SOVEREIGN WEALTH FUNDS IN EAST ASIA

Poverty Reduction and Economic Management (PREM) Sector Unit
East Asia and Pacific Region, World Bank

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1 This paper has been prepared by a team led by Sudarshan Gooptu (Lead Economist, EASPR). The authors for Part I of this Report were Sudarshan Gooptu (Lead Economist, EASPR); Timothy Gable (Consultant, EASFP); James Seward (Senior Financial Sector Specialist, EASFP); Hiroshi Tsubota (Regional Financial Officer, EASPR). The authors for Part II of this Report were Ronald Johannes (Consultant, EASPR) and Sung-Soo Eun (Senior Economist, EASPR) and overall guidance was provided by Vikram Nehru (Sector Director, EASPR/FP). Opinions expressed in this paper are those of the authors and do not necessarily reflect the views of the World Bank, its Board of Executive Directors or any of the countries that they represent.
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PART II: Overview of Selected SWFs in Asia

... SINGAPORE: Government of Singapore Investment Corporation (GIC)
... CHINA: China Investment Corporation (CIC)
... SINGAPORE: Temasek Holdings
... BRUNEI: Brunei Investment Agency (BIA)
... MALAYSIA: Khazanah Nasional
... KOREA: Korea Investment Corporation (KIC)
... TIMOR-LESTE: Timor-Leste Petroleum Fund
... KIRIBATI: Revenue Equalization Reserve Fund
... MONGOLIA: Mongolian Development Fund

PART III: References
PART I: Emergence of Sovereign Wealth Funds in Asia

I. Introduction

The massive size, rapid growth, and high-profile investments of Sovereign Wealth Funds (SWFs) in the U.S. and elsewhere in 2007 has attracted the attention of the media, politicians, regulators, and academics over the past year. Some of the SWF investments have been viewed as market stabilizing, for instance the substantial equity investments in large U.S. financial institutions that were recently in financial trouble after the sub-prime mortgage crisis. However, there is great suspicion from many political and academic quarters that SWFs are politically motivated with many SWFs in Asia now at the center of the storm.

Although SWFs have been in existence for many decades worldwide, most SWFs in the East Asia and Pacific Region (EAP) are relatively new. The emergence of the SWFs in Asia is largely a by-product of the strong economic development at East Asian countries and the attendant accumulation of foreign exchange reserves, however, there are other types of SWFs in the region. The Governments have taken a concerted strategy to enhance the returns on these excess reserves. Thus, SWFs no longer recycle capital without economic and political disruption, as many SWFs have opted for higher returns through diversified investment portfolios instead of largely taking conservative approaches by holding only government bonds (generally U.S. Treasury bonds).

This more aggressive investment approach has generated much debate and politicians and financial officials from the U.S., United Kingdom, France, Germany and others have called for more intensive scrutiny of SWF investments. This call has come due to three primary reasons: (i) SWF investments could potentially be used to exert economic influence and to acquire strategic assets such as infrastructure and industry companies; (ii) a perceived lack of transparency of SWF operations; and (iii) seemingly opaque corporate governance structures.

The EAP region is an ideal region to take a look at the issues surrounding SWFs since Asia has the full range of funds – from long-established funds to brand new funds; from passive portfolio investors to more aggressive strategic investors; from resource-backed funds to foreign reserve-backed funds; and, based in the largest, most highly developed economies to the smallest, poorest economies in Asia. Therefore, the objective of this Report is to document the status of Sovereign Wealth Funds in the East Asia Region and to understand the implications of their rapid growth. It presents facts from publicly available sources on their size, institutional structure, and investment operations. The

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3 The universe of information on SWFs is vast, but often incomplete since there are no consensus international standards of measurement and limited transparency of disclosure by SWFs. Given the scope and resources of this report, the research was as exhaustive as possible.
survey covers all known SWFs in the EAP region, but the survey does not cover public pension funds or central banks.

II. **DEFINITION OF SWFS**

There is no commonly agreed definition of sovereign wealth funds. For the purposes of this report, a sovereign wealth fund will be defined as a long-term investment fund owned by a sovereign nation, distinct from investments by national pension funds, state-owned-enterprises and development banks, and distinct from central bank management of liquid official foreign exchange reserves. Typically, sovereign wealth funds are funded from commodity (natural resource) revenues, currency intervention, or fiscal savings.

Box 1 provides a framework for categorizing SWFs based on the underlying purpose of the funds. This framework is according to guidelines in an IMF paper entitled *Sovereign Wealth Funds – A Work Agenda*. One additional category could be added to this list, which is the “legacy” fund. The legacy fund is one in which the SWF was formed to manage the assets of the state, which were held as a legacy of past economic policies. In these cases, the SWF was established as the holding company for the Government’s shareholdings in state owned enterprises (SOEs) with a mandate to maximize shareholder value in those companies, and in some instances, fully or partially divest the state’s shareholdings. The purposes of the SWFs are inter-linked with the funding sources of SWFs. For instance, reserve investment funds are an obvious product of excess foreign currency reserve accumulation and savings and stabilization funds are largely funded by revenues from oil and gas, minerals, and other commodities.

Other definitions of SWFs vary from the simple to the abstruse. The Federal Reserve Board has referred to an SWF simply as an investment fund that is owned by a national or state government. The US Department of the Treasury considers an SWF to be a government investment vehicle which is funded by foreign exchange assets, and which manages these assets separately from official reserves. Standard Chartered Bank uses a

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**Box 1: Purposes of SWFs in East Asia and Pacific**

1. **Stabilization Fund** – meant to insulate the budget and protect against volatility in commodity prices.
2. **Savings Fund** – aims to convert nonrenewable assets into a more diversified portfolio of assets which will provide income/savings for future generations.
3. **Reserve Investment Fund** – geared towards enhancing the returns on reserve assets.
4. **Development Fund** – helps to fund projects or industrial policies that increase economic output.
5. **Contingent Pension Reserve Fund** – provides for contingent unspecified pension liabilities on government’s balance sheet.

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definition similar to what is used in this Report. Morgan Stanley defines an SWF as having five characteristics: sovereign; high foreign currency exposure; no explicit liabilities; high risk tolerance; and long investment horizon. The International Monetary Fund (IMF) defines SWFs as special investment funds created or owned by governments to hold foreign assets for long-term purposes. As mentioned above, the IMF also introduces a taxonomy of SWFs based on policy objectives: stabilization funds; savings funds; reserve investment corporations; development funds; and pension reserve funds. The Peterson Institute for International Economics refers to SWFs as separate pools of international assets owned and managed by governments to achieve a variety of economic and financial objectives. The objectives include: accumulation and management of a tranche of reserve assets, the stabilization of the macroeconomic effects of sudden increases in export earnings, the management of pension assets, or the transfer of national wealth across generations. The Institute also defines SWFs broadly as stabilization funds, renewable resource funds, and government investment holding companies.

III. THE RISE OF SWFs WORLDWIDE

The past five years has seen a massive build-up of international liquidity globally. This has important implications for emerging markets, including in East Asia and the Pacific region, both in terms of the challenges it poses for macroeconomic management, and in terms of risks it poses to their domestic economies. Since 2002, global foreign exchange reserves (including gold) have increased at an average rate of 20 percent each year. This compares to a rate of 6 percent per year, on average, that was observed during 1997-2001. According to the World Bank’s Development Finance Report 2008, foreign exchange reserves rose by $1.03 trillion in 2007, up from $634 billion in 2006 and approximately $400 billion in 2004 and 2005. Reserve holdings by all developing countries increased from 23 percent of their GDP in 2006 to 27 percent in 2007 (Figure 1). At the end of 2007, the BRICs (i.e. Brazil, Russia, China and India) held $2.4 trillion in foreign reserves, an amount equal to 5.7 times the value of principal and interest payments due in 2008, compared with 1.8 times for other developing countries. Developing countries now account for almost 60 percent of global foreign reserve holdings, up from 40 percent in 2003 (Figure 2) most of which are held in the form of US dollar- and Euro-denominated assets (60 and 28 percent respectively in end-2007 according to the Currency Composition of Official Foreign Exchange Reserves database maintained by the IMF.

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Many developing countries have recently shifted a higher proportion of their foreign currency earnings from official foreign currency reserves to sovereign wealth funds. Sovereign wealth funds have an estimated $600 billion in assets under management in developing countries, dominated by China ($200 billion held by the Chinese Investment Corporation and $68 billion held by the Central Huijin Investment Company) and Russia ($130 billion held in the Reserve Fund and $33 billion held by the Fund of Future Generations). It should be noted that this amount is small relative to the total level of reserves held by developing countries (estimated at $3.7 trillion at end 2007).

Despite the shift in assets into SWFs by developing countries, the value of assets managed by SWFs worldwide is dominated by high-income countries. The range of estimates varies considerably (between $2 trillion and $3.5 trillion), implying that sovereign wealth funds in developing countries manage around 20 to 30 percent of the total. The wide range of estimates largely stems from uncertainty about the value of assets managed by some SWFs. For instance, the Abu Dhabi Investment Authority and Corporation is estimated to manage between $250 billion and $875 billion at end 2007; Singapore’s Government Investment Corporation (GIC) manages between $100 billion to $330 billion, while its Temasek Holdings manage between $66 billion to $160 billion. The Kuwait Investment Authority allegedly managed between $160 billion to $250 billion in end-2007.11

IV. OVERVIEW OF SWFS IN ASIA

Asian countries currently account for about a quarter of the total global SWF assets. As was mentioned in Section IV above, the growth of SWFs in Asia is in fact a relatively new phenomenon which emerged as a consequence two primary economic factors. Firstly, as the large export-driven East Asian countries accumulated a large of foreign currency reserves, policy makers started evaluating the desirable level of reserves.

Secondly, the US dollar, the main reserves currency, depreciated significantly in the recent years and the returns of these reserves investments came under scrutiny. Thus, a number of SWFs were established as a tool to address these two issues.

In contrast, large development funds in the East Asia, such as Singapore’s Temasek and Malaysia’s Khazanah Nasional, were originally established in order to enhance the efficiency of managing the governments’ holdings in the domestic corporations, which were accumulated in the process of the government-led economic development. Subsequently, these funds started to invest internationally, and today these funds operate more like a commercial investment company. In addition, there are also a few funds which were established by the countries with commodity revenues, such as Brunei and Timor-Leste, which were established as saving or stabilization funds. These types of funds have relatively less need for short term income streams but rather high long-term returns with prudent levels of risk so as to support productive investment in growth-enhancing and poverty-reducing spending on essential infrastructure, agriculture, education, health and basic service delivery in their countries. However, history has shown that in some instances, these funds have actually amplified rather than mitigated the adverse effects of oil and gas windfalls.

Table 1 table below presents a typology for four different types of SWFs based on their funding source: (i) Fiscal surplus; (ii) commodity revenues – oil and gas, mining, (iii) legacy state ownership asset holding companies; and (iv) foreign currency reserves. As the Table shows, there are several large reserve investment funds and a few development funds. Reserve investment funds include the China Investment Corporation, Korea Investment Corporation, Government and Investment Corporation of Singapore (GIC) among others.

<table>
<thead>
<tr>
<th>Country</th>
<th>Name of Fund</th>
<th>Purpose15</th>
<th>Assets (USD)</th>
<th>Year of Inception</th>
<th>Source of Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>Future Fund</td>
<td>Savings Fund</td>
<td>52.3 bn</td>
<td>2004</td>
<td>Fiscal Surpluses</td>
</tr>
<tr>
<td>Brunei</td>
<td>Brunei Investment Agency</td>
<td>Stabilization Fund</td>
<td>30 bn</td>
<td>1983</td>
<td>Commodity – Oil and Gas</td>
</tr>
<tr>
<td>China</td>
<td>China Investment Corporation</td>
<td>Reserve Investment Fund / Development Fund</td>
<td>200 bn</td>
<td>2007</td>
<td>Foreign Reserves / Legacy State Ownership</td>
</tr>
</tbody>
</table>

12 For example, Temasek does not regard itself as a sovereign wealth fund.
13 Timor-Leste’s Petroleum Fund can be seen as a saving fund as well as stabilization fund considering the country’s still fragile economic conditions,
15 It should be noted that SWFs will have multiple or vague purposes which are subjective. Purposes of SWFs also change. To the extent that information is available and for the purposes of this, SWFs are categorized by their primary intent.
<table>
<thead>
<tr>
<th>Country</th>
<th>Fund Name</th>
<th>Fund Type</th>
<th>Size</th>
<th>Year</th>
<th>Source of Funds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hong Kong</td>
<td>Hong Kong Monetary Authority Investment Portfolio</td>
<td>Reserve Investment Fund</td>
<td>163 bn</td>
<td>1993</td>
<td>Foreign Reserves</td>
</tr>
<tr>
<td>Kiribati</td>
<td>Revenue Equalization Reserve Fund</td>
<td>Stabilization Fund</td>
<td>470 m</td>
<td>1956</td>
<td>Commodity revenues – Phosphates</td>
</tr>
<tr>
<td>Korea</td>
<td>Korea Investment Corporation</td>
<td>Reserve Investment Fund</td>
<td>20 bn</td>
<td>2005</td>
<td>Foreign Reserves</td>
</tr>
<tr>
<td>Malaysia</td>
<td>Khazanah Nasional</td>
<td>Development Fund</td>
<td>15 bn</td>
<td>1993</td>
<td>Legacy State Ownership</td>
</tr>
<tr>
<td>Mongolia</td>
<td>National Development Fund</td>
<td>Development Fund</td>
<td>0.011-0.020 bn</td>
<td>2007</td>
<td>Mineral windfall revenues</td>
</tr>
<tr>
<td>Nauru</td>
<td>Phosphate Royalties Trust Fund</td>
<td>Stabilization Fund</td>
<td>70 m</td>
<td>1968</td>
<td>Commodity revenues – Phosphates</td>
</tr>
<tr>
<td>New Zealand</td>
<td>Superannuation Fund</td>
<td>Savings Fund</td>
<td>13.8 bn</td>
<td>2003</td>
<td>Fiscal Surpluses</td>
</tr>
<tr>
<td>Singapore</td>
<td>Temasek Holdings</td>
<td>Development Fund</td>
<td>100 bn</td>
<td>1974</td>
<td>Legacy State Ownership</td>
</tr>
<tr>
<td>Taiwan</td>
<td>Taiwan Stabilization Fund</td>
<td>Reserve Investment Fund</td>
<td>15 bn</td>
<td>2000</td>
<td>Foreign Reserves</td>
</tr>
<tr>
<td>Timor-Leste</td>
<td>Timor-Leste Petroleum Fund</td>
<td>Stabilization Fund</td>
<td>1 bn</td>
<td>2005</td>
<td>Commodity revenues – Oil and Gas</td>
</tr>
<tr>
<td>Vietnam</td>
<td>State Capital Investment Corporation</td>
<td>Development Fund</td>
<td>2 bn</td>
<td>2005</td>
<td>Legacy State Ownership</td>
</tr>
</tbody>
</table>

Source: Compiled by authors from various published sources.

