berhad's (FFB) recent foray into the ice cream business. Investment analysts have maintained a positive stance on FFB following the dairy producer's proposal to acquire a controlling stake in ice-cream company The Inside Scoop Sdn Bhd (TISSB).

FFB announced the proposed acquisition of a 65% stake in TISSB, an ice cream maker with 37 retail outlets nationwide, for RM83.9 million via share purchase and subscription.

Analysts have been largely optimistic on the acquisition citing the positive business synergies across its value chain and the potential foray into the consumer-packaged goods (CPG) ice cream market.

Having retail ice creameries as a new revenue stream offers various businesses synergies to FFB through product cross-selling opportunities, regional store expansions and wider product distribution network capabilities.

The investing fraternity generally views such related forays positively.

Holding company discounts

When a PLC diversifies into many sectors, there is what is known as the 'holding company discount'. The share price is discounted because the PLC is invested in many unrelated sectors – 1+1+1 is less than three. That is why the concept of 'unlocking the value' is a popular way to create value for shareholders. This is when the conglomerate lists its other related businesses as separate PLCs – in which case, 1+1+1 may be more than three.

Pure play and conglomerate

At one time, the concept of a conglomerate was popular with many investors - the huge ambling lumbering giant of a PLC with fingers across many unrelated sectors. Size mattered then. But with size came the loss of agility and nimbleness. They were not the bamboo that could bend with the strong winds. They were the sturdy erect trees that would break at the onslaught of strong winds.

Such conglomerates generally fell out of favour with investors who seemed to prefer pure-play PLCs. Investors who see a bright future for palm oil, prefer to invest in companies whose business focus was palm oil, i.e., oil palm plantation companies. So, the conglomerate with palm oil as one of its businesses was not the preferred choice of the investor who may see a future for palm oil but not for the other unrelated sectors within the conglomerate.

Pure play

An example of the 'holding company discount' and 'unlocking of value' through pure play restructuring was Sime Darby Berhad's (SDB) restructuring plan in 2017 that created three independent pure-play companies which was listed on the Main Market of Bursa Malaysia Securities Berhad (Bursa Securities).

The intended corporate structure aimed to maximise the value for shareholders who will eventually hold shares in three exciting pure plays.

The plan involved an internal restructuring and share distribution exercise before listing its plantation and property businesses. With the listing, the three companies, namely, Sime Darby Plantation Berhad, Sime Darby Property Berhad and Sime Darby Bhd, with their focused businesses were well positioned for further growth in their respective sectors globally and regionally.

With direct access to capital markets and funding flexibility, each pure-play company benefited from better-focused capital management and customised growth strategies. Meanwhile, shareholders could participate directly in the equity and growth of the three companies with greater visibility on the financial performance of each listed entity.

Shareholders could choose which pure-play sector they wanted to be invested in.

Management capability

When diversifying, boards must consider whether they and the management have the capability and capacity to execute the diversification successfully. That is the same question a minority shareholder should ask when a PLC announces a diversification. The further away the diversification is from the core business of the company, the greater the risk that things might go wrong.

Conglomerates tend to have big boards at the holding company level as they need expertise in the various sectors in which they are invested in. Thus, the conglomerate which is invested in palm oil, property and heavy machinery will have to have directors with knowledge in these sectors. Big boards have a risk of becoming dysfunctional. There is also a risk that focus would be lost if the board, as a holding company board, covers many different sectors.

Conglomerates also tend to have an elaborate 'multi-tiered' reporting hierarchy – a holding company with many subsidiaries with each one being involved in an unrelated sector. The bureaucracy and the multi-tiered reporting structures may be a hindrance rather than a help. The preference now is for flatter reporting structures.

So, it is understandable if minority shareholders tend towards pure-play PLCs and if there is any diversification, it is either upstream or downstream. That way, they can invest in sectors that they want to be invested in.

Devanesan Evanson
Chief Executive Officer

MSWG AGM/EGM Weekly Watch 27 February – 3 March 2023

For this week, the following are the AGMs/EGMs of companies in the Minority Shareholders Watch Group's (MSWG) watch list.

The summary of points of interest is highlighted here, while the details of the questions to the companies can be obtained via MSWG's website at www.mswg.org.my.

