

# Invest Malaysia 2007

21<sup>st</sup> March 2007

## Three Anniversaries and a Prayer

*Reflections on the Malaysian Capital Markets, GLC Transformation  
& the Iskandar Development Region*

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*\*Views of the speaker are strictly his; usual caveats apply in that the views may or may not reflect those of Khazanah's.*

*Distinguished audience, ladies and gentlemen*

## **Introduction**

Thank you once again to the organisers for this invitation to address this august gathering, and for the third year running at that. It is a deep honor and I have come to look forward to this annual event as an opportunity to dialogue with the investment community on the work that we are doing and to outline some of the key things on our minds as we shape our immediate and longer-term future.

Invest Malaysia has become somewhat of a ritual on our annual calendar, and while one is reminded of the foreboding verse “Beware the Ides of March”, on the contrary, we meet this year against the backdrop of a Malaysian market that I believe is in its best shape for the good part of the last ten to even fifteen years. While there remains much to be done, in both the financial and the real economy, I believe it should not go unrecognised that from the capital markets’ standpoint, we are undoubtedly today reaping the benefits of many years of hard toil of rebuilding from the Asian Financial Crisis of the late 1990s.

The 2007 Invest Malaysia also holds extra meaning in that 2007 is a year of several milestones and anniversaries. Indeed, as will be obvious, my speech today is titled *Three Anniversaries and a Prayer*, with the sub-text of *Reflections on the Malaysian Capital Markets, GLC Transformation and Developing the Iskandar Development Region (“IDR”)*.

The three anniversaries refer to first of all, 2007 being three years after the start of the Khazanah and GLC revamp that was first launched in May 2004. Three years that coincide with the KPI-driven performance contract terms that were one of the first measures put in place for the GLC Transformation Programme. I shall use this

opportunity to give you an update as to the progress achieved over the last three years and to highlight the challenges and outlook of the next three years to 2010.

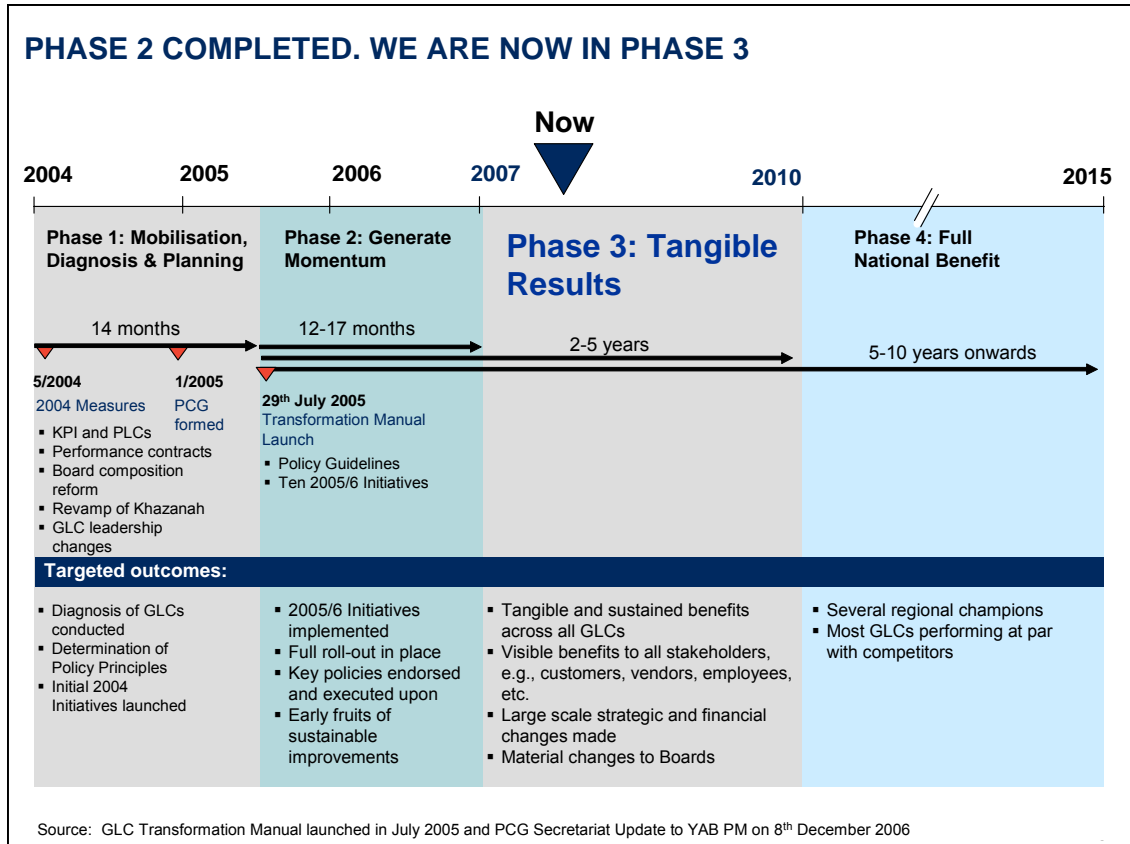
The second milestone refers to 2007 being the tenth anniversary of the onset of the Asian Financial Crisis. Indeed this will be a good time to ask the question whether the last decade was a lost decade or are we on the threshold of a new growth era. It will be an opportune exercise to check on progress made on structural reforms in areas such as corporate restructuring, corporate governance and the strengthening of the financial sector.