V. INVESTMENT APPROACHES OF SWFS IN ASIA

The largest and most visible East Asian SWFs are, as described above, reserve investment funds. The underlying logic of establishing these SWFs is that these EAP countries have excess foreign currency reserves which will not be needed for a foreseeable future, and such excess reserves can be invested more aggressively to enhance returns. Conceptually, by slicing the foreign currency reserves into tranches according to the likelihood of being needed for central bank operations, the excess reserves which are not likely to be liquidated for a foreseeable future are treated as if they were equities. Being freed from the need for maintaining liquidity and stable nominal market value, these SWFs seek returns more aggressively for the excess reserves by investing them also in riskier assets with a longer investment horizon (Chart 1 below).

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16 This approach is akin to tranching techniques for securitized products, such as Collateralized Debt Obligations (CDOs).
Chart 1: Conceptual Framework of Reserve Investment SWFs

<table>
<thead>
<tr>
<th>Investments</th>
<th>Foreign currency reserves</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>SWFs</strong></td>
<td>“Excess” reserves</td>
</tr>
<tr>
<td>High risk – high return and illiquid assets, such as equities and alternative investments</td>
<td>(Will not be liquidated for a foreseeable future)</td>
</tr>
<tr>
<td>Central bank reserves investments – High-grade fixed income assets</td>
<td>Foreign currency reserves for central bank operations (may need to be liquidated)</td>
</tr>
</tbody>
</table>

Source: Compiled by authors from various published sources.

However, discussions on the desirable level of foreign currency reserves remained in the domain of rules of thumb such as Guidotti-Greenspan rule, as there is no reliable analytical method to determine the appropriate reserve levels today. Based on these commonly used rules of thumb, the East Asian countries with SWFs set their SWFs’ asset volumes at conservative levels (see Table 2 below).

Table 2: “Excess Reserves” and Assets Under Management of East Asian SWFs

<table>
<thead>
<tr>
<th>Country</th>
<th>Volume of FX reserves (in USD bn)</th>
<th>Volume of excess reserves based on Guidotti Rule (in USD bn)</th>
<th>Volume of excess reserves based on 6-month import cover (in USD bn)</th>
<th>AUM of SWFs (in USD bn)</th>
<th>AUM of SWFs/Excess reserve (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>1081</td>
<td>897</td>
<td>618</td>
<td>200</td>
<td>22-32%</td>
</tr>
<tr>
<td>Korea</td>
<td>239</td>
<td>128</td>
<td>83</td>
<td>20</td>
<td>15-24%</td>
</tr>
<tr>
<td>Singapore</td>
<td>136</td>
<td>6</td>
<td>1</td>
<td>430</td>
<td>316%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>83</td>
<td>54</td>
<td>13</td>
<td>25</td>
<td>46-192%</td>
</tr>
<tr>
<td>Thailand</td>
<td>67</td>
<td>50</td>
<td>-6</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Philippines</td>
<td>23</td>
<td>9</td>
<td>-6</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Indonesia</td>
<td>43</td>
<td>20</td>
<td>2</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Vietnam</td>
<td>13</td>
<td>5</td>
<td>1</td>
<td>2</td>
<td>15%</td>
</tr>
</tbody>
</table>

1 Volume of Foreign Exchange reserves is sourced from World Development Indicators and Global Development Finance Database
2 Short-term external debt for Guidotti Rule for Singapore is sourced from the Joint BIS/World Bank Database "Joint External Debt Hub". Imports for Singapore are sourced from World Development Indicators and Global Development Finance Database. Assets under foreign currency reserves and debt service payments for next 12 months, 2) import coverage (the ratio of foreign currency reserves and import bills for 6 months and 3) the ratio of foreign currency reserves and the broad money (M2).
unexpectedly, the SWFs would likely instead pursue asset allocation and investment strategies that are closer to those of traditional reserves management by central banks, defeating the purpose of establishing them in the first place.

V.1 Sources of Funding and Nature of Liabilities

Looking at the source of funding, the SWFs in the EAP can be divided into the ones that are funded through the revenue from sales of commodities, such as the Timor-Leste Petroleum Fund, Brunei Investment Agency, and Kiribati Revenue Equalization Fund, or non-commodity funds which are more common to East Asia and Pacific. For these SWFs funded with commodity revenues, the nature of their liabilities depends on the economic and fiscal conditions of each country. The SWFs of wealthier countries with strong fiscal positions would serve more as savings funds, which allows them to treat the funds as equity, may be invested aggressively to enhance long-term real returns. In contrast, the SWFs of the countries with fragile economy or unstable fiscal positions would serve more as stability funds, which require them to treat the funds as temporary resources. Consequently, as these temporary funds would need to maintain a high level of liquidity and nominal value.

The source the non-commodity funds also deserves a closer look. The East Asian countries with SWFs are all large exporters that have accumulated large foreign exchange reserves. These countries generally conducted foreign exchange intervention operations, often in form of sterilized interventions. They also typically have relatively small external debts. This means, their foreign currency reserves are funded largely by broad money and domestic debts; and their liabilities are mostly in denominated in domestic currencies and may be better measured in real terms.18 In case of China Investment Corporation, the funds are sourced by the Government’s domestic debt issuance, which made the source and cost of the funds very explicit. The Ministry of Finance issued a number of tranches of special 10-15 year treasury bonds, totaling approximately US$200 billion, to buy the foreign currency from the US$1.4 trillion in foreign exchange reserves (at rates ranging between 4.3% – 4.68%) and then injected the funds into the CIC.19 By doing so, the CIC has an implicit nominal hurdle rate, which is the sum of ca. 4.5% plus appreciation (or minus depreciation) of RMB.

V.2 Investment Objectives and Approaches

The common features of SWFs in terms of investment objectives are to earn superior returns in a risk controlled manner over a long investment horizon. However, they typically do not elaborate much further, providing little information in terms of investment styles, benchmarks, or asset allocations. However, it appears that the East Asian SWFs can be broadly classified into two categories; balanced funds which aim to

18 These domestic liabilities are a part of the country’s fiscal and monetary policies. The part funded with debts must be repaid with the future fiscal surplus, and the rest is effectively financed by seigniorage.
19 In the case of the CIC, the complexities are compounded by the fact that the liabilities are in local currency, but over one-third of the investments are in foreign currency, thus requiring a higher level of currency risk management processes in place.
earn real rate of returns, are benchmarked to inflation indexes, and quasi “private equity funds,” which focus on strategic investments aimed at earning absolute returns in nominal terms. The GIC and KIC can be classified in the first category and Temasek and Khazanah in the latter.

In case of GIC, its investment objective is to achieve a real rate of return over and above the G3 inflation rate over a long-term horizon.\textsuperscript{20} Korea Investment Corporation appears to pursue a similar investment objective. Despite a few widely publicized strategic investments by SWFs, this type of SWF typically maintains balanced and diversified portfolios. For example, the GIC invested $6.88 billion in Citigroup and $9.75 billion in UBS, however such investments are relatively small in comparison with their reportedly $330 billion of assets under management. As the GIC aims to earn a real rate of return over the G3 inflation rate, it would by default force the GIC to maintain a balanced portfolio, which consists of the sub-portfolios with investments in diverse asset classes. KIC would presumably follow a similar investment approach. Overall, their investments are well diversified in terms of asset classes as well as geography, to allow them to meet their investment objectives.

The investment approach of Singapore’s Temasek Holdings and Malaysia’s Khazanah Nasional resemble that of a private equity fund. Despite their holdings being concentrated in equities in terms of asset class, they also diversify their holdings, avoiding any concentration in a single company or industry. However, in terms of geographical distribution, they are significantly exposed to their home markets, as well as to the Asia-Pacific region. While these institutions operate on a commercial basis today, these institutions are established as a tool to pursue national economic development policies. In that sense, it is fully consistent that they allocated a large volume of funds to the home market. Furthermore, considering that they focus on strategic investments, it is crucial for them to have comparative advantage in analyzing the local market conditions and specific investee companies. This will also support their home market bias. Box 2 below provides three examples of Asian SWF investment approaches and allocations.

The China Investment Corporation may be seen as a hybrid between a reserve fund like the GIC or KIC and that of a private equity fund. Its current investment portfolio resembles more of that of private equity fund and indeed even less diversified than that of a typical private equity fund. The CIC has a large exposure to a few local banks, and some minority stakes in Morgan Stanley and Blackstone, but approximately two-thirds of their assets are investments in domestic financial institutions (the big state commercial banks). This is largely a legacy of state ownership in the financial sector as the state shareholdings were transferred into the CIC when it was created. For one reason, unlike.

Box 2: Investment Approaches and Allocations

Most Sovereign Wealth Funds have not fully disclosed their investment strategies, activities, and allocations. However, the three examples in this box provide some indications.

**Temasek Holdings** is more or less the Government of Singapore’s investment holding company that now has assets of US$100 billion. It was originally setup to run the strategic investments of the government in order to avoid conflict of interest that may arise from the government pursuit of commercial returns versus public interest role of policy and market regulations. It currently has the mandate to own and manage its assets on a commercial basis. As an active shareholder with a flexible time horizon, Temasek influences the management of the companies in its portfolio. Approximately 60 to 70 percent of Temasek’s portfolio in recent years included investments where the total equity stake exceeded 20 percent. Temasek invests in a wide array of sectors, asset classes and markets. The portfolio is geographically allocated: 38% in Singapore, 40% in the rest of Asia, 20% in OECD countries, and 2% in other markets. Sector exposures are as follows: 38% in Banking and Financial Services, 12% in Transportation and Logistics, 6% in Infrastructure, 9% in Real Estate, 23% in Telecommunications and Media, 2% in Bioscience and Healthcare, 1% in Consumer and Lifestyles, 6% in Energy and Resources, 2% in Technology, and 3% in Others.

**New Zealand Superannuation Fund** was created to assist future governments in meeting the cost of providing retirement income. Established in 2003 the Superannuation Fund has reached US$ 13.8 billion using a blend of passive and active investor practices and well-diversified portfolio management. Investments range from currency, asset classes and alternative investments. The Superannuation Fund also makes use of External Fund Managers. The current tactical asset allocation consists of: New Zealand equities at 7.5%, Global Small Cap equities at 7.5%, Global Large Cap Equities at 42.5%, Emerging Market Equities at 2.5%, Property at 7%, Private Markets at 8%, Commodities at 5%, and Fixed Interest and Cash at 20%. The long-term strategic asset allocation is very similar except for current overexposure in Global Large Cap Equities and Fixed Interest and Cash which are 34.5% and 15% respectively. This is at the expense of Private Markets which have a 20% percent allocation in the long-term strategic asset allocation and only 8% in the tactical allocation. Over the long-term the Superannuation fund aims to hold 83% of its assets in NZD and the remaining 17% in foreign currency.

**Hong Kong Monetary Authority Investment Portfolio** is managed under two distinct portfolios. The Backing Portfolio provides full support to the currency board arrangements and passively holds liquid USD denominated assets. The Investment Portfolio is somewhat more actively managed in OECD bond and equity markets with the explicit goal of preserving long-term purchasing power. Although specific holdings and positions are not revealed the Hong Kong Monetary Authority Investment Portfolio bond-to-equity ratio is 77 to 23 percent and currency mix is 88 percent USD to 12 percent in other unspecified foreign currencies. External fund managers are used for approximately one third of all assets including all equity positions. Hong Kong Monetary Authority staff manages entire Backing Portfolio, all currencies and major fixed income positions.

Source: Compiled by authors from various published sources.
Singapore or Korea, China has a large development need and absorption capacity for these investments. Considering that China’s foreign currency reserves are funded by liabilities denominated in domestic currency, it may also argue for local currency investments in terms of asset-liability-management. However, this will call for strong policy coordination among the central bank, the Ministry of Finance, CIC and other relevant institutions, as a large volume of inward application of funds may affect monetary and fiscal policies and the concentration to the financial sector does not seem to be consistent with its investment objectives.

One other aspect of the investment approach that has emerged in SWFs worldwide, and in the SWFs of the EAP region, is the setting of limitations on the maximum shares held in a single company and forgoing voting rights in investments. This approach has been taken by some SWFs to mitigate concerns that the funds are seeking a controlling stake in target companies and to ensure host country regulators and politicians that the SWF investments are long-term, commercial shareholdings. The most prominent example of this in the EAP region is the China Investment Corporation, which has stated that it has limited its investments to a minority stake (less than 10 percent) with non-voting rights.\(^{21}\) The New Zealand Superannuation Fund does set investment limits in their Investment Guidelines and the investment policy states explicitly that “the Fund will not own any business outright.”\(^{22}\) Although the limits are not specified, the fund is highly diversified and does not have any disclosed significant holdings that are more than about US$92 million, or 1% of the total value of the fund. However, many SWFs are not following this approach for various reasons and will not likely do so in the future. For example, the Australia Future Fund does not have any such limitations to share ownership and has an explicit policy of exercising voting rights with all of its investments as its investment policy states that “the Board recognizes the strong link between good corporate governance and investment value and that the exercise of voting rights allows the Board to influence a company’s approach to corporate governance. The Board applies this view across both its Australian and international holdings.”\(^{23}\) The Korea Investment Corporation also follows this model and its investment policy states that “KIC shall exercise the voting rights attached to the investment assets and the rights relating to class actions or other litigations as mandated by clients.”\(^{24}\)

Given the relative paucity of information on the investment strategies and approaches of SWFs in Asia, it will be necessary for these SWFs to make a clearer statement on their investment style, as well as to provide more precise information on asset allocations, benchmarks and performance. While the SWFs may have valid arguments for keeping

\(^{21}\) According to the financial press, in May 2007 the CIC made its first investment in a 9.4％ non-voting share valued at US$3 billion in the US private equity firm the Blackstone Group, and in December 2007 the CIC invested US$5 billion for a 9.9％ stake in Morgan Stanley.


the details of their holdings or short-term investment performance confidential, their investment objectives and activities call for a more information to determine if SWFs are contributing to the Government’s overall economic policy implementation.

V.3 Socially Responsible Investing

Another emerging element of SWF investing has been the adoption of codes of ethics and pursuing socially responsible investments (SRI). Some SWFs in the EAP region are following this SRI approach. For instance, the newest SWF in the EAP region, the China Investment Corporation, has stated that it will avoid politically controversial and polluting industries, for example arms manufacturing, tobacco, and gambling companies. Additionally, SWFs use principles such as those of the Korean Investment Corporation and New Zealand Superannuation Fund that both have explicit policies to invest in companies that uphold certain standards in governance, environment and social issues as well as the avoidance of political impropriety. The New Zealand Fund’s policies are very detailed and uphold a variety of investment principles on human rights, labor standards, anti-corruption, and the environment, and as with other types of SRI, there is a negative list of investments that violate this criterion. Both of these funds also have specific ethical codes for the management and staff of the SWF, and the KIC’s Code of Ethics and Code of Conduct are very detailed and explicit on the issues. The basic idea behind these types of policies is to improve the international reputation of these SWFs and reassure their domestic constituencies that they are managing the public’s funds responsibly and in a way that is not harmful to the environment and other industries that are potentially dangerous to humans.

