

Lobbying for control of Khazanah Nasional begins

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A QUESTION OF BUSINESS | Some one and half years before Azman Mokhtar steps down after a 15-year stint as managing director of Khazanah Nasional Bhd, the government's wholly-owned strategic investment fund, it looks like the daggers are drawn to poke holes in what is by and large an impressive achievement.

Unlike the other so-called strategic investment fund, the notorious 1MDB, which has already lost the country almost all the long-term money it borrowed with US\$7 billion (some RM28 billion) unaccounted for, Khazanah has been transformed since 2004 into a solid entity which has strong controls, procedures, a chain of accountability, and a team of competent professionals managing over RM145 billion in investments.

It is not only extremely ironic but the height of ridiculousness that among the names being considered as Azman's replacement is Arul Kanda Kandasamy, the chief executive of 1MDB since January 2015, who has done nothing to clarify the sad state of affairs at 1MDB or even to ensure the release of its long overdue annual report.

His appointment would make a mockery of Khazanah's much stronger governance, good board representation, greater accountability, more transparency and much better performance than 1MDB which may be too much to make even for Prime Minister Najib Razak, who if he survives the elections, will make the final decision.

The major salvo against Khazanah, as with one or two other puzzling stories (see for instance, "[Spinning 1MDB's lopsided settlement](#)"), came from across the Causeway from the *Singapore Straits Times* which made an unfair and ultimately wrong assessment of Khazanah's performance over the years since 2004.

In a report titled "Khazanah feels the heat amid push to change its investment strategy", the newspaper said: "Malaysia's sovereign wealth fund Khazanah Nasional is under pressure to show higher returns to boost government coffers, with senior state officials lobbying for changes to its management and investment strategy."

Then it went on to add: "The bulk of the government's direct business investments is managed by Khazanah, which has returned an average of just RM825 million (S\$270 million) in dividends annually over the past four years, from its RM145 billion worth of assets. This amounts to a less than 1 percent return a year between 2013 and last year.

"The *Straits Times* understands that there is a push by some within the Prime Minister Najib Razak's vast circle of advisers to change Khazanah's investment strategy, especially since the fund's managing director, Tan Sri Azman Mokhtar, is due to leave in mid-2019, after a 15-year run at the helm."

Now, anyone who has the slightest knowledge of fund management should know that dividends alone is not the way to measure a fund's return. You have to take into account the increase in the value of investments that it owns and gains from investments sold. And why choose just the period from 2013 to 2016? A fund is best assessed over a longer period.

Misleading analysis

The best way to report a fund's performance is its total return - this is accepted as the *de facto* measure of fund performance in investment analysis. This includes realised as well as unrealised gains on investments plus dividends. Khazanah calls this the net worth adjusted (NWA) value.

The other performance measure it uses is the realisable asset value (RAV), which is essentially the market value of all its investments. When you subtract the liabilities, mainly borrowings, from RAV, and make adjustments to account for dividends as well as realised investment gains through sales of investments, you obtain the NWA value.

The *Singapore Straits Times* report pointed out that the NWA value actually declined eight percent over the last two years, but failed to point out that such fluctuations are normal and happen because of market and currency fluctuations amongst others.

Unlike many other sovereign wealth funds, Khazanah has many large core holdings such as Tenaga Nasional, Telekom Malaysia, Axiata, CIMB, IHH Healthcare, etc, which it holds through good and bad times and when the market rises or falls. Market volatility plays havoc with NWA.

In 2008 for instance, in the aftermath of the world financial crisis, its NWA value tanked nearly 50% as markets collapsed but recovered by 68% and 39% respectively in the following two years, 2009 and 2010, as markets recovered. It would be wrong to think that Khazanah did badly in 2008 and well in 2009 and 2010 - the events that led to the fall and rise were beyond its control.

To prevent that kind of misleading analysis, it is common to compare fund performance over a period of time and against a set benchmark - for Khazanah that benchmark, because most of its holdings are Malaysian, would be the Kuala Lumpur stock market which is measured by the FBM KLCI index.

As Khazanah pointed out in [its retort](#) to the *Singapore Straits Times* report, its NWA value increased annually by 9.3% on a compounded basis between 2004 and 2016 which is very much in line with the FBM KLCI index growth of 9.4% over the same period. During the period the NWA value of its investments rose over two times to RM102.1 billion from RM33.3 billion, creating value of RM68.9 billion. In contrast, 1MDB destroyed nearly half of the value Khazanah created over 12 years in less than a handful of years.

That 9.3% annual compounded growth of NWA over 2004-2016 - the best measure of Khazanah's performance - was mentioned towards the end of the *Singapore Straits Times* article. And even then, the article mentioned it was lower than the performance of the broad market without actually giving the 9.4% figure.

This figure is pretty alright considering that many of Khazanah's investments have long gestation periods such as the Iskandar corridor development and others may be historically making losses, for example, Proton, Malaysia Airlines and Silterra.

Erroneous comparison

Further, the article makes an erroneous comparison between Khazanah and the Employees Provident Fund.

It said: "The fund performs poorly when compared with the country's Employees Provident Fund (EPF), which all private workers and employers must contribute to. Since Mr Azman took over Khazanah in 2004, it has returned a total of RM9 billion in dividends, which works out to an average annual return of below 1 percent of the fund size. Meanwhile, the EPF has added more than 5 percent annually to its members' retirement savings."

The EPF has a major part of its investments invested in government bonds, much of which give fixed returns over 4% per year. It supplements this by booking in realised profits from its equity trading and other businesses - it has no strategic holdings. Thus it can return close to 5% in dividends but the value of its funds don't increase as much, if you take out increased contributions from members. The correct comparison should be between the 9.3% annual return and the EPF dividend rate of 5% plus any unrealised gains.

Also, the article makes a comparison, again erroneous, comparing pre-tax profit as a percentage of total asset size with other funds. It said: "Khazanah's profit before tax - not including unrealised capital gains - also lags behind those of its peers, such as Singapore's Temasek Holdings, China Investment Corporation (CIC), Alaska Permanent Fund Corporation (APFC) and the world's largest sovereign fund, Norway's Government Pension Fund Global (GPF)."

But the key phrase there is "not including unrealised capital gains" - as a strategic investment fund, it holds stakes in sizeable companies that it does not sell off. The others play no such role and are free to take profits from their investments as and when they see fit.

Overall, the *Singapore Straits Times* article is rather unbalanced and lopsided, and looks very much like it was planted there via the provision of selective information by those who want to smear Khazanah's name and have their own agendas in terms of lobbying for some people to take over when Azman's term ends.

That article has been picked up and quoted widely among the press in Malaysia, both online and print, and has had its intended effect by those who may have planted it

there. It is however lamentable that a respected publication in terms of reporting regional affairs has been so used.

Meantime, one hopes the powers-that-be don't try to fix what isn't broken and continue to give support for Khazanah to operate conservatively and competently with proper checks, balances and accountability, unlike what has happened at 1MDB.

To do anything otherwise is to rain down more suspicion and lack of confidence on a country already beleaguered by a plethora of governance ills and all that comes with it such as market and currency weakness. We simply can't afford another fund debacle.

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