Date & Time	Company	Quick-take
27.02.23 (Mon) 09.30 am	Hong Seng Consolidation Berhad	The Group recorded normalised revenue post-pandemic with revenue of RM198.40 million in FY2022, mainly contributed by the healthcare segment on supplying COVID-19 PCR test kits, medical supplies and providing laboratory services for COVID-19 PCR tests. Due to the change of financial year end from 31 March to 30 September, no comparative financial information is available for the FYE 2022. Overall, it recorded a net profit of RM97.19 million for FY2022 mainly contributed by the Healthcare Segment and gain on disposal of subsidiaries.
28.02.23 (Tue) 02.30 pm	APB Resources Berhad	APB group recorded improved financial performance in FY2022 with a 37% increase in revenue to RM78.02 million from RM56.87 million the year

		before, mainly due to higher project revenue. As a result of the higher revenue and recovery for impairment losses on trade receivables, the Group registered a net profit of RM8.6 million against net loss of RM5.3 million in FY2021. The Group expects FY2023 to remain challenging due to slower capital spending in the fabrication sector coupled with the sector's overcapacity situation.
02.03.23 (Thur) 09.30 am	Notion VTEC Berhad	The Group's revenue of RM334.1 million (FY2021: RM352.9 million) was 5% lower than FY2021. Yet, the Group recorded a net profit of RM9.4 million compared to a loss of RM7.8 million in the previous year, mainly due to higher other income recorded amounting to RM50.8 million (FY2021: RM16.5 million). It is seeking shareholders' approval to grant an ex-gratia payment of RM150,000 to its long serving independent non-executive director who has resigned on 20 January 2023. MSWG does not support such ex-gratia payment to non-executive directors and will vote against Ordinary Resolution 7.
03.03.23 (Fri) 03.00 pm	Hubline Berhad	Hubline's revenue for FY2022 was RM 228.44 million compared to RM 152.93 million a year ago. The improvement was primarily due to the following: i) improved number of shipments performed, higher freight rates, as well as increased operational efficiencies in the shipping segment ii) successful procurement and implementation of aviation contract for the aviation division. However, net earnings for FY2022 were 42% lower at RM11.3 million mainly due to lower income, higher administrative expenses and other operating income, and higher taxation.

One of the points of interest to be raised:	
Company	**Points/Issues to Be Raised**
Hong Seng Consolidation Berhad	1. Inventories written down increased significantly to RM2.8 million (18-months FPE2021: RM0.79 million). (Page 68 of AR2022). What comprises these inventories that have been written down? Are these inventories written down still usable or salable? 2. Impairment loss on trade receivables increased significantly to RM6.6 million (18-months FPE2021: RM0.4 million). The Group's impairment loss on trade receivables written off amounted to RM8.1 million (18-months FPE2021: Nil) (Note 11, page 113 of AR2022). (a) What is the reason for the substantial increase in impairment loss on trade receivables? To-date, how much of the RM6.6 million impaired trade receivables have been collected? (b) What comprises the trade receivables that have been written off? What were the measures taken to recover the RM8.1 million prior to being written-off?
APB Resources Berhad	APB group recorded improved financial performance in FY2022 with a 37% increase in revenue to RM78.02 million from RM56.87 million in the year before, mainly due to higher project revenue amid a slight improvement in the operating environment. As a result of the higher revenue and recovery for impairment losses on trade receivables, the Group registered profit after taxation of RM8.6 million against loss after taxation of RM5.3 million for FY2021 (Page 10 & 11 of Annual Report (AR) 2022). a) At last year's AGM, the Board replied to MSWG's question that the bulk of the Group's current order book will be completed in FY2022. What is the value of the remaining order book to be delivered by the Group? How long would these works sustain APB's operation? b) What are the new projects and order book value secured to-date? c) What is the visibility of replenishing the orderbook in view of the ongoing conflicts in Ukraine, the rapid rise in global inflation and the challenges in the process

	equipment industry? What is the Group's internal target for order book replenishment in FY2023?
Hubline Berhad	"In spite of various challenges within the South East Asian region, we continue to invest our resources into this geographical region because we see good potential growth over the longer term. Moreover, the challenging economic backdrop may actually produce several business and investment opportunities which may yield tangible results for us in the longer term provided that these opportunities fall within the Group's risk-adjusted return profile." (page 6 of FY2022 annual report) How much capital expenditure is allocated for FY2023 and what are the investments to be made in FY2023?

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DISCLOSURE OF INTERESTS

• *With regard to the companies mentioned, MSWG holds a minimum number of shares in all* the companies covered in this newsletter.