V.4 Use of External Fund Managers

SWFs do not release much information on their investment activities, and they also do not disclose much information on the use of external fund managers. Of all the SWFs in East Asia and Pacific researched for this report, only four reported using external fund managers and what percentage of the portfolio designated to their supervision. These were: (1) New Zealand Superannuation Fund at 100 percent, (2) Brunei Investment Agency at 60 percent of assets, (3) Hong Kong Monetary Investment Portfolio at 33 percent of assets, and (4) Korea Investment Corporation at 75 percent of assets. SWFs with balanced portfolios are likely to determine the asset allocation and mandate the

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28 The New Zealand fund does not specify the percentage of assets managed by external managers, only that 41 asset management mandates have been given by the fund since 2003 and that the fund appoints external managers and that it is “not involved in individual investment decisions as to which shares or bonds are in a portfolio” (http://www.nzsuperfund.co.nz/index.asp?pageID=2145846741).
external fund managers to manage the sub-portfolios in each asset class. However, it is unknown if the East Asian SWFs today have institutional capacity to determine the appropriate asset allocation for their funds or to evaluate the performance of the fund-managers. Presumably, established ones like GIC would have strong institutional capacities, but others may need focused efforts to build in-house capacity to use the external managers effectively.

V.5 Investment Performance of SWFs in Asia

Some East Asian SWFs disclose sample of past medium-term investment returns. However, such figures do not provide much information on their performance as they do not provide any information on the risks they took to realize these returns. While established SWFs in the EAP region are reputed to have performed well, we can only speculate given there is no reliable information on their performance. However, there are a few good exceptions. The Timor-Leste Petroleum Fund reports that as of the year end 2006, it earned a profit of US$48.3 million from a portfolio mostly in liquid U.S. Treasury Notes. Earnings were measured against the 1-5 year Merrill Lynch Government Bond Index with the initial goal of return within 25 basis points while maintaining the modified duration of the investment portfolio.\textsuperscript{29} Australia Future Fund and New Zealand Superannuation Fund also provide detailed information on their investment performance. Box 3 below provides an example of some indicative performance results from the same three SWFs in the EAP region as outlined in Box 2.

VI. CORPORATE GOVERNANCE OF SWFs IN ASIA

Most SWFs in East Asia and Pacific appear to have a straightforward legal status though a legislative act or ordinance. However, such legal structures do not necessarily flow through to the effectivenes of their operational independence. Although operational independence is an assumed fact due to the legal foundations of the SWFs, in practice, operational independence can be obscured by a lack of transparency on the decision-making processes and actual fund performance. In principle, there is a clear separation of responsibility between the governmental authority (usually the Central Bank or Ministry of Finance), which provides oversight and supervision of the SWF, and the daily operations which are left to the management of the SWF. The SWF management is then held accountable for the performance of the fund. More often than not the separation of responsibilities is elaborated in the Articles of Agreement of the SWF (as is the case with

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**Box 3: Investment Performance and Benchmarks**

There is a lack of international standards concerning performance reporting for Sovereign Wealth Funds. Thus, there is little reliable information on the benchmarks and actual performance of SWFs. However, the three examples below provide some indication.

**Temasek Holdings** reported 18 percent growth in market value on a compounded basis from inception in 1974 to 2006. In terms of its assets under management, its portfolio grew from US$ 170 million to US$ 64 billion during the same time period. In spite of the lack of reliability and transparency in performance reporting, there is some industry consensus that Temasek has been a successful investor. Most recently, the portfolio of Temasek increased over 35 percent over the year end March 2007, yet only reported a 27 percent shareholder returns. This suggests that some of these returns were kept as retained earnings. This is compared to year end March 2006 when shareholder returns were 24 percent. Temasek does not report a specific performance benchmark.

**New Zealand Superannuation Fund** expects a performance of at least 2.5 percent greater than the risk-free rate over a 20 year rolling period. From its inception to year end June 30, 2007, the Superannuation Fund returned 11.32 percent per annum versus 6.7 percent per annum portfolio benchmark. It has since lost NZD 860 million due to the recent downturn in financial markets. When looking at risks and returns the Superannuation Fund uses the industry accepted benchmark that corresponds with a respective asset class. When using External Fund Managers, the returns are measured over a 1 to 5 year rolling period that focus on the information ratio in public markets and absolute returns in private markets. The Superannuation Fund has also decoupled active and passive management since investments began in September of 2003.

**Hong Kong Monetary Authority Investment Portfolio** returns have not been decoupled from those of the larger Exchange Fund. However, the Exchange Fund returned 11.8 percent compared to 10.6 percent return of the portfolio benchmark in 2007. It earned a gross investment income of HKD 142.2 billion in 2007 of which HKD 55.8 was attributed to Hong Kong Equities, HKD 6.7 billion from foreign equities and HKD 18.7 from a foreign currency revaluation. From 1999-2007 annualized returns were 6.8 percent compared to the portfolio benchmark returns of 5.6 percent. The annual report broadly mentions attribution analysis as a tool for assessing returns. Risk is likewise measured in terms of market risk both in normal and adverse market conditions.

**Source:** Compiled by authors from various published sources.
the Pacific Island Countries\textsuperscript{30} and the Articles may or may not be disclosed to the public. This set-up appears to be most strictly applied in the case of savings funds, such as the Australian Future Fund and New Zealand Superannuation Fund.

However, in many SWFs across Asia, the separation of responsibilities is unclear between the governmental authority and SWF management in terms of operations and oversight. The Brunei Investment Agency (BIA) and Temasek Holdings of Singapore offer two different examples as to how the lines responsibilities are ambiguous. Temasek Holdings seems to have a clear delineation of responsibility with an experienced management team, a supervisory board of directors and oversight by the Ministry of Finance. However, the president of Singapore has an independent an executive clause in the Fifth Companies Act – safeguard critical assets and reserves of Singapore. The Brunei Investment Agency has put in place a vague set of bylaws setting forth delegation of responsibility. However, many bylaws are attached with the caveat such as that in the Powers, Duties and Functions of Agency section, “…there shall be vested in the agency such other functions, duties and powers as His Majesty may, from time to time, by notification of Government Gazette, specify.”\textsuperscript{31} This statement appears to give the Sultan, the ruler of Brunei Darussalam, ultimate responsibility and discretion regarding activities of the Brunei Investment Agency.

\section*{VI.1 Governance Structures}

SWFs in East Asia and Pacific have largely followed common global standards for corporate structures. Although there are no international standards for the corporate governance of SWFs, the International Monetary Fund, along with a number of SWFs, worked to establish such standards and many other organizations have taken various initiatives in this regard.\textsuperscript{32} Box 4 below summarizes the new “Generally Accepted Principles and Practices for SWFs” that sets forth the new standards for the governance of SWFs worldwide.

\begin{boxedminipage}{\textwidth}
\textbf{Box 4: “Santiago Principles” on Sovereign Wealth Funds}

The investments and operations of SWFs have many potential global economic benefits. For instance, SWFs improve the management of public finances and macroeconomic policy of their home country, and bring stability to global financial markets, using a long-term investment horizon, liquidity and risk. In order to capture these benefits, and avoid protectionist sentiment amongst countries, a blueprint based on a mutual understanding of best practices needed to be put forth to the global community.

In October of 2008 the International Working Group of Sovereign Wealth Funds (IWG) created the Generally Accepted Principles and Practices for SWFs, known as the Santiago Principles”, to establish a


\textsuperscript{32} For more on this debate, see: Seward, James, “Should there be common standards for Sovereign Wealth Funds in Asia?,” World Bank East Asia and Pacific Region Blog, February 26, 2008, \url{http://eapblog.worldbank.org/content/should-there-be-common-standards-for-sovereign-wealth-funds-in-asia}. 
\end{boxedminipage}
framework that defined suitable governance structures, accountability practices and criterion for commercial based investment policies. To encourage further understanding of SWF and build trust between governments, investors and regulators, the objectives behind the Santiago Principles are: 1) to maintain global financial stability and free flow of capital, 2) to abide by regulatory requirements in countries with investments, 3) to invest based on financial risk and return and 4) to instill governance mechanisms that provide for risk management, operational procedures and transparency.

The Santiago Principles are voluntary and non-binding for members of the IWG and are subject to host and home country laws and intergovernmental agreements. Although the principles represent a standard of best practices of existing and future SWFs, the principles are meant to be applied as needed for SWFs. In general, the twenty-two principles of the Santiago Principles address key areas of SWFs, including legal framework, coordination with greater macroeconomic policies, institutional framework and investment disclosure practices.

Regarding the East Asia and Pacific region, only five countries, and thus only seven SWFs, took part in the twenty-six IMF member country discussions of the IWG. These countries include: Australia, China, Korea, New Zealand, Singapore and Timor-Leste. While this captures many of the SWFs in the region, it means that other countries, such as Brunei, Malaysia and Taiwan, Mongolia, Vietnam and Pacific Island countries, with SWFs did not participate, and may have less incentive and information to partake in the Santiago Principles. While these principles are a good first step, there is likely to be more discussion and implementation to promote standard, regulation and transparency for SWFs if they are to continue to undertake cross-border transactions. The results of this remain to be seen.


A complete list of the principles is available at http://www.iwg-swf.org/

The responsibilities of the Board of Directors for SWFs in the EAP region are generally threefold: (1) supervisory role through the use of committees, (2) decision-making regarding investment strategy and operations, and (3) liaising with a governmental authority, i.e. Central Bank or Ministry of Finance. The Board of Directors of these SWFs generally also has a committee structure with standard committee functions such as Executive, Investment, Remuneration and Audit. Investment committees oversee SWF performance, discuss overall risk profile, and evaluate new asset classes review portfolio strategies. The Korean Investment Corporation goes so far as to divide the investment committee into sub-committees such as the Investment Strategy Team, Equity Investment Team, Fixed Income Team, Alternative Investment Team and External Fund Management Team. Executive committees - which in most cases include the Chief Executive Officer – make general recommendations to the Board and provide the overall strategy and performance of the SWF. To oversee human resources and compensation issues, Remuneration committees are often established. The other responsibilities are integrated into the review and oversight process of the Board of Directors. The broad investment objectives are then given downstream to the Board of Management with oversight by the Board of Directors.

Members of the Board of Directors are usually a mixture of experienced private sector executives and influential public sector figures. Positions are selected either by official appointment, elected through internal voting, or based on de facto membership as an executive director. In the case of the China Investment Corporation, there is an eleven member Board consisting of ten appointees with the eleventh elected internally by
employees. The members range in background from Lin Jiwei, a former Minister of Finance for China and of its most able fund managers, to Gao Xiping, a current executive director to Fu Ziyi, the current Assistant Minister of Commerce.33

The management structure of SWFs in the EAP region is largely based on the functions of designated business units and nature of the SWF investments. For example, in the Australia Future Fund, there are five business units that consist of: (1) investment strategy, (2) investment operations, (3) finance, (4) corporate services, and (5) corporate support. Conversely, the China Investment Corporation is divided into three bodies with different investment objectives: (1) Central Huijin Investment Company is responsible for CIC investments in domestic financial institutions, (2) China Jianyin Investments manages the non-performing loans and assets; and (3) a newly created department to oversee external investments. The extent and variation of the management structure depends on the institutional capacity and objectives of the SWF.

In East Asia and Pacific SWFs, it is typical that each business unit that appoints an executive director – such as Chief Investment Officer or Chief Financial Officer - who reports up the hierarchy to a managing director to a Chief Executive Officer. An example of this is spelled out in the Articles of Agreement of the Timor-Leste Petroleum Corporation.34 Conversely, in the case of Brunei, the Managing Director is also the Permanent Secretary of the Ministry of Finance, blurring the separation of responsibilities. While these seems simple enough, much of the decision-making and information channels are more obscured.

On this same note, critics have openly questioned the management capabilities of SWFs, particularly in emerging economies. In some cases this may be true as the SWFs may not have the same ability to compensate management and staff at levels seen in competing private sector institutions. Thus, some SWFs, especially the newer funds such as the China Investment Corporation, have expressed legitimate concerns over their own ability to pursue active investment strategies due to human resource constraints. However, many SWFs in Asia do possess very qualified management and staff. An example is Azman bin Hj. Mokhtar, the Chief Executive Officer of Khazanah Nasional in Malaysia. Prior to this position, he was head of research at both Salomon Smith Barney and UBS in Malaysia.35

VI.2 Conflict of Interest and Fiduciary Responsibilities

Given the nature of SWFs, it is essential that they engender public trust, safeguard against potential mismanagement of assets, and are accountable for their performance. Policies dealing with conflicts of interest and fiduciary responsibility are meant to preserve these qualities. SWFs in East Asia and Pacific offer not only a unique snapshot of approaches meant to solve conflict of interest and fiduciary issues, but also provide some striking

examples of why such policies are necessary. In its simplest form, conflicts of interest are solved with a code of conduct policy that outlines decision-making mechanisms and channels the exchange of information. This is done by the Australia Future Fund, New Zealand Superannuation Fund, and Hong Kong Monetary Authority Investment Portfolio. The internal checks and balances provided by the corporate governance structures also strengthen such conflict of interest policies. Fiduciary responsibility is preserved with a combination of adhering to the SWF’s purpose, appropriate fiscal treatment and effective withdrawal rules. The risks of problems appear to be greatest with commodity funds where there is no real liability for the funds, but these are far less prevalent in East Asia and Pacific region than other regions. Box 5 on Brunei provides a striking example where the combination of weak internal controls, a lack of transparency and public accountability, and limitations in the corporate governance of the SWF led to fiduciary mismanagement and the loss of SWF funds.

**Box 5: Brunei Investment Agency Scandal**

The national wealth of Brunei is intertwined with that of the royal family given the discretionary role of the Sultan in the oversight and operations of the Brunei Investment Agency (BIA), including authority over the appointment of the managers of the BIA. The accounting and reporting regime governing the BIA is also very limited (more on this in the following sections of this Chapter).

In 1998, the combination of great discretionary authority and a lack of transparency became a problem when Amedeo – Brunei’s biggest conglomerate – came under international scrutiny because it was reported that it had collapsed, leaving $16 billion in bad debts. These were essentially deducted from the coffers of the Brunei Investment Agency. The assets were under the supervision of Prince Muda Haji Jefri Bolkiah, who was both the Finance Minister and Head of the Brunei Investment Agency, and most notably was appointed to these positions by his elder brother, the Sultan of Brunei.

