Article Reprint

Stay Tuned: Sovereign Wealth Funds

By Hank Boerner

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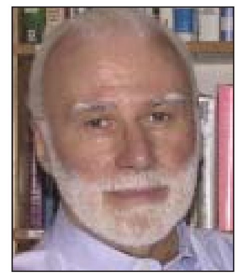
STAY TUNED

Sovereign Wealth Funds — Wealthy, Growing, Interested in the USA

BY HANK BOERNER

Looking for investors? Such as institutions, capital pools and asset managers willing to invest in U.S. equities, fixed-income, real estate, hedge funds, private equity, seed monies for emerging technologies, options and other financial instruments, even willing to buy up entire companies? Well, who isn't these days?! As corporate management and boards respond in differing ways to the ongoing credit crunch and myriad challenges posed to accessing domestic and global capital markets, a distinct class of investors has come into sharper view. You've been hearing a bit more about these institutions: they are the world's Sovereign Wealth Funds ("SWFs") and certain related entities.

SWFs are not altogether unknown to us — we have some SWFs of our own in the United States. Think of large public employee pension funds such as CalPERS (California's, the largest), New York State Common Fund, Connecticut's state employee fund, and others in their class — there are dozens of state pension funds that in effect, hold the investable wealth of sovereign U.S. states for beneficiaries current and future.



Hank Boerner

Looking beyond the U.S., we've identified and are monitoring at least 50 to 60 investment pools owned and directed by national and city-state governments around the world that could be considered SWFs. These come in a variety of sizes, and operate in very different ways. Some are very transparent — the gold standard is Norway's SWF — and some operate in near secrecy.

Definitions can vary — *what is a SWF*? The U.S. Department of Treasury, which tracks SWFs and other foreign investors, sees them as a distinct pool of investment monies funded by [foreign] governments but managed separately from the respective governments' foreign reserves. These are institutions controlled by a wide range of governments on virtually all continents and their investment strategies are as varied as the countries, cultures and economic systems in which they originate. Treasury has negotiated agreements with a few SWFs on their U.S. investment activities, especially where sensitive industries or sectors are concerned. In 2007, Congress adopted legislation that requires additional scrutiny and higher-level clearances for transactions involving foreign government control (which in effect is how SWFs are structured and managed).

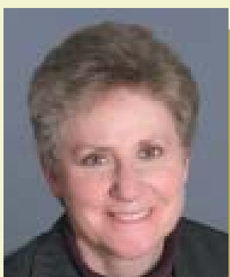
But large or small, transparent or opaque, capitalist-leaning or not, SWFs are poised to become more important investors in a broadening range of investments in the U.S. and other nations.

2009 NIRI ANNUAL CONFERENCE GENERAL SESSION SPEAKERS

Todd Buchholz

Just Announced!

Former White House Senior Economic Adviser Todd Buchholz will deliver keen insights to you in Monday's conference keynote address. A well known economist, author, and lecturer, Buchholz is one of the country's leading experts on financial markets, politics and the economy. Buchholz's books, including *New Ideas from Dead CEO's: Lasting Lessons from the Corner Office, and Market Shock* are studied around the world for their insights into cutting edge issues that shake the financial markets, politics and the economy. In addition to serving the White House, he has advised such leading firms as Microsoft, Merrill Lynch, IBM, SAP and Toyota.



Abby Joseph Cohen

The Senior Investment Strategist for Goldman Sachs and noted economist will provide thoughtful insights to attendees.

Chunka Mui

Corporate innovator Chunka Mui will share insights and help you guide your communications strategy in today's market as Wednesday's keynote conference speaker.

Author of *Billion Dollar Lessons: What You Can Learn from the Most Inexcusable Business Failures of the Last 25 Years,* Mui is also a leading consultant on strategy, innovation, and the organizational inhibitors to success. He has deep insight on the breakthrough possibilities at the intersection of business and technology. At the same time, he has pragmatic appreciation of the challenges in harnessing such opportunities. He'll inspire you to think hard about strategic opportunities in your market while at the same time offering well-grounded, sensible advice on how to maximize your chance of success.

Stay Tuned to … SWFs bargain-hunting in U.S. equities markets as share prices are at levels attractive to SWFs, which are mostly free to invest through the world's capital markets in instruments that are traded in open markets: stock indexes, common stock and corporate bonds are the easiest of SWF transactions. Some American IROs have been lately getting calls from SWF offices or their external managers to discuss long-term fundamentals of their companies and the possibilities of investment. And IROs are making the rounds of SWFs in Europe and the Middle East as they seek new investors.

Stay Tuned to … increasing direct and significant equity investments in American companies by SWFs. Remember the recent headlines? Morgan Stanley received $5 billion from the China SWF (China Investment Corporation). The United Arab Emirates (UAE) SWF — Abu Dhabi Investment Authority — bought a 4.9 percent share of Citibank. Merrill Lynch got a $5 billion infusion from Temasek Holdings, one of two SWFs in the wealthy city-state of Singapore (just before the Bank of America acquired M-L). The Blackstone Group (a leader in private equity) sold a 10 percent stake to China's SWF. Its competitor, Carlyle Group sold seven percent of the firm to Abu Dhabi. Even the clothing store, "Barney's" in New York City is owned by a SWF.