The third and last milestone refers to 2007 being the 50<sup>th</sup> anniversary of Malaysia as an independent nation. Such a major milestone calls for both quiet celebration and thanks, and to also look forward on the truly important things, the big long-run factors that ultimately drive the competitiveness of nations. This is a big topic that I will not have the time nor the analysis to table today, but in its stead I would like to take this opportunity to introduce the development of the Iskandar Development Region (“IDR”) in Southern Johor that we are in the midst of implementing, to be positioned as an Asian regional metropolis of the future that showcases the best of the world and the best of Malaysia.

### **First milestone: the 3<sup>rd</sup> Anniversary of Khazanah Revamp and GLC Transformation**

At Invest Malaysia in early 2005, as the GLC Transformation Programme began to take root from its launch in May 2004, I emphasised the importance of execution, or as what has come to be remembered as to “execute or be executed”, while in early 2006, in the midst of considerable cleaning-up of legacy balance sheets, I ended with the prognosis, that we were on track and that we were certainly “staying the course”. Indeed in 2006 we had reiterated that the GLC Transformation Programme was always intended to be a long-term program running over ten years to 2015.

*Exhibit 1: Phases of the GLC Transformation Programme*



Today, almost three years into the program, I am happy to report that the program is very much on track, having successfully completed phases 1 and 2 of mobilisation and gathering momentum. The efforts, we are happy to note, are beginning to bear fruit, and more importantly, we believe the stage has been set to allow for these results to be sustained and more broad-based as we enter Phase 3 of the GLC Transformation Programme covering the period 2007 to 2010.

Phases 1 and 2 that started in May 2004 culminated in the launch of all 10 GLC initiatives, as planned, by December 2006, by YAB Prime Minister. December 2006 also saw the publication of the *Progress Review*, an important document that critically assesses the performance of the program and defines specific actions to drive towards the sustainability of the program. There were many important lessons

