THE RISE OF SOVEREIGN WEALTH FUNDS: IMPACTS ON U.S. FOREIGN POLICY AND ECONOMIC INTERESTS

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CONTENTS

THE RISE OF SOVEREIGN WEALTH FUNDS: IMPACTS ON U.S. FOREIGN POLICY AND ECONOMIC INTERESTS

WEDNESDAY, MAY 21, 2008

HOUSE OF REPRESENTATIVES,
COMMITTEE ON FOREIGN AFFAIRS,
Washington, DC.

The committee met, pursuant to notice, at 9:36 a.m., in room 2172, Rayburn House Office Building, Hon. Howard L. Berman (chairman of the committee) presiding.

Chairman BERMAN. The committee will come to order. As I was telling the ranking member for this hearing, my fantasy is that the three of us are the only ones who come because this subject is so interesting, we could then take four or five rounds of questions and get every issue that I am confused or concerned about clarified. But I very much appreciate our witnesses being here today.

Today, we are taking a closer look at an issue that has received a lot of notice in global finance circles. It has also started to receive greater attention and some apprehension by those who are focused on U.S. foreign policy.

Sovereign wealth funds have been around for decades, but China's recent entry into this field, together with investments in large Wall Street firms by the funds of Middle Eastern countries, have raised questions about the power that these massive funds may have over United States national security interests.

Part of the anxiety comes from the notion that the choices guiding sovereign wealth funds, operated by governments that are sometimes unfriendly, sometimes untrustworthy, may well be based on strategic or political considerations rather than purely economic ones. Since many of these funds lack transparency, legitimate concerns have surfaced about the motivations behind the investment decisions being made.

If Russia's fund decided to invest in energy assets in the United States, would they be able to use it to their political advantage, as they have done in Europe?

How would we react if China's fund wanted to invest in a United States telecommunications company with access to critical national security technology?

The good news is that we have a process by which to guard against investments into the United States that have national security implications.

Last year, this Congress revised the procedures by which the U.S. Government conducts its investigations into all entities, in-

cluding sovereign wealth funds, wishing to make sensitive investments here, and, by "sensitive," I mean those investments that could potentially give these funds and, by extension, their governments, controlling stakes in firms that are critical to U.S. national security. Such investigations are done through the Committee on Foreign Investment in the United States, known sometimes as "CFIUS."

So while I absolutely advocate greater transparency, accountability, and consistency in the administration of these funds, we also have to be very judicious about any new regulation in this area.

There is also much to be said about the positive effects that the influx of foreign direct investment can have on foreign policy. I subscribe to the adage that "when goods and capital are able to cross borders, it is more likely that tanks and missiles don't." I also think the United States should retain its principles of free and open markets and be very wary of what might happen if we start to close our borders to market-driven investment.

That is why I advocate a balanced approach to sovereign wealth fund. I support the work of the International Monetary Fund to create a set of best practices for such funds, and I look forward to its report on the matter later this year. Multilateral guidance from the IMF could help those who run sovereign wealth funds create more transparency and clarify their investment objectives, which ultimately could provide greater comfort for those who might question their motives.

I am very pleased that we have a distinguished panel of witnesses to help this committee understand the foreign policy and national security implications of the rise of sovereign wealth funds.

We will introduce the panel in just a moment, but, first, I would like to turn to my good friend from Illinois, Mr. Manzullo, for any remarks he wishes to make. Mr. Manzullo.

Mr. MANZULLO. Mr. Chairman, thank you for holding this important hearing on the impact of sovereign wealth funds on America's national security. Let me begin by saying that I am honored to be filling in for my good friend, Representative Ileana Ros-Lehtinen, the distinguished ranking member, who is with the President at the White House commemorating Cuba Solidarity Day.

In March of this year, the issue of sovereign wealth funds was examined in a Financial Service Committee hearing, of which I am also a senior member. I believe that the more attention this issue has, the better it is for the American people. In fact, I raised serious concerns about China's sovereign wealth fund as early as April 2007 during an Asia Subcommittee hearing. Thus, I commend your interest in the area of America's international economic relations.

Although sovereign wealth funds are not new to the world of finance and international business, surging trade surpluses in commodity-rich countries and large foreign exchange reserves have raised the influence of sovereign wealth funds worldwide. When combined with the lack of transparency that characterizes many sovereign wealth funds, Members of Congress and the American people have good cause for concern.

In the past, the process of reviewing foreign investment through the Committee on Foreign Investment in the United States, better

known as "CFIUS," was not adequate enough to take into consideration the new clout of the sovereign wealth funds.

The enactment of the Foreign Investment and National Security Act of 2007 greatly strengthened the CFIUS review process and eliminated potential loopholes that allowed questionable investments to go forward.

I worked closely with my colleagues on the Financial Services Committee to insert a provision into the final bill that boosts national security by scrutinizing acquisitions and investments made by foreign, state-owned enterprises in the United States.

We all remember, not too long ago, that an oil company controlled by the Chinese Government tried to purchase an American oil company. At that time, those in favor of the transaction argued that the American company being purchased was of insignificant scale to adversely affect the national security. With oil costing over $130 a barrel, I would argue that those of us in Congress did the right thing by opposing the purchase; otherwise, in 2008, our dependence on foreign sources of oil would be even greater.

In America, the growing footprint of sovereign wealth is felt most directly in the banking sector, where turmoil in the subprime mortgage market and other credit derivatives caused huge losses for investment and commercial banks. Since the credit crunch first unfolded last year, funds from the Middle East and Asia have invested about $70 billion in recapitalizing the rich world's biggest investment banks.

In general, there is nothing particularly new or threatening when foreign investors, be private or state, seek investments in the U.S. in nonsensitive areas of the economy. Indeed, foreign investment is a boon to our economy. The U.S. subsidiaries of foreign companies employ approximately 5.1 million Americans, of which 30 percent are in the manufacturing sector. They have a payroll of $336 billion and account for 19 percent of all U.S. exported goods.

Foreign direct investment, including sovereign wealth funds, provide capital to purchase companies in the U.S. where there may be no domestic financing available, thereby saving thousands of U.S. jobs. Thus, when investment decisions are made on market fundamentals, the outcome is often a win-win scenario for everyone involved.

For example, the foreign-owned companies play a positive role in the Northern Illinois district that I represent by providing significant jobs, mostly manufacturing. In Rockford, Illinois, firms from Japan and Italy own T.H. Foods and Ingersoll Milling Machine, Atlas Cold Storage, and Belvedere is owned by a Canadian company; Nissan Forklift is in Marengo; Eisenmann Corporation is an American subsidiary of a German firm in Crystal Lake; and Cadbury-Schweppes, which owns the Adams confectionery plant in Loves Park, is a British firm. In my congressional district, there are over 7,000 manufacturing jobs that are directly related to direct foreign investment.

Illinois is fifth, in U.S. terms, in the number of employees supported by foreign subsidiaries per state. Indeed, most sovereign wealth funds have proven they are beneficial vehicles for foreign investment. Norway, for example, is a close ally, with transparent governance for its sovereign wealth fund, the second largest in the

world. However, we must acknowledge that all sovereign wealth funds are not created equal. Sovereign wealth funds from China, the United Arab Emirates, and Qatar are troublingly secretive and appear to have political or strategic investment objectives.

These activities speak to the need for the U.S. to continue to be on guard against efforts by foreign government-owned and influenced entities to secure control over U.S. companies with sensitive technologies and other assets related to national security.

In this context, I applaud the administration for issuing clarifying regulations concerning the 10-percent ownership threshold for CFIUS review. The acquisition agreement that governs how much management control any investors, whether public or private, may have is of prime importance. By removing the presumed threshold 10 percent, the U.S. Government is putting sovereign wealth funds on notice that noneconomically driven decisions will be detected.

Congress should also examine the economic security risks associated with allowing sovereign wealth funds to invest large sums of money into our economic infrastructure. Appropriate risk-management structures should be in place, and sound management of assets should be guaranteed. We must ensure that fair investment strategies are the standard and that a foreign government is not using its deep pockets to subsidize a company that it owns, putting other potential private sector bidders at a distinct competitive disadvantage.

Furthermore, sovereign wealth funds investing in the U.S. should be encouraged to adopt the "best practices" put forward by the IMF.

Mr. Chairman, it is important that we strike the appropriate balance when it comes to foreign investments in this country. It is worth mentioning that keeping America open to positive, employment-creating investment is in the interest of all Americans.

I look forward to the testimony, and thank you for having this hearing.

Chairman BERMAN. Thank you very much, Mr. Manzullo.

As I mentioned, I am going to recognize the chairman of the Subcommittee on Terrorism, Nonproliferation, and Trade for an opening statement of 3 minutes, as well as the ranking member, Mr. Royce, and note the presence of not a member of our committee, but he is a co-chair of the Sovereign Wealth Fund Working Group that has been set up, bipartisan, in the House, Mr. Moran, and welcome him to the hearing.

Mr. Sherman?

Mr. SHERMAN. Thank you. Sovereign wealth funds are just a part of the greater problem, which is sovereign wealth. We have pursued insane trade policies over the last generation that have taken us from the world's largest creditor nation to the world's largest debtor nation, and no matter how it is structured, whether it is through sovereign wealth funds or otherwise, this economic power that we have transferred from our country to others does lead to political power as well.

Whether it is sovereign wealth funds, which we will discuss today, or even the most benign possible investment of sovereign wealth, and that is Chinese investment in United States Treasury

bonds, there is this concern that we have to kowtow to those who are our bankers.

Part of this is, I think, wrongheaded and comes from our personal experience. In our personal experience, our creditors are powerful. If we do not pay them, they take our house or our car. We should point out that, in the international world, if you do not pay your creditor, it is kind of like being a debtor to a bank in the United States, if my most liberal friends wrote the bankruptcy laws; that is to say, the creditor had better be nice to me, or I may just not pay. Third-world nations learned this a while ago. The days are gone when Marines can take over ports to enforce the debts of a country.

The Arabs have used their economic power for wrongful political purposes for a long time. Since the 1950s, they have had a secondary boycott of Israel. We saw the oil boycotts, OPEC, et cetera, and that is when they had very little sovereign wealth. Today, they have enormous sovereign wealth. However, as the chairman points out, there is also a bit of a silver lining, in that this gives those who invest in our country a stake in U.S. economic success, ties them to us.

Sovereign wealth funds are one species of the problem, but if countries did not have sovereign wealth funds, they would either be investing in U.S. stocks individually, and they might have influence over the entire Fortune 500. Who wants to ignore entities that control 2, 3, 4 percent of your stock, should they choose to try to influence the political policies or politically relevant policies of our corporations?

As to disclosure, there are two kinds of disclosure. The disclosure by the sovereign wealth fund to its own people as to how much money they have, and how it is being invested and how it is going to benefit them is something the World Bank and others concerned with international world development should be concerned with. But in terms of protecting the United States, it is not so much a balance sheet of the entire fund, which, in some cases, we are very unlikely to get, but, rather, a disclosure of their behavior here in the United States, particularly their level of ownership of our strategic corporations. I yield back.

