

A full-page background image showing the silhouettes of two fishermen on a boat. They are positioned on a wooden structure, possibly a mast or part of the rigging, against a dramatic sunset sky filled with orange and yellow clouds. The boat's rigging and nets are visible, extending from the top towards the bottom of the frame. The water is visible at the very bottom.

Risks & Opportunities

TEMASEK REVIEW 2008

**TEMASEK
HOLDINGS**



“For the first time, our net investments for the year outside Asia exceeded our net investments in Asia.”

S DHANABALAN
Chairman

To My Fellow Stakeholders

While we started the last financial year preparing to stay on the sidelines, it turned out to be another active year for us.

The confluence of a US housing bubble correction, the underpricing of risks by lenders and financial institutions, and the ensuing credit crisis led to the sudden demise of Bear Stearns in the US towards the end of March 2008. The shock failure of Wall Street's fifth largest broker-dealer illustrates the kind of massive adjustments needed to deal with the global credit crisis, with bold and innovative measures by the US authorities to stem a dangerous systemic failure.

For the last two years, we have been concerned over the prospects of a major correction, but did not anticipate the speed and depth of the dislocation. A total of US\$400 billion was written off by banks around the world in the space of one year since June 2007. Its epicentre in the capital of global finance, New York, also surprised us.

The fallout of the credit crisis affected markets worldwide, and will continue to dampen the global economy over the next 24 months. In addition, sharply escalated oil and food prices are beginning to test inflation expectations.

We had a busy year, with some S\$32 billion of new investments and S\$17 billion of divestments, compared to S\$16 billion and S\$5 billion respectively the previous year. On a gross basis, we made just under S\$17 billion of investments in Asian economies, and S\$15 billion outside Asia.

For the first time, our net investments for the year outside Asia exceeded our net investments in Asia, with S\$10 billion

or 68% outside Asia and a balance of S\$5 billion or 32% in Asia. In the previous five years, we made a total net investment of S\$26 billion in Asia, and only S\$1 billion into non-Asian economies.

Group net profit doubled from the year before to S\$18 billion on the back of healthy realised gains from our divestments as well as the strong operating performance of our blue chip portfolio companies.

S\$18b

Group Net Profit doubled

Delivering Shareholder Returns

Our portfolio grew almost 13% as at 31 March 2008 from S\$164 billion to S\$185 billion on a marked-to-market basis, or a healthy 24% growth in US dollar terms from US\$108 billion to US\$134 billion. Shareholder equity increased by 26% to S\$144 billion over the same period.

Part of the increase in portfolio size came from a net fresh capital injection of S\$10 billion from our shareholder as part of its asset allocation rebalancing. On a cumulative basis Temasek continues to be a net contributor in dividends to our shareholder.

Excluding new capital, we delivered a modest Total Shareholder Return (TSR) of 7% by market value, including dividends, and a solid 17% by shareholder funds for the year.

Our TSR since Temasek's inception in 1974 remains a healthy 18% by market value and more than 17% by shareholder funds.

7%

Total Shareholder Return
for the year

Economic profit or Wealth Added (WA) for the Group touched a negative S\$6 billion for the year. This measures our returns above a risk-adjusted hurdle on the market value of our assets at the start of the year and excludes new capital. With the sharp global corrections, our direct investments delivered negative WA as at 31 March 2008. Further, our long-term blue chip investments just about met their risk-adjusted cost of capital for the year, on an aggregate basis. Our five-year cumulative WA was a healthy S\$60 billion above our risk-adjusted cost of capital hurdle.

Risks and Opportunities

The unfolding credit crisis in the US continues to wend its way across other markets, including Europe and Asia. The risks of a major systemic failure and meltdown in the US have been largely averted by swift and groundbreaking regulatory and policy responses. However, the risks of stagflation have become more apparent with the twin bogeys of high oil and food prices.

While uncertain in the short term, the environment also presented various long-term opportunities.

In December 2007, we anchored Merrill Lynch in its capital raising exercise with an investment of about US\$4.9 billion for approximately 9% of Wall Street's third largest broker-dealer. In July 2008, we invested a further US\$3.4 billion in the company, of which US\$2.5 billion was from a reset payment from Merrill and US\$900 million was new capital. With well-established franchises in wealth management and global markets, Merrill presents strong growth potential for the longer term, though near-term strains in the economy remain.

Over in the UK, we also invested £975 million (approximately S\$3 billion or US\$2 billion) in Barclays PLC and increased our stake in Standard Chartered Bank to about 19%.

These moves tie in with our strategy to invest in companies with strong comparative advantages and sound leadership.

We also took advantage of the recent market dislocations to invest in new asset classes including commodities, fixed income, credit products and distressed assets. We continue to increase our exposure globally, including to new markets such as Russia and Latin America, through funds and direct investments.

Negative S\$6b

Group Wealth Added for the year
below our risk-adjusted cost of capital

At the same time, we actively monetised and rebalanced our portfolio, as we anticipated a massive structural adjustment.

During the year, we divested our stake in China COSCO Holdings. We also entered into an agreement to divest our indirect stake in PT Bank Internasional Indonesia. However, the buyer was not able to complete the transaction as scheduled on the closing date of 31 July 2008.

S\$60b

Five-year cumulative Wealth Added above risk-adjusted hurdle

In March 2008, we sold Tuas Power for S\$4.2 billion to SinoSing Power, a 100% subsidiary of leading power group China Huaneng, via a competitive international bidding process. Tuas Power generates nearly one third of the electricity needs of Singapore.