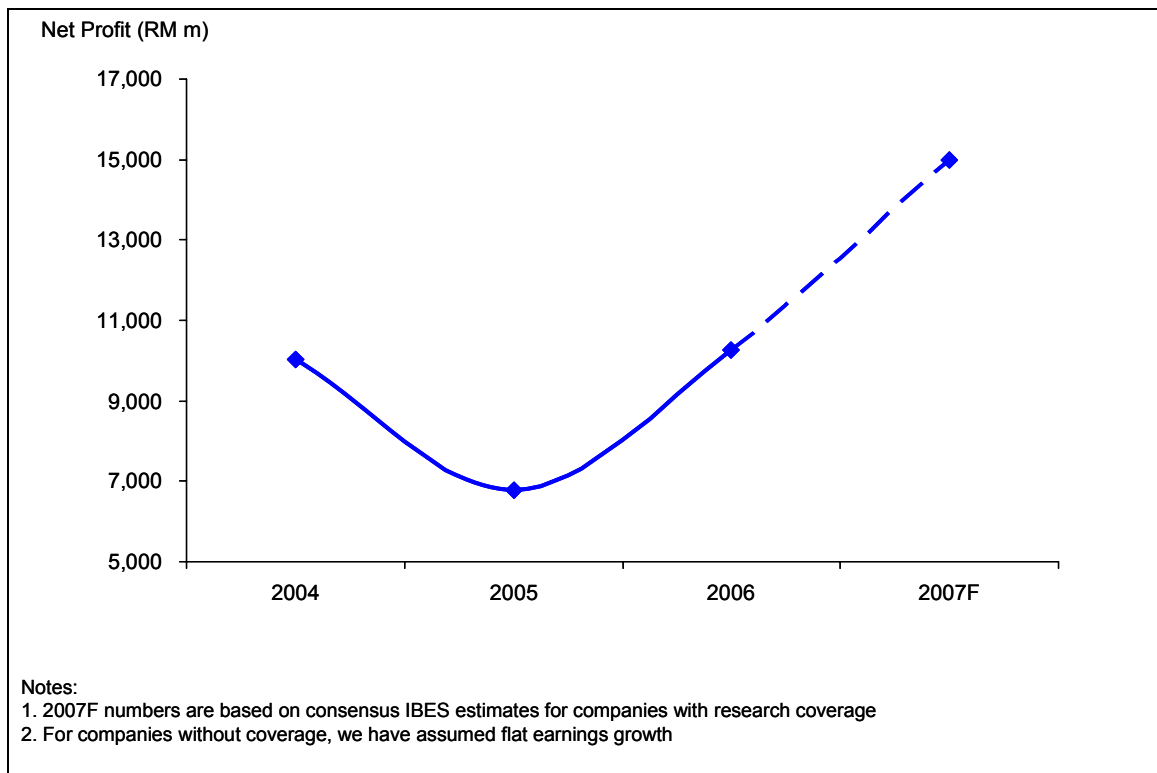
and insights. One was that the program management methodology led by the Putrajaya Committee for GLCs (“PCG”) was instrumental in ensuring all 10 GLC initiatives were rolled-out on schedule. The PCG, chaired by YB Second Finance Minister, continues to meet religiously and thus far has had 13 meetings over the space of 26 months. The Review also concludes that all major change agents in driving the transformation program from GLC management, boards, Government-Linked Investment Companies or GLICs and the Government itself have played an increasingly active and value-driving role.

With the benefit of the full year 2006 results now announced, it is now evidently clear that GLCs financial performance improved very significantly in 2006. We are pleased to report<sup>1</sup> that in Financial Year 2006, the G-20 – the group of 20 leading listed GLCs that constitute some 71% of the market capitalisation of the 48 listed GLCs – achieved a very commendable 60% increase in earnings over FY 2005, approximately four times the earnings growth rate of the broader market. Furthermore, as market gets more visibility on the transformation taking place, analyst forecasts for FY2007 continue to point to strong earnings momentum continuing, with consensus forecast of earnings growth of 43% for the G-20 in FY2007, almost three times the expectations of the broader market. As we chart the results of 2006 against the results of 2004 and 2005 and the expectations of 2007, what emerges is a clear J-Curve of recovery that we had first predicted or targeted last year, in large part due to 2005 as the clean-up year where many GLCs provided or wrote-off many legacy items.

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<sup>1</sup> Refer to the publication *Progress Review March 2007 Update* that we are issuing today