Chairman BERMAN. The time of the gentleman has expired.

The gentleman from California, Mr. Royce, ranking member of the subcommittee with jurisdiction on this issue.

Mr. ROYCE. Thank you, Chairman Berman, for holding the hearing, and, as my colleagues have outlined here, the growth of sovereign wealth funds raise a number of significant policy questions.

Many well-known U.S. financial institutions have been on the receiving end of support from sovereign wealth funds in recent months. These investments have had a positive impact during a tumultuous period in our capital markets. It is important that we continue to send a message of openness to foreign investment. Were it not for this infusion, we may have seen the global credit crisis spread or intervention from the Federal Government similar to what transpired following the Bear Stearns collapse.

Now, that does not mean that we should let our guard down. Sovereign wealth funds are not ordinary investments. As one witness today pointed out, at a time of U.S. surpluses, Alan Green-

span warned against the government accumulating private wealth. Why? Because of the difficulty in separating market decisions from political decisions. Being ultimately controlled by governments, sovereign wealth fund transactions may be political, as much as they are commercial. State capitalism is not a positive development in this world, and, increasingly, political pull might replace market-driven factors.

Robert Morgenthau, the Manhattan district attorney who investigated the BCCI affair, recently recounted to the Wall Street Journal that the head of Abu Dhabi at the time of the investigation once called the State Department to inform him that if Morgenthau indicted anyone in the royal family, he would pull billions out of the United States. A figure like Morgenthau was able to stand up to such intimidation; others may not.

Especially post-9/11, commercial transactions must also consider national security. Our system to do just that, CFIUS, must be robust enough to handle evolving challenges while, at the same time, we must push for greater transparency, openness, and reciprocity by these sovereign wealth funds.

While properly monitored sovereign wealth funds should be welcomed in our economy, the unfortunate reality is that much of this sovereign wealth is wealth that individual Americans no longer possess. With the oil price spike, we are in the midst of an unprecedented wealth transfer from the U.S. to oil-exporting countries.

While it is good that some of this money comes back into the U.S., that is little consolation for the harsh reality that sovereign wealth is money no longer in American wallets, and, again, I thank you, Chairman, for holding this committee hearing today.

Chairman BERMAN. The time of the gentleman has expired.

To our witnesses. We have a distinguished panel. First, we will hear from Dr. Gerard Lyons. Dr. Lyons is chief economist, group head of global research at the Standard Chartered Bank. He is an expert in microeconomic policy and an acclaimed international economist in his 20 years' experience and senior roles with some of the world's leading financial institutions.

Both a commentator and publisher, Dr. Lyons has testified with both the United Kingdom Parliamentary Committees and in the United States Congress. We are grateful for having him here and look forward to his contribution to today's hearing.

We also welcome Dr. Edwin Truman, who is currently a Senior Fellow at the Peterson Institute for International Economics. Dr. Truman served in many capacities for the United States Government, most recently as assistant secretary of the United States Treasury for international affairs from 1998 to 2001.

He directed the Division of International Finance of the Board of Governors of the Federal Reserve System and has been a member of many international working groups on financial stability and emerging economies. He has published articles and studies on sovereign wealth funds, including, "A Blueprint for Sovereign Wealth Funds Best Practices." Dr. Truman, we welcome your unique insight to today's discussion.

Finally, we will hear from Dr. Gal Luft. Currently, Dr. Luft is executive director of the Institute for the Analysis of Global Security. An expert in the geopolitics of economic and energy security,

Dr. Luft is a prolific writer, having published numerous articles and studies in renowned publications. With a unique understanding of the interrelation between economic stability and national security, he has testified before the House and Senate committees and has consulted for various policy organizations.

He has also been an individual that I am aware of who has done more to sort of integrate the whole notion of our energy policy and its impact on not only economic and environmental issues but foreign policy and national security issues. So we are glad to have you here as well, Dr. Luft.

Dr. Lyons?

STATEMENT OF GERARD LYONS, PH.D., CHIEF ECONOMIST, STANDARD CHARTERED BANK

Mr. LYONS. Good morning, and thank you, Chairman. Chairman, Ranking Member, and members of the committee, it is a pleasure and an honor to be here this morning to speak before you. I have written testimony that I would respectfully ask this committee to insert into the record. That written testimony looks at sovereign wealth funds in terms of their background, basically the context issues, and implications.

Chairman BERMAN. Your entire statement will be included in the record of this hearing.

Mr. LYONS. Thank you. Maybe, in the next 5 minutes or so, in my oral comments, I can focus on three areas that I think are particularly relevant for your hearing this morning: First, sovereign wealth funds in macroeconomic terms; second, state capitalism, which I think is the key issue; and, third, a code of conduct for sovereign wealth funds.

First, in macroeconomic terms, I believe that sovereign wealth funds should be seen in the context of a significant shift in the world economy. Emerging economies are seeing a significant rise in their economic and financial power. One of the aspects of that is what I would call "new trade corridors," rising intra-Asian trade but, more particularly, rising inter-regional trade between Asia and Africa, Asia and the Middle East, and Asia and Latin America. This implies, in my mind, that, in the future, sovereign wealth funds will allocate more of their money to emerging economies and, in all probability, a shift away from the dollar, which I would call "passive diversification" out of the dollar.

In addition, high commodity prices and China's foreign exchange policy are important contributing factors to the current growth in the size of sovereign wealth funds.

Another aspect of this is the current imbalance in the world economy. As this imbalance unwinds, and, indeed, as we are seeing now in the U.S., one is likely to see a period of weak, below-trend growth in the United States, a weaker dollar, but also, at the same time, I think it is important in this debate to try to encourage the surplus countries across the Middle East and Asia to move their savings into increased demand. The way to do that is to encourage these countries to open up further, to deepen and broaden their financial markets. Some are doing that, and I think we should encourage them to do more.

In addition, I think there should be encouragement of China, as part of that financial sector development, to allow their currency policy to see a stronger renminbi.

The second are, in addition to that macroeconomic background, is what I would call "state capitalism." State capitalism, rather than sovereign wealth funds, is, in my mind, the issue that should concern us. The key factor regarding sovereign wealth funds is not that they are foreign but that they are government owned. Government-controlled funds, as has been touched on, are very different from private sector flows. They act in the interests of a state, on behalf of its people, rather than for company or individual investors.

This raises, at least, the question of how these funds might use their investments and the leverage this brings. It is important, in my mind, to stress that these are generic issues. While most sovereign wealth funds are good investors, have purely a commercial focus, if one steps back, I think many of the concerns are not just about sovereign wealth funds but, more often, about government-controlled funds, and even though one government-controlled fund may act as a business, and the sovereign wealth fund as an investor, I think it is that generic government-control aspect that is important.

In terms of your debate or discussion this morning, a number of issues arise from that. The U.S., like the U.K., has no problem with foreign investment, but I think both countries need to ensure that there is complete confidence in its legal, competition, and regulatory setup. From where I sit, the U.S. approach looks pretty good.

Also, when one views the role of government alongside energy security, I think one needs to be very aware of the wider issue, and I touched on the new trade corridors. I think this is perhaps best highlighted by China's involvement in Africa.

Also, one issue not fully covered in much of the debate about sovereign wealth funds since last summer has been the whole issue of intellectual property rights and how to safeguard them. I think the issue this raises has probably more to do with level playing fields and removing restrictions on the markets which the sovereign wealth funds emanate from.

And, finally, to conclude this section, I think the U.S. and the U.K. must remain open to trade and provide input into the multilateral approaches of the IMF and OECD.

Third, and finally, a code of conduct for sovereign wealth funds. I am speaking here in a personal capacity. Sovereign wealth funds invest in my own company. Some of them are our clients, so I have engaged in discussions with them since last summer.

Sovereign wealth funds are not new. Some of the oldest are over 50 years old, some of them having established investment records without problems.

Are they a risk, or are they a perceived risk? Whether they are a risk or a perceived risk, I think there are issues. I have looked at sovereign wealth funds in terms of their openness and transparency. One can link that into the wider debate about accountability, governance, and their investment strategy.

Also, because sovereign wealth funds are basically government owned, it raises the issue as to whether they are commercially or

strategically driven. Last summer, I was arguing that, in my view, sovereign wealth funds would be likely to invest in other areas in the future: One, emerging markets, and that makes economic sense, as well as political sense; second, alternative investments like private equity and hedge funds; third, investing more in economies in countries, which, shall we say, are shunned by globalization, such as in Africa; and, finally, strategic stakes, which I then defined as "access to intellectual property, energy, telecommunications, and the financial sector."

Obviously, since then, we have, as has been mentioned, seen a huge infusion of capital by sovereign wealth funds, which has prevented, or maybe delayed, the consolidation of the Western financial sector. That has resulted in a shift in attitudes toward this money coming in. But I still think the principles are the same as outlined last summer.

I think it is hard to argue against an investment framework that is fair and commercially driven, with clear, predictable rules that apply to everyone. Many of the sovereign wealth funds I speak to fear that they will be discriminated against. They argue that their track record is good.

My view is that, in an environment where openness and transparency should be encouraged, there should be a code of conduct, and maybe there should be a code of conduct for other areas, such as hedge funds, as well. But I certainly would argue that the work on the code of conduct currently being pursued by the IMF should be encouraged, and I think that is an important area. Ideally, in a voluntary code of conduct, as I mention in my written paper, certain issues do need to be addressed.

So, in conclusion, I would say, there are three broad areas very important for your discussion this morning: One, to put sovereign wealth funds in the global context, in macroeconomic terms, and they are very much, in my mind, a reflection of the shift under way in the global economy, and they will play a part in that future shift.

Second, state capitalism. This applies to only one, or a part, of the aspects of sovereign wealth funds, but also it applies, in my mind, to government-controlled companies which are not sovereign wealth funds.

Third, and finally, in terms of sovereign wealth funds themselves, I think it is important to work with the sovereign wealth funds to try to devise a workable code of conduct that will satisfy both sides. Thank you.

[The prepared statement of Mr. Lyons follows:]

PREPARED STATEMENT OF GERARD LYONS, PH.D., CHIEF ECONOMIST, STANDARD CHARTERED BANK

1. ORAL TESTIMONY AND OVERVIEW

Chairman Berman, Ranking Member Ros-Lehtinen and members of the Committee, I appreciate the opportunity to testify here before you on the rise of Sovereign Wealth Funds and the impact on US foreign policy and economic interests. I will offer brief oral testimony and respectfully request that my complete written statement be entered into the record. That written statement is a short background paper that looks at Sovereign Wealth Funds (SWFs) in terms of the context surrounding them, issues they raise and the implications. In the brief time we have this morning I would like to make some specific points directly linked to the topic

of today's session, namely the implications for US foreign policy and economic interests.

SWFs are not new. Some of the oldest funds have been around for half a century. Many SWFs have a long history of investment without problems. Thus it is important to take a balanced perspective of SWFs, and for many people SWFs are not a concern. However, as these funds increase in size, importance and economic impact, many issues arise that need to be considered. I would like to highlight three broad areas.