The sale of Tuas Power marked a 14-year journey from 1994 when Temasek prepared to take over the corporatised power generating and grid assets. Since then, much thought and effort have gone into a patient restructuring of the power generating sector with various independent and competing companies such as Tuas Power. We cooperated closely with the relevant Singapore government agencies to institutionalise a sustainable, robust and market-oriented regulatory framework for the electricity market. The power generation market has operated on a soundly regulated but highly competitive basis since 2003.

This successful evolution from a state-run monopoly into independent commercial operators is due in no small measure to the enlightened support of the unions involved. Their leaders and members understood the

rationale for a forward-looking framework of a competitive energy market for Singapore.

We expect to complete the sale of our remaining two power generating companies over the next 12 months. This will complete our undertaking to help establish an open, robust and competitive electricity market in Singapore.

Outlook

Volatility remains high. The credit crisis is not over – we expect to see further contagion in the real economy in the US, Europe and also Asia over the next 24 months.

On the other hand, bold policies have averted a serious meltdown but pushed up the spectre of inflation. Growth will be muted as excesses are wrung out. There may be opportunities as imbalances are corrected.

The credit crisis is not over – we expect to see further contagion in the real economy in the US, Europe and also Asia over the next 24 months.

We are concerned with the emerging risks of stagflation. This presents huge socio-political as well as economic risks in the next three to five years. Opportunities may be limited in such a scenario.

Sustainable growth over the longer term, however, will require some difficult decisions by policymakers, regulators and political leaders. These include the removal of price controls or energy subsidies, which have created highly distortive incentives and misallocation of capital, endemic to many

To My Fellow Stakeholders

fast-growing economies. The sooner these difficult decisions are taken, the faster and less painful will be the eventual dislocation and repositioning to a more sustainable long-term growth trajectory.

We will continue to broadly focus on Asia with its long-term trend of growth and development in the next decade or two. In addition, we are setting up offices in Mexico and Brazil to deepen and broaden our exposure to Latin America.

Engaging the Wider Community

We continue to share our experience freely with a view to promoting dialogues on corporate governance.

We engaged in international discussions about sovereign wealth funds (SWFs). In particular, we shared extensively with lawmakers and officials in the US and the EU, our philosophy as an independent, professionally managed and commercially disciplined investment firm, with a strong ethos of integrity, good governance and performance. We supported the International Monetary Fund-led International Working Group of Sovereign Wealth Funds in the drafting of the Generally Accepted Principles and Practices for SWFs.

We will continue to broadly focus on Asia.

Closer home, the Temasek Alumni Network was launched in January 2008, bringing together more than 300 former Board directors and staff as members.

We are also very pleased to note that the Temasek Foundation has had a fruitful and satisfying first year since its establishment in May 2007. A total of 14 programmes with clearly stated criteria and outcomes were supported across Asia. Commitments of some S\$16 million were made in line with the Foundation's mandate of building people through education, healthcare and research, building bridges among diverse peoples, and building institutions through good governance and ethics. These and other pro bono beneficiaries are supported by a donation of S\$500 million that had been endowed to the Temasek Trust last year.

S\$16m committed

In 14 Temasek Foundation programmes across Asia

On our part, we remain firmly committed to supporting Asia's development by extending our friendship, sharing our experiences, and strengthening ties with our friends and partners.

Tribute to Mr Sim Kee Boon

I would like to take this opportunity to pay a special tribute to the late Mr Sim Kee Boon.

Kee Boon was a Board member of Temasek, a position he had held since the turn of the millennium. Among his various responsibilities, he was also a board member of Fullerton Financial Holdings, a member of the Temasek Advisory Panel and a founding trustee of the Temasek Trust.

As one of the stalwarts of modern Singapore, responsible for building and pushing the boundaries of excellence, including the world-renowned Changi International Airport and the Tanah Merah Country Club, Kee Boon was also instrumental in the growth and success of the Keppel Group. Upon his retirement from active executive roles, he joined the Temasek Board where his vision, astute judgement and acumen greatly benefited Temasek. His insightful advice and wise counsel provided the compass by which we set our course, and shape our future directions.

His passing is a great loss to both Temasek and to Singapore. He will be remembered as a man of utmost integrity, and a gracious, thoughtful and incisive leader.

Board Changes

We welcome Marcus Wallenberg as a Board member. Marcus joined us on 8 July 2008. He has a distinguished career in the global business community and has been a firm advocate of international trade and investment. His knowledge and experience will be invaluable to Temasek as we chart our course ahead.

In Appreciation

Temasek is the embodiment of the unwavering dedication and contributions of its Board, management and staff, past and present. I extend my heartfelt thanks to them for giving so much of their time and effort towards ensuring the success of the firm.

To the boards, management and staff in our portfolio companies, I commend you for your foresight, commitment, and success in building outstanding companies which continue to deliver sustainable growth and results.

You have been the foundation of Temasek's sterling performance over the decades.

I also wish to thank members of the Temasek Advisory Panel for their insights and guidance. They have enabled us to create and add value to the companies and communities we invest in.

I am also grateful to the members of the Temasek International Panel. Particularly in a time of market turbulence, their views and insights have been helpful in guiding the direction of Temasek. Some like Leon Davis and Lucio Noto have stepped down, while others have answered the call of public duty, like Dr Han Seung-Soo who became the Prime Minister of the Republic of Korea. We will miss their frank input and perspectives. We are also happy to welcome new member Lee Raymond.

Finally, I wish to express my deep appreciation to our many other stakeholders – our shareholder, bondholders, business partners and friends, advisors, unions, governments and regulators around the world, as well as interested members of the public. We look forward to your continued support so that we may, together, contribute to a richer and more vibrant global community.



S DHANABALAN
Chairman
August 2008