Relieved of his titles, Prince Jefri fled the country whereby the Sultan filed a lawsuit accusing his brother of squandering over USD $40 billion in state funds. In the ensuing trial and investigation, news reports indicated that Prince Jefri not only had many failed business investments, but also spent USD $2.75 billion over a ten year period on trophy investments for personal use.

It is significant that the Sultan chose to use legal institutions to publicly seek restitution. However, this method was used only after private negotiations failed. After a countersuit filed by Prince Jefri, an out-of-court settlement was reached in which the Sultan announced that Prince Jefri would return all of the assets he had taken from the Brunei Investment Agency. The exact terms of the settlement were not publicly released.

*Source: Gunn 2008.*

Fiduciary responsibility also seems to improve when the returns of the SWF are integrated into the fiscal framework. Of the SWFs in East and Pacific region, ten disclosed the fiscal treatment, but not in great detail in most cases. Of these ten SWF, five integrated the receipts of the SWF into a broader fiscal framework – Australia, New Zealand, Timor-Leste and Taiwan. However, it should be noted that these are Savings or Stabilization Funds. With the exception of Taiwan, the remaining SWFs that were integrated into a fiscal framework also three of the six highest ranking SWFs on the Transparency and Accountability Scorecard of SWF released by the Peterson Institute for
More specifically, the Australia Future Fund has passed a Freedom of Information Act that requires the SWF to release financial transactions, savings and returns of the SWF to the public. In Norway, which is seen by many observers to be a “best practice” example of a SWF, the returns from its SWF, the Government Pension Fund Global, are not transferred into the budget until it is balanced which is then measured to see the actual amount of assets accumulated by the State. This could offer a model for SWFs East Asia and Pacific. To help encourage sound fiduciary responsibility in the Timor-Leste Petroleum Fund the returns are earmarked to fund the non-oil revenue portion of the budget.

Though withdrawal rules are different than integrating a SWF into a fiscal budget, it still encourages fiduciary responsibility and deters frivolous use of resources. Given the limits of available information – or perhaps narrowly used practice – the Pacific Island Countries are the best example of the use of withdrawal rules. These basically regulate when and how SWFs can be used, mostly in coordination with fiscal policy. In countries like Kiribati, Timor-Leste and Papua New Guinea withdrawal rules are anchored in the principle of sustainable income over the long-term. For Timor-Leste, sustainability and withdrawal rules are measured against a non-oil budget deficit; whereas in Kiribati withdrawal is linked to the drawdown period of the SWF. This provides an expectation as to how and why assets should be used. If flexibility is needed in the event of stabilization or other crises, permission is granted through processes between the Board of Directors and Ministry of Finance.

### VI.3 Transparency and Reporting

As was mentioned in an earlier section, East Asia and Pacific region SWFs are targets of the same criticisms surrounding any other SWFs – they lack transparency. The key concept to keep in mind is that the SWFs are acting as a public trust for the funds of the governments and by extension the people and thus, should be accountable (by law) for their actions. This accountability ideally should also take a public, transparent form in periodic reports regarding their activities and the submission to annual, independent audits of their activities. Such disclosure could also include the SWF’s overall investment strategy, financial condition, and performance against specified objective benchmarks. In terms of international financial markets, SWFs could reinforce stability – given their increasing size and influence – and prevent potential contagion effects with minimum and timely reporting size of funds, broad strategy of management and

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37 The Transparency and Accountability Scorecard is ranked on the following criteria: 1) Structure, 2) Governance, 3) Transparency and Accountability and 4) Behavior.


investment objectives. In East Asia and Pacific SWFs, accountability seems to be better in SWFs that have more explicit purposes and future liabilities. For instance, the Taiwan Stabilization fund needs to be accountable in a time of currency crisis. To be prepared it invests its assets in liquid investment vehicles.

Regarding commercial desirability, it is understandable and expected that a government entity in the form of SWF does not want to compromise its capacity, maneuverability and competitive advantage when making strategic investments. In the East Asia and Pacific context, Temasek and Government of Singapore Investment Corporation seem to demonstrate this practice. The Singapore Companies Act – which both SWFs are eligible – stipulates that a private company with no more than 20 shareholders and no corporate shareholder is exempted from filing its audited financials with the public registry. Despite this, Temasek has been voluntarily more forthcoming with its investment practices of late and ranks respectively on the SWF Accountability and Transparency Scorecard. The China Investment Corporation also exhibits this behavior, which is shown in public statements by CIC officials, “...adopt a prudential accounting systems...adhere to commercial lines on the condition that company interest will not be jeopardized.” Yet another example is the Taiwan National Stabilization Fund, which makes an annual report available to the public that includes the account balances and details of the fund operations. All the same, it still vigorously guards the confidentiality of its practices and commercial interests by imposing fines or imprisonment for leaking information by managers or other persons associated with the SWF.

Table 3: Auditing of SWFs in East Asia and Pacific

<table>
<thead>
<tr>
<th>Sovereign Wealth Fund</th>
<th>Internal Audit</th>
<th>External Audit</th>
<th>Audit / Annual Report</th>
<th>Accounting Standard</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Audit Committee</td>
<td>Audit Department</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Australia Future Fund</td>
<td>Y</td>
<td>PwC</td>
<td>Y</td>
<td>Australian Accounting Standards</td>
</tr>
<tr>
<td>New Zealand Superannuation Fund</td>
<td>Y</td>
<td>Ernst &amp; Young</td>
<td>Y</td>
<td>New Zealand Auditing Standards</td>
</tr>
<tr>
<td>Brunei Investment Agency</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>China Investment Corporation</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

45 When seeing an N/A either audits were not made available to public, or not required, or there was no information available. Research on the audit issues was as exhaustive as possible, but meant only as a stock-taking exercise and the research results are not necessarily conclusive.
<table>
<thead>
<tr>
<th>National Sovereign Wealth Fund</th>
<th>Audit Committee</th>
<th>Auditor</th>
<th>Internal Auditing</th>
<th>Standards of Professional Practice of Internal Auditing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hong Kong Monetary Authority Investment Portfolio</td>
<td>Y</td>
<td>N/A</td>
<td>Y</td>
<td>N/A</td>
</tr>
<tr>
<td>Korean Investment Corporation</td>
<td>Y</td>
<td>PwC</td>
<td>Y</td>
<td>Korean Auditing Standards</td>
</tr>
<tr>
<td>Malaysia Khazanah Nasional</td>
<td>Y</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Temasek Holdings</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Singapore Standards of Auditing</td>
</tr>
<tr>
<td>Government of Singapore Investment Corporation</td>
<td>Y</td>
<td>Auditor-General of Singapore</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>Taiwan National Stabilization Fund</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>Y</td>
</tr>
<tr>
<td>Timor-Leste Petroleum Fund</td>
<td>Y</td>
<td>Deloitte Touche</td>
<td>Y</td>
<td>International Financial Reporting Standards</td>
</tr>
<tr>
<td>Pacific Island Countries⁴⁶</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>Y</td>
</tr>
</tbody>
</table>

Source: Compiled by authors from published sources.

Although SWFs are entrusted with public funds, reporting and auditing of SWFs is largely not in line with the requirements for other public companies and financial institutions. SWFs are generally not covered by conventional regulatory requirements for reporting and auditing, such as those used for pension and investment funds, and are rightfully criticized for lack of transparency. Auditing of this kind is difficult to enforce because SWFs operate at an international level and are owned and supervised by sovereign states, which complicates the issue of enforceability. In spite of this, efforts are being made by SWF both internationally and in East Asia and Pacific as a result of the acknowledgement that public funds are becoming more systemically important to financial markets. Table 3 provides a snapshot of the available auditing information for SWFs in the East Asia and Pacific region. In almost all cases, except for China Investment Corporation and Brunei Investment Agency, there is some sort of audit activity. Employing an audit committee seems to be the preferred method of auditing rather than developing a full internal department. Another positive sign is the presence of external auditors in some of the SWFs auditing and reporting process and the issuance of annual reports. Conversely, it is troubling that China Investment Corporation, one of the region’s largest SWFs, does not disclose audit details.

⁴⁶According to IMF Working Paper: Sovereign Wealth Funds in the Pacific Island Countries: Macroeconomic-Fiscal Linkages, there are strict rules for auditing and financial reports in the Pacific Island Countries but information is usually unreliable and inaccurate.
VII. Future of SWFs in Asia

Although SWFs have been in existence around the world for many decades, the creation and growth of SWFs in the East Asia and Pacific is a relatively recent occurrence. The emergence of SWFs in Asia is actually a by-product of the strong economic development in the region and a desire by governments to enhance returns for the surplus foreign exchange reserves and fiscal and commodities-related revenues that have accumulated. The SWFs in the region are diverse and have various purposes, historical backgrounds, source of funds, investment strategies and governance structures. The largest, newest, and most prominent SWFs in the region are those created from surplus foreign exchange reserves. Despite a series of visible strategic investments, they typically pursue a balanced portfolio investment strategy. The other type of large SWFs are so-called “legacy funds,” which were originally established as national development funds, however operate more like private-equity funds today.

It remains to be seen if SWFs in Asia will ultimately be successful. It is difficult to ascertain sufficient data to make such judgments given that the reporting and auditing of SWFs is largely not in line with the requirements for other public companies and financial institutions, and disclosure by SWFs is generally limited. In any case, success will depend to a large extent if the size of volume of SWFs is set at an appropriate level so that any adverse events would not pose any risks to the Government’s overall fiscal conditions, and if these funds produce the superior returns in a risk controlled manner as their institutional mandates call for. It seems that the sizes of SWFs in the EAP have so far generally been set at relatively conservative levels. Therefore, there is substantial room for the growth of SWFs across Asia.
PART II: FUND FACTS
1. Fund name, size and history

*Name:* Government of Singapore Investment Corporation (GIC)

*Website:* http://www.gic.com.sg/

*Fund size:* $215 - $330 billion. GIC states that it manages “well above $100 billion”. Market estimates range from $215 billion (Lyons/Standard Chartered, 2007b) to $330 billion.

*Date established:* May 1981 to manage country’s foreign reserves and government’s assets efficiently.

*History:* The origin of GIC lies in Singapore’s high savings rate. Singapore’s financial reserves grew rapidly with increased private savings, yearly public sector surpluses and strategic currency and bond investments. In 1981, the government decided that the bulk of reserves should be invested in longer-term and high-yielding assets, managed by GIC. The reserves were seen as a way to protect against some of the upheavals of the 1970s, including power strikes, budget deficits, economic recession, tax hikes, currency volatility oil price rises, and global disinflation. The first chairman was then prime minister Lee Kuan Yew, and the first deputy chairman was Dr Goh Keng Swee.

2. Source of funding

*Source:* Foreign exchange reserves. GIC does not own the funds it manages, but manages them on behalf of its clients, the Government of Singapore and the Monetary Authority of Singapore. The Ministry of Finance represents the Government in dealing with GIC, and is the legal owner of the funds.

GIC receives transfers from the Government of Singapore from budget surpluses (out of the “honorary account”), in amounts at the discretion of the Government.\(^47\)

*Borrowed funds:* GIC does not have any fixed liabilities in the sense of borrowings. It does pay net income to the Government in the following way, however. Annual transfers are made back into the honorary revenue budget; at present, the amount is 50% of net income and dividends, net of expenses.

\(^{47}\) Presumably, transfers from the budget are denominated in Singapore dollars and GIC has a certain leeway to diversify the currency composition.
GIC does not leverage its entrusted funds with borrowings. It does use a variety of investment vehicles, however, which are tantamount to employing leverage: for example, leveraged buyouts, private equity funds, equity holdings in banks and other financial institutions. GIC does not own foreign reserves which it manages. Main purpose of GIC is to “preserve and enhance reserves by achieving rate of return over or above G3 (US, EU and Japan) inflation” (www.gic.com.sg). Its mid-term objective is to outperform recognized market indices, such as the MSCI. Currently GIC is managing above US$ 100 billion (GIC, 2008).

3. Governance and mandate

Ownership: GIC was established in May 1981 as a private company under the Company’s Act, wholly owned by the Government of Singapore.

Governance (including Management):
GIC reports to its own Board of Directors, which meets at least twice a year. Although GIG is government-owned and manages government funds, the relationship between GIC and the government is that of a fund manager and a client.

The current composition of GIC’s board is as follows:

... Chairman: Lee Kuan Yew, Minister Mentor
... Deputy Chairman: Lee Hsien Loong, Prime Minister
... Deputy Chairman and Executive Director: Dr. Tony Tan Keng Yam
... Group Managing Director: Lim Siong Guan
... Other directors: Lim Hng Kiang; Tharman Shanmugaratnam; Raymond Lim; Peter Seah Lim Huat; Chew Choon Seng; Hsieh Fu Hua; Ng Kok Song; Quah Wee Ghee; Dr Seek Ngee Huat; Dr Richard Hu Tsu Tau; Ang Kong Hua; Dr The Kok Peng.

The Ministry of Finance (MoF) is the main authority overseeing GIC. MoF pays GIC a fee for managing the funds, and specifies the risk parameters under which the funds are managed. GIC’s objective is not profit maximization, but rather wealth preservation. Accordingly, GIC spreads its investments widely and takes relatively small stakes in a large number of companies. GIC argues that its recent investments in UBS and Citicorp were unusual because they do not normally undertake very big investments, preferring to keep a low profile.
The above figure shows the structure of GIC’s subsidiaries in relation to the board. The board has various committees, such as the Investment Committee, the Risk Committee, and the Remuneration Committee. The board acts to ensure that GIC acts in an ethical and fiscally positive manner.

**Mandate (both financial and non-financial):**
GIC’s stated mission is to achieve good long-term returns on state assets placed under its charge by investing internationally, with due regard to risk and the nature of associated liabilities.

Its stated objectives are:

... To preserve and enhance the international purchasing power of Singapore’s reserves, by achieving a real rate of return over and above the G3 (US, EU and Japan) inflation rate over a long-term horizon.
For medium-term performance monitoring, to outperform an appropriate composite of recognized market indices, through optimal allocation among and within asset classes.

To build a cohesive organization of excellence that will attract, develop, motivate and retain quality employees.

In the 2000s, GIC has also helped to develop the local fund management industry in Singapore. GIC disavows being a “strategic investor” which buys into e.g. a bank for wider political purposes.

4. Operations and staffing
GIC operates, invests, measures its performance and rewards its employees no differently from a global fund management company. As a “fifth schedule” company under the Constitution of Singapore, it is required to submit its financial statements and budget to the President of Singapore, and it is regularly audited by the Auditor-General.