First, in macro-economic terms

I believe SWFs should be seen in the context of a significant change in the world economy, whereby emerging countries are seeing a rise in their economic and financial power; whilst high commodity prices and China's exchange rate policy are important contributory factors to the growing size of SWFs.

Another aspect of this shift in the global economy is rising intra-regional trade within Asia, largely because of the opening up of China, and increasing inter-regional trade between Asia and other regions such as Africa, Latin America, the Middle-East. This includes increased flows of goods, commodities, people, remittances and increased capital flows. These new trade corridors need to be taken into account when one views the likely future role of SWFs. I would expect SWFs to allocate an increased amount of their future investment to emerging economies and, in all probability, away from the dollar. And, if recent experience with SWFs is a guide, we should expect to see governments playing an increasing role in future business flows.

One way to view SWFs is a reflection of imbalances in the world economy. This imbalance has seen a sizeable US trade deficit and flows of capital from the East to the West. A correction of this imbalance is underway. From a US perspective this is already evident in terms of a period of weaker, below trend growth and a weak dollar. For the rest of the world there is a need for steady growth in other major economies such as Europe and Japan and, equally importantly, the need for surplus economies in the Middle East and across Asia to switch their savings into increased domestic demand at home. This will require a number of factors, including deeper and broader financial markets across economies in regions such as Asia and the Middle East. Although this is happening in some countries, it needs to occur on a broader scale. In the case of China, as part of this financial development there is a case for arguing that their currency should appreciate at a faster pace.

Second, State Capitalism and the role of governments

In my view, it is what I call State Capitalism that should concern us, rather than SWFs themselves. State Capitalism is the rising role of government ownership and management of international assets. Indeed, the important issue regarding SWFs is not that these are foreign but that they are government owned. Many countries in the West, including the US and UK, have no problem with foreign investment. Indeed both have a long history of welcoming such inward foreign investment. Government controlled funds are different from private sector flows, acting in the interests of a state, on behalf of its people, rather than a company or individual investors. This raises at least the question of how these funds might seek to use their investments and the leverage they bring. It is important to stress that there are some generic issues. Many of the concerns are not, strictly speaking, just about SWFs but are often more about government controlled companies, particularly in countries such as Russia and China.

I think it is important that the government and business in the US—and indeed in other Western economies—need to have complete confidence in the robustness of their present legal, competition and regulatory set-up to cope with any issues arising from SWFs. Just as the UK needs to be able to safeguard British interests, so too must the US safeguard American interests, and both countries must ensure they remain open to investment and provide input into the current multilateral approaches being adopted by both the International Monetary Fund (IMF) and the Organisation for Economic Cooperation and Development (OECD).

When one views the role of government alongside the matter of energy security there are wider issues that need to be considered. This is perhaps best highlighted by the increased flows between China and Africa, where China's interest in Africa has helped to correct perceptions of the chronic undervaluation of African assets. This raises the possibility of sizeable capital inflows to developing countries, on a scale that would dwarf traditional reliance on aid flows. The OECD has made this point, highlighting that, "If SWFs chose to allocate 10 per cent of their portfolio to emerging and developing economies over the next decade, this could generate inflows of $1,400 billion, more than all OECD countries' aid to developing economies put together." The developmental impact, allowing for much more rapid progress, would be huge. But the nature of the new economic engagement must also be closely

monitored. Vulnerable states, in need of quick financing, with no access to international capital markets and the investor scrutiny that results from such access, may build up debt at a rapid and unsustainable pace. Even more worrying, with little experience in dealing with SWFs, or with government controlled firms, they may not pay much attention to what is required of them in return.

One issue not fully covered in the present approach is that of intellectual property. If a SWF acquired a minority stake, such intellectual property may not be lost, but it could with a majority stake. But even then, how could safeguarding intellectual property be enforced, particularly where the people in any company may be a key part of that skills advantage? Moreover, if a fund owned the company or was the majority investor then it would be entitled to the intellectual property, and the innovator would be rewarded, whilst the country of the SWF benefits from the knowledge. The issue this raises may be more to do with the need for a level playing field, and the need to remove restrictions in a SWF's own market. This issue, moreover, also needs to be seen in the context where there is a general assumption that as the world economy changes, it is economies in the West that will gain from being knowledge based economies. That cannot be taken for granted, as there is every reason to believe that economies around the world, including those that have SWFs, will be keen to move up the value added curve very quickly. Ensuring enforceable global standards on patents and intellectual property appears an important aspect of this debate.

Third, a Code of Conduct for SWFs

In its Statement at the October 2007 IMF, the G7 said that they see, "merit in identifying best practices for SWFs in such areas as institutional structure, risk management, transparency and accountability."

One can analyse SWFs in terms of their openness and transparency. Some funds, such as Norway, Temasek and Alaska, are open and transparent, providing detailed information on their size, returns and portfolio composition. In turn, some SWFs are very opaque. One can link this issue of openness and transparency into the wider debate over accountability, governance and their investment strategy. Because SWFs are government controlled an issue is whether their investments are commercially or strategically driven. The record to date is that investments appear largely commercially driven.

In a detailed analysis last summer, I suggested that in the future SWFs will take bigger financial stakes in equity and bond markets across emerging economies; to feed more money into alternative investments such as hedge funds and private equity; to boost strategic links with countries that have not shared fully in globalisation or which have been shunned by the West; and to take strategic stakes in sensitive areas within developed countries. My view of strategic stakes included securing intellectual property rights, or taking positions in key industries such as telecommunicatons, energy and the financial sector. The subprime crisis has, indeed, seen huge capital injections by SWFs into many western financial firms, but this has been generally welcomed, with such stakes preventing, or at least delaying, a consolidation of the financial sector. It has also prompted debate as to whether SWFs should take a more active role in poorly managed firms, or should continue to invest passively, often through third parties as they do at the moment.

In recent months SWFs have been more prepared to engage in discussion on these issues. This has been welcome. It is clear from much of that debate that SWFs do not wish to be discriminated against. That is fair. The feeling amongst many is that is that their record of being responsible and disciplined investors makes the case for increased regulation and for a Code of Conduct unnecessary.

It is hard to argue against an investment framework that is fair and commercially driven, with clear, predictable rules that apply to everyone. But, in my view, this does not argue against a Code of Conduct. Rather such a Code is there to reflect the growing scale of these funds and their increasing importance. And of course there may be the need for Codes to be introduced in other areas. Ideally this Code should be voluntary and should include: clarity over the motivation for the Code; the need for clarity of objectives and investment strategies; the need for best practice on corporate governance and on accountability and the need for greater transparency regarding transactions. The issue of enforceability also needs to be considered. Whilst secrecy in itself does not mean that a fund will be a bad investor, in a global financial environment where transparency and accountability are seen as important positives, such opaqueness should not be encouraged.

There is a need for common ground rules, best practice, and the need to promote an investment framework that is fair and commercially driven. Any constraints on SWFs should be based on an objective appraisal of facts within a stable framework of roles and processes. Yet, as long as investments by SWFs are made for commercial reasons and not for political purposes then these funds should be accepted.

Here follows the briefing paper on SWFs.

2. SWFS IN CONTEXT

SWFs are not new, in fact the oldest dates from 1953. Given how old some of these funds are, one might ask, why all the recent fuss? There are a number of reasons. The number of countries with SWFs is increasing, the amounts at their disposal are rising and the possible investments are becoming more controversial. Moreover, to quote European Commissioner Peter Mandelson, "there is a heightened need for reassurance" when one considers that the biggest new funds are in countries such as Russia and China, countries that as he says are,"new investors, with huge reserves, backed by governments with mixed democratic credentials, substantial foreign policy projection and no track record as investors." Whereas, Mandelson goes on to say that he believes the risks are overstated and our ability to cope with them is likely understated, the main point is that there are risks.

There is an important aspect that needs to be addressed up front, and that is how one defines a SWF? The IMF recently noted twenty six different definitions. The key characteristic is that they are owned by a sovereign state. Exceptions being, subnational level funds financed by foreign exchange assets, resulting from commodity exports, which allows one to include Alaska from the US or Alberta from Canada. They are not central banks and, in that respect, I would not include Saudi Arabia's funds managed by their central bank, although some others do. SWFs are not pension funds, unless financed by foreign exchange assets from commodity exports, such as Norway's Government Pension Fund.

There are four main sources for where SWFs derive their funds: (a) revenue from commodities, with 16 of the largest 22 funds depending on commodity income; (b) foreign exchange reserves, particularly important for China's SWF; (c) investment income, which is very important for, for instance, Temasek; and (d) discretionary factors that may influence how much money governments allocate in the start-up phase.

The US Treasury, in their various comments on SWFs, tends to differentiate between SWFs funded by commodities and those funded by non-commodities and, in turn, has linked this to the different asset-liability structure of such funds. Also, the funding of SWFs from non-commodities can be linked to the debate about foreign exchange rates and, in particular, to intervention by China to keep its currency undervalued, whilst building up its foreign exchange reserves.

The size of SWFs is also an issue. In a detailed analysis carried out last summer, we estimated their size at $2.3 trillion, but there is a wide range of opinion. Generally $2–3 trillion is cited, although in an analysis in April 2008 by the London based International Financial Services (IFSL) put their size at $3.3 trillion. Whether one views this as large or small depends on the benchmark, but they are getting bigger. This amount is small in one respect, representing 1.3% of global financial assets, but is sizeable in another respect, being larger than hedge funds, which are between $1 trillion to $1.5 trillion, although they leverage up, and larger than private equity, at $0.7 trillion to $1.1 trillion. It is hard to gauge the future size of SWFs, but on current trends they could exceed foreign exchange reserves in five years or so and even reach $13.4 trillion in a decade. However, an unwinding of global economic imbalances could, it is said, significantly reduce their future rate of growth. All things considered, it is hard to quantify the future scale of SWFs, but in qualitative terms they are likely to be sizeable.

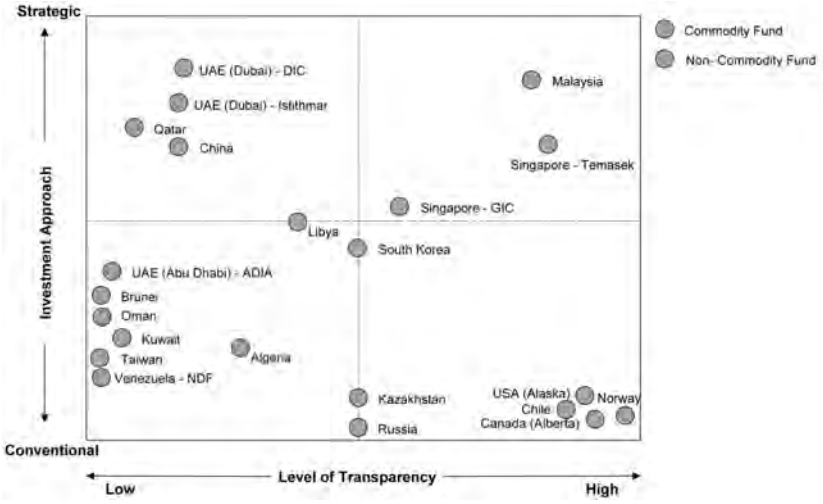
In our analysis of SWFs we determined that there is also significant concentration amongst SWFs, with a Super Seven funds. Using the recent data from the ISFL, the size of these funds is now: Abu Dhabi Investment Authority (ADIA) ($875 billion); Norway ($396.5 billion); GIC of Singapore ($330 billion); Kuwait ($213 billion); China ($200 billion); Russia ($128 billion); and Temasek of Singapore ($108 billion).

