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Plagiarism Statement

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School of Business Studies**Plagiarism Statement**

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We confirm that the submitted work are all our own work and are in our own words.

Name (Block Capitals) Regn. No. Signature

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Part A

Write a report on how the current Global Financial Crisis impacted the financial strategies of Malaysian a Malaysian company. The report should include the background of the Global Financial Crisis, steps taken by governments to mitigate it and how it may have impacted the financial strategies of a chosen Malaysian company.

1.0 Executive summary

The global financial crisis has been one of the worst to ever hit the developed and developing nations since the Great Depression, and has quickly burgeoned into a global economic crisis. This report gives an overview of the crisis, and how it has impacted our nation.

Steps have been taken by the government to mitigate this crisis. This has been done through two economic stimulus packages meant to inject funds into the Malaysian economy to produce a multiplier effect for boosting the economy.

We then take a look at the effects of the sector on Gamuda Berhad, a company in the construction and property development sector. We see how the economic stimulus package has benefitted it through the granting of the Electrified Double Tracking Project from Ipoh to Padang Besar worth RM12.5 billion, and its effect on the company's financial strategies.

As steel is a major raw material in the construction of buildings and infrastructure, we also analyze the impact on the financial strategies of a steel company in Malaysia, Choo Bee Metal Industries Berhad. The report ends with a future outlook of the following two companies in the near future.

2.0 Global financial crisis- Background

Plummeting stock markets have wiped out 33% of the value of companies, \$14.5 trillion.

The effects of the global financial crisis have been such that a massive \$14.5 trillion in the value of companies has vanished into the thin air in a matter of months. It has been the most serious financial crisis since the Great

Depression of 1929, causing business failures, increased unemployment, and significant decline in economic activity. What happened?

August 2007 had seen the world economy plunged into intensive financial disorder and turmoil. Fannie Mac and Freddie Mac, the two largest mortgage companies in the US fell into conservatorship. A week later, Lehman Brothers went bankrupt when the US government refused to rescue the investment bank, triggering the financial crisis.

Banks became reluctant to lend to one another, allowing only overnight borrowing to institutions. With banks refusing to provide credit, and the imposition of more stringent regulations on borrowings, businesses found it more and more difficult to borrow money for their operations and long-term expansionary plans.

In Iceland, the banking system crippled and the government had to borrow from the IMF and other neighbors for funds to save their economy. The country could not pay back its external debts, and the Icelandic currency- the Krona has become valueless. Virtually bankrupt, the three largest banks in Iceland: Kaupthing Bank, Landsbanki and Glitner Bank has been nationalized.

Insurance giant, AIG had to be rescued by the US government by the approval of an \$85 billion bailout to prevent it from going under because it was “ too big to fail”. All the above events accumulated to signal the lack of confidence in the US economy, plunging stock prices downwards, weakening the economy which quickly affected the economies of other countries due in part to globalization through increased connectivity.

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The reason for the financial crisis cannot be pinpointed to any one specific cause, but is a result of a combination of factors which converge to tip the scale to cause a major change. However, the main cause for the crisis can be said to be attributed to sub-prime mortgage lending in the US. Simply, the appreciation of property prices coupled with easy credit offered by banks on the acquisition of property attracted people to purchase property, not only for personal but for investment purposes. Banks creatively pooled these loans into mortgage-backed securities and sold them off as derivatives to other investors. This is also known as the securitization of debt.

In order to encourage more customers to obtain loans from banks, the banks approved loans even to sub-prime buyers. These buyers have shaky financial background, but were also approved by the banks. With the burst of the US housing bubble, declines in real housing prices and higher mortgage rates eventually resulted in defaults in payments, leading to foreclosures and the collapse of the sub-prime mortgage industry. This then led to the fall of several prominent financial institutions, sending shock waves around the world. The financial system became dysfunctional and this marks the commencement of a financial crisis.

To date, the UK and other European countries have spent some \$2 trillion on rescues and bailout packages to prevent various major financial institutions from failing. Among other effects of the crisis are lesser financing and foreign aid for development in poorer countries. The economy is said by analysts to enter into global rebound and recovery in year 2010.