In 1999, GIC was restructured to reflect its three major business lines: publicly quoted securities, real estate, and special investments, comprising venture capital, private equity and direct investments in private companies. The corresponding three subsidiaries (as shown in the figure above) are:

   ... GIC Asset Management Pte Ltd,
   ... GIC Real Estate Pte Ltd
   ... GIC Special Investments Pte Ltd.

GIC Asset Management group manages investments in equities, fixed-income, foreign exchange (including money markets and commodities), and alternative investments (including private equity). GIC Real Estate group is reckoned to be one of the 10 largest global real estate investors in the world. It holds hundreds of investments in more than 30 countries, including holdings of offices, retail stores, residential property, hotels etc. It also invests in property indirectly, through investments in property funds, real estate investment trusts (REITS), real estate debt, and other vehicles. GIC Special Investments group is one of the world’s largest private equity investors. The group is sub-divided according to geography (of investment) or industry (e.g. global technology). Its investment vehicles include leveraged buyouts, venture capital, growth capital, mezzanine financing (i.e. subordinated debt), distressed debt, and infrastructure.

Office locations:
Besides Singapore, GIC has offices in the following cities, often more than one office in a single city: Beijing, London, New York, San Francisco, Seoul, Shanghai, and Tokyo.
Staffing:
GIC has about 1000 staff around the world, including some 40% who are foreigners. Approximately one-third is investment professionals, two-thirds support staff. GIC has grown its staff rapidly in the 2000s: its team numbered around 200 in 2001.

5. Investment policy
GIC’s annual rate of return on the foreign exchange reserves that it has managed, over a period of 25 years to March 2006, has averaged 9.5% in US dollar terms. The average rate of return over global inflation was 5.3% p.a. 48

Investment guidelines:
The GIC Board approves a policy asset mix, which is periodically reviewed. This comprises policy weights for different asset classes such as equities, bonds and cash. The Board also approves long-term allocations for private equity and real estate investments.

Within the respective asset classes, GIC investment professionals manage the allocated funds to achieve GIC’s investment objectives, deciding in which countries, sectors and companies to invest.

Medium-term performance is measured against well-known market indices, and the investment objective is to outperform the indices. The indices include the Morgan Stanley Capital International (MSCI) World Equity Index and an enhanced Lehman Brothers World Bond Index.

GIC invests in more than 40 countries, diversified across major asset classes: money markets, equities, fixed income, foreign exchange, commodities, and alternative investments (including real estate and private equity). In all, its operations now extend over nine asset classes:

... Developed market equities
... Private equity
... Nominal bonds
... Inflation-linked bonds
... Real estate
... Commodities
... Hedge funds
... Short-term assets (including currency overlay)

48 These figures were revealed by the chairman, Lee Kuan Yew. GIC does not publish detailed year-by-year performance figures.
The majority of GIC’s investments are in developed countries in Europe. In the last few years, GIC has increased the amounts invested in emerging countries, and in private markets.

*Figure 5. GIC’s Investment Process*

![GIC’s Investment Process Diagram](image)

*Source: GIC website*

The above figure summarizes GIC’s investment process. Among GIC’s major public direct investments are the following (ownership figures rounded):

<table>
<thead>
<tr>
<th>Company</th>
<th>Country</th>
<th>Industry</th>
<th>% ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gravity Co. Ltd</td>
<td>South Korea</td>
<td>Industrial</td>
<td>24%</td>
</tr>
<tr>
<td>Beijing Capital Land</td>
<td>China</td>
<td>Financials</td>
<td>16%</td>
</tr>
<tr>
<td>Thakral Holdings Group</td>
<td>Australia</td>
<td>Financials</td>
<td>13%</td>
</tr>
<tr>
<td>Reef China Commercial Trst</td>
<td>Hong Kong</td>
<td>Financials</td>
<td>11%</td>
</tr>
<tr>
<td>UBS</td>
<td>Switzerland</td>
<td>Financials</td>
<td>11%</td>
</tr>
<tr>
<td>AEI</td>
<td>United States</td>
<td>Energy</td>
<td>11%</td>
</tr>
</tbody>
</table>

*Source: GIC website and other public sources*

Among GIC’s major private sector direct investments is a 9.5% stake in Pepsi-Cola (Philippines) Inc.

*Recent investment activities:*
... February 2008: GIC purchased Westin Tokyo Hotel for $715 million.
... January 2008: $6.9 billion stake in Citigroup, in the form of convertible notes
... December 2007: $9 billion stake in UBS, in the form of convertible notes
... July 2007: Joined consortium to purchase Myer Melbourne (redevelopment site), Australia, for $895 million.
... July 2007: Acquired 50% stake in WestQuay Shopping Centre, UK, for $600 million.

In the cases of both UBS and Citicorp, GIC has declined to nominate a representative to sit on their respective Boards.
1. Fund name, size and history

Name: China Investment Corporation (CIC)

Website: [http://www.cic-recruit.cn/](http://www.cic-recruit.cn/)
(Also: [http://www.china-inv.com/user/](http://www.china-inv.com/user/) for external managers)

Fund size: $200 billion

Date established: September 2007

History:
China’s foreign exchange reserves stood in the region of $1.4 trillion at end April 2008. Consequently, the Chinese authorities have shown a desire to increase returns, to broaden diversification of foreign assets, and perhaps to reduce the percentage of dollar assets in foreign exchange holdings.

It is an open question, however, whether the desire to increase returns on foreign investments is a more important motivation than the desire to relieve domestic pressures (of excess liquidity build-up) by opening the capital account. Related to the latter, there is a desire to relieve pressures on the renminbi to appreciate.49

The creation of CIC should be seen in the broader context of China exploring various ways to accumulate and manage foreign assets, including the recapitalization of China Development Bank (CDB), and increased foreign investment by state banks and state firms. The significance of these developments is that there are many channels through which China (as a state) can acquire foreign assets.

CIC was officially established in September 2007, but in fact operated in May 2007 to buy a stake in Blackstone, the US private equity group.50

When CIC was first being set up, CIC chairman Lou Jiwei indicated that one-third of its $200 billion capital would be used to purchase Huijin Investment, an investment arm of the Chinese government; another third would be injected into state-owned banks for shareholding reforms; and the remaining about $70 billion was earmarked for overseas

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49 As claimed, for example, in the Financial Times, November 29, 2007.
50 As noted below, the $3 billion stake subsequently dropped precipitously in value.
investment in a wide range of portfolios, but such investment would not seek control.\textsuperscript{51} Similarly, a statement by Finance Minister Li Yong indicated that around one-third or about $67 billion, would be injected into China Development Bank (CDB) and Agricultural Bank of China (ABC).\textsuperscript{52}

In April 2008, however, it emerged that CIC now has as much as $90 billion to spend on assets abroad, its president and chief investment officer, Gao Xiqing, said.\textsuperscript{53} The reason for the increase is that the government reduced the amount needed to restructure certain state-owned institutions, including ABC and CDB. Also it was confirmed that the state-owned Central Huijin Investment Corporation had been absorbed by CIC.

The significance of the absorption of Huijin is that it shows that CIC, in fact, has two quite separate purposes: one being to provide funding for recapitalization of state banks, the other being to manage externally-invested excess reserves. In respect of the former purpose, CIC for financial institutions to some degree parallels SASAC\textsuperscript{54} for state enterprises: that it, it manages the state’s ownership stake in certain enterprises.\textsuperscript{55}

In accordance with that purpose, in December 2007, Lou Jiwei, CIC chairman, stated that CIC would inject capital into Agricultural Bank of China (ABC) and China Development Bank (CDB) to finance their restructuring in the near future.\textsuperscript{56} The ABC had a non-performing loan ratio of above 23\% at end 2006, much higher than the other three major banks, and is the only one of the “big four” commercial banks that has not undergone share-holding restructuring. The aim of the CDB restructuring, according to State Council decisions, is to make CDB more commercialized.

CIC signed an agreement with China Development Bank (CDB) to inject $20 billion into the bank. This and other injections of capital were injections of foreign exchange. The deal was conducted through Central Huijin (as a subsidiary of CIC), and had been in the works prior to CIC’s launching.\textsuperscript{57} Earlier CIC chairman Lou confirmed that CIC had injected capital into China Everbright Bank in the amount of dollars-equivalent to yuan 20 billion, equaling about $2.73 billion.\textsuperscript{58}

\textsuperscript{51} Source: China Daily, e.g. December 20, 2007.
\textsuperscript{52} Source: China Daily November 11, 2007.
\textsuperscript{53} Source: Financial Times, April 25, 2008.
\textsuperscript{54} SASAC denotes the State-Owned Assets Supervision and Administration: Commission of the State Council.
\textsuperscript{55} SASAC chairman, Li Rongrong, has said he had discussions with the CIC about joint financing of overseas investment (source: Financial Times, September 13, 2007).
\textsuperscript{56} Source: China Daily, December 26, 2007.
\textsuperscript{57} Source: China Daily, December 31, 2007.
\textsuperscript{58} Source: China Daily, November 30, 2007.
2. Source of funding

Source: In effect, foreign exchange reserves. More precisely, transfers from foreign exchange reserves to CIC by the Ministry of Finance (MoF).

MoF buys the foreign exchange from PBoC (People’s Bank of China), taken from the stock of foreign exchange reserves. An important consequence of this arrangement is that, it would seem, MoF (not CIC) bears the foreign exchange risk, as elaborated in the following paragraphs.

Borrowed funds:
CIC’s chairman, Lou Jiwei, has said that CIC is under “big pressures” to turn a profit, as it has to earn $40 million a day to offset the cost of the 5% annual interest rate it pays on the special bonds sold by the Ministry of Finance to capitalize CIC. It is not clear whether the reference to “5%” is an actual rate of cash payment by CIC (e.g. dividends paid to MoF) or, as seems more likely, a notional rate against which to measure performance. In either event, the claim of “big pressures” seems to be an over-statement, since CIC seems to escape costs of exchange rate appreciation (renminbi against the US dollar), and hence should reasonably hope to generate 5% from risky assets in advanced economy financial markets.

CIC does not borrow funds. Rather the MoF has borrowed in its (MoF’s) name in RMB (renminbi) in order to capitalize CIC. MoF uses the domestic currency raised to purchase foreign exchange from PBoC (from the reserves), and transfers the foreign exchange to CIC. MoF has borrowed about $200 billion equivalent in RMB. As a practical matter, one can infer from the above Lou quote that CIC’s (internal) performance benchmark is based on the cost of borrowing, namely 5%.

It is important to note that that excludes the potential cost of RMB appreciation (versus the dollar), which is borne by MoF. In effect, the appreciation cost is an accounting allocation to MoF of the exchange rate cost of holding foreign reserves.

The quoted cost of 5% in itself suggests that the borrowing was subsidized, in the light of current market conditions in China, and indeed the bonds issued by MoF were placed with PBoC. Further, it appears (source: Setser 2008) that PBoC has funded the purchases of MoF bonds with short-term (RMB) funding, thereby incurring interest rate risk.


60 Moreover, the “5%” seems to be a rounded figure for MoF borrowing costs that have varied between 4% and 5%.

61 The exact $ amount is not known publically: it depends on the RMB/$ exchange rate at the time the proceeds from borrowing were converted to foreign exchange holdings.
In conclusion, the creation of CIC has led to a form of sterilization of foreign exchange intervention. Because it has been done on non-market terms, however, it has induced the PBoC to incur interest rate risk, rather than fund long-term at an explicit loss.

3. Governance and mandate

*Ownership:* Chinese government (People’s Republic of China). 62

*Governance (including Management):*

... Chairman: Lou Jiwei
... President and Chief Investment Officer: Gao Xiqing
... Executive Vice President: Jesse Wang

Lou is Deputy Secretary-General of the State Council. The significance of this is that CIC is a ministerial-level organization answering directly to the State Council.

Besides Chairman Lou, other board members include:

... Two executive directors—Gao Xiqing and Zhang Hongli
... Five non-executive directors—Zhang Xiaoqiang, Li Yong, Fu Ziyi, Liu Shiyu and Hu Xiaolian.
... One independent director—Liu Zhongli.
... One director to be elected from the company's employees.

Gao Xiqing has been vice chairman of the National Council for Social Security Fund. Zhang Hongli and Li Yong are vice finance ministers. Zhang Xiaoqiang is vice minister of the National Development and Reform Commission (NDRC), Fu Ziyi assistant minister of commerce, Liu Shiyu central bank vice governor, Hu Xiaolian head of the State Administration of Foreign Exchange (SAFE) and Liu Zhongli former finance minister. The presence on CIC’s board of representatives from various ministries suggests that both the purposes of CIC and its origins reflect a balance of the interests of the various ministries.

Gao Xiqing was also designated the company’s general manager, and Zhang Hongli, Yang Qingwei, Xie Ping and Wang Jianxi were appointed as deputy general managers. 63

62 Technically, it would seem that the Ministry of Finance holds the full ownership stake, on behalf of the government.

Previously, Yang Qingwei was department head of fixed assets investment with the NDRC, Xie Ping was the general manager of the Central Huijin Investment Corporation, and Wang Jianxi was a vice board chairman of the Central Huijin. Hu Huaibang, Commissioner of Discipline Inspection with the China Banking Regulatory Commission, took the post as chief supervisor.64

*Mandate (both financial and non-financial):* CIC is charged with managing the portion of foreign exchange reserves allocated to it. A precise mandate for CIC has not been established, however.

As noted above, CIC also fulfils a role in domestic restructuring and management of banks. For example, Chairman Lou has stated that after the reform of the Agricultural Bank of China, the CIC will have a hand in the daily management of the ABC and a place on the ABC board.65

Broadly perceived, therefore, CIC’s role is seen as promoting China’s overseas expansion and rescuing domestic banks; supporting Chinese companies overseas IPOs and enhancing returns on foreign exchange reserves. Since this role is played out in the context of other state actors, there is the potential for duplication or conflicting strategies.

4. Operations and staffing

Some commentators have claimed that CIC’s operations are modeled on Singapore’s Temasek Holdings, or on both Singapore GIC and Temasek. There is some element of truth in this. It seems to be based on the fact that those funds were visited by the Chinese in preparation for setting up CIC. GIC and Temasek try to benefit from technology transfer through their investments e.g. in telecoms and banking. Arguably, CIC is similarly motivated.

*Office locations:*

Beijing

As funds rapidly accrue to CIC from foreign exchange reserves, it seems probable that it will open offices abroad, following the model of, for example, Singapore GIC. The location of any future international offices will provide clues to CIC’s longer run investment strategy. Speculation has suggested that CIC might open an office in Hong Kong, and is also considering offices in London and somewhere in emerging markets.

64 Source: Xinhua, September 29, 2007.
The City of London has attempted to woo CIC into setting up an office in London. The Lord Mayor, John Stuttard, met with Lou Jiwei in October 2007.\textsuperscript{66}

\textit{Staffing:}  
Staff numbers were initially, about 70 persons,\textsuperscript{67} now about 180 (source: CBS 60 minutes interview with Gao Xiqing, April 6, 2008). Apparently, CIC staff is technically civil servant, earning civil servant pay. Managers have been listed above.