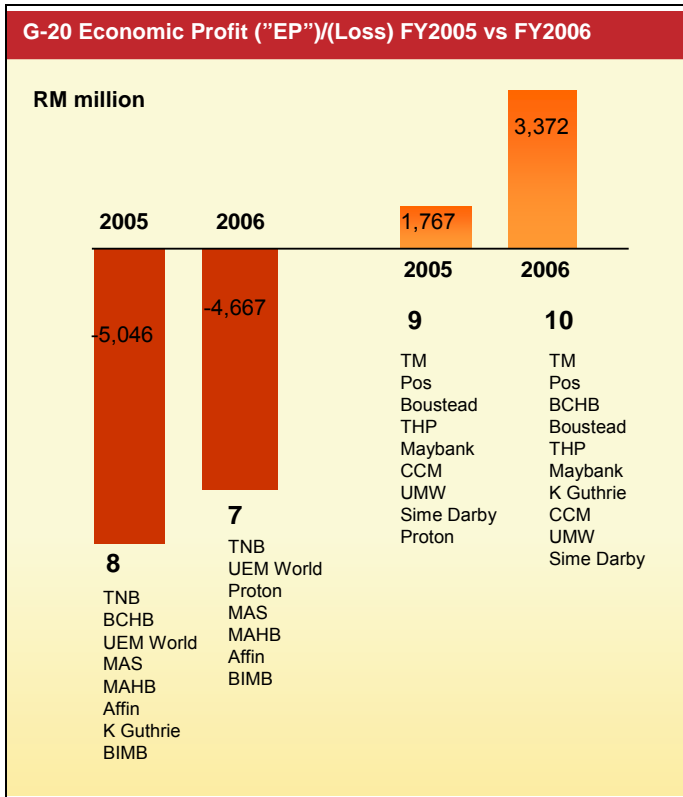
**Exhibit 2: G-20 Aggregate Net Profit – “The J-Curve”**



Source: Khazanah analysis

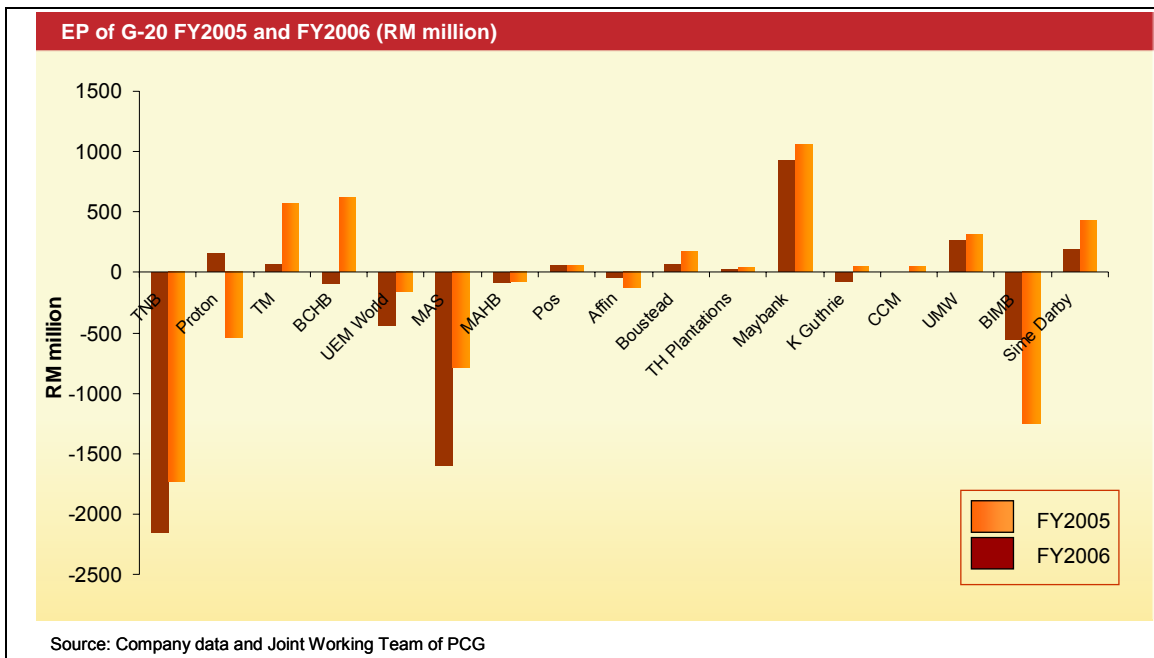
Moreover, it was encouraging that the strong results extended beyond these headline earnings improvements. A more fundamental measure of value creation that we track is economic profit, where much progress was achieved in FY2006 with collective economic profit of the G-20 improving by RM2 billion. While still posting a collective economic loss of RM1.3 billion in FY2006, the outlook to turn this into an economic profit in FY2007 is promising underpinned primarily by Tenaga’s continuing improvements in profitability.