Overall the top ten SWFs are probably now around $2.3 trillion. In terms of concentration this compares with: the top ten asset managers, $13.4 trillion; the top ten central banks $4.4 trillion; the top ten state pension funds $2.9 trillion; the top ten corporate pension funds $0.7 trillion; the top ten hedge funds around $252 billion; and top ten private equity $236 billion. One could also include wealthy individuals.

Another distinguishing characteristic is to define SWFs in terms of their openness and transparency. Some funds, such as Norway, Temasek and Alaska, are open and transparent, providing detailed information on their size, returns and portfolio composition. In turn, some SWFs are very opaque. One can link this issue of openness and transparency into the debate over accountability and governance. One could also try and differentiate between SWFs based on whether their investment strategy is commercially or strategically driven. Examples of conventional investors

would be Chile, Russia, Kazakhstan or Norway, whilst strategic investors might include Malaysia or some of the Middle East funds. The following chart compares the major funds in terms of transparency and investment.

CHART 1: THE LARGEST SOVEREIGN WEALTH FUNDS OVERVIEW OF INVESTMENT APPROACH AND TRANSPARENCY



Source: Standard Chartered and Oxford Analytica

Based on the main objective of each fund, the IMF has identified five types of SWFs: (a) stabilisation funds, whose aim is to insulate the economy and budget from swings in oil or commodity prices; (b) savings funds, aimed at converting non-renewable assets into a more diversified, longer-term portfolio; (c) reserve investment funds, whose aim is to increase the return on reserves; (d) development funds, that help fund or promote policies in the home country; (e) contingent pension reserve funds, that add towards funding pension liabilities. Yet, these need not be distinctive features of a SWF, and a fund may have multiple, overlapping objectives that change over time. Chairing a session on SWFs at an OECD conference at the end of March there was much suggestion from the funds present there that they would focus more on the development agenda in their own country in the future.

Deputy Secretary of Treasury, Robert Kimmitt, in a recent article on Foreign Affairs, has talked about how one would view SWFs alongside other government financial groups, and thus he has talked about this in terms of the four sovereigns: international reserves; public pension funds; state owned enterprises; and SWFs. McKinsey's, meanwhile, have talked about the new power brokers, including: SWFs alongside; foreign exchange reserves; hedge funds and private equity. SWFs are becoming more important, both in their own right, and in the context of the ever changing global financial environment.

3. THE ISSUES RAISED

A sound analysis and clear understanding is needed of all the issues raised by SWFs. The question that immediately arises is whether SWFs represent a real or a perceived threat?

If I take the UK's experience, it would suggest the threat is more perceived than real. The UK's experience shows few examples of actual problems with SWFs; one such concern was in 1988, when there were concerns that Kuwait, which then had a 22% stake in BP, would bid for the company—the fear being an OPEC state would buy a stake in a leading oil company. But even if there have been few actual threats, the UK like other countries still needs to safeguard against any perceived threats, as well as wider ranging issues emanating from SWFs. Indeed, it could be argued that increased attention on SWFs in recent months has led to the funds themselves being more aware of the need for increased transparency.

At the World Economic Forum meeting in Davos this January, in the public session on SWFs, the point was made that SWFs are being seen as guilty until proven innocent! Furthermore, one could argue that many SWFs have a long track record as good investors. And, throughout much of the emerging world, SWFs are seen as a force for good. There are many aspects to this debate.

In my view, the main issue is not that SWFs are foreign but that they are government controlled. This means these funds could play by different rules, with possible different outcomes to those that would happen in a purely commercial environment, with national interest taking precedence over shareholder value. This links into a number of areas:

- Fiduciary responsibility: as government controlled funds may not be driven by the same commercial considerations as private firms this raises many possible issues, of which corporate governance and the fiduciary responsibility to shareholders are key.
- Inefficient allocation of capital: could such funds lead to an inefficient allocation of capital, as they are not driven by the same near-term commercial pressures as private companies?
- Financial stability concerns: There seems to have been a shift in thinking on this in recent months. Previously, there were concerns about their impact on future financial stability because of potentially large, concentrated and often non-transparent positions in certain markets and asset classes. Previously, to minimise the impact of rumours and speculation disrupting financial stability, there appeared to be a desire for greater predictability regarding SWF activity, although in practice it is hard to see how this could be possible. The sub-prime crisis appears to have changed sentiment. The injection of capital by SWFs into Western financial firms has prevented, or at least delayed, the consolidation of the financial sector. This welcome injection led SWFs to be seen as a stabalising influence. As John Lipskey, the IMF's First Managing Director said, "From the viewpoint of international financial markets, SWFs can facilitate a more efficient allocation of revenues from commodity surpluses across countries and enhance market liquidity, including at times of global financial stress."
- Strategic aims: A worry is that these funds see an opportunity to acquire strategic stakes in key industries around the globe. It is this that I call this State Capitalism aspect of SWFs that is of most concern. That is strategic investments in sensitive sectors whether telecoms, energy, media, maybe not necessarily in the financial sector, or whether it's to secure intellectual property rights in other fields. It might make complete economic sense for countries, particularly as they need to move up the value curve, and it is clearly an issue that needs to be addressed.

According to the IMF, "It is unclear how active a role they have in these companies (in which they take stakes). However, the evidence suggests that SWFs are generally passive and long-term investors with no desire to impact company decisions by actively using their voting right. . . . That means that they vote by proxy and often ask external managers to vote on their behalf."

Also, it is important to stress that there are some generic issues. Many of the concerns are not, strictly speaking, just about SWFs but are often more about government controlled companies. For instance, Russia's SWF is relatively transparent, yet worries are very much focussed on Russian government influenced companies, such as Gazprom.

Is it possible to ensure that SWFs or government controlled companies like Gazprom will be good citizens? Can we seek some understandings that make a clear statement? For instance, in terms of a bid, is there a need to ensure that any offer documents include commitments on behalf of SWFs? One example might be the commitment that if an energy company was bought then there would be continuity of supply. But in addition to such a commitment, there is a need to consider how it can be enforced.

Other issues raised, include the role of SWFs on the decisions taken by the companies in which they invest. This has raised issues as to whether SWFs should be prevented from taking board seats; whether they should be limited to non-voting shares; or even whether where clear statements of commercial motive have not been forthcoming that guidelines could be set to include upper limits to investment stakes, setting these at a level significantly below the threshold of a controlling minority stake. Or, indeed, whether SWFs should be forced to invest via third parties. What happens if SWFs moved from minority to majority stakes, or if they take controlling stakes in monopolies? An interesting aspect of the recent debate has been

the argument by some that rather than being passive investors, SWFs should be encouraged to be more active, particularly in terms of their recent investments in financial firms; the argument being that in such firms this would ensure management was kept on its toes!

The important issue is to address such concerns without unnecessary constraints on achieving an open and stable financial system, and one which encourages international flows. And it is important to ensure that recipient countries treat all investors, including SWFs, fairly. Indeed, various recent comments and speeches from US Treasury officials, including Mr Kimmitt, have focussed on the need to: a) avoid protectionism and counter product barriers; b) uphold fair and transparent investment frameworks; c) respect investor decisions; d) and treat investors equally. I agree with all these points.

In addition, the issue of reciprocity needs to be considered. The issue really should be about level playing fields and open access. In an ideal world it would be desirable to ensure that level playing fields exist between countries, but in practice this is hard to enforce, and it may be viewed as something that whilst desirable, could back-fire if seen as a necessary precondition before SWFs could invest in some economies or markets. The worry being that such an approach could provide an excuse for countries to pursue a protectionist stance. Furthermore, the West's approach to being open has not been based on ensuring level playing fields; rather it accepts that with countries at different stages of development, a level playing field is not a pre-requisite to allow foreign firms to operate in the West. In the case of SWFs it would be hard to argue that a different approach should be adopted now, but other countries should be encouraged to cooperate fully in multilateral approaches to free-trade.

Quoting from this February's European Commission's report on SWFs, some underlying concern was evident, "Investment targets may reflect a desire to obtain technology and expertise to benefit national strategic interests, rather than being driven by normal commercial interests in expansion to new products and markets. By the same token, holdings could influence decisions by companies operating in area of strategic interest or governing distribution channels of interest to the sponsor countries. More generally, business and investment decisions could be influenced in the political interest of the SWFs owners."

One issue not fully covered in much of the debate—and a question is whether it needs to be—is that of intellectual property. If a SWF acquired a minority stake, such intellectual property may not be lost, but it could with a majority stake. But even then, how could safeguarding intellectual property be enforced, particularly where the people in any company may be a key part of that skills advantage? But rather than prevent majority stakes being bought, a better option may be to seek advances on transparency and motives behind these SWFs.

One issue that goes to the heart of the debate on globalisation, is that in the West there is an assumption that western economies will become the knowledge based economies, but SWFs and the shift in the balance of power, is likely to seriously challenge this thinking. Economies across the Middle East and Asia, for instance, will be keen too to become knowledge based economies themselves.

4. IMPLICATIONS

SWFs represent and reflect a major shift in the global balance of power.

SWFs also point to a dramatic rise in the role of government ownership and management of international assets, particularly commodities.

In the future, I would also expect the influence of SWFs on markets to grow, with SWFs investing more in four areas: in the nascent bond and equity markets across emerging economies; putting more funds into alternative investments, such as hedge funds and private equity; playing greater role in terms of State Capitalism, making strategic investments in sensitive areas; and investing in countries not benefiting from globalisation, such as across Africa, and this investment linked in to resource nationalism.

Thus, this issue needs to be addressed on a national and international basis.

Last October, at the International Monetary Fund (IMF) meetings in Washington, the US Treasury hosted an 'outreach dinner' with the IMF, OECD, World Bank and eight SWFs from Norway, Russia, Kuwait, UAE, Saudi Arabia, Singapore, South Korea and China. The day after that dinner the International Monetary Financial Committee (IMFC) then asked the IMF to look further into this subject. Since then there has been intense focus on this topic, at a global, regional and national level, with the OECD focussing on this issue from the perspective of recipient countries and the IMF looking at best practice for SWFs.

In its Statement at the October 2007 IMF, the G7 said that they see, "Merit in identifying best practices for SWFs in such areas as institutional structure, risk management, transparency and accountability." Furthermore, some of the issues raised regarding SWFs apply to government controlled companies across countries such as Russia and China.

The IMF is working on a framework for a voluntary code of conduct for SWFs, whist the OECD is focusing on how recipient countries of the money from SWFs should respond.