\textbf{5. Investment policy}  
CIC is hiring external fund managers.\textsuperscript{68} Gao Xiqing stated he hoped to hire managers within the next few months. Gao said “The asset classes we are hiring managers for include the cash market, fixed income, equity, and hedge funds. We will also be hiring managers for private equity.”

External managers are expected to manage at least half of the overseas investment (i.e. half of what was projected at $70 billion, now $90 billion).\textsuperscript{69} Following the enlargement of the allocation to $90 billion, Gao has said that most of additional allocation would go to external managers to invest in equities, fixed income products and alternative investments.\textsuperscript{70}

\textit{Investment guidelines:}  
Requirements for external managers in terms of experience are, for example, 6 years investment experience in the asset class applied for (in the case of fixed income) with fixed income assets (excluding money market funds) under management of not less than $15 billion. In practical terms, this means that CIC is looking at the top tier of fund managers globally—the best and most sophisticated.

CIC has advertised for external fund managers in the following asset classes:

\begin{itemize}
  \item Active global fixed income  
  \item Active emerging market debt  
  \item Global equity active  
  \item MSCI active (a Morgan Stanley equity index)  
  \item Emerging market active  
  \item Asia excluding Japan equity active
\end{itemize}

\textsuperscript{66} Source: China Daily, October 26 2007.  
\textsuperscript{67} Source: Financial Times, November 29, 2007.  
\textsuperscript{68} Source: International Herald Tribune, February 28 2008.  
\textsuperscript{69} Source: Financial Times, November 29, 2007.  
\textsuperscript{70} Source: Financial Times, April 25, 2008.
This indicates that CIC intends to follow a broadly diversified portfolio in its holdings of publicly trade securities. Such a portfolio is very much in line with what more advanced pension funds or global asset managers would deploy. It has set performance targets that are also very much in line with the practice of the best-managed global funds. For instance, for emerging market debt, the performance target is 200 basis points, net of fees, over the benchmark, and for global equity active, it is 300 basis points, net of fees, over the benchmark.

Recent activities:
CIC does not disclose its external portfolio. Details of specific deals, however, are known. In December 2007, CIC announced that it would invest $5 billion in Morgan Stanley, in the form of mandatorily convertible preferred stock carrying a fixed interest rate of 9%, and convertible in August 2010 into 9.9% of Morgan Stanley common shares.71

CIC’s statement stressed that the purchase is a “long term, passive financial investment” and does not lead to a role in management of Morgan Stanley. For Morgan Stanley, the motivation for such a deal (beyond the finance) is that it could help in securing licenses and approvals for future business ventures in mainland China.

Table 3 shows details of some of CIC’s recent investments.

<table>
<thead>
<tr>
<th>Company</th>
<th>Stake</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Blackstone Group*</td>
<td>Stake: 10%</td>
<td>$3 billion</td>
</tr>
<tr>
<td>Morgan Stanley</td>
<td>Stake: 9.9%</td>
<td>$5 billion</td>
</tr>
<tr>
<td>Visa</td>
<td>IPO</td>
<td>$100 million</td>
</tr>
<tr>
<td>JC Flowers Fund+</td>
<td>Stake: about 80% (of fund)</td>
<td>$4 billion</td>
</tr>
</tbody>
</table>

Notes:
The Blackstone stake, acquired in May 2007, subsequently dropped in value (on paper) by more than 40%.
* Private equity conglomerate
† Upon conversion
➕ Private equity fund. The investment will be aimed at distressed financial institutions.

Source: Compiled by authors from various published sources.

Additionally, CIC reportedly bought HK$780 million of stock in China Railway Group Ltd., the world's third-biggest construction company, in a Hong Kong initial public, in December 2007.72 Recently, CIC has also been reported to be in discussions to buy

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72 Source: JetFin Emerging Markets Hedge Fund News.
Dresdner Bank\textsuperscript{73}; and to have expressed an interest in buying the Swedish government’s 19.9\% stake in Nordea AB, Sweden’s biggest bank.\textsuperscript{74}

6. Other
Arguably, CIC influence over foreign assets amounts to much more than its capitalization of $200 billion, because of its ownership stakes in CDB, ABC and China Everbright, which deploy substantial foreign assets. It is not clear, however, to what extent CIC has or will have sway over the operations of these banks. In July 2007, prior to CIC’s formation, CDB, along with Temasek, had taken a stake in Barclays Bank.\textsuperscript{75} From a purely analytical point of view, taking a stake in a financial institution (such as CDB, ABC, Evergreen or, for that matter, Blackstone, or Morgan Stanley) is a way of leveraging the CIC portfolio indirectly, since all these institutions borrow funds themselves.

\textsuperscript{73} Source: Sueddeutsche Zeitung, March 30, 2008.
\textsuperscript{74} Source: Forbes, March 6, 2008.
\textsuperscript{75} Source: The Economist, July 26, 2007.
SINGAPORE: Temasek Holdings

1. Fund name, size and history

   Name: Temasek Holdings

   Website: http://www.temasekholdings.com.sg/

   Fund size: $108 billion (Singapore dollars: S$164 billion).

   The value of Temasek’s portfolio grew by 35% over the year to end March 2007, while
   shareholder returns were stated to be 27%. This suggests that, besides holding some very
   profitable investments, Temasek retained cash flow (that might otherwise have been paid
   out as dividends) of some $8 billion.

   Date established: June 1974

   History: Temasek was established in 1974 to “hold and manage investments and assets
   previously held by Ministry of Finance of Singapore” (Temasek, 2007). Some 30 of start-
   up investment, an initial portfolio of S$354 million, held by MOF since independence of
   Singapore in 1965 were transferred to Temasek. Bonds issuing and borrowing have been
   another source of funding although not much. It has a unique characteristic as a SWF in
   the context that its source of funding is not natural resources or foreign reserves but state
   owned enterprises. This arrangement represents a policy commitment that the
   investments be managed on a sound commercial basis, as distinct from the government’s
   public interest role of policy-making and market regulation. By contrast, GIC manages
   the foreign reserves entrusted by Monetary Authority of Singapore (MAS) and Ministry
   of Finance. The portfolio of Temasek has grown to S$ 164 billion (US$ 108 billion) as of
   March 2007. Temasek’s main mission is to “create and maximize long-term shareholder
   value as an active investor and shareholder of successful enterprise” (Israel, 2008).

   Temasek differs from Singapore GIC in that it is a holding company (and therefore owns
   the funds that it deploys). When Singapore became independent in 1965, its prospects
   were unclear and it had difficulty attracting investment. This was the rationale for the
   Government to set up companies like Singapore Airlines and DBS Bank. Originally,
   these investments were held directly by the Ministry of Finance in Singapore. The
   principal common feature between Temasek and GIC is that both are owned by the

   76 In this regard, Temasek may not be classified as SWF which is defined “to be owned by government as a
   form of foreign exchange assets and managed separately from official reserves” by some scholars (Jen,
   2007).
Singapore Government. (See below under *Mandate* for operational relations, or rather non-relations.) Temasek works under a mandate from the Singapore Government.77

Temasek is a private investment company, operating strictly as a commercial entity. The MOF is not involved in investment, business and commercial decision. But it is naturally accountable to its shareholder; Ministry of Finance, for overall performances as other commercial entities is to their shareholders. It submits annual financial statement, performance review and pays dividends to MOF. It is not unknown whether the dividends have been used as a part of budget or reinvested in Temasek. Meanwhile, the elected President of Singapore 78 has authority to approve the appointment or removal of Temasek’s Board members and CEO. Term of Board members is three years and they can be re-appointed with the approval of the President. The Singapore constitution limits the government to using critical assets and past reserves accumulated from investments by requiring the Temasek Board to seek the approval from the President (Temasek, 2006). The elected President plays a role to ensure that there is no undue government influence towards Temasek’s day-to-day operations.

2. **Source of funding**

*Source:* Temasek is the investment holding arm of the Government of Singapore, owning commercial assets of the government that have been transferred to it. The underlying source of funds, therefore, is fiscal surpluses and, more generally, government ownership of commercial assets.

*Borrowed funds:* Temasek incurs debt to a moderate degree in order to fund its investments. At end March 2007, its net debt in Singapore dollars was about S$24 billion, compared to total assets of S$242 billion.

3. **Governance and mandate**

Temasek is an investment management company that owns and manages its assets on a commercial basis.

*Ownership:*
Temasek is owned by its sole shareholder, the Minister of Finance (i.e. in effect, the Government of Singapore). In this context, the “Minister of Finance” is an incorporated legal entity.

**Governance (including Management):**
Temasek operates under the purview of the Singapore Companies Act and related laws. Within this regulatory framework, it operates with full commercial discretion and flexibility, under the direction of its Board of Directors. It provides audited annual financial reports, as well as periodic updates, to the Minister of Finance. While not required to release financial statements publicly, since 2004 it has chosen to publish group financial highlights in its annual Temasek Review. It sets a dividend policy, providing cash returns to its sole shareholder.

Under the constitution of Singapore (as amended in 1991), Temasek is designated a “Fifth Schedule company”. (GIC is also a Fifth Schedule company.) Temasek does not manage the reserves of the Singapore Government (or the reserves of any other Fifth Schedule company/entity). Each Fifth Schedule company is managed independently, and is separately accountable to the President through its own Board and CEO for the protection of its past reserves.

In accordance with its Fifth Schedule designation, the President’ concurrence is required for the appointment and removal of Temasek Board members and its CEO. Each Board appointment is for a fixed term not exceeding three years (and may be renewed). In addition to its normal fiduciary duties, the Board is accountable to the President to ensure that every disposal of investment is transacted at a fair market price.

An important requirement is that the Board must ensure that its annual operating budget and any proposed transaction does not diminish its past reserves. The Board is required to seek the approval of the President before it draws on or diminishes its own past reserves. In this context, past reserves refers to accumulated net income accounted for before the current term of office of the Singapore Government.

Investment, business or commercial decisions are the responsibility of the Board and management. Neither the President nor the Singapore Government is involved in directing Temasek’s investment, divestment or other business decisions. Temasek does not direct the commercial or operational decisions of companies held in its investment

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79 Temasek has published ‘Temasek Review’ every year since 2004. The review includes corporate governance, risk management, asset mix by sector and geography and financial performance. The review can be accessible its website, [www.temasek.com.sg](http://www.temasek.com.sg), which contains previous reviews and basic information. Since Temasek has issued its international bond, it should also provide financial performance and data to credit rating companies and stakeholders.
portfolio. Companies in the portfolio are managed by their respective managements; they are guided and supervised by their respective boards of directors.

The majority of the Temasek Board consists of independent private sector business leaders (see nearby table). The Board meets at least quarterly through the fiscal year, and generally more often. Its committees include: the Executive Committee (EXCO), the Audit Committee (AC), and the Leadership Development & Compensation Committee (LDCC).

Table 5. Temasek’s Board Membership

<table>
<thead>
<tr>
<th>Position</th>
<th>Name</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chairman</td>
<td>S. Dhanabalan</td>
</tr>
<tr>
<td>Deputy Chairman</td>
<td>Kwa Chong Seng</td>
</tr>
<tr>
<td>Deputy Chairman</td>
<td>Lim Siong Guan(1)</td>
</tr>
<tr>
<td>Member</td>
<td>Sim Kee Boon</td>
</tr>
<tr>
<td>Member</td>
<td>Koh Boon Hwee</td>
</tr>
<tr>
<td>Member</td>
<td>Kua Hong Pak</td>
</tr>
<tr>
<td>Member</td>
<td>Goh Yew Lin</td>
</tr>
<tr>
<td>Member</td>
<td>Teo Ming Kian (2)</td>
</tr>
<tr>
<td>Executive Director</td>
<td>Simon Claude Israel (3)</td>
</tr>
<tr>
<td>Director &amp; CEO</td>
<td>Ho Ching 80</td>
</tr>
</tbody>
</table>

Notes:
1 Mr Lim Siong Guan relinquished his position as Deputy Chairman of the Board on 1 October 2006 but remained a Board Member. He stepped down from the EXCO and was appointed to the AC on 1 October 2006. He left the Board on 13 July 2007 after having served more than a decade.
2 Mr Teo Ming Kian joined the Board with effect from 1 October 2006 and was appointed to the EXCO at the same time.
3 Mr Simon Israel joined the Board on 1 August 2005 and was appointed to the EXCO on 1 September 2005. He became Executive Director on 1 July 2006.

Source: Temasek Review 2007

The Board of directors is the highest decision making body of Temasek. BOD is responsible for investment, divestment, and other business decisions. BOD also provides overall guidance and policy direction to management team. Currently BOD is comprised of eight members, five non-executive private sector business leaders, two executive directors and one from MOF. The sub-committees assist the Board, addressing specific matters as delegated by the Board. Among them are the Executive Committee, the Audit Committee and the Leadership Development and Compensation Committee whose chairs are non-executive directors. Executive Committee handles matters relating financing, funding, dividend and major business decision. The audit Committee reviews financial reporting, internal & external auditing and compliance. The Leadership development and

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80 Some have questioned the independence of Temasek, since its CEO Mme. Ho Ching is the daughter-in-law of H.E. Mr. Lee Kuan Yew and the wife of his son, Prime Minister Lee Hsien Loong
Compensation Committee is responsible for renewals of Board members and key positions of the Temasek, and compensation scheme.

**Mandate (both financial and non-financial):**
Temasek’s stated mission is to create and maximize long-term shareholder value as an active investor and shareholder of successful enterprises.

With regard to relations between Temasek and GIC, the two operate entirely separately and are very scrupulous about maintaining their distinction. They have no common officers, they do not discuss strategies or what to do. They are very careful because in some cases when both Temasek and GIC have shareholdings in a company, it is important that they should be regarded as two separate entities, not two entities working in concert. They never invest together, nor hold investment discussions, nor exchange views on news developments.\(^1\)

**4. Operations and staffing**

*Office locations:*
Temasek is headquartered in Singapore. Temasek also has an office in Hong Kong, and representative offices in Beijing, Shanghai, Mumbai, and Ho Chi Minh City, consistent with its focus on Asian investments. In May 2008, Temasek management announced that it will increase its focus on Latin America, with a presence in perhaps Brazil and Mexico.

*Staffing:*
Temasek has a multinational staff of more than 300 people. As a global investor, around 40 percent of its staffs at the senior level are foreigners. It introduced performance-based compensation plans to recruit quality staffs and draw high performance. Temasek staff is compensated, in part, through a “wealth added bonus plan”. Whenever Temasek achieves positive wealth added, a fraction is set aside as a performance driven staff incentive pool.

