

LETTER TO SHAREHOLDERS



PETER SEAH LIM HUAT (Left)
Chairman

TANG KIN FEI (Right)
Group President & CEO

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Dear Shareholders,

2006 has been an exceptional year of performance and transformation for SembCorp Industries.

PERFORMANCE

We achieved record financial results. Our profit after tax and minority interest (PATMI) grew 240% over the previous year to S\$1.03 billion, while turnover for the Group increased to S\$8.1 billion. PATMI before exceptional items from the Group's continuing operations grew 52% to S\$371.9 million driven by the robust growth of our Utilities and Marine & Offshore Engineering businesses.

Excluding exceptional items, our return on equity was 18% compared to 14% in 2005 and our return on total assets was 8% compared to 6% in the previous year. Our economic value added was a healthy S\$924.7 million.

Beyond the delivery of a solid financial performance, significant milestones were further achieved in the past year to better position ourselves for the future. Our aim is to deliver lasting value and attractive returns to our shareholders. To this end, bold steps were taken to focus SembCorp on businesses that are market leaders and capable of delivering quality earnings and sustainable growth.

In 2006, both our Logistics and Engineering & Construction businesses

were divested. SembCorp Logistics was sold to Australia's Toll Holdings for S\$793 million, and SembCorp Engineers & Constructors was divested to Punj Lloyd of India for S\$38 million. Progress was also made towards streamlining our operations, with the rationalisation of our industrial park and leisure investments on the Indonesian Riau Islands of Batam and Bintan. These investments were consolidated under Gallant Venture, which was subsequently listed on the Singapore Exchange in June 2006.

Since our formation in 1998 from the merger of Singapore Technologies Industrial Corporation and Sembawang Corporation, our divestment programme has generated more than S\$4.3 billion of proceeds. Now substantially completed, it has undoubtedly unlocked significant value for our shareholders. More importantly, we believe that our management expertise and capital can now be focused on businesses that will enable SembCorp to continue delivering value and growth for many years to come.

In 2006, we reached a full and final settlement of the dispute between Sembawang Corporation and Allseas, relating to the conversion of the pipe-laying vessel *Solitaire*. Full payment was made in April 2006.

We believe that our businesses can deliver returns that are secure and growth that is sustainable in the long term.

STRATEGY

SembCorp is now a focused utilities and marine group, poised for growth, with strong business fundamentals in each of our businesses. Coupled with the reliability associated with the SembCorp brand and a disciplined approach towards investment and growth, we believe that our businesses can deliver returns that are secure and growth that is sustainable in the long term.

In our **Utilities** business, we have established a niche as a global leader for the provision of centralised utilities and services to multiple customers in energy intensive industry clusters, such as chemical and petrochemical hubs. We aim to replicate this model in key markets across the globe through strategic partnerships with our international customer base. In addition, we participate in projects that provide secure offtake and that give us potential to grow. Our strategy of establishing and growing beachheads in target markets is bearing fruit. The exceptional strength and growth of our facilities in Singapore and the UK reflect what we believe can be achieved in each of our new profit centres.

Backed by a solid 43-year track record and a global network of strategically located yards, our **Marine & Offshore Engineering** business is a global leader with a portfolio that encompasses various segments of the value chain in the global marine and offshore industry. From ship repair, shipbuilding, ship conversion, rig repair and rig building to topsides fabrication and offshore engineering,

we have a comprehensive portfolio that can support growth and healthy margins. For example, even as we enhance our capabilities in delivering offshore production facilities, we continue to grow and enlarge our baseload earnings from ship repair by serving and satisfying the needs of our customers. As we continuously improve and develop proprietary technologies, optimise production processes and enhance capacity, the strategies we adopt and the investments we make are all designed to achieve one aim – sustained growth and the maximisation of returns over the long term.

Our **Industrial Parks** business performed well. Over the years, SembCorp Parks Management has established its brand name in developing, marketing and operating industrial parks in China, Indonesia and Vietnam. Leveraging on our industrial park management and investment promotion expertise, more than 370 multi-national investors have been attracted to our parks to-date. We see growing potential for industrial park development in Asia, and we believe we can leverage on this business opportunity to grow.

The performance of our **Environmental Management** unit in 2006 was disappointing due to competitive pressures in its municipal waste collection business in Singapore. Nevertheless, we continue to nurture this fledgling business. We have intensified our focus on the development of pre-disposal treatment methods and waste-to-resource businesses. Appropriate

steps have also been taken to streamline the unit's operations.

We believe that we have opportunities for growth in our businesses. Backed by a strong balance sheet and favourable industry prospects, our company is in a better position than it has ever been to seize opportunities and grow.

STATUS AND OUTLOOK

In 2006, we continued to make progress in building a foundation for long-term growth.

In November, we completed the acquisition of 40% of an independent water and power plant in Fujairah (Fujairah I) in the UAE. Our first power and water investment in the Middle East, the project comprises the acquisition, ownership, operation and maintenance of an existing 535 megawatt power and 100 million imperial gallons per day seawater desalination plant as well as the expansion of a further 225 megawatts of power generation capacity. Fujairah I not only affords us a base from which to grow our utilities business in the booming Gulf region, but the success of our bid following a highly competitive bidding process testifies to our strong operating track record and competitive position in the global utilities arena. Together with our existing operations in China, Singapore, the UK and Vietnam, this strategic beachhead in the Middle East will provide the momentum for future growth and expansion of our utilities business.