3. 0 Steps taken by the Malaysian government to mitigate the financial crisis:

It is a well-known saying that, “ If the United States sneezes, the rest of the world catches a cold.” This is true to a certain extent. Developed countries such as the United Kingdom and Europe were among the first to be hit by the effects of US “ flu”. Developing countries such as Malaysia caught on slower, not having entirely opened up its economy to the rest of the world. However, effects were being felt. Deterioration in US market, being a major trading partner of Malaysia (3rd largest trading partner) eventually affected our country’s economy.

Among the impact of the global economic recession are:

- Sharp decline in exports (e. g. Jan ‘ 09 down by 27. 8%)
- Sharp decline in export commodity prices (crude oil and palm oil)
- FDI inflows expected to halve (‘09: RM26bln, ‘08: RM51bln)
- Unemployment rate to rise to 4. 5% (‘08: 3. 7%)
- Global meltdown continues to weaken Bursa Malaysia’s performance

This eventually prompted a response from the Malaysian government.

On the 4th of November 2008, the first economic stimulus package of RM7 billion was approved in order to boost the Malaysian economy. This was mainly financed through savings from fuel subsidies, which has decreased due to lower oil prices. This package was primarily directed at certain major projects mainly in the construction industry and was hoped to start off a positive ripple through the multiplier effect.

It was found to be ineffective when economic conditions worsened, and a second stimulus package was proposed. A further RM60 billion was pumped

into the economy. Of this amount, RM15 billion is fiscal injection, RM25 billion Guarantee Funds, RM10 billion equity investments, RM7 billion private finance initiative (PFI) and off-budget projects, as well as RM3 billion worth of tax incentives. This RM60 billion accounts for almost 9% of the Malaysian GDP.

The implementation of such a large stimulus package is unprecedented in the nation's economic history. Training and job placement opportunities were initiated in both the public and private sectors to ensure acceptable unemployment rates. In addition, it is aimed at facilitating private sector activities and easing the burden of vulnerable groups.

The 2nd stimulus package is to be implemented in four thrusts:

RM

- Thrust 1: Training, education, employment creation, retrenched 2 billion workers welfare & reduction of foreign workers
- Thrust 2: Home ownership, public infrastructure, savings bonds, 10 billion school facilities, rural areas amenities, Sabah & Sarawak infrastructure, microcredit schemes, retrenched workers welfare
- Thrust 3: Guarantee scheme (working capital & loan restructuring), 29 billion promote automotive, aviation & tourism sectors, higher windfall

profit levy threshold on palm oil, tax incentives (accelerated capital allowance, carry back losses) and reducing time-to-market to access of the capital market

telecommunication infrastructure, PFI (Tanjung Agas industrial park in ECER, biotechnology cluster in IDR, traffic infrastructure system around KL Sentral), enhancing GLCs' CSR activities in human capital, new FIC role & enhancing Government procurement

Aware that most SMEs have been affected by the worsening global economic environment, particularly from the contraction in export markets, the Government has established a Working Capital Guarantee Scheme totalling RM5billion to provide working capital to companies with shareholder equity below RM20 million.

In the Bank Negara Malaysia (BNM), the Overnight Policy Rate (OPR), which determines banks' base lending rate, has been reduced by 75 and 50 basis points to 2% in Jan and Feb respectively, and resulted in the lowered base lending rate of 5.53%. This is to encourage lending between banks. The statutory reserve requirement has also been cut by 3%-1% to help reduce the cost of funds and sustain the flow of lending.

Among other initiatives taken by the government are: the guarantee of bank deposits until the end of 2010 by the BNM. What is more, to encourage foreign direct investments, Bumiputera ownership in the acquisition of equity stakes, mergers, and takeovers has also been

lifted. Guidelines on property transactions has also been relaxed, and Danajamin had also been set up by the government in May 2009 to facilitate capital-raising by local companies who face problems in doing so.

4. 0 Impact of the global financial crisis:

Sector: Construction

I have chosen the company, Gamuda Bhd as the subject of analysis for this purpose. First, a brief introduction on the business of Gamuda, the company situation before and after the crisis, and its potential effects on the company's financial strategies.

4. 1 Gamuda Berhad

Gamuda is among the largest builders in Malaysia, second only to IJM Corporation. Among Gamuda's other competitors are WCT Berhad and Malaysian Resource Corporation Berhad, all of which have been affected by the crisis.