Ho Ching  Executive Director & Chief Executive Officer
Vijay Parekh  Senior Managing Director, Chief Operating Officer
Charles Ong  Senior Managing Director, Chief Strategist
Jimmy Phoon  Senior Managing Director, Chief Investment Officer
Tow Heng Tan  Senior Managing Director, Co-Chief Investment Officer

**5. Investment policy**

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\(^1\) Source: *Financial Times*, February 3, 2008.
Temasek is an active shareholder and investor in diverse industry sectors such as banking and financial services, real estate, transportation, infrastructure, telecommunications and media, healthcare, and energy and natural resources. Temasek has invested in private equity funds for more than 15 years.

Total shareholder returns since inception amount to more than 18% (compounded annually). The accompanying figures show both portfolio value and financial highlights.

*Figure 6. Value of Temasek’s Portfolio has been rising rapidly*  
(in billions of Singapore dollars)

Temasek has a corporate credit rating of AAA/Aaa by Standard & Poor’s and Moody’s respectively. Temasek has acquired a fund management company, Fullerton Fund Management, but its operations are kept strictly separate from those of Temasek by a ‘Chinese Wall’.

*Investment guidelines and disposition:*  
Temasek’s investments are heavily focused in the Asian region, which accounts for 78% of the portfolio, excluding Japan (of which 38 percent is invested in Singapore and 40 percent in the rest of Asia) as of end-March of 2007. OECD economies (excluding Korea) account for a further 20%. Temasek has sought to diversify its investments in recent years, with the share outside of Singapore increasing.

Taking highly rated investments together, defined as AAA/AA-rated or OECD economies, accounts for 60% of the portfolio. Some 80% of the portfolio is accounted for by listed or liquid assets. Some 61% of the portfolio is accounted for by financial services and the telecommunications and media sectors. Temasek views these as sectors that correlate with the growth of the emerging middle class in Asia. In June 2007,
Temasek set up an oil exploration subsidiary to help diversify its financials-heavy portfolio.\textsuperscript{82}

Figure 7. Temasek’s Recent Financial Highlights

<table>
<thead>
<tr>
<th>GROUP INCOME STATEMENTS (IN $ BILLION)</th>
<th>FOR THE FINANCIAL YEAR ENDED 31 MARCH</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2003</td>
</tr>
<tr>
<td>Revenue</td>
<td>49.6</td>
</tr>
<tr>
<td>Profit before exceptional items</td>
<td>4.1</td>
</tr>
<tr>
<td>Net profit attributable to equity holder</td>
<td>0.2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>GROUP BALANCE SHEETS (IN $ BILLION)</th>
<th>FOR THE FINANCIAL YEAR ENDED 31 MARCH</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2003</td>
</tr>
<tr>
<td>Total assets</td>
<td>140.0</td>
</tr>
<tr>
<td>Shareholder equity</td>
<td>54.5</td>
</tr>
<tr>
<td>Net debt*</td>
<td>22.1</td>
</tr>
</tbody>
</table>

\textsuperscript{82} Source: Reuters, April 24, 2008.
Currently, Temasek reportedly guides its investment decisions by four investment themes:

... Transforming economies: Temasek invests in industry sectors that correlate with the economic transformation of the country

... Thriving middle class: Temasek finds opportunities in companies and industries whose growth is fuelled by the increasing purchasing power of the middle class.

... Deepening comparative advantages: Temasek taps the potential of competitively-positioned companies

... Emerging champions: Temasek identifies companies proving to be best-in-class, be it regionally or globally

Recent activities and significant stakes held:
Barclays Bank plc  Almost $2 billion: announced July 2007
Standard Chartered Bank  19% (approximately), raised from 17% in February 2008
China Eastern Airlines Corporation  24% (held together with Singapore Airlines)

Table 6. Selected financial sector holdings for Temasek

<table>
<thead>
<tr>
<th>Company</th>
<th>Country</th>
<th>Industry</th>
<th>% ownership (approx)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lai Fung Holding Ltd.</td>
<td>Hong Kong</td>
<td>Financials</td>
<td>20%</td>
</tr>
<tr>
<td>Standard Chartered plc</td>
<td>UK</td>
<td>Financials</td>
<td>19%</td>
</tr>
<tr>
<td>Bank of China</td>
<td>China</td>
<td>Financials</td>
<td>16%</td>
</tr>
<tr>
<td>Merrill Lynch</td>
<td>United States</td>
<td>Financials</td>
<td>9%</td>
</tr>
<tr>
<td>Hana Financial Group Inc.</td>
<td>S. Korea</td>
<td>Financials</td>
<td>9%</td>
</tr>
<tr>
<td>ICICI Bank Ltd.</td>
<td>India</td>
<td>Financials</td>
<td>9%</td>
</tr>
<tr>
<td>DBS Holding Group</td>
<td>Singapore</td>
<td>Financials</td>
<td>28%</td>
</tr>
<tr>
<td>China Construction Bank</td>
<td>China</td>
<td>Financials</td>
<td>5%</td>
</tr>
<tr>
<td>PT Bank Danamon Indonesia</td>
<td>Indonesia</td>
<td>Financials</td>
<td>59%</td>
</tr>
<tr>
<td>PT Bank Internasional Indonesia</td>
<td>Indonesia</td>
<td>Financials</td>
<td>34%</td>
</tr>
</tbody>
</table>

Source: Temasek Review 2007

In November 2007, Temasek was found guilty of engaging in monopolistic practices in Indonesia cellular market, by the Indonesian Commission for the Supervision of Business Competition (KPPU). The finding was related to Temasek’s holdings in Telkomsel and Indosat. Temasek has appealed the decision to the Indonesian Supreme Court.

In 2006, Temasek took a $3.8 billion stake in the Thai telecommunications group Shin Corporation.
BRUNEI: Brunei Investment Agency (BIA)

1. Fund name, size and history

Name: Brunei Investment Agency (BIA)

Website: http://www.mof.gov.bn/mof/en/departments/bia/

Fund size: $60 billion - $75 billion

Market estimates usually place the size of the fund at $30 billion. In the judgment of the present paper, the above range is more accurate. In addition, it is estimated that the present rate of accumulation of the fund is in the region of $15 billion - $20 billion per annum (based on a current oil price in the region of $130 per barrel).

Date established: 1983
Established by Brunei Investment Agency Act.

History:
BIA was created in 1983 to replace the largely British Investment Advisory Board, shortly before independence from Britain.83

2. Source of funding

Source: Oil and natural gas revenues are the underlying source.

BIA is the main agency that holds and manages the Government of Brunei’s General Reserve Fund and its external assets, i.e. BIA manages the country’s foreign exchange reserves. Brunei operates a currency board.

Transfers to the BIA are essentially derived as a residual after Government revenues are allocated to three funds: (a) The Stabilization Fund for the budget; (b) The Pension Fund; (c) The Domestic Development Fund. In addition, revenues may be allocated to the personal wealth of the Sultan. In current circumstances (oil prices in excess of $130 per barrel), the residual transferred to BIA could easily be in the region of $15 billion per annum or higher.

Borrowed funds:
None known.

83 Prior to 1983, the British Crown Agents had handled certain banking services for Brunei.
3. Governance and mandate

Ownership:
BIA is a department in the Ministry of Finance. (The Ministry of Finance regulates all commercial banking activity, since Brunei does not have a central bank.). Ownership of the funds resides with the Government of Brunei. Some commentators argue that that effectively means ownership by the Sultan.

Governance (including Management):
The BIA Chairman is: Pehin Orang Kaya Seri Utama Dato Seri Setia Hj Yahya
The chairman is also Brunei’s Minister of Energy. The Managing Director is: Dr Mohd Amin Liew Abdullah. Directors are appointed to the Board of Directors by His Majesty the Sultan for a term of three years (renewable).

Mandate (both financial and non-financial):
In formal terms: (a) To hold and manage in Brunei and overseas the General Reserve Fund and all external assets of the Government; (b) To provide the Government with money management services; and to protect or recover assets and property of the Government or the Agency. These efforts have de facto led to an increase the real value of Brunei’s foreign exchange reserves.

4. Operations and staffing

Office locations:
Brunei Darussalam and Paris. BIA has maintained offices in the past in London and Brussels.

Staffing:
Funds are largely managed by external managers, drawn from Wall Street, European and Asian investment houses, and also private equity and hedge fund managers.

5. Investment policy

Investment guidelines:
BIA has diverse holdings in both public and private companies, real estate and currency portfolios.

Recent activities and investment portfolio:
BIA has major investment holdings in OECD and ASEAN countries. For example, BIA owns the Dorchester Group of hotels.

84 Source: Brunei Times.
85 Source: Brunei Times.
BIA may invest in alternative investments, including hedge funds. In January 2008, BIA launched BICB Capital, Brunei's first investment company that will offer open-ended fund Shariah-compliant investment opportunities.
MALAYSIA: Khazanah Nasional

1. Fund name, size and history
   
   **Name:** Khazanah Nasional Berhad


   **Fund size:** $26 billion

   **Date established:** September 1993

   **History:**
   Khazanah Nasional is the investment holding arm of the Government of Malaysia, empowered as the Government's strategic investor. It is entrusted to manage the commercial assets held by the Government and to undertake strategic investments. Khazanah was incorporated under the Companies Act 1965 in September 1993 as a public limited company and commenced operations a year later.

   The primary objectives of Khazanah Nasional are:

   ... To hold and manage the investments entrusted to it by the Government of Malaysia; and
   ... To undertake new investments where there are strategic opportunities, in new sectors and in new markets

   Khazanah has investments in over 50 major companies. These companies are involved in various sectors such as: banking; semiconductor; steel production; airport management; automobile and motorcycle manufacture; power; broadcasting; infrastructure; investment holding; port development and management; property; electronics; telecommunications; research technology and venture capital; healthcare.

2. Source of funding

   **Source:** Khazanah is the investment holding arm of the Malaysian Government, owning commercial assets of the government that have been transferred to it. The underlying source of funds, therefore, is fiscal surpluses and, more generally, government ownership of commercial assets.

   **Borrowed funds:**
   Khazanah undertakes significant borrowings, in order to augment the funding of its portfolio. In recent years, its debt/equity ratio has been a little below 2:1.
Khazanah issued the world’s first exchangeable ‘Sukuk’ bond (i.e. Sharia-compliant bond, structured by bundling leasing transactions) in October 2006, in an amount of $750 million. Khazanah, therefore, is considered an innovator in Islamic finance. In respect of sources of funds and borrowing, Khazanah is similar to Temasek in its relation to the Government of Singapore.

3. Governance and mandate

Ownership:
All of the equity of Khazanah Nasional is owned by MOF (Inc), which is in turn owned by the Ministry of Finance (except for one share owned by the Federal Land Commissioner). In essence, Khazanah is a wholly owned entity of the Malaysian Government. As of end May 2007, Khazanah’s net worth was $18.3 billion.

Governance (including Management):
Khazanah Nasional has an eight-member Board (see nearby table) comprising representatives from the public and private sectors. Dato' Seri Abdullah bin Haji Ahmad Badawi, the Honourable Prime Minister of Malaysia, is the Chairman of the Board. The Board of Directors is assisted in the discharge of its duties by an Executive Committee and an Audit Committee established by the Board.

Table 7. Khazanah’s current Board of Directors:

| Dato' Seri Abdullah bin Haji Ahmad Badawi |
| Tan Sri Dato' Nor Mohamed Yakcop |
| Tan Sri Dato' Sri Dr Zeti Akhtar Aziz |
| Tan Sri Md Nor Yusof |
| Dato' Mohammed Azlan bin Hashim |
| Dato' Mohamed Azman bin Yahya |
| Raja Datuk Seri Arshad Raja Tun Uda |
| Tan Sri Azman bin Hj. Mokhtar |

Source: Khazanah website

The organizational structure of Khazanah is shown in figure 7. The most senior management is as follows:

Tan Sri Azman bin Hj. Mokhtar – Managing Director

86 Subsequently, the IFC and World Bank have issued sukuk bonds denominated in ringgits.

87 Tan Sri Azman bin Hj. Mokhtar was appointed as Managing Director of Khazanah Nasional in June 2004. Between 1994 and 1998, he was a Director and Head of Research for Union Bank of Switzerland in Malaysia. Between 1998 and 2002, he was Director and Head of Research at Salomon Smith Barney in Malaysia.
Mandate (both financial and non-financial):
As trustees to the nation's financial assets, Khazanah’s main objective is to promote economic growth and make strategic investments on behalf of the Government which would contribute towards nation building in the long run.

Key themes of Khazanah Nasional's mandate as a strategic investment house include:

... Creating sustainable value
... Raising national competitiveness
... Cultivating a culture of high performance
These are to be achieved via four strategic pillars; namely:

... Legacy investments: Streamline, restructure, nurture
... GLC transformation: Increase shareholder and strategic value
... New investments: New sectors, cross border
... Human capital management: Active leadership management

According to the Malaysian authorities, the framework for change in Khazanah Nasional's mandate announced by the Prime Minister in May 2004 is within the broader context of the very important task of improving national competitiveness. This is especially pertinent in view of the increasing pressures of liberalisation and globalisation.

Khazanah is to take on a proactive role to catalyze the transformation of the Government-Linked Companies (GLC) into high-performing entities that are better prepared for a more liberalized world. GLCs are companies that have a primary commercial objective and in which the Malaysian Government has a direct controlling stake. The GLC transformation program is part of an ongoing effort by the government to drive the development of and grow the Malaysian economy by enhancing the performance of the companies under its control.

In this respect, Khazanah’s role as an active strategic investor now involves driving and creating greater shareholder and strategic value. This may involve, where appropriate, taking calculated risks on behalf of the nation in new sectors and new markets that are deemed important in terms of penetration, linkages and potential for the nation's long-term competitiveness.

4. Operations and staffing

Office location(s):
Kuala Lumpur City

Staffing:
In June 2007, Khazanah’s staffing headcount was 228 employees, up from only 33 employees in May 2004.

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88 To facilitate this transformation, the Putrajaya Committee on GLC High Performance (PCG) was set up. http://www.pcg.gov.my. Its principal mandate is to design and implement comprehensive national policies and guidelines, and subsequently to oversee the execution of these policies and guidelines.
5. Investment policy

Investment guidelines:
Khazanah’s investment policy is best defined by its mandate (as stated above), and its investment practice (as described below).

Recent activities and current holdings:
In May 2008, Khazanah announced that it was forming a joint venture with the Dubai Banking Group and Asia Capital Reinsurance to establish the world’s largest retakaful group, capitalized at $300 million and operating in Kuala Lumpur and Dubai. (Retakaful is an Islamic financial instrument similar to reinsurance.)

Khazanah’s investment portfolio is heavily concentrated on Malaysia, which accounts for 91% of the total. Outside of Malaysia, Khazanah holds investments in 12 Asian countries (notably, Indonesia, India, China and Singapore), and also Saudi Arabia, the UAE, New Zealand and the UK (Proton, the Malaysian national carmaker). By sector value, the main areas of investment are utilities (some 24% of the portfolio), media and communications (22%) and infrastructure and construction (18%).