**Exhibit 3: G-20 Economic Profit (“EP”)/(Loss) FY2005 vs. FY2006**



Source: Company data and Joint Working Team of PCG

**Exhibit 4: EP of G-20 FY2005 and FY 2006 (RM million)**

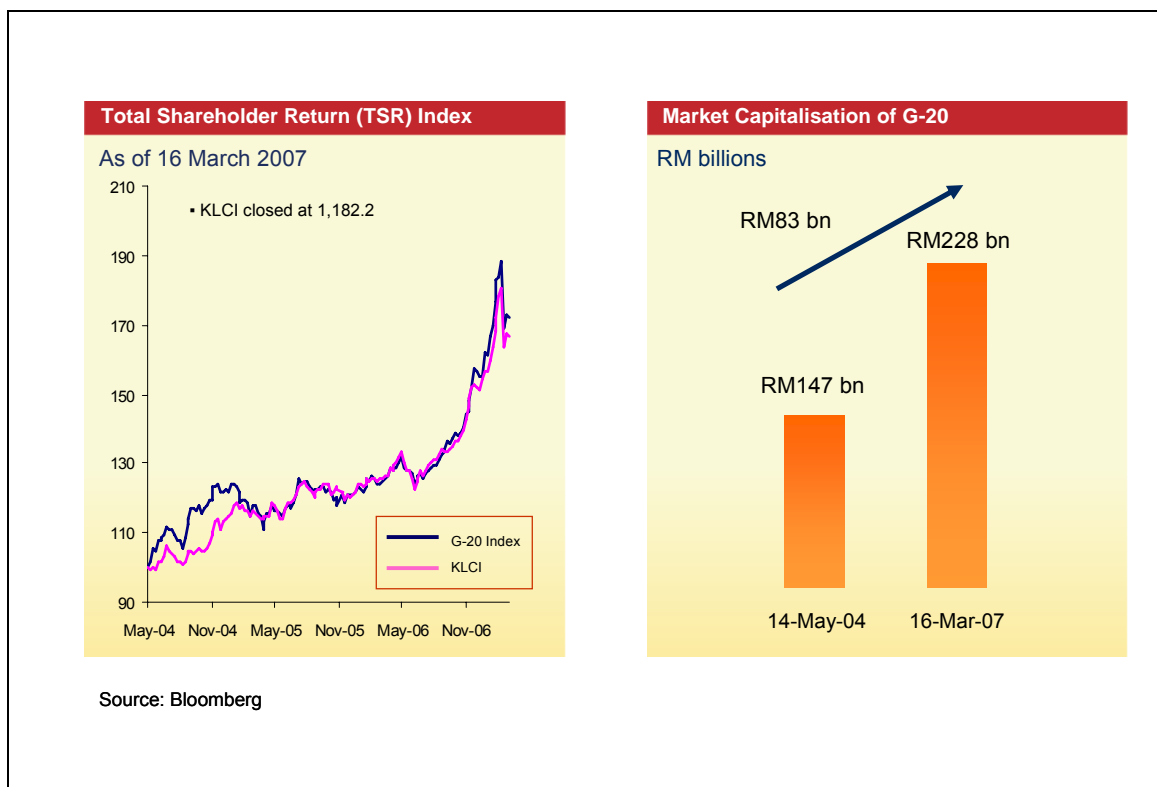


Source: Company data and Joint Working Team of PCG

The G-20, also collectively outperformed both headline KPIs targets and analyst market expectations for FY2006. 72% of headline KPIs were met while only three out of the 17 GLCs tracked by analysts had a shortfall of more than 5% against market expectations.

Underpinned by this strong fundamental showing, shareholder value has increased tremendously since the program started in May 2004<sup>2</sup>, with total shareholder return for the G-20 rising by 71.8%, outperforming the KLCI by 4.9% and translating into an additional market capitalization of RM 83 billion.

