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The Role of Sovereign Wealth Funds in the Global Economy: Conclusions for Poland

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Sovereign wealth funds (SWF) have become important investors in the global economy. However, they are not only a source of capital but also instruments of foreign policy. From Poland's point of view, cooperation with such funds can be beneficial in, for example, the realisation of an investment, such as infrastructure, as well as in the development of a capital market. Nevertheless, some challenges related to these funds must be considered, such as the frequent lack of transparency. There is also debate in Poland about the creation of the country's own wealth fund. It can be used for investing abroad and attracting other funds for projects in Poland.

SWF are public institutions that manage assets funded by a country's capital reserves, accumulated from, for example, sales of raw natural resources (mainly oil and gas, but also diamonds or copper), a trade or budget surplus, as well as profits from privatisation. The first SWFs were established in the Middle East in the 1950s. Their aim was to invest profits from the oil trade. In the beginning of the 21st century, there was a dynamic rise in the number of SWFs, from around 20 to more than 90 in 2016, and in the value of their assets. This was the effect primarily of high raw material prices and the rapid growth of emerging economies (mainly China), which recorded significant trade surpluses. It is estimated that SWFs have assets under control worth around $7.3 trillion as of the end of 2016 (in 2007, it was around $2.6 trillion), or more than 15 times Poland's GDP. SWFs are larger by value than hedge funds or private equity assets but less than pension funds, which are valued at more than $36 trillion. By the end of 2016, the biggest SWFs were the Government Pension Fund Global (GPFG) in Norway (with assets worth around $860 billion), the China Investment Corporation (or CIC, $814 billion), and the Abu Dhabi Investment Authority (ADIA) from the United Arab Emirates ($773 billion).

Activity Profile. SWFs are designed to conduct special tasks not directly connected to the current management of an economy. Their aims can embrace financing unexpected spending or future pensions (savings funds), hedge raw material prices (stabilisation fund), or support investments in the country of origin (development funds). In comparison to private investment funds, they are focused on long-term activity and the realisation of risky projects (such as startups). The long-term approach lessens the possibility to withdraw funds in case of an economic decline to stabilise markets (this was visible during the recent global financial crisis).

SWFs vary in investment strategy and legal form. Their managers diversify the portfolio and invest in a wide array of assets, including government bonds and company shares (e.g. in the financial, mining, and industrial sectors), but also in real estate or infrastructure projects. Usually, SWFs are minority investors that derive profits from, for example, a dividend. The funds can be managed directly by state agencies (as in the case of the GPFG), state-owned enterprise (Korea Investment Corporation from South Korea), or a trading company owned by the national treasury (Temasek Holdings from Singapore).

A Tool of a Foreign Policy. Government control of an SWF means it can be used as an instrument of foreign policy and might be used in various ways. They can invest in specific countries as a reward for favourable actions. For example, the Chinese fund State Administration of Foreign Exchange (SAFE) committed to buy government bonds from Costa Rica, which contributed to that country's decision to cancel diplomatic relations with Taiwan. Then, there is the possibility to threaten to withdraw assets as a form of political pressure. An SWF's investment strategy can support a country's policy in a specific area. An example of this is the Norwegian GPFG. It does not invest in companies connected to allegations of human rights abuses. Moreover, it supports Norway's climate policy, backing away from investment in firms that contribute to environmental pollution (including coal mining). In turn, Chinese CIC avoids investment in the gambling or alcohol industries. SWF investment strategy and investment itself (or even just announcements) can contribute to a positive image of a country in the world.

The funds also may be used to strategically control important companies in key sectors, such as telecommunications or energy. SWFs can support securing raw materials indispensable for economic development (e.g., by investing in mining companies). Moreover, if fund representatives are appointed to a company's board, there is the possibility to acquire information, for example, leakage of sensitive data, including technological know-how. It can then be passed on to firms in the SWF's home country.

It is worth mentioning that most SWFs, as well as their assets, are controlled by developing states (e.g., countries in the Middle East and Southeast Asia) and emerging powers, such as China. Therefore, their SWFs can support political goals that strive to change the global order in their favour. In this context, the lack of transparency in relation to a given fund may raise anxiety regarding the actual aims of its activity. This is particularly the case for certain SWFs from developing countries and from China or Russia.

SWFs in Poland. The scale of these funds' engagement in Poland is difficult to determine as most are not transparent and conduct transactions via other subjects, such as subsidiaries, special purpose vehicles, or private investment funds.

The most noticeable fund in Poland is Norwegian GPFG. Globally, it holds shares in around 9,000 companies (more than 1% of all shares listed worldwide) from almost 80 countries. By the end of 2016, the fund's combined investment portfolio in Poland was 92 firms (including companies in the financial, production or construction sectors) worth $670 million, and bonds of three subjects (including the Treasury) worth $2.6 billion.

Investments have been made by other funds, including ADIA, the Qatar Investment Authority, Kuwait Investment Authority, SAFE (real estate), Government Investment Corporation from Singapore (finances), and CIC (healthcare, telecommunications). However, one can assume that investment in Poland, and across Central and Eastern Europe, is less significant than in Western Europe or North America, where capital markets are much more developed.

Conclusions. SWFs can contribute to the economic development of their country of origin and create a financial cushion for long-term challenges, such as demographic changes. Given their financial potential and government control, these funds are becoming important tools of countries' foreign policy. Despite the risks, attracting SWFs can be beneficial for Poland because they can support the development of the local capital market and finance major investments, such as infrastructure projects or startups. This resource is important to Poland given the probable reduction of structural funds in the EU's financial framework for 2021-2027. As eager as any fund may be to conduct activities in Poland, its actions should be transparent, for example, in terms of investment policy and financial data, based on the Santiago Principles agreed in 2008. These elements can be proposed to be included into the EU's discussed mechanism of verification of foreign investment (so called "screening").

In considering the rationale behind establishing a Polish SWF, one should consider the sources of capital, the long-term approach, and means of transparency (patterned on such developed states as Norway or Australia). It also can be based on a combination of features of saving and development funds. If so, it would be able to invest accumulated capital (e.g., from the Demographic Reserve Fund) or incomes from state-owned enterprises, but above all used to attract other SWFs to Poland and co-invest with them (such as the French fund CDC IC).