Among Khazanah’s most prominent holdings include the following:
Telekom (Telekom Malaysia Bhd); Tenaga Nasional (Tenaga Nasional Bhd), the largest Malaysian electricity utility; CIMB Group, Malaysia’s second largest financial services provider; MAS (Malaysian Airline System Bhd), Malaysia’s national air carrier; PROTON (Proton Holdings Bhd), the leading Malaysian national car manufacturer, which has a dominant market share of the local automotive market; and Tradewinds Hotels and Resorts (Tradewinds Hotels and Resorts Sdn Bhd), a Malaysian hotel management and operation company.
Figure 9. Khazanah: Major Investment Holdings by Industry

Source: Khazanah website.
KOREA: Korea Investment Corporation (KIC)

1. Fund name, size and history

*Name:* Korea Investment Corporation (KIC)


*Fund size:* $20 billion
Fund size expected to rise to $30 billion in the near future.

*Date established:* July 2005
KIC’s first investment was launched in November 2006.

*History:
KIC was established under the Korea Investment Corporation Act. It was launched with a view to help stimulate the development of a stronger asset management industry in the country.

KIC is to some extent modeled on, or at least influenced by, Singapore GIC. A spokesman for KIC has stated that “We benchmarked GIC when we prepared for KIC’s launch”.89

2. Source of funding

*Source:
Initially and to date, KIC manages $20 billion derived from two distinct sources: $17 billion of foreign exchange reserves from the Bank of Korea, and $3 billion of the foreign exchange stabilization fund from the Ministry of Finance and Economy.90 Recently, KIC has announced that it will receive from the Government a further $10 billion allocation of funds.91 The Government plans to increase assets of the fund to $50 billion by 2010.

*Borrowed funds:
KIC does not employ borrowed funds. In principle, KIC may employ a variety of financial instruments as specified in the Investment Management Agreement between KIC and its client (i.e. either the Bank of Korea or the Ministry of Finance and Economy). It would appear that borrowed funds are not an approved instrument.

89 Source: Reuters August 1, 2007.
90 From January 1, 2007, KIC may also manage monies allocated from funds specified under the National Finance Act.
3. Governance and mandate

Ownership:

KIC is a government-owned investment management company, specializing in overseas investments. The funds that KIC manages are not owned by KIC, but merely entrusted to it. The capital contribution for KIC from the government is 1 trillion won. Paid-in-capital to date has been 100 billion won.

In order to maximize efficiency of its investments, KIC has been designed to be run commercially and independently. The Korea Investment Corporation Act emphasizes and ensures KIC’s independence with regard to both its organization and its investment management. In part, this is ensured by the high proportion of civil members on the Steering Committee (see below).

<table>
<thead>
<tr>
<th>Name</th>
<th>Affiliation</th>
<th>Terms</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-June Kim</td>
<td>(Chairman) Professor, Department of Economics, Seoul National University</td>
<td>Aug. 20, 2007~Aug. 19, 2009</td>
</tr>
<tr>
<td>Jaeuk Khil</td>
<td>Professor, Department of Business Administration, Hanyang University</td>
<td>Aug. 20, 2007~Aug. 19, 2009</td>
</tr>
<tr>
<td>Young Won Yoon</td>
<td>Senior Corporate Advisor, Samsung Investment Trust Management Company</td>
<td>Nov. 7, 2006~Nov. 6, 2008</td>
</tr>
<tr>
<td>Sung Hwan Shin</td>
<td>Associate Professor, College of Business Administration, Hongik University</td>
<td>Aug. 20, 2007~Aug. 19, 2009</td>
</tr>
</tbody>
</table>

Source: KIC website

Governance (including Management)
KIC’s highest governing body is its Steering Committee. The Steering Committee sets basic business policies, reviews management performance, and deliberates and resolves matters pertaining to mid-and long-term investment policies, etc. The Committee is composed of not more than twelve members, including one chairman (currently there are 9 members). The Committee includes the President and CEO of KIC, representatives of the institutions that have entrusted assets to KIC, and six civil members with terms of two years. The Chairman is elected from among the civil members. The current President and CEO is Mr. Serck-Joo Hong and its Chief Investment Officer is Mr. Guan Ong. KIC also has a Board of Directors that consists of the KIC President and directors. Roughly speaking, the Board of Directors resolves any matters that might otherwise be deliberated and resolved by the Steering Committee.

KIC has undertaken to enhance its level of transparency by disclosing its financial statements, mid- and long-term investment policies, total amount of assets under management (AUM) and rate of return, composition ratio and rate of return for each asset class.

*Figure 10. Organizational Chart for the Korean Investment Corporation (2008)*

Source: KIC website

*Mandate (both financial and non-financial):*
KIC is mandated to manage part of Korea’s foreign exchange reserves and other public funds by investing in a variety of financial assets in the international financial markets.
As noted above, KIC was launched with a view to help stimulate the development of a stronger asset management industry in the country. The Korean government expects KIC to attract foreign financial institutions to Korea, and accelerate the transfer of financial knowledge and global best practices to the local managers. In line with its mission, KIC will strive to contribute toward further developing the asset management industry in Korea.92

4. Operations and staffing93
Office location(s): Seoul

Staffing:
KIC does not state the number of staff employed, but it seems likely to be less than 100 persons. KIC may re-entrust the entrusted assets to domestic or overseas asset management companies, i.e. KIC may use external managers. Generally, KIC is obliged to manage the assets in foreign currencies (as opposed to holding Korean won denominated assets).94

5. Investment policy
KIC’s investment objective is to achieve a stable and continuous return exceeding the benchmark within an appropriate level of risk.

Investment guidelines:
KIC’s investment principles are:

... To minimize the risks from individual markets and assets through portfolio diversification
... To exercise proper flexibility to seize investment opportunities actively as they occur, while pursuing a sustainable increase in return under prudent and responsible asset management policies.

KIC’s asset classes may include securities (including stocks and bonds), foreign currencies and derivatives. Specific asset classes are those specified in the Investment Management Agreement between KIC and its client.

92 Source: KIC website.
93 Media reports suggest that there could be significant turnover in the senior management ranks of several funds with government appointees, possibly including KIC. This follows the gains by the Grand National Party (GNP) in February and April elections. Source: Business Week, April 28, 2008.
94 It would appear that KIC already employs external managers: its website lists a number of KIC staff whose job it is to deal with external managers.
Recent activities:
KIC investment operations started recently (November 2006) and it has not released details of its investments as yet.
1. Fund name, size and history

Name: Timor-Leste Petroleum Fund

Website: Banking and Payment Authority of Timor-Leste:
http://www.bancocentral.tl/en/

Fund size: $3 billion (this is the expected size by end 2008)
At end 2007, the Fund’s balance was a little in excess of $2 billion.

Date established: 2005

History:
The formation of the Petroleum Fund was announced by the government in August 2005. The Fund was then built up from oil and gas revenues, exceeding $1 billion by late 2006. Revenue has been enhanced by the Bayu-Undan project, a gas field.

2. Source of funding

Source: Oil and gas revenues

Borrowed funds:
None known.

3. Governance and mandate

Ownership:
The Government of Timor-Leste (East Timor)

Governance:
The Minister of Planning and Finance is responsible for managing the Fund. Management of the Fund has been delegated by signed agreement to the Banking and Payment Authority.

Mandate (both financial and non-financial):
No explicit mandate is known. There is a desire on the part of the government to earn returns higher than those from US Treasuries, in order to help rebuild the economy.

4. Operations and staffing

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95 Democratic Republic of Timor-Leste, sometimes referred to as East Timor.
Office locations:
Dili, Timor-Leste (East-Timor)

Staffing:
President Ramos-Horta has stated that the Fund may hire fund managers to diversify its US Treasury holdings into better performing assets.\textsuperscript{96} From this, one can infer that current investment practices are rudimentary.

5. Investment policy

Investment guidelines:
The Fund currently can invest only in US and other sovereign debt instruments.

\textsuperscript{96} Source: Thomson Reuters, May 27, 2008.
KIRIBATI: Revenue Equalization Reserve Fund

1. Fund name, size and history
   Name: Revenue Equalization Reserve Fund

   Website: Ministry of Finance & Economic Development website:
   http://www.mfep.gov.ki/

   Fund size: Market estimates vary between $400 million and $520 million.

   Date established: 1956

   History:
   In 1956, Kiribati (then the Gilbert Islands) was under British Administration. Phosphates were a finite (non-renewable) resource. Consequently, the administration placed a levy on phosphate exports, and placed the revenue in an equalization reserve fund, i.e. a fund designed to produce investment income.

2. Source of funding
   Source: Phosphates: guano (bird manure) mined for fertilizer.
   It would appear that the Fund can be used to finance budget shortfalls.

   Borrowed funds:
   None known.

3. Governance and mandate
   Ownership:
   Government of Kiribati.

   Governance:
   Information on governance and management of the Fund has not been found. It would appear that the Fund falls under the purview of the Ministry of Finance & Economic Development.

   Mandate (both financial and non-financial):
   To provide financing for domestic enterprises

4. Operations and staffing
Information on operations and staffing of the Fund has not been found.

5. Investment policy
The basic investment objective is to maintain real per capita value of the Fund over time.

*Investment guidelines:*
The Fund is managed in accordance with a general rule of prudence. As of 2001, it appears that the Fund was invested entirely in offshore funds.
MONGOLIA: Mongolian Development Fund

1. Fund name, size and history

Name: Mongolian Development Fund

Website: Ministry of Finance website is http://www.mof.gov.mn/

Fund size: Financial portfolio in the range $11.2 to $19.8 million.
Initially, in 2008, total Fund resources have been forecasted to reach Tögrög 363 billion, or about $313 million (at current exchange rates). A more recent statement from the Ministry of Finance places the amount at Tögrög 366 billion.

Of this amount, Tögrög 235 billion would be devoted to investment; Tögrög 105 billion to a social protection program (cash allowance through the child money program); and Tögrög 13 billion [sic] would remain in the Development Fund account, i.e. as financial portfolio investment.

The numbers cited here (source: footnote below) do not add up: Tögrög 23 billion is the balance available for portfolio investment, if the other figures are correct. Taking a range of Tögrög 13 – 23 billion gives a $ equivalent range for financial portfolio investment of $11.2 – $19.8 million (at current exchange rates).

Date established: February 2007

History:
Because of the boom in global copper and gold prices, Mongolia introduced a windfall tax in June 2006. The tax is levied in respect of copper concentrate and gold on the difference between, in effect, market price levels and a standard level, representing production costs. To manage these revenues, the Mongolian Development Fund was established by law in February 2007.

2. Source of funding

Source:
The sources of funding are:

... Budget revenues derived from the windfall tax.

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97 The description of the Mongolian Development Fund is largely based on material produced by World Bank staff.
... At the discretion of Parliament, an allocation from the previous year’s budget surplus, if any, over and above the windfall tax revenues. The allocation may be up to 100% of the budget surplus (net of windfall tax revenue).

... The unspent balance of the contingency fund.

... Interest earnings on the Development Fund account may be retained.

In addition, there may be other (miscellaneous) revenues.

**Borrowed funds:**
None known. Projects funded by the Development Fund, however, will typically be funded in part by borrowings.

**3. Governance and mandate**
The Mongolian Development Fund was established in order to manage the fiscal revenues accruing from the windfall tax (noted above) on copper and gold production.

**Ownership:**
The Government of Mongolia is the owner of the Development Fund. By law, the Ministry of Finance must incorporate the Fund’s audited operations in the government’s annual financial statements.

**Governance:**
The Development Fund is, in effect, an instrumentality of the Ministry of Finance. Any specific allocations of resources must be proposed by the Executive branch of government and approved by Parliament. Development Fund resources are held in a special (i.e. segregated) account at the Treasury, and interest earnings are placed in the Treasury Single Account.

**Mandate (both financial and non-financial):**
The Development Fund has a twofold mandate:

... To finance specific spending (developmental) priorities.

... To fulfill a budget stabilization objective.

By law, the windfall tax revenues should be apportioned in equal one-third parts to three objectives—domestic investment, social protection, and stabilization—as follows: (i) domestic investment; (ii) social protection programs to support children and families; (iii) savings that would compensate for “revenue loss due to force majeure conditions”. Any allocation of fiscal surplus net of windfall taxes (see above) should be spent on public investment in the current year.
4. Operations and staffing

Office location:
Ulaanbaatar

Staffing:
The Development Fund employs a Manager and heads of spending units. No further information has been found on staffing.

5. Investment policy

No information has been found on investment guidelines for financial portfolio investment.

Public investment decisions are guided by various considerations (such as the government action plan, regional development, youth activities, and investment efficiency), and are embodied in the Public Investment Program, which comprises a list of projects for each ministry.
PART III: REFERENCES


Davos. 2008. *Panel discussion on sovereign wealth funds.* Panel discussants were: Mohammad Al-Jasser, Vice Governor, Saudi Arabian Monetary Agency; Bader Al-Saad, Managing Director, Kuwait Investment Authority; Kristin Halvorsen, Finance Minister of Norway; Richard Fuld, CEO, Lehman Brothers; Robert Kimmitt, Deputy Secretary, US Treasury; Alexei Kudrin, Finance Minister of Russia; Stephen Schwarzman, Chairman and CEO, Blackstone Group; Lawrence Summers, Charles Eliot Professor, Harvard University. Bloomberg video, dated January 23, 2008. Bloomberg.


Gunn, Geoffrey C. Brunei’s Fund of Wealth and Scandal. Asia Times Online, April 1, 2008


Sovereign Wealth Fund Institute, 2008. www.swfinstitute.org


Sovereign Wealth Fund Institute: Website at http://www.swfinstitute.org/


Temasek Holdings (2007), Temasek Review 2007 Creating Value

Temasek Holding (2006), Temasek Revies 2006 Managing For Value


**Memo item: websites**

**Brunei**

*Name:* Brunei Investment Agency (BIA)


**China**

*Name:* China Investment Corporation (CIC)


**Kiribati**

*Name:* Revenue Equalization Reserve Fund


**Korea**

*Name:* Korea Investment Corporation (KIC)


**Malaysia**

*Name:* Khazanah Nasional Berhad


**Mongolia**
Name: Mongolian Development Fund
Website: Ministry of Finance website is [http://www.mof.gov.mn/](http://www.mof.gov.mn/)

Singapore
Name: Government of Singapore Investment Corporation (GIC)

Name: Temasek Holdings

Timor-Leste (East Timor)
Name: Timor-Leste Petroleum Fund
Website: Banking and Payment Authority of Timor-Leste: [http://www.bancocentral.tl/en/](http://www.bancocentral.tl/en/)