**Exhibit 5: Total Shareholder Return Index and Market Capitalisation of G-20**



<sup>2</sup> 14 May 2004 to 16 March 2007

## **Second milestone – 2007 as the tenth anniversary of the onset of the Asian Financial Crisis**

Secondly, 2007 will mark the tenth anniversary of the onset of the Asian Financial Crisis. Indeed, many of us would recall quite vividly the events leading up to the crash of July 1997, from the untimely death of the late Tan Sri Yahya Ahmad, a true leader of Corporate Malaysia who embodied all that was right and good of the go-go Nineties, through to the equally shocking meltdown of markets shortly after. I was then a sell-side analyst, and in hindsight we should have known that we were hitting the market peak when, with impeccable timing in July 1997, we organised a very well attended high-profile investment seminar not unlike this in Kuala Lumpur, extolling our bullishness on Malaysia. Needless to say, our sessions lost hands down in competing for the attention of nervous fund managers busily unwinding their many long positions in the Asian markets!

To my mind, 10 years on, this is quite a different conference and it is clear that both macro and firm level fundamentals have significantly improved. The nation's finances and trade balances have seldom been stronger, corporate balance sheets have been greatly repaired and earnings momentum as measured by analyst consensus is at a healthy tack. Further, corporate governance practices and market regulation, have by many external measures, made major advances in the post-crisis environment while the emergence of an active, market-driven, competitive and sometimes hostile market for corporate control through mergers and acquisition also portends well for the future strength of corporations and the robustness of our capital markets.

I believe this is not a coincidence in that, in addition to the commendable efforts across the board among companies, this is also a direct outcome of a series of institutional interventions and policy enhancements through the diligent work of agencies and institutions new and old, including the Ministry of Finance, the NEAC, Bank Negara, Danaharta, Danamodal, the Corporate Debt Restructuring Committee,

the Securities Commission, Bursa Malaysia and others. Other institutional measures include the roll-out and implementation of landmark master plans and frameworks for the financial sector, capital markets, liberalisation of exchange controls, Islamic Finance and corporate governance. Regulatory efficiency has also improved with the setting up of dedicated regulatory commissions in key sectors such as multimedia and telecommunications, in energy and in highways.

When viewed against the broad sweep of the last twenty years or so, the current wave of GLC restructuring or transformation should be viewed as part of an ongoing process of corporate and micro-economic renewal that can be traced to the crisis and even pre-crisis. Indeed, our *GLC Progress Review of December 2006* had highlighted that GLCs are not a homogenous group, and can be broadly categorised under four different categories<sup>3</sup> – the Malaysianised companies mostly under the PNB Group such as Sime Darby and Guthrie, to Khazanah's corporatised companies such as Tenaga, TM and POS, restructured companies such as UEM, MRCB, MAS and Proton and Financial Institutions. While each category clearly has different antecedents and hence different emphasis in terms of actions required to increase performance, what is clear is the need to step up performance levels in view of increased market liberalisation and the rise of new competitors.

As the GLC Transformation Programme moves into Phase 3, a period covering 2007 to 2010, the program's aims are to deliver sustainable and tangible results, building on the base built over the last three years and the ongoing implementation of the 10 GLC initiatives. Emphasis will shift towards GLC-specific programs or business transformation plans (as opposed to program level initiatives) and building and institutionalising execution capabilities. Stakeholder management will remain on the critical path. Ongoing and selective regionalisation of activities will continue as emerging national champions reap the benefit of cross-border activities.

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<sup>3</sup> Refer page XIII of the GLC Progress Review, December 2006

Overall, while we continue to remind ourselves that there is clearly some way to go and that the gains are not fully broad based as yet, we are nonetheless reaching our first intermediate checkpoint of three years in fairly good shape and with a clear road map and good provision to move into the next stage.

### **The third milestone: The 50<sup>th</sup> anniversary of independence**

As the nation crosses this major milestone this year, clearly there are many important structural drivers of competitiveness that we need to collectively address and improve upon. While we are proud of what we have achieved over the last fifty years, the next fifty or even the next thirteen towards 2020 will continue to become progressively harder. It will be the subject of another day to discuss in greater detail the issues around specific drivers of long-term development including the education system, social cohesion and social capital, delivery systems, hard and soft infrastructure and so on.