Gamuda is a leader in Build-Operate-Transfer (BOT) civil engineering infrastructure and township development. The core business segments in Gamuda are three: Engineering & Construction, Infrastructure Concessions, and Township Developments

Percentage-wise, the Engineering & Construction is the most important sector as it takes up 75. 9% of total revenue. Among projects included in this sector are the constructions of railway tracks, hydroelectric dams, airports, waterways and tunnels, etc. Infrastructure Concessions- 19. 6% include: highway toll concessions, water supply, and hydropower. Township Developments- 4. 4% include: various

townships in Malaysia- Valencia, Jade Hills, Kota Kemuning, Bandar Botanic, the Yen So Park in Vietnam,

4. 1. 1 Industry Overview

The property and construction industry are capital-intensive sectors requiring sophisticated technologies, high levels of labour and manpower, and large amounts of raw materials such as iron, steel, and cement. These three inputs make up most of the costs in any given project, and an increase in the following costs would decrease profit margins and therefore returns from the projects.

Due to the large amounts of money invested in a project (larger projects involves billions of dollars exchanging hands), cashflow management and cash conservation is crucial. Risks involved are also high, and investors expect higher returns and consistent dividends compared to a more stable sector such as food and beverages. A project has to ensure stringent safety and health policies, to minimize hazards and prevent accidents from occurring.

At the strategic level, a company dealing in these industries would also have to be proactive in scouting for projects where opportunities exist. Detailed cost-benefit analysis will have to be undertaken not only to determine quantitative costs and benefits in calculating how much to bid for, but also qualitative factors such as the necessity and urgency of the project to the company, whether as a strategic move into new markets, reputation/brand building, or to increase confidence in the company and ease shareholder concerns.

To sum it up, these sectors are susceptible to:

- Rise in inflation
- Increase in prices of iron, steel, and cement
- Cancellation of orders due to economic downturn
- A country's political influence
- Cashflow management

However the two real key risks faced by the construction industry remains to be delays in implementation and sub-par margins due to stiff competition.

4. 1. 2 Property and Construction

The property and construction sectors are sensitive to economic conditions. Thus it is no surprise that companies dealing in the two sectors were the most badly hit when the market plunged, following the onset of the global economic crisis. As Gamuda's operations in these 2 sectors consist of 95. 5% in 2008, this makes it extremely susceptible to economic risk.

We can evaluate the impact of the crisis by the construction sector's key performance indicators:

àNumber of sales permit: Falling since July 2008, but the figures have reflected the pessimism of the industry distinctly since August 2008. Earlier in the year, it has reached 87 per month, fell to 58 in August and 41 in December 2008.

àNumber of housing approvals: On the downtrend.

àProduction of construction-related products: In September 2008, there was a 6.8% increase (year-on-year) in this index. It fell by 1.9% in October 2008, but most alarmingly there was a contraction of 5.1% in November 2008. This change shows the bleak outlook of the industry.

4. 1. 3 Government steps

The Government of Malaysia has benefited Gamuda after it won the bid for the Ipoh-Padang Besar electrified double-tracking railway project (EDTP) worth RM12.5 billion as part of the stimulus package to boost the economy. Among other projects by the government are the Pahang-Selangor Interstate water transfer project, the new Sepang low-cost carrier terminal, and the extension of the Klang Valley Light Rail Transit, all three contracts of which have been bid for by Gamuda. As a major construction company with an excellent track record, there is a high chance of winning the bid, hence increasing its construction order book by several billion dollars.

In addition to that, the Government has also implemented a new ‘Deferred Payment’

mechanism, where Bank Pembangunan has been mandated to pay on behalf of the government up to a total of RM6.75bn representing 54% of the total value of the EDTP project.

As for the property sector, the Government is allowing individuals or foreign entities to buy commercial real estate worth RM500,000 and above without any Foreign Investment Committee (FIC) Approval. This move would encourage more buyers to buy properties here in the country and help encourage investment in real estate.

4. 1. 4 Ratio Analysis- Highlights:

The following can be seen from Gamuda's financial ratios:

- Gamuda's ROA has increased from 3.32% in 2007 to 5.58% in 2008, signifying increased efficiency in the use of its assets in generating profits.
- Gearing ratio remains at high levels, increasing slightly from 41.9%-43.5%.
- Net dividends per share decreased from 40sen/share in 2007 to 18sen/share in 2008. Profits were retained to fund operations and projects obtained by the company.

Other than the high gearing ratio, other financial aspects in 2008 are favourable overall.

4. 1. 5 Capital structure

Gamuda's capital structure consists of a combination of debt instruments and RM2,005,016 worth of shares.

