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**Seminar**

**on**

**Sovereign Wealth Funds: Issues and Challenges for India**

**Monday, 5 May 2008 at 3.00 p.m., RIS Seminar Hall,  
India Habitat Centre, New Delhi**

# On Sovereign Wealth Funds: Issues and Challenges for India

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A Presentation at Seminar on

**“Sovereign Wealth Funds: Issues and Challenges for India”**

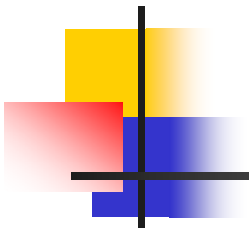
New Delhi  
May 5, 2008

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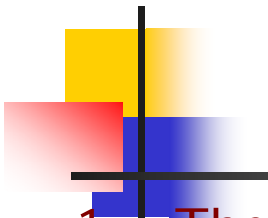
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*"When we force-feed \$2bn daily to the rest of the world they must invest in something here. Why should we complain when they choose stocks over bonds?" Warren Buffet, the "Sage of Omaha", March 2, 2008*

# Three Issues:

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1. Should India have a Sovereign Wealth Fund?
  2. If yes, what should be its modalities?
  3. What should be our position on the growing clamor in the West for 'guidelines' on investments by SWF?

# SWF for India

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1. The official view until recently was against SWFs. Reasons: mandate of RBI and prudence of investing in SWFs when India has current account deficit.
  2. Fortunately, both issues resolved in favor of SWFs.
  3. Our estimate is that after adequate provision for transaction and precautionary needs, India has excess foreign exchange reserves of at least \$100 billion. Thus the present program of investing some \$5 billion in "SWF" is too conservative.

# Modalities of Indian SWF

1. "SWF" in India is wisely planning to avoid direct investments in foreign companies. The program is for using these funds to support imports for infrastructure investment. That is safe but too limited. May not help much in stimulating infrastructure investment. Most infrastructure investments have externalities that are not captured by private investors. Filling financial viability gap is essential for private sector led infrastructure investment. The present program does not help in that respect.
2. An alternative is to use the SWFs more aggressively and use the profits to fill financial viability gap and thus leverage infrastructure investment more than what is possible through direct financing of imports.
3. Investment in equity indices at national or regional level can be a safe way of depoliticizing investments by SWFs and still earn higher ROR on the long-term.
4. On the basis of past experience \$100 billion in SWF can earn extra \$5 billion per year and if it is used to finance "financial viability gap" (estimated to be about 20%) it can mobilize about \$20 billion of additional investment per year thus meeting about 20% of the infrastructure investment needs of the 11th FYP.

# The Western Clamor on SWFs


- The clamor is largely unjustified

First, these funds have been in existence for a long time and there is no evidence of misuse of these funds for political purposes. In fact their recent performance in the context of sub-prime crisis is a model of good conduct.


Second, the concerns expressed by the North about SWF are not just about these funds. Similar fears may also be raised with even greater validity with State-owned enterprises in financial and non-financial sectors. How can international guidelines be set up for such a diverse set of players under state ownership?

Third, the argument that if the SWFs want to be driven by economic and not political motive, they should have no problem in making such a commitment at an international level is incredibly naive. Commitments will require a verification process and in case of suspected non-compliance, an enforcement mechanism.

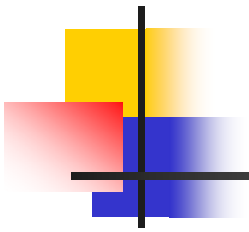
Fourth, it is the recipient country that has to develop its own mechanism for surveillance of foreign investors when political and security concerns are present. Whatever a foreign SWF may claim to be doing about the nature of its investments, the recipient country will have to satisfy itself through its own review mechanism that the inward investment is not violating its own laws and rules and regulations.



While not acceding to the demands of the North for international norms, the South in its own interest should consider mechanisms for transparency and de-politicization of SWFs. The managers of the SWFs, particularly in a democracy, will be concerned about the risks of being accused for unfair practices in their portfolio management. In that context, the idea of investing in equity indices may be considered seriously. In most countries, equity indices do better than the 80% of the active managers and from information provided by SWFs in countries such as Singapore and Norway, it seems that they do not perform much better than the long-term performance of equity indices a such as Standard and Poor in the US. So why not go for investment in equity indices either at global or regional level?



Beyond depoliticization of investment by SWFs, it is necessary to correct the fundamental factor behind the uproar about the SWFs which is the inability of the US to realize that is now a debt-distressed country and cannot play the role of economic hegemon that it has become accustomed to. In fact until it comes to terms with new reality, it will keep getting deeper into the debt trap with more and more severe consequences for its own people and the rest of the world. Now is the time the South should stand up and take more of leadership role in managing world economic affairs. The Regional Sovereign Wealth funds could be utilized not only to assist development of the South but also to manage the debt problem of the North, mainly the US. This leads to a proposal for a Reserve Bank of Asia, elaborated most recently in RI S Discussion Paper No. 135, May 2008.



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*Thank You*