All countries, including the UK and US need to have complete confidence in the robustness of their present legal, competition and regulatory set-up to cope with any issues arising from SWFs. They need to be both able to safeguard national interests, ensure their countries remain open to investment and to provide input into the current multilateral approaches being adopted by both the IMF and the OECD.

The US Treasury has argued that a voluntary code should address four areas: (a) the need for SWFs to invest commercially, not politically; (b) For SWFs to convey world class institutional integrity, particularly with respect to increase transparency; (c) to compete fairly with the private sector; and (d) to respect host country rules.

The US has a strong position, and is implementing the Foreign Investment and National Security Act (FINSA) through the Committee on Foreign Investment in the US (CFIUS), to ensure robust reviews of investment transactions, based on the consideration of genuine national security concerns and it requires heightened scrutiny of foreign government-controlled investments. In the UK, and indeed across Europe, there may be a need to view particular transactions on a case by case basis, particularly if they involve a change of ownership from private into public hands.

The UK's present approach also warrants international attention, as the UK is often seen as one of the economies most open to international business. The UK's approach is largely based on the view that ownership is not the issue. Whilst this may hold up with private companies (domestic or foreign) it needs to be established that this approach is also sufficient with respect to government ownership. Under the present UK regime, it is felt that competition and regulation are covered. Competition is covered by independent competition authorities, who provide sensible restraint without political interference. Likewise with regulation. In addition, the Enterprise Act covers exceptions, protecting sensitive areas, such as national security and the media.

One issue, sometimes raised by SWFs, is their desire for more clarity on what sectors they may, or may not, be able to buy into. That is more clarity on sectors that could give rise to problems. Many countries seek to protect their defence areas. The challenge is to impose safeguards on other sectors without been seen to be protectionist. But other countries do outline areas. For instance, France has a Code Monetarie and Financier. The law requires that investment in certain sectors require a specific authorisation by the French Minister of Finance: (i) sectors related to public security or national defence; and (ii) sectors in R&D or trading of arms. The regulations are more specific and define eleven sectors, related to areas such as defence, transmission technology and casinos.

Finally, if there was to be a Code of Conduct then, ideally, it should be voluntary, and it needs to cover:

a) The motivation for the Code needs to be made clear;
b) There is the need for clarity of objectives and investment strategies;
c) The need for best practice on corporate governance and on accountability;
d) There is a need for greater transparency regarding transactions;

The issue of enforceability needs to be considered.

a) The motivation for the Code needs to be made clear

The Code of Conduct should outline a set of factors SWFs should satisfy. The Code should ensure a balanced and rationale approach is adopted, recognising that in many instances the risks associated with SWFs are more perceived than real. The Code needs to allow the recipient countries to have confidence that the aims of SWFs are commercially driven and do not pose any risks. The Code also accepts that it is in the interests of countries that favour an open investment climate, and the countries owning SWFs, to engage in international dialogue to promote and sustain investment flows. The Code needs to address concerns about the transparency of objectives of the institutional structure and about their portfolios. In addition to conforming to this Code, SWFs should be encouraged to develop their own code of best practice. The aim is to encourage a discussion aimed at achieving best practice guidelines for both sides. Whilst there are no specific international rules on SWFs,

various agreements on investment will apply to investments made by SWFs. And, like other investors, SWFs already have to comply with applicable regulatory and disclosure requirements in the countries in which they invest. These best practice guidelines should apply in addition to such existing investment rules:

b) There is the need for clarity of objectives and investment strategies

- The aim is not to differentiate against SWFs compared with other groups and not to compromise the need for SWFs to safeguard sensitive information regarding future commercial investments.
- SWFs should have a clear mandate set around commercial objectives. The investment practices of the funds should be made public.
- Even where SWFs direct investments via third-parties, the overall guidelines should be made clear.
- Set out risk management objectives and policies.

c) The need for best practice on corporate governance and on accountability

- The desire should be to convey world class institutional integrity.
- These funds should be seen as independent bodies, free of government control, and statutory independent from government in the way they pursue their objectives.
- There is a need for clarity of the institutional structure and lines of responsibility within SWFs.
- Good governance guidelines for SWFs could be outlined. There has to be a fiduciary responsibility to shareholders. How should one define such a responsibility needs to be made clear.
- A pre-commitment by SWFs to uphold established guidelines should be called for.
- State corporate responsibility and ethical guidelines.

d) There is a need for greater transparency regarding transactions

- Minimum standards of transparency should be outlined.
- SWFs should be asked to specify a minimum set of information, including size, returns achieved and portfolio composition.
- The best practice of the most open and transparent SWFs should be adopted, with annual statements clarifying investment performance and goals and guidelines around their objectives.
- These annual accounts should be subject to independent and public audits.
- SWFs should make clear any concentrated positions.
- Reporting requirements need to be made clear.
- Some countries may also be worried about leverage and SWFs to make clear any leveraged positions, although that is not, in my view, a concern for many of these SWFs.

Finally, the issue of enforceability needs to be considered. Given the challenge of enforceability when it comes to sovereign nations, it is important that the guidelines outlined are developed in dialogue with the countries from which SWFs emanate. Countries should reserve the right to veto investments by funds not pursuing best practice but need to do this in a way in which is still seen as open to business.

In conclusion, I have focussed on the context, issues raised and implications. There is a need for common ground rules, best practice, and the need to promote an investment framework that is fair and commercially driven. Any constraints on SWFs should be based on an objective appraisal of facts within a stable framework of roles and processes. Yet, as long as investments by SWFs are made for commercial reasons and not for political purposes then these funds should be accepted.

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Chairman BERMAN. Thank you very much, Dr. Lyons.

Dr. Truman?

STATEMENT OF EDWIN TRUMAN, PH.D., SENIOR FELLOW, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. TRUMAN. Thank you, Mr. Chairman and Ranking Member Manzullo and members of the committee. It is a pleasure to testify before you today. I have a longer testimony, which, I assume, will be put in the record.

Chairman BERMAN. Yes.

Mr. TRUMAN. Sovereign wealth funds are funded from foreign exchange reserves, earnings from commodity exports, receipts from privatizations, other fiscal revenues, and pension contributions.

Table 1 in my testimony, which I think you have before you, lists 56 funds of 38 countries. The international assets of all such funds total at least $4 trillion.

These funds, as has been mentioned by Gerard Lyons, have been around for more than half a century. They have a range of structures, mandates, and economic, financial, and political—both domestic and international—objectives, normally a mixture. Consequently, it is perilous to generalize about sovereign wealth funds and any associated potential threats to U.S. foreign policy, national security, or economic interests.

Nevertheless, my summary conclusions are three: First, sovereign wealth funds do not endanger U.S. security or economic interests. We have adequate mechanisms to manage any potential threats they pose, which, at this point, are minimal.

Second, sovereign wealth funds are one of many challenges of global economic and financial change in the 21st century. Whether these particular challenges of globalization are appropriately addressed will have profound implications for the United States and for the world economy and financial system.

Third, the United States should continue to press countries with sovereign wealth funds to design and embrace best practices for those funds to enhance their accountability to citizens of the countries with the funds, as well as to the citizens and markets in which they invest, most relevantly, here in the United States.

At the same time, the United States should minimize economic and political barriers to foreign investment in all forms and from all sources here and around the world.

It is useful to place the activities of sovereign wealth funds in a broader perspective. The estimated size of global capital markets is

more than $190 trillion. Financial assets owned by, or controlled by, governments are, at least, $15 trillion. U.S. Government units own or control more than $3 trillion in assets. The international assets of U.S. sovereign wealth funds are more than $800 billion, mostly in the form of pension funds of state and local governments.

As a result, United States funds are second in combined size to those of the United Arab Emirates. The United States is in the business of sovereign wealth management. We should be careful about what we wish for.

The challenge is to make the world safe for sovereign wealth funds by establishing a voluntary set of best practices. The natural place to start is with current practices. To this end, with the assistance of Doug Dowson, I have created a scoreboard rating 46 of the 56 funds listed in Table 1.

Table 2, attached to the testimony, provides a summary of our results. They point to three take-away observations: First, all sovereign wealth funds are not the same; nor is there one cluster of good funds and another cluster of bad funds. The overall scores range from 95 to 9 out of a possible 100.

Second, although each of the 12 representative pension sovereign wealth funds, shown in italics on the table, is in the top group. That group of 22 funds, which score above 60 on our scale, also includes 10 nonpension sovereign wealth funds. Thus, it is not unreasonable, in my view, to hold nonpension sovereign wealth funds to the standard of accountability of pension funds.

Third, a glance at the order of countries in the table indicates that it is essentially impossible to correlate the ratings of individual funds with the economic or political characteristics of the government investors. For some, this diversity of current practice illustrates the challenge in developing an agreed set of best practices.

In my view, it illustrates an opportunity to converge on a common high standard. For example, a senior representative of the Abu Dhabi Investment Authority in the United Arab Emirates, whose sovereign wealth fund scores at the bottom of my ranking, is co-chairing the IMF-sponsored International Working Group of Sovereign Wealth Funds to develop "a set of sovereign wealth fund principles that will properly reflect their investment practices and objectives."

In my view, the decision by the authorities of the United Arab Emirates to provide a co-chairman for this group implies a commitment by them to enhance substantially the accountability and transparency of the sovereign wealth funds.

In conclusion, the phenomenon of sovereign wealth funds is a permanent future of our global economy and financial system. Their potential implication to the United States' foreign policy, national security, and economic interests may be disquieting, but they do not endanger the United States.

The U.S. authorities should exhaust all multilateral approaches to make the world safe for sovereign wealth funds, in the form sovereign wealth fund best practices and open financial environments, before turning to any additional unilateral remedies for concerns that, to date, are between minimal and nonexistent. Thank you very much.

[The prepared statement of Mr. Truman follows:]

PREPARED STATEMENT OF EDWIN TRUMAN, PH.D., SENIOR FELLOW, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

Chairman Berman, ranking member Ros-Lehtinen, and members of the House Committee on Foreign Affairs, it is a pleasure to testify before you today on the rise of sovereign wealth funds and their potential impacts on U.S. foreign policy and economic interests.

The broadest definition of a sovereign wealth fund (SWF) is a collection of government-owned or government-controlled assets. Narrower definitions may exclude government financial or non-financial corporations, purely domestic assets, foreign exchange reserves, assets owned or controlled by sub-national governmental units, or some or all government pension funds. I use "sovereign wealth fund" as a descriptive term for a separate pool of government-owned or government-controlled assets that includes some international assets. I include all government pension, as well as nonpension, funds to the extent that they manage marketable assets. The basic objectives of both types are essentially the same. They raise virtually identical issues of best practice—the focus of my research and analysis—in government control and accountability regardless of their specific objectives, mandates, or sources of funding.

Sovereign wealth funds are funded from foreign exchange reserves, earnings from commodity exports, receipts from privatizations, other fiscal revenues, or pension contributions. (Table 1 lists 56 sovereign wealth funds of 38 countries.) These funds have been around for more than half a century with a range of structures, mandates, and economic, financial, and political (domestic and international) objectives—normally a mixture.[1] Consequently, it is perilous to generalize about sovereign wealth funds and associated potential threats to U.S. foreign policy, national security, or economic interests.

