Khazanah struggles to revamp state-backed groups

INVESTMENT COMPANIES

News analysis

The wealth fund's hands are tied by the government, say Kevin Brown and Henny Sender

Khazanah Nasional has pulled off a double surprise in recent months, scoring a crushing victory in a $3.6bn takeover battle with India's Fortis for Singapore's Parkway Holdings healthcare group and then selling 30 per cent of the restructured target to Mitsui, the Japanese trading house, for $1.1bn.

The double-pronged Parkway deal demonstrates a degree of nimble-footed aggression that few expected from Malaysia's state investment fund, better known as the custodian of the state's shareholdings in troubled government-linked companies (GLCs) such as Proton, the national carmaker.

Yet big questions remain about Khazanah's ability to deal equally decisively with the rest of its portfolio, not least because of government opposition to radical surgery on any of its significant companies.

Khazanah, which means "treasure" in Malay, has significantly less firepower than some sovereign wealth funds. Its net portfolio value of M$75bn ($24.6bn) at the end of December compares with more than S$186bn ($149bn) managed by Temasek, its Singapore counterpart.

The agency is also burdened by a complex mandate, with potentially conflicting instructions to grow the portfolio, earn significant returns, lead the government's GLC transformation programme and help Malaysia's drive to become an advanced economy by 2020.

However, Azman Mokhtar, Khazanah's managing director, argues that the agency is delivering on most of these fronts, citing an increase in the portfolio value of 39 per cent last year, with compounded annual growth of 13 per cent from its level of M$33.3bn when he took over in 2004.

"We are in the seventh year of a major transformation programme, and we have achieved a lot in terms of making the GLCs more efficient while also growing the value of our portfolio and playing our part in helping Malaysia to develop," Mr Azman, a former UBS and Salomon Smith Barney banker, tells the Financial Times.

Much of the investment has been in new economy areas such as healthcare, leisure and tourism, clean energy, life sciences and education – notably in the Iskandar development, twice the size of Singapore, being built by Khazanah in the southern Malaysian state of Johor.

At the same time, the group has sold its 32 per cent stake in Pos Malaysia, the national postal operator, reduced its holdings in successful companies such as Malaysia Airports, and strongly encouraged regional expansion by successful portfolio companies such as Axiata, the telecommunications group, and the banking group CIMB.

"The GLCs have conclusively improved their performance as a result of the management and other changes we have made, with aggregate earnings for the 20 biggest rising by 49 per cent in 2010 to M$17.3bn and total shareholder returns of 16.4 per cent since 2004," says Mr Azman.

That compares with an average annual rise of 14.5 per cent in the Kuala Lumpur Composite index over the same period. However, Khazanah's ability to turn round the biggest legacy companies is tightly bound by government limitations on its freedom of manoeuvre.

For example, Mr Azman has promised to list the healthcare division, now known as Integrated Healthcare Holdings, within three years. But ministers are reluctant to see Khazanah divest strategic companies such as Proton and Malaysian Airlines System, especially if foreign buyers are involved.

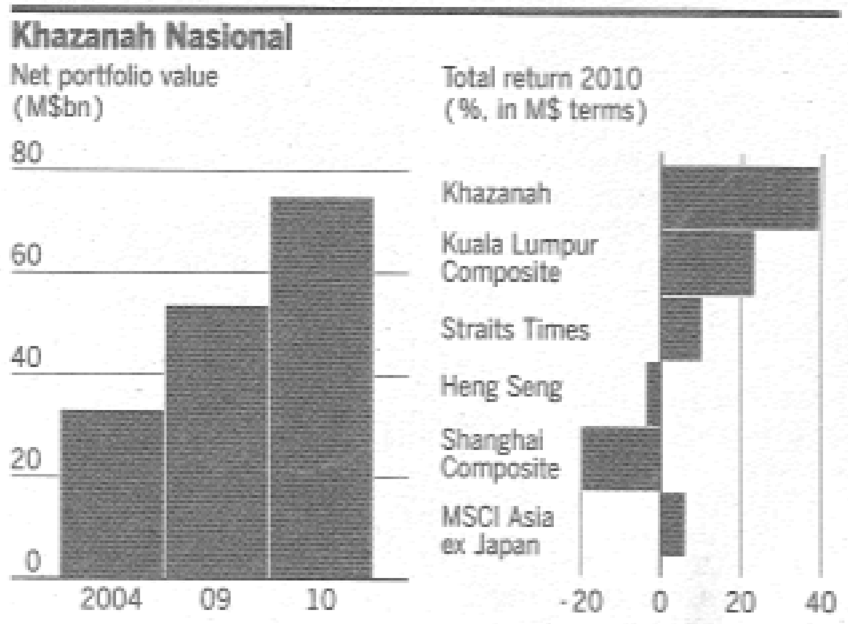
People close to the group say that Khazanah often finds itself arguing against the senior managers of its own portfolio companies, which have become adept at lobbying against change, especially when it comes to ownership. For example, airline executives have fought hard to stay within the Khazanah stable.

The impact of the political framework is clear in detailed financial information released by Khazanah this year, which shows its newer investments achieving an average annual growth in value of more than 20 per cent, while older investments are growing at only 5 per cent.

"We have had our frustrations, and there have been areas, mostly in the regulated sectors such as electricity, automobiles and aviation, where value has stagnated or even declined," Mr Azman admits.

To critics, this failure to turn round the biggest legacy companies undermines the successes Khazanah has had in other areas. "I think there are a lot of very capable and committed people in Khazanah, but there are a lot of political obstacles to real reform," says Tan Teng Boo, chief executive of Capital Dynamics, a Kuala Lumpur investment adviser.

"They may have had some growth, but they are supposed to be a transformer of the GLCs, not a portfolio manager, and they have failed miserably to do that. But it's not really their fault. It's the politicians who won't allow them to do what is necessary."



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