During the year, good progress was also made in achieving organic growth of our Utilities' operations in Singapore and the UK. In Singapore, new contracts worth a total of S\$68 million per year were clinched. We also expanded our demineralised water, high-grade industrial water and wastewater

treatment capacities in tandem with customer demand. In terms of industrial wastewater treatment, our facilities worldwide now have a combined capacity of around 40,500 cubic metres per day, with a further 30,000 cubic metres per day in development. In the UK, new utilities and services contracts amounting to S\$136 million were secured, while Wilton 10, our 30 megawatt biomass power plant, is on schedule to start operation in the second half of 2007.

In August, we also undertook significant restructuring within the Group through the sale of SMOE and Sembawang Bethlehem to SembCorp Marine and its subsidiary Sembawang Shipyard. In enabling SembCorp Marine to optimise the use of the land at Admiralty in Singapore and on Batam Island in Indonesia, as well as the resources of SMOE, we are now able to operate more efficiently and seize more opportunities in rig building and semi-submersible projects as well as offshore engineering. With a credible track record in the conversion of Floating Production Storage and Offloading (FPSO)/Floating Storage Offloading/Floating Production Units, mega FPSO solutions, topsides and fixed platforms, we are well positioned to participate in the expected growth of the offshore production market. In addition, ship repair demand is expected to be strong especially in the specialised market of liquefied natural gas/liquefied petroleum gas tankers, very large crude carrier tankers and container vessels.

In September 2006, our Industrial Parks business celebrated the tenth anniversary of Vietnam Singapore Industrial Park (VSIP). Leveraging on its success, we embarked on the development of VSIP II, our second industrial park in Vietnam. During the year, our Environmental Management unit also

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invested in the waste-to-resource business when we partnered China's largest lead recycler, Jiangsu Chunxing Alloy in March to undertake the recovery and sale of processed lead from used lead acid batteries to battery manufacturers.

Barring unforeseen circumstances, the Group's overall operating performance in 2007 is expected to be better than that of 2006 on a comparable basis, which excludes net profits arising from exceptional items in 2006.

SHAREHOLDER RETURNS

The year has been rewarding for our shareholders. A total of S\$264.6 million, or 57% of the gain arising from the divestment of our stake in SembCorp Logistics, was returned to shareholders via a capital reduction of 15 cents per share paid in August.

In addition, our Board of Directors is proposing a final gross dividend of 28.9 cents per ordinary share (net: 28.0 cents) for 2006, amounting to five times the net dividend paid in 2005. This comprises a 12.9 cents per share ordinary dividend (net: 12.0 cents), representing a payout of 56% of net profit from operations and a 16.0 cents per share special dividend (1-tier). The special dividend together with the capital reduction (tax exempt) paid in August accounts for a payout of 84% from exceptional profits.

Together with a 37% appreciation in our share price during the year, the total

shareholder return (TSR) for 2006 was 44%, relative to the benchmark Straits Times Index's TSR of 27%. At the close of the year, our market capitalisation stood at S\$6.8 billion, a S\$2.0 billion increase compared to S\$4.8 billion at the end of 2005.

Our balance sheet is healthy and the Group's business models generate strong operating cash flow. As such, we believe that we remain well placed to seize anticipated growth opportunities while continuing to return value to our shareholders through a progressive yet sustainable dividend policy. We also continue to review our capital structure and dividend policy with the aim of maximising value for our shareholders.

SUSTAINABILITY

It is worth emphasising that the growth we are committed to achieving is growth that is sustainable over the long term.

This means that it is vital that we maintain a balanced approach to achieving growth. First, even as we pursue expansion opportunities, we will continue to follow strict investment guidelines and maintain financial discipline. This will not only assist in focusing our project development efforts but will also ensure competitive returns and the management of risk. Second, it is our firm belief that high standards in governance and corporate responsibility go hand in hand with outstanding performance. It is only our adherence to a rigorous system

of policies, practices and internal controls that will ultimately enable us to deliver value and sustainable growth to our shareholders. At all levels, the commitment to good corporate governance must continue.

Our responsibilities also extend to society at large. In 2006, the cornerstone of our ongoing community efforts, the Trailblazer-Wong Kok Siew Fund, continued to support a wide range of programmes in Singapore for children and education as well as stroke victims. We also funded scholarships for children in Vietnam and contributed to the setting up of Ho Chi Minh City's first public children's library.

A NOTE OF THANKS

Building on these proven foundations, we believe that we can approach the future with confidence. This is not only because SembCorp is a robust and growing enterprise, but because we know that we can depend on the knowledge, skill, passion and commitment of SembCorp's employees, who provide the means for our development, performance and prospects. On behalf of the Board, we would like to pay tribute to their achievements in 2006 and thank them for the value they have created.

On February 14, 2006, Lua Cheng Eng, a Director since 1998, stepped down as Director and Chairman of the Audit and Risk Committees. He was succeeded as Chairman of the Audit and Risk Committees by Richard Hale, OBE, who is an independent director. We have benefited immeasurably from Cheng Eng's astute and judicious counsel and would like to record our deep appreciation to him. We would also like to thank Dr Vichit Suraphongchai and Colin Au Fook Yew, who resigned from our Board on May 8, 2006 and November 6, 2006 respectively,

for their contributions to SembCorp.

Our appreciation must also go to our customers and partners for their support. The entire SembCorp organisation is driven by a strong, shared commitment to be the partner of choice for customers in order to create value and sustainable growth for the people who trust us with their investments. With their support, we are confident that the coming years will see SembCorp creating more value and delivering sustainable growth. We look forward to an exciting future together.



PETER SEAH LIM HUAT
Chairman,
February 16, 2007



TANG KIN FEI
Group President & CEO,
February 16, 2007