In its place, I would like to describe the Iskandar Development Region or IDR, encompassing an area of some 2,200 square km at the southern-most part of Peninsular Malaysia. The IDR offers us a glimpse of what the future may hold. This bold and visionary development was from the start envisioned and driven by the YAB Prime Minister to be an outstanding example of an Asian regional metropolis of the future, showcasing sustainable development and the best of what Malaysia is, and a test-bed for what Malaysia can and should be, and also how Malaysia will continue to work profitably together with its foreign partners. This is especially timely as the IDR has many factor endowments that will allow it to benefit greatly from globalisation, while ensuring that such growth is accompanied with proper distribution and equity and a sensitive regard to the nation's rich cultural and environmental endowments.

By the time the development planning period of 20 years to 2025 is completed, the IDR is expected to receive some USD 105 billion in investments, and to have seen

GDP per capita more than double to USD 31,100 on a PPP basis and with more than 800,000 additional jobs generated.

Khazanah has been given two tasks in regard to the IDR. The first, its planning role, was completed in November 2006 after a period of 15 months, with the launch of the IDR master plan that we refer to as the Comprehensive Development Plan or CDP.

We are now in the midst of our second role in the implementation phase, assisting the Government in the setting up of the Iskandar Regional Development Authority (“IRDA”) and in driving catalyst developments through the South Johor Investment Corporation (“SJIC”). SJIC will be owned 60% by Khazanah, 20% by EPF and 20% by KPRJ, a Johor state entity, with the SJIC starting with total assets of approximately RM3.4 billion. We are pleased to report that we believe much progress has been achieved in a relatively short period of time. The last six months alone has seen the completion of master plan, the passage of the IRDA Act and the formation of IRDA, including the appointment of a distinguished advisory panel. Khazanah and later, SJIC, will continue to drive the development of strategic or catalyst projects that have the ability to generate considerable economic activity and branding for IDR. Several catalyst developments in the leisure, education and healthcare services sectors, among others, have been identified and are in various stages of negotiation and completion. Several existing private developers such as Nusajaya, Danga Bay and PTP have already seen a significant pick-up in activity and sales recently.

While much momentum has been generated, I should caution that 2007 must realistically be viewed as a mobilisation year where the key institutions of IRDA and SJIC will be in start-up mode, RMK9 projects will begin to get scoped and implemented, and several key catalyst developments will be secured. In this regard, it is important that steady and sustainable progress be made befitting of the aspirations of IDR to set new benchmarks of best practices as a showcase of a new and better nation.

### **In closing**

I have not covered a progress update of Khazanah *per se* as this will be the subject of our annual review come June 1<sup>st</sup>. Suffice to say at this stage that in line with improved GLC performance, considerable financial progress has been achieved with the Net Worth<sup>4</sup> of Khazanah's portfolio rising by some RM 23.8 billion since May 2004<sup>5</sup>. Overall, as is evident from the results to date of GLC transformation, the planning and mobilisation work on IDR and the Khazanah portfolio performance to date, we believe we are on track and have made considerable progress.

As we have covered, it is clear by any measure, that Malaysia's macro economic and capital market fundamentals are sound. At Khazanah, the GLC transformation and IDR programs meanwhile have built-up considerable momentum that will bode well for the immediate future. As we celebrate the coming together of two important anniversaries in the history of our nation and one milestone on Khazanah's journey, it is imperative to recognise that there remain many challenges. Hence in closing I would like to end with the prayer that as we continue to diligently focus on sustainable value creation, may our efforts be anchored in the right intentions and the right actions, may each one of us play our respective roles well in the proper functioning of the market place and in nation building and long may we continue to make our own luck!

Thank you

Kuala Lumpur City Centre

21st March 2007

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<sup>4</sup> Total Assets less Total Liabilities at Market Value

<sup>5</sup> As at 20<sup>th</sup> March 2007