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* **Temasek: China banks in which it invested are well capitalised**

* Foreign banks are cutting holdings in China banks

* Temasek: China structural change may yield opportunities

By Saeed Azhar and Anshuman Daga

SINGAPORE, July 4 (Reuters) - Singapore state investor Temasek Holdings Pte Ltd stood by its investments in China's top banks on Thursday, saying they were well equipped to cope with disruptions like the recent interbank credit crunch.

It also said structural change in China could yield further investment opportunities, both in state-owned enterprises and private companies.

The sovereign wealth fund's relatively positive outlook for China's long-term prospects comes at a time when foreign investment banks are cutting their direct exposure to the country's banking sector and when last week's cash crunch in the interbank market has unnerved investors.

The squeeze - aimed at punishing Chinese banks for risky lending - could be a preview of greater instability to come if China's leaders push ahead with liberalising interest rates and capital controls, some traders believe.

"My sense is China is still a real risk for Temasek," said Melvyn Teo, Professor of Finance at Singapore Management University

"The tightening of the credit in China, the increased cost of capital, and the end of the investment-led-boom will conspire to drive down the stock prices of the Chinese banks that Temasek has a significant stake in," he said.

Temasek - headed by Ho Ching, the wife of Singapore's Prime Minister Lee Hsien Loong - reported an 8.6 percent rise in its portfolio size to a record S$215 billion ($170 billion) in its last financial year that ended in March, helped by a rebound in Asian shares. That compared with a 2.6 percent rise in the previous year.

China accounts for 23 percent of Temasek's portfolio, the second largest region after Singapore, and much of that is in banks. It has a 7.4 percent stake in China Construction Bank which is worth about $12.3 billion and it has also invested about $2.4 billion in Industrial and Commercial Bank of China since 2012 alone.

"There is sufficient liquidity in the system, so we are not concerned about a liquidity crunch over a prolonged period," Chia Song Hwee, head of Temasek's investment group and co-head of China, told a news conference on Thursday.

"The banks that we have invested in, they are actually very well capitalised."

Foreign banks, however, are on the retreat. Goldman Sachs Group Inc raised $1.1 billion in May by selling its remaining shares in Industrial and Commercial Bank of China, ending a seven-year old investment.

"The China miracle is over," said Thomas Monaco, a managing director at Hong Kong-based independent research firm Forensic Asia Ltd.

"You just think about what's going on: most of the western firms such as Goldman Sachs, Bank of America, HSBC, they are exiting China, they are leaving. What does that tell you?" Monaco said.

Temasek's Chia stressed that the Singapore's second-biggest state investment fund was investing in China's banks long-term and as a proxy to the underlying economy.

"Our view of the economy in China, at least over the next 15-20 years continues to be positive, mainly because of the demography."

Temasek also said it plans to step up investments in the United States and Europe and is setting up offices in London and New York to support its investments. It sees opportunities in the energy, resources, life sciences, consumer and technology sectors.

Europe and North America accounted for 12 percent of its portfolio, up from 11 percent a year earlier.