Long-term borrowings consist mostly of Murabahah Medium-term Notes (MTN) of RM850 million, and a smaller portion of secured and unsecured term loans.

Short-term borrowings include commercial papers of RM35million, unsecured term loans of 25million, and revolving credits of RM722,253 million.

There is a debt-equity ratio of 60% compared to 42% in the previous year.

Thanks to the RM12.5 billion Ipoh-Padang Besar rail project won by Gamuda through the stimulus package, this has benefited Gamuda and boosted its order book. Hence the impact of the crisis on Gamuda is largely cushioned compared to its competitors. Revolving credits of RM288.5 million is used in relation to design, construction, testing, commissioning and maintenance of the electrified double track.

There is an existing proposal that Lingkaran Trans Kota Holdings Bhd (LITRAK), of which Gamuda is a substantial shareholder- owning 44.8% of LITRAK undergo a capital repayment exercise of 93 sen, of which Gamuda will receive an amount of RM462 million. The Selangor government also offered to take over Splash for RM2.975 billion, both of which will improve Gamuda's net gearing.

4.2 Steel

Steel is a major raw material in the construction industry. Therefore we will now take a look at the impact of the financial crisis on the steel industry.

Steel is a major raw material in the construction sector for the building of its properties and infrastructure. We shall now study Choo Bee Metal Industries Berhad to gauge the effects of government economic stimulation in this industry.

The global economic crisis has had a major negative impact, on the international and domestic demand for Hot Rolled Coil ("HRC") steel sheets, which is the main export of Choo Bee.

The strong demand for steel, and high steel prices, in the early part of 2008 were reversed by the global financial crisis from September

2008. Prices of steel and steel products dropped rapidly on falling demand. Prices increased from US\$700 per tonne in June 2007, to US\$1,100 per tonne by June 2008, and collapsing even lower in 2009. This has affected the sales of Choo Bee, as the price at which its HRC can be sold has dropped sharply.

Government efforts to improve the economy through its economic stimulus packages has benefited the construction industry, and has indirectly created opportunities for local steel manufacturers like Choo Bee to supply their steel to the market. However, Choo Bee being a relatively smaller steel company could not match the giant steel companies like Malaysian Steel Works, Ann Joo Resources, and Southern Steel Bhd. Raw materials for projects received by construction companies would most likely be given to larger steel companies which could provide lower prices due to economies of scale.

The government is also implementing a proposal where a reduction of import duties of raw materials of 10% in 2009 and another 5% every subsequent year, which is expected to reduce Choo Bee's costs of production. This however, would also not be of much help, due to the dropping steel prices.

Choo Bee currently has a very low gearing ratio of only 2.75%, signifying that it is operating on a very conservative level. It also has very high levels of reserves and retained earnings which are not being in use effectively for generating profits to maximize shareholder wealth.

5.0 Conclusion

Future outlook:**Gamuda Berhad**

Performance is likely to be weaker than 2008 amidst economic uncertainties in the construction and properties sector. Borrowings and gearing ratio is expected to be high. However, if Splash is successfully sold to the government at a reasonable price, the substantial amount of cash received can be used to fund operations, reducing its gearing ratio and allowing further loans to be obtained if necessary. As cashflow management becomes a primary focus, and financial prudence necessary, this would most likely result in a lower dividend of 25sen received by shareholders in 2008. The “ Deferred payment” mechanism is also expected to help manage working capital more effectively.

A more conservative strategy would be used of where the focus would be on surviving the economic meltdown. This entailed taking drastic measures to curb expenses, consolidate operations, streamline capex programs and defer expansion plans.

With Gamuda’s strong reputation and experience in the construction industry, coupled with a strong order book caused by the Government’s economic stimulus package will probably last it for the next 2-3 years. It is expected to regain its performance once the global recession lifts in year 2010.

Choo Bee Metal Industries

Outlook in year 2009 is likely to be negative for Choo Bee and the steel industry in general. As the demand for steel is highly dependent on the

performance of construction sector, it will determine the demand for steel. Since the overall outlook on the construction sector has weakened due to the financial crisis, this would mean demand for steel, hence lower profits.

Although the projects mooted out by the government through the stimulus package will indirectly benefit the steel industry, the overall demand for steel will still be low, but is expected to pick up when the recession enters into recovery.