Nevertheless, my summary conclusions are three:

First, sovereign wealth funds do not pose a significant new threat to U.S. security or economic interests. We have adequate mechanisms to manage any potential threats they pose, which at this point are likely to be minimal.

Second, SWFs are one of the many challenges of global economic and financial change in the 21st century. Whether these particular challenges of globalization are appropriately addressed will have profound implications for the United States and for the world economy and financial system.

Third, the United States should continue to press countries with sovereign wealth funds to design and embrace best practices for these funds to enhance their accountability to citizens of the countries with the funds as well as to the citizens and markets in which they invest. At the same time, the United States should continue to try to minimize economic and political barriers to foreign investment in all forms from all sources here and around the world. Financial protectionism is the wrong answer to the very real challenges of financial globalization and the associated potential for global financial turbulence. The United States cannot disengage from evolving changes in the global financial system. If we were merely to hint that we are tempted to do so, we would risk catastrophic damage to the U.S. and world economies.

It is useful to place the activities of sovereign wealth funds in a broader perspective. At the end of 2006, the estimated size of global capital markets was $190 trillion.[2] A conservative estimate of financial assets owned or controlled by governments is $15 trillion, or about 8 percent of global financial assets.[3] Governments in

[1] Table 1 also lists the dates when the funds were established, the sources of their funding, and estimates of their size. The table includes 44 SWFs that I have been able to identify that are not hard-wired to government pension funds and 12 representative pension SWFs. Note that the data in table 1, in the other tables attached to this testimony, and described in the text include the government pension SWFs of Chile and Thailand that were not part of the analysis presented in my *Blueprint for Sovereign Wealth Fund Best Practices* released as Policy Brief 08–3 by the Peterson Institute for International Economics, April 1, 2008.

[2] International Monetary Fund, *Global Financial Stability Report*, April 2008, table 3. The total includes stock market capitalization, public and private debt securities, and commercial bank assets.

[3] This estimate includes $6 trillion in foreign exchange reserves, $6 trillion in government pension funds (excluding the U.S. social security fund and government pension funds that invest exclusively in government assets or are not involved in the management of marketable assets), and $3 trillion in assets of nonpension sovereign wealth funds.

the United States own or control more than $3 trillion (20 percent) of the total.[4] Thus, the United States is in the business of sovereign wealth management. Consequently, we should be careful what we wish for.

International assets owned or controlled by governments are at least $10 trillion: $6 trillion in foreign exchange reserves, $2.7 trillion in assets of nonpension SWFs, and at least $1.3 trillion in government pension funds.[5] Excluding our modest holdings of foreign exchange reserves, international assets of U.S. SWFs are about $800 billion mostly in the form of the pension funds of state and local governments. Thus, U.S. sovereign wealth funds, as a group, are second to the United Arab Emirates in their holdings of international assets.

As an additional point of reference, at the end of 2006, U.S. total holdings of foreign assets were $13.8 trillion. About 92 percent was managed by the private sector. Foreign holdings of U.S. assets were $16.3 trillion. At least 17 percent was managed by the public sector.[6] U.S. holdings of international financial assets are at least 20 percent of the global total. In other words, the U.S. economy is thoroughly intertwined with the global financial system on both the asset and liability side of our balance sheet through both the private and public sectors.

Over the past five years, the size of the global capital market has doubled, but asset holdings of SWFs have at least tripled. The explosive growth of SWFs reflects the sustained rise in commodity prices as well as global imbalances. However, the increased international diversification of financial portfolios—the weakening of so-called home bias—is as least as important as macroeconomic factors in explaining the growth of SWFs.

The increasing relative importance of SWFs has exposed two tensions as part of the ongoing globalization of the international financial system.

The first is the dramatic redistribution of international (or cross-border) wealth from the traditional industrial countries, like the United States, to countries that historically have not been major players in international finance. The newcomers have had little or no role in shaping the practices, norms, and conventions governing the system.

The second is the fact that governments own or control a substantial share of the new international wealth. This redistribution from private to public hands implies a decision-making orientation that is at variance with the traditional private-sector, market-oriented framework with which most of us are comfortable even though own system does not fully conform to that ideal.

These twin tensions, in turn, are manifested in five broad concerns.

First, governments may mismanage their international investments to their own economic and financial detriment, including large-scale corruption in handling the huge amounts involved. It is a well known, though often ignored, regularity that governments are not good at picking economic winners; for example, government-owned banks tend to be less profitable than private banks. This concern about mismanagement is the principal reason why it is in the interests of every country with a SWF to favor the establishment of internationally agreed SWF best practices. Moreover, greater accountability of such funds is in the foreign policy interest of the United States because the mismanagement of SWF investments could lead to political as well as economic instability in countries with such funds.

Second, governments may manage SWF investments in pursuit of political objectives—raising national security concerns—or economic power objectives—for example, promoting state-owned or state-controlled national champions as global champions. Such behavior contributes not only to political conflicts between countries but also to economic distortions.

Third, financial protectionism may be encouraged in host countries in anticipation of the pursuit of political or economic objectives by the funds or in response to their actual actions. Development of and compliance with SWF best practices would help

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[4] U.S. governmental financial assets include $3 trillion in state and local government pension funds, $50 billion in other sub-national SWF assets, and $40 billion in foreign exchange reserves.

[5] Based on various estimates, government pension funds around the world hold about $6 trillion in assets and roughly 25 percent of those are foreign.

[6] U.S. and foreign data on the international stocks and flows of financial assets generally do not distinguish government from non-government holders. The above estimate of assets controlled by U.S. governmental units includes federal government assets as reported by the Commerce Department (The U.S. Net International Investment Position at Yearend 2006, Bureau of Economic Analysis, BEA 07–31, June 28, 2007) plus estimated holdings of $750 billion by state and local government pension funds that are included in our statistics among private sector assets. In the same Commerce Department release, foreign official assets in the United States include foreign exchange reserves and some holdings of sovereign wealth funds, but the data as collected do not distinguish between the two categories.

to diffuse this source of backlash against globalization. At the same time, countries receiving SWF investments should be as open as possible to such investments subject to the constraints of national security considerations narrowly defined.

Fourth in the management of their international assets, SWFs may contribute to market turmoil and uncertainty. They also may contribute to financial stability, but their net contribution is difficult to establish a priori, in particular if their operations are opaque but also because judgments can only be reached on a case by case basis.

Fifth, foreign government owners of the international assets may come into conflict with the governments of the countries in which they are investing. For example, government ownership adds a further dimension in balancing open markets and appropriate macroprudential regulation.

At this point, these concerns, with the important exception of the first—potential adverse implications for the home countries—are largely in the realm of the hypothetical. The others are much more salient in the context of cross-border investments by government-owned or government-controlled financial or non-financial corporations. Nevertheless, a loud, often acrimonious, public discourse about SWFs is underway in many countries, and not only in countries receiving SWF investments.

In my view, the challenge is to make the world safe for sovereign wealth funds through the establishment of an internationally agreed voluntary set of best practices. The natural place to start is with the current practices of individual funds today. To this end, I have created with the assistance of Doug Dowson a scoreboard for 46 of the 56 funds listed in table 1, including the 12 pension SWFs.[7] The scoreboard rates funds on their current practices and includes 33 elements grouped in four categories: structure, governance, accountability and transparency, and behavior. We have scored the funds based on systematic, regularly available, public information. At least one fund receives a positive score on each element. In fact at least several do.

Table 2 attached provides a summary of the scoreboard results for all elements and for each of the four categories.[8] These results point to three take-away observations:

First, all sovereign wealth funds are not the same. Nor is there one cluster of "good" funds and another cluster of "bad' funds. The overall scores range from 95 to 9 out a possible 100. The rating of each of them can be improved. The funds fall in three broad groups: 22 funds with scores above 60, 14 funds with scores below 30, and 10 funds in a middle group. Moreover, the grouping of scores is essentially identical if one examines only the category of accountability and transparency.[9]

Second, although each of the 12 representative pension SWFs is in the top group, that group of 22 funds also includes 10 nonpension SWFs. Thus, it is not unreasonable to hold nonpension SWFs to the standard of accountability of pension funds. Chile's pension and nonpension SWFs both score in the top group. On the other hand, China's National Social Security Fund is in the top group, but the China Investment Corporation is in the bottom group.

Third, it is essentially impossible to correlate the ratings of the individual funds with the economic or political characteristics of their government owners. For example, the top group includes seven of the 14 funds with estimated assets of more than $100 billion, but four are in the second group, and two are in the third group.[10] The top group includes funds of a number of developing countries, including Azerbaijan, Chile, China, Kazakhstan, Thailand, and Timor-Leste. The middle group includes funds of non-industrial countries as diverse as Russia, Mexico, Kuwait, and Singapore, whose two funds are in this group. Singapore's two funds have close-to-identical overall scores, but their scores differ on many individual elements. The bottom group includes three funds from Abu Dhabi each of which has an excellent reputation in financial markets.

For some this diversity of current practice illustrates the challenge in developing a common set of best practices. In my view, it illustrates the opportunity to converge on a common high standard. A senior representative of the Abu Dhabi Investment Authority is co-chairing, with the director of the IMF's monetary and capital markets department, the International Working Group of Sovereign Wealth Funds to

[7] We scored the two new Russian SWFs as the single fund it was before its recent transformation. The remaining nine funds, indicated by "c" in table 1, are either too new to score or we could not find sufficient information to do so.

[8] Table 3 provides the results for each fund on each element. The appendix provides a list of the 33 elements.

[9] The two exceptions are the National Oil Account of São Tomé and Principe, which drops into the bottom group of funds, and Singapore's Temasek, which moves into the top group..

[10] The fourteenth was not scored: the nonreserve holdings reported by the Saudi Arabian Monetary Agency.

develop "a set of SWF principles that properly reflects their investment practices and objectives."[11] The decision by the authorities of the United Arab Emirates to provide a co-chairman for this group implies a commitment by them to enhance substantially the accountability and transparency of their SWFs.

In his letter of invitation to testify before this committee today, Chairman Berman raised three issues, other than the phenomenon of SWFs and their accountability and transparency, on which I have not yet commented explicitly.

First, he asked whether sovereign wealth funds have the potential to disrupt financial markets. All investors with large portfolios have the potential to disrupt financial markets whatever their motivation. However, the very size of their portfolios helps to inhibit them from doing so, in other words, discourages them from shooting themselves in their feet.

At the same time, it is inappropriate in my opinion to view SWFs as cornucopias available to be tapped to rescue the U.S. or the global financial system. For every SWF investment in a U.S. financial institution, that fund has to disinvest, or not invest, in some other asset, normally in the United States or at least in U.S. dollars.

