

Background and history of ranhill utilities berhad flashcard



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Ranhill Utilities was incorporated in 30 August 2000 as a public limited company under the name of Insan Utiliti Berhad and assumed its present name on 25 January 2002. RUB is principally an investment holding company. SAJH, it's wholly owned subsidiary has been granted a 30-year Concession by the state Government to supply treated water to consumers in Johor commencing 1 March 2000. Through the Concession, SAJH is an integrated water supply services company.

Principally involved in sourcing of raw water, treatment and distribution of treated water to consumers. Potable water is supplied from 43 water treatment plants located throughout Johor state. The Initial Public Offering of RUB According to the company's prospectus dated 16 May 2002, the company proposed to issue 77, 000, 000 new ordinary shares of RM1. 00 each at an issue price of RM2. 50 per share in conjunction with the listing of Ranhill Utilities Berhad on the main board of the Kuala Lumpur Stock Exchange.

All the 77, 000, 000 public issue shares are in full application. The public issue adviser, underwriter and placement agent for Ranhill Utilities Berhad was Alliance Merchant Bank. The Public Issue Price of RM2. 50 was determined using Discounted Cash Flow (DCF) method of valuation as agreed by Ranhill Utilities and Alliance as Adviser, Managing Underwriter and Placement Agent for the Public Issue. The DCF method of valuation entails deriving the net present value per share of the future economic benefits of investing in a particular company.

Future economic benefits are represented by net cash flows available for distribution to ordinary shareholders of the company over the remaining concession period. Net present value is obtained by discounting this net cash flow using an appropriate rate of return to represent the opportunity cost of investing in the company. Given the cash flow forecast and projections as presented in the Prospectus, the public issuing price implies the discount rate of approximately 12.57% was applied for the valuation.

The issue price of RM2.50 per share for the public issue shares was determined after taking into consideration a number of factors, including the Group's financial and operating history and condition, its prospect and the prospects of the industry in which the group operates, the management of the group, the market price for shares of companies engaged in business similar to that of the group and the prevailing market conditions at the time when the issue price was determined.

The company starts trading on the KLSE main board (under Infrastructure Project Company, IPC sector) by 27 June 2002 initial price of RM2.50 and the first day closing price was RM2.39 (Rashid Hussein Securities, 2002). The percentage change from IPO price was -4.40%. Obviously, the stocks have been overpriced. The possible reason for the overpricing may be due to the investors' pessimistic view towards the current market condition. The bear market was still under the pressure of the 911 incidents and the economic slowdown.

To add fuel to the fire, during that particular period, the KLCI was trading at 705, the stock index had dropped 3 days continuously, which result a total

dropped of 50 points. This is due to the resignation news of the Malaysia Prime Minister, Dato' Sri Dr. Mahathir. Besides, there may be internal problems in determining the IPO price. Since the IPO price was derived based mostly based on assumptions, the figure obtained may be inaccurate.

The major advantage of DCF method as compare to conventional method is that it takes time value of money into consideration by discounting the future cash flow with a discount rate. Besides, this method also provides a good insight into the development of costs and revenues over the period. Furthermore, there were no “ hidden” assumptions possible because the company is required by the SC to disclose all possible assumptions being made.

This may provide verifiable results because of the clarity of the method. Lastly, the calculation can be done efficiently by using computer software. However, there are some pitfalls of DCF method. First of all, it will be difficult to determine the appropriate discount rate to discount the cash flow. Secondly, the cash flows are based on estimation. It will be a question mark on how the company derived the cash flow since future is unpredictable, not one would know what would be the tomorrow's world.

Hence, the forecasted cash flow is questionable. Time between valuation date and last lease expiry date is too long. Besides, the company had make an assumption that inflation rate remains at 4% throughout 27 financial years, which is quite impossible. Furthermore, this method requires far more inputs and information than other valuation approaches. This inputs and

information are not only difficult to estimate, but can be manipulated by the company to provide the conclusion it wants.