It would be hard to find large institutions anywhere in the world that have not suffered losses in the current bear market. SWFs are no exception; some are down 30 to 40 percent in this bear market. But while many institutional investors — mutual funds, hedge funds, private equity managers — may be looking forward to the day when they can replenish their investable dollars or other currencies, a number of the SWFs are very capable of accumulating cash and reserves right now, thanks to the modern era's efficient transfers of wealth. Think "natural resources," commodities like oil, gas, ores, precious stones, and other "extractable" forms of wealth. As countries like the United States, Japan and EU nations import these resources, some of the industrialized nations' wealth is transferred to other countries — to oil-producers in the Middle East or Africa or even Northern Europe.

The global oil and gas production leaders, experiencing less cash flow these days (now that crude prices have dropped significantly), may still be able to build investable pools in SWFs as U.S. dollars and euros and yen continue to flow to national treasuries of Kuwait, Saudi Arabia, Venezuela, Nigeria, Russia, Norway or other countries that can accumulate investable funds in their respective SWFs to invest outside of their respective nations.

Stay Tuned to … dramatic SWF asset growth when the global economy revives. Collectively, the Federal Reserve estimates total SWF capital is from $3.5 to $5.0 trillion in assets (stated in U.S. dollars). Abu Dhabi's SWF had almost $900 billion in assets at year-end 2008. Norway's fund, recently pumped up by increased revenues from North Sea oil sales, had just shy of $400 billion. Using year-end data, if we stay with the conservative estimates from the Chicago Federal Reserve, the $3.5 trillion of the 40 SWFs examined at year-end compared in this way to other global categories of investors: hedge funds, $1.4 trillion; the world's pension funds, $15 trillion; insurance companies, $16 trillion; and all mutual funds (investment companies), $21 trillion. Some experts predict total Sovereign Wealth Fund total pools of between $10 trillion and $15 trillion in the next decade.

THE OLDEST SWF IN THE WORLD IS KUWAIT'S; THE OIL-RICH NATION THAT SITS BETWEEN IRAQ AND SAUDI ARABIA AND ON TOP OF A SIGNIFICANT TREASURE OF OIL AND GAS RESERVES LOCATED IN FIELDS BENEATH THE SANDS.

The Federal Reserve lists the 10 largest SWFs in this order (with year-end estimated holdings): UAE's Abu Dhabi fund ($875 billion); Norway ($380B); Singapore — Government Fund ($330B); Saudi Arabia ($300B); Kuwait ($250B); China ($200B); China/Hong Kong ($163B): Singapore — Temasek ($159B); Australia ($61B); and Qatar ($60B).

Stay Tuned to … especially large SWFs that derive major funding from oil and gas. Extractable resources are very fungible to a growing number of countries around the world; as revenues for these resources rise (think of last year's oil price spikes), and as more of these resources flow to markets old and new, revenue streams flow to state treasuries, and a portion is allocated to the country's SWF.

The oldest SWF in the world is Kuwait's; the oil-rich nation that sits between Iraq and Saudi Arabia and on top of a significant treasure of oil and gas reserves located in fields beneath the sands. This 56-year-old SWF offers an example of how government investment vehicles work. The Kuwait Investment Authority manages the General Reserve Fund and Future Generation Fund, operating from offices in Kuwait City and London. These are sophisticated managers: consider that Dow Chemical Company received $4 billion funding from investor Warren Buffett ($3 billion) and the Kuwait Investment Authority ($1 billion) in recent months related to the planned acquisition of Rohm & Haas (a chemical manufacturer).

Stay Tuned to … some activist SWFs who invest in American companies and then pressure management for changes … or, divest shares and make noise about the reasons why. Norway's SWF — the Norwegian Government Pension Fund, Global — holds such multinationals as Nestle, BP, Royal Dutch Shell and Total, but one-third or more of equities held are American issuers. The fund has noisily divested Wal-Mart (alleging use of child labor) and Boeing (for weapons manufacture) and recently divested shares of Barrick Gold Corporation, Canada's largest market cap company (citing pollution in its New Guinea mine operations).

Stay Tuned to … rising concerns about some SWFs and some aspects of SWF operations as their visibility increases along with their investments in the U.S. *The Economist* magazine pointed out that *"…SWFs could soon become the most important buyers of assets vital to national security, such as energy, IT, telecom and defense, and others … if so, we could witness the intriguing spectacle of the largest private companies owned by governments whose belief in capitalism is often partial …"*

We can be sure of this: SWFs — welcomed as investors … or not … sure to be front-of-mind for more corporate managements and boards and IROs in the global search for capital in the months ahead! IRU

***Hank Boerner** is editor of* IR Update *and long-time member of NIRI. He tracks the activities of Sovereign Wealth Funds and their investment activities in the United States and around the globe. E-mail him at **hboerner@niri.org**.*