Some observers of private equity firms and hedge funds have concerns about their implications for the stability of our economy and financial system. I do not share most of those concerns though I have long favored increased transparency for large private equity firms and hedge funds. However, the facts do not support those who argue that SWFs are not like hedge funds and private equity firms in their speculative activities. Sovereign wealth funds invest in hedge funds, in private equity firms, and in other highly leveraged financial institutions whose activities, including the use of leverage, are indistinguishable from hedge funds and private equity firms. In effect, sovereign wealth funds are providing the capital that those firms subsequently leverage to generate high rates of return for the funds. They are no different from other investors except that their stakes may be measured in the billions rather than in the hundreds of millions of dollars.

Second, Chairman Berman asked more generally whether the foreign policy and national security interests of countries with sovereign wealth funds pose a threat to the United States. It follows from what I have already said that my short answer is no.

I am not an expert on the foreign policy and national interests of each of the more than 30 countries with nonpension SWFs to say nothing of the additional countries that only have pension SWFs. However, it is clear that the interests the individual countries are diverse, and perceptions of those countries fluctuate over time, in part, reflecting differences in the development and evolution of their political and social systems.

Policymakers are primarily interested in issues of underlying investment control even if they do not agree on how to define that concept. In this context, government owned or controlled financial and nonfinancial corporations are much more relevant because, in general, their activities are more focused and more easily integrated with foreign policy and national security objectives.

Although some SWFs do take controlling interests via their investments, more than half of the 46 funds we scored have explicit policies against doing so. A substantial proportion of the remaining 22 funds also do not seek controlling interests, but they do not have explicit, public policies in this area. Of course, it is possible to pursue foreign policy or national security interests without taking a controlling investment interest, but it is more difficult, and the investment interest is likely to be more narrowly focused and more easily identified. The essential point is that the activities of a few countries that have sovereign wealth funds and may use them to pursue political and economic interests should not be conflated with the motivations of the vast majority of countries that have such funds.

Finally, Chairman Berman asked for thoughts on how the U.S. Congress and the Administration can best "manage" sovereign wealth fund investing in the United States. I interpret his question as asking how the Congress and Administration should best respond to the phenomenon of sovereign wealth funds.

Notwithstanding my view that the greatest risks associated with SWFs are to the citizens of the countries whose governments have accumulated the large stocks of international assets, authorities in the United States and other countries where those assets are invested also have legitimate concerns about how they will be managed. Those concerns focus primarily on acquisition of large or controlling stakes by foreign governments in private institutions. As noted, at present this is the exception not the rule for SWFs. However, one area of concern and potential conflict is

[11] See IMF press release 08/97 dated May 1, 2008, "International Working Group of Sovereign Wealth Funds is Established to Facilitate Work on Voluntary Principles."

the apparent use by a few countries, such as China and potentially Brazil, to use their SWFs to promote the expansion of their own economic enterprises.

Of course, the current, largely benign pattern could change, and foreign government-owned or government-controlled financial and nonfinancial corporations do acquire stakes in companies in other countries, including controlling stakes. The 2007 Foreign Investment and National Security Act (FINSA) revised the framework and procedures of the Committee on Foreign Investment in the United States (CFIUS). With these changes and the existing powers of the Securities and Exchange Commission as well as other U.S. financial regulators, we are well positioned to evaluate and, if necessary, to mitigate, to block, or to pursue any U.S. acquisitions or investment by a SWF or other foreign government entity to protect our national security or to enforce our laws and regulations governing financial markets and institutions.

With respect to economic security concerns, the greatest risk to the U.S. economy is that we will erect unnecessary barriers to the free flow of capital into our economy and, in the process, contribute to the erection of similar barriers in other countries to the detriment of the health and continued prosperity of the U.S. and global economies. We may not in all cases be comfortable with the consequences of the free flow of finance and investment either internally or across borders, but on balance it promotes competition and efficiency. We should exhaust all multilateral approaches before pursuing bilateral remedies, and any such bilateral remedies should be narrowly focused.

To this end, I endorse the Administration's support of the OECD process designed to strengthen the framework that the United States and other OECD member countries use to govern foreign investment including by governmental entities. At present that framework does not, in principle, extend to non-members of the OECD though often it does in practice. The United States should support its explicit extension to all countries.

My hope is that the OECD process will provide sufficient reassurance to countries with sovereign wealth funds so that, with the facilitation of the IMF, they can reach agreement on and fully comply with a voluntary set of best practices for their funds.

How should that IMF-facilitated effort be judged when it is completed in the fall of this year?

One test is whether the resulting set of best practices covers substantively all the elements included in my scoreboard. Of course, it is not essential to cover them precisely in the form outlined in the appendix to this testimony. However, each element should be adequately addressed. A significant omission should be seen as falling short of expectations.

A second test of success is whether the best practices are embraced by substantially all countries with large SWFs. Table 1 lists 14 SWFs with more than $100 billion in total assets. If each of them were to adhere to the prospective set of best practices, it is less critical that the others do so immediately. For each country, including those that choose not to adhere fully or at all, the minimum expectation should be that the country would comply, or it should explain why it does not do so in whole or in part.

A third test is the quality of compliance by the countries that embrace the best practices. If they are drawn up properly, the best practices should be self-enforcing. Politicians, the media, financial-market participants, and the general public in the home and host countries should be able to determine the degree of compliance.

On the other hand, if the voluntary best practices agreed under the auspices of the IMF are less precise than they should be, it will be necessary to have some mechanism to report on compliance. That function might be lodged in the IMF or the World Bank, which have experience with respect to overseeing compliance with 12 of the many existing international standards and codes. As is the case with existing standards subject to IMF and World Bank surveillance and oversight, the resulting process of implicit naming and shaming, combined with peer pressure from other SWFs that want to avoid the application of draconian restrictions to their activities, should contribute to a high level of compliance within a short period.

Some may favor supervisory inspections of SWFs beyond those that would be covered by IMF and World Bank surveillance plus published, independent audits as called for in my scoreboard. To my knowledge, no official has said so publicly. However, to advocate this type of supervision would sharply escalate the SWF debate from one about the content of and adherence to internationally agreed voluntary best practices to one about explicit regulation. At this point, such an escalation is neither appropriate nor justified on the merits.

On the recipient side, many countries today have (very diverse) regimes covering foreign direct investment in their countries. Pending the establishment of a broad consensus on those regimes as they apply to government investments, such as is being pursued within the OECD, and perhaps even in that context, the United

States and other similarly situated countries might reasonably decide to take account of a country's voluntary compliance with the international best practices for SWFs as one of a number of factors considered in making determinations about whether a particular SWF's investment should be blocked because of a threat to national security. For example, in a March 13 letter sent to U.S. Treasury Secretary Henry Paulson, Representatives Barney Frank, Carolyn Maloney, and Luis Gutierrez suggested that a country's compliance with aspects of SWF best practices could be used by the CFIUS as a factor in determining whether the committee should grant that country a waiver from a full investigation under FINSA of an investment, for example, by a government-owned pension fund.

More controversially, some observers have suggested that an SWF that takes even a noncontrolling stake in a company should be forbidden from voting its shares, presumably increasing the probability that the investment is "passive." My understanding is that there is no generally accepted legal definition of a passive investment. (I note that the proposed CFIUS regulations implementing the FINSA instead seek to define interests that are "solely for the purpose of investment," which is a more limited approach.) To limit the voting rights of government investors, if applied uniformly, would disenfranchise as much as several trillion dollars of investments by U.S. state and local government pension funds. If the United States did not apply this type of restriction to domestic pension SWFs, it would still risk disenfranchising U.S. government pension funds in their investment operations abroad. The reason is that it would be difficult to apply such a restriction to foreign nonpension SWFs and not to foreign pension SWFs. As a consequence, foreign governments almost certainly would retaliate in kind.

U.S. Treasury Assistant Secretary Clay Lowery has suggested a more sensible approach: either an SWF should choose voluntarily not to vote its shares or it should disclose how it votes, as is now done voluntarily by some U.K. institutional investors and is required by the Securities and Exchange Commission for U.S. mutual funds. The objective of the SEC rule for mutual funds is to address concerns about conflicts of interest and, as noted earlier, similar concerns arise with respect to SWFs. Presumably, the SWF would not face a formal SEC reporting requirement in this area; that would raise a host of other process and jurisdictional issues and also serve to escalate the SWF debate.

In conclusion, the phenomenon of sovereign wealth funds is a permanent feature of our global economy and financial system. Their potential impacts on U.S. foreign policy, national security, and economic interests may be disquieting, but they do not endanger the United States. U.S. authorities should exhaust all multilateral approaches to make the world safe for SWFs—in the form of SWF best practices and open financial environments—before turning to any additional, bilateral remedies for concerns that to date are between minimal and nonexistent.

Table 1: Sovereign wealth funds

Country	Current Name	Date Established	Source of Funds	Current Size[a] (billions of US dollars)	
NONPENSION FUNDS					
Algeria	Revenue Regulation Fund	2000	Natural resources	47	
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	1999	Natural resources	2	
Botswana	Pula Fund[b]	1993	Natural resources	7	
Brunei	Brunei Investment Agency	1983	Natural resources	35	(e)
Canada	Alberta Heritage Savings Trust Fund[d]	1976	Natural resources	17	
Chile	Economic and Social Stabilization Fund	2006	Natural resources	15	
China	China Investment Corporation[d]	2007	Foreign exchange reserves	200	
	Shanghai Financial Holdings[c,d]	2007	Fiscal surpluses	1	(e)
Gabon	Fund for Future Generations[c]	1998	Natural resources	0.4	(e)
Hong Kong	Exchange Fund Investment Portfolio[b,d]	1993	Foreign exchange reserves, fiscal surpluses	139	
Iran	Oil Stabilization Fund	2000	Natural resources	10	
Kazakhstan	National Fund for the Republic of Kazakhstan	2000	Natural resources	23	
Kiribati	Revenue Equalization Reserve Fund	1956	Natural resources	1	(e)
Korea	Korea Investment Corporation[b]	2005	Foreign exchange reserves	30	
Kuwait	Kuwait Investment Authority[d]	1953	Natural resources	213	
Libya	Libyan Investment Authority[c]	2006	Natural resources	50	
Malaysia	Khazanah Nasional[d]	1993	Fiscal surpluses	18	
Mexico	Oil Income Stabilization Fund	2000	Natural resources	5	
Nigeria	Excess Crude Account[b]	2003	Natural resources	17	(e)
Norway	Government Pension Fund – Global	1990	Natural resources	375	
Oman	State General Reserve Fund	1980	Natural resources	13	(e)
Qatar	Qatar Investment Authority	2005	Natural resources	60	(e)
Russia	National Wealth Fund[b]	2008	Natural resources	32	
	Reserve Fund[b]	2008	Natural resources	128	
São Tomé and Príncipe	National Oil Account	2004	Natural resources	0.02	(e)
Saudi Arabia	Saudi Arabian Monetary Agency[c]	1952	Natural resources	270	
Singapore	Government of Singapore Investment Corporation[b]	1981	Foreign exchange reserves, fiscal surpluses, employee contributions	200 – 330	(e)
	Temasek Holdings[d]	1974	Government enterprises	110	
Sudan	Oil Revenue Stabilization Account	2002	Natural resources	0.1	
Timor-Leste	Petroleum Fund	2005	Natural resources	2	
Trinidad and Tobago	Heritage and Stabilization Fund	2007	Natural resources	2	(e)
United Arab Emirates	Emirates Investment Authority[c]	2007	Natural resources	n.a.	
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	1976	Natural resources	500 – 875	(e)
	International Petroleum Investment Company[c]	1984	Natural resources	12	
	Mubadala Development Company	2002	Natural resources	10	(e)
United Arab Emirates (Dubai)	DIFC Investments[c]	2006	Natural resources	n.a.	
	Dubai International Capital[c]	2004	Natural resources	13	
	Investment Corporation of Dubai[c]	2006	Natural resources	82	(e)
	Istithmar	2003	Natural resources	12	(e)
United States	Alaska Permanent Fund[d]	1976	Natural resources	37	
	Permanent Mineral Trust Fund (Wyoming)[d]	1974	Natural resources	4	
	Severance Tax Permanent Fund (New Mexico)[d]	1973	Natural resources	5	
Venezuela	Macroeconomic Stabilization Fund	1998	Natural resources	1	
	National Development Fund	2005	Natural resources	21	
Subtotal[e]				**2,972**	
PENSION FUNDS					
Australia	Future Fund[d]	2006	Fiscal surpluses	53	
Canada	Canada Pension Plan[d]	1966	Employee contributions	121	
	Caisse de dépôt et placement du Québec[d]	1965	Employee contributions	157	
Chile	Pension Reserve Fund	2006	Fiscal surpluses	2	
China	National Social Security Fund[d]	2000	Fiscal surpluses	71	
France	Fonds de réserve pour les retraites[d]	2001	Fiscal surpluses	50	
Ireland	National Pensions Reserve Fund[d]	2001	Fiscal surpluses	31	
Japan	Government Pension Investment Fund[d]	1961	Employee contributions	1,274	
Netherlands	Stichting Pensioenfonds ABP[d]	1922	Employee contributions	316	
New Zealand	Superannuation Fund[d]	2001	Fiscal surpluses	10	
Thailand	Government Pension Fund[d]	1996	Employee contributions and fiscal surpluses	13	
United States	California Public Employees' Retirement System[d]	1932	Employee contributions	237	
Subtotal				**2,337**	
Total[e]				**5,308**	