Part B

Write a report on the development of the capital/financial market in Malaysia and how with this development more financial products could be used by Malaysian companies to finance operation, expansion locally and in the international markets. The report should include the development of the conventional capital and Islamic capital market, the take-up rate of financial products such as sukuk zero-coupon bond by Malaysian companies and how it changes their choice of financing and capital structure.

1. 0 Executive Summary

The financial and capital markets in Malaysia have been experiencing exponential growth during the past few decades, especially where the advancement of Islamic financial products is concerned.

This report is meant to give an overview of the development of these markets in Malaysia, with a focus on financial products, such as the sukuk by Malaysian companies. Malaysia has been at the advent of Islamic financing, and much effort has been taken by the government

to establish Malaysia as an Islamic financial hub. Steps taken, and an examination of the popularity and advantages of these Islamic products are explored.

In order to discover the take-up rate of financial products, eight major companies from different sectors in Malaysia have been chosen for this analysis. They comprise companies ranging from the industrial sector to the food & beverage industry.

Finally, a conclusion as to the popularity of Islamic products and the potential changes as to the way businesses choose to fund their operations.

2. 0 Introduction to financial and capital markets

2. 1 Financial markets

A financial market is a mechanism that allows the trading of financial assets or securities. This includes mortgages on a house or lease on a car to securities that are traded on financial markets, termed marketable securities. The trading of commodities such as precious metals and agricultural goods are also a part of the financial markets.

Financial markets primarily facilitate:

- The raising of capital
- The transfer of risk
- International trade

They can be said to consist of the following six categories:

Money market, Capital market, Derivatives market, Foreign exchange market, Fixed income stock, Equity.

2. 2 Capital market

The capital market, as mentioned above- is a type of financial market, which includes the stock and bond market.

They function in two important ways:

In the primary market- to provide new capital for businesses in the form of share issues and loans

In the secondary market- to enable the exchange and trading of securities and bonds to other players

3. 0 Development of the financial and capital market in Malaysia

In Malaysia, Government securities through issues of Malaysian Government Securities (MGS) account for the bulk of funds raised in the private sector. Private Debt Securities (PDS) are the main source of capital market funding for the private sector, with the equity market also providing a sizeable portion through rights issues and Initial Public Offerings (IPOs).

Singapore, once being part of Malaysia, companies in these two countries was listed on both KLSE and the Stock Exchange of Singapore (SES) until the end of 1989. Since then, KLSE has taken various measures, including the introduction of computerized trading, a central depository, and efficient clearing and settlement systems, to develop market infrastructure. In addition, the regulatory framework has been reviewed to promote IPOs and equity investments by domestic and foreign investors.

As a result, some big privatized companies (e. g., Telekom Malaysia Berhad and Tenaga Nasioni Berhad [TNB]) were listed on KLSE, making it one of the fastest-growing markets in the region in the mid-1990s. By the end of the 1980s, the primary market for Government bonds was relatively developed. The Government introduced the principal dealer system to develop the secondary market as well, and at the same time, an auction system for Government securities to promote fair pricing. Although the private debt securities (PDS) market had deepened when the first Cagamas bonds were issued in October 1987, it did not develop until the mid-1990s.

The Government has introduced various measures to enhance market infrastructure and put in place an appropriate regulatory framework. These included the establishment of a credit rating agency (1990), guidelines on PDS issues (1992), tax exemption on interest income from PDS (1993), scripless trading for unlisted PDS (1996), an auction system for the PDS primary market (1996), and a bond information and dissemination system (1997). Despite Government efforts, a lack of benchmark yield curve hinders the development of the bond market.

3. 1 Developments of Islamic Finance

Malaysia is one of the unique countries which operate a dual banking system where the Islamic banking system operates in parallel with the conventional system. Similar to conventional banks, all banking facilities such as deposit account, financing and other products and services are available at Islamic banks. An important milestone taken by the government in positioning Malaysia as an international Islamic

financial hub was to bring forward the liberalization of its Islamic banking sector to 2004, three years ahead of the World Trade Organization's deadline.

The development of the Islamic financial system in Malaysia started with the establishment of pilgrimage fund (Tabung Haji) in 1963 as the first Islamic savings institution. The idea was mooted out of the necessity to develop a mechanism to encourage the Muslims to save for their pilgrimage as the Malaysian Muslims in the past had resorted to various traditional means of saving and keeping their money for the sacred journey. After a few years of break, the first full-fledged Islamic bank was estab