(e) = estimate; n.a. = not available

a. Data are from the end of 2007 or the most recent date available.
b. Some or all assets are included in reserves.
c. Excluded from scoreboard.
d. A portion of the holdings is in domestic assets.
e. Total uses the midpoint of the range of estimates.

Sources: National authorities, IMF, other public sources.

Table 2: Summary sovereign wealth fund scoreboard (percent of maximum possible points)

Country	Fund	Structure	Governance	Accountability & Transparency	Behavior	Total
Canada	*Canada Pension Plan*	100	100	96	83	95
New Zealand	*Superannuation Fund*	100	100	100	75	95
United States (Alaska)	Alaska Permanent Fund	100	80	100	83	94
Canada (Québec)	*Caisse de dépôt et placement du Québec*	100	100	89	83	92
France	*Fonds de réserve pour les retraites*	100	100	89	83	92
Norway	Government Pension Fund – Global	94	100	100	67	92
United States (California)	*California Public Employees' Retirement System*	100	100	96	67	92
United States (Wyoming)	Permanent Mineral Trust Fund	100	90	82	100	91
Japan	*Government Pension Investment Fund*	100	90	80	83	87
Ireland	*National Pensions Reserve Fund*	100	100	86	58	86
United States (New Mexico)	Severance Tax Permanent Fund	100	50	86	100	86
Netherlands	*Stichting Pensioenfonds ABP*	100	100	86	50	85
Thailand	*Government Pension Fund*	100	100	88	42	84
Australia	*Future Fund*	100	80	68	83	80
Timor-Leste	Petroleum Fund for Timor-Leste	100	40	96	50	80
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	88	60	89	50	77
China	*National Social Security Fund*	100	40	82	67	77
Canada (Alberta)	Alberta Heritage Savings Trust Fund	94	60	79	50	74
Chile	Economic and Social Stabilization Fund	94	60	86	17	71
Chile	*Pension Reserve Fund*	94	60	86	17	71
Hong Kong	Exchange Fund	88	40	79	33	67
Kazakhstan	National Fund for the Republic of Kazakhstan	88	60	64	33	64
Botswana	Pula Fund	69	60	54	33	55
Trinidad and Tobago	Heritage and Stabilization Fund	100	60	46	0	53
Korea	Korea Investment Corporation	75	60	45	25	51
Russia	Reserve Fund and National Wealth Fund	72	40	50	33	51
São Tomé and Príncipe	National Oil Account	100	60	29	17	49
Kuwait	Kuwait Investment Authority	75	60	41	0	49
Mexico	Oil Income Stabilization Fund	69	20	43	50	47
Singapore	Temasek Holdings	50	50	61	0	45
Singapore	Government of Singapore Investment Corporation	63	40	39	17	41
Malaysia	Khazanah Nasional	44	50	46	0	38
China	China Investment Corporation	50	50	14	17	29
Kiribati	Revenue Equalization Reserve Fund	69	60	7	0	29
Algeria	Revenue Regulation Fund	56	40	11	17	27
Nigeria	Excess Crude Account	50	30	14	17	26
Iran	Oil Stabilization Fund	50	20	18	0	23
Venezuela	Macroeconomic Stabilization Fund	50	0	18	17	23
Venezuela	National Development Fund	38	0	27	0	20
Oman	State General Reserve Fund	50	0	18	0	20
Sudan	Oil Revenue Stabilization Account	56	0	14	0	20
Brunei Darussalam	Brunei Investment Agency	31	0	25	0	18
United Arab Emirates (Abu Dhabi)	Mubadala Development Company	44	10	7	0	15
United Arab Emirates (Dubai)	Istithmar World	38	10	7	0	14
Qatar	Qatar Investment Authority	34	0	2	0	9
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	25	0	4	8	9
Subtotal Nonpension		68	41	44	25	46
Subtotal Pension		99	89	87	66	87
Total		76	53	55	35	56

Note: Pension funds are in italics.

Table 3: Scoreboard for sovereign wealth funds

		Structure								
			Fiscal Treatment							
		Objective Stated	Source of Funding	Use of Fund Earnings	Integrated with Budget	Guidelines Followed	Investment Strategy	Changes in the Structure	Separate from International Reserves	Subtotal
NONPENSION FUNDS										
Algeria	Revenue Regulation Fund	1	1	0.5	0	0	0	1	1	4.5
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	1	1	0.5	1	1	0.5	1	1	7
Botswana	Pula Fund	1	0.5	1	1	1	1	0	0	5.5
Brunei Darussalam	Brunei Investment Agency	1	0.5	0	0	0	0	1	0	2.5
Canada (Alberta)	Alberta Heritage Savings Trust Fund	1	1	1	1	0.5	1	1	1	7.5
Chile	Economic and Social Stabilization Fund	1	1	1	1	1	0.5	1	1	7.5
China	China Investment Corporation	1	1	0	0	0	1	0	1	4
Hong Kong	Exchange Fund	1	1	1	1	1	1	1	0	7
Iran	Oil Stabilization Fund	1	1	0.5	0	0	0	0.5	1	4
Kazakhstan	National Fund for the Republic of Kazakhstan	1	1	1	1	0.5	1	0.5	1	7
Kiribati	Revenue Equalization Reserve Fund	1	1	1	1	0	0.5	1	0	5.5
Korea	Korea Investment Corporation	1	1	0	1	1	1	1	0	6
Kuwait	Kuwait Investment Authority	1	1	0	1	0	1	1	1	6
Malaysia	Khazanah Nasional	1	1	0	0	0	0.5	0	1	3.5
Mexico	Oil Income Stabilization Fund	1	1	0.5	1	0	0.5	0.5	1	5.5
Nigeria	Excess Crude Account	1	1	1	0	0	0	1	0	4
Norway	Government Pension Fund – Global	1	1	1	1	0.5	1	1	1	7.5
Oman	State General Reserve Fund	0.5	1	0.5	0.5	0	0	0.5	1	4
Qatar	Qatar Investment Authority	1	0	0	0	0	0.25	0.5	1	2.75
Russia	Reserve Fund and National Wealth Fund	1	1	0.5	1	1	0.25	1	0	5.75
São Tomé and Principe	National Oil Account	1	1	1	1	1	1	1	1	8
Singapore	Government of Singapore Investment Corporation	1	0.5	1	1	1	0.5	0	0	5
Singapore	Temasek Holdings	1	1	0	0	0	1	0	1	4
Sudan	Oil Revenue Stabilization Account	0.5	1	0.5	1	0.5	0	0	1	4.5
Timor-Leste	Petroleum Fund for Timor-Leste	1	1	1	1	1	1	1	1	8
Trinidad and Tobago	Heritage and Stabilization Fund	1	1	1	1	1	1	1	1	8
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	0.5	0	0	0	0	0.5	0	1	2
United Arab Emirates (Abu Dhabi)	Mubadala Development Company	1	0	0	0	0	0.5	1	1	3.5
United Arab Emirates (Dubai)	Istithmar World	1	0.5	0	0	0	0.5	0	1	3
United States (Alaska)	Alaska Permanent Fund	1	1	1	1	1	1	1	1	8
United States (New Mexico)	Severance Tax Permanent Fund	1	1	1	1	1	1	1	1	8
United States (Wyoming)	Permanent Mineral Trust Fund	1	1	1	1	1	1	1	1	8
Venezuela	Macroeconomic Stabilization Fund	1	1	0	0	0	0.5	0.5	1	4
Venezuela	National Development Fund	0.5	0.5	0	0	0	0	1	1	3
Total [a]		**32**	**28.5**	**18.5**	**20.5**	**15**	**20.5**	**23**	**26**	**5.4**
PENSION FUNDS										
Australia	Future Fund	1	1	1	1	1	1	1	1	8
Canada	Canada Pension Plan	1	1	1	1	1	1	1	1	8
Canada (Québec)	Caisse de dépôt et placement du Québec	1	1	1	1	1	1	1	1	8
Chile	Pension Reserve Fund	1	1	1	1	1	0.5	1	1	7.5
China	National Social Security Fund	1	1	1	1	1	1	1	1	8
France	Fonds de réserve pour les retraites	1	1	1	1	1	1	1	1	8
Ireland	National Pensions Reserve Fund	1	1	1	1	1	1	1	1	8
Japan	Government Pension Investment Fund	1	1	1	1	1	1	1	1	8
Netherlands	Stichting Pensioenfonds ABP	1	1	1	1	1	1	1	1	8
New Zealand	Superannuation Fund	1	1	1	1	1	1	1	1	8
Thailand	Government Pension Fund	1	1	1	1	1	1	1	1	8
United States (California)	California Public Employees' Retirement System	1	1	1	1	1	1	1	1	8
Total [a]		**12**	**12**	**12**	**12**	**12**	**11.5**	**12**	**12**	**8.0**
GRAND TOTAL[a]		**44**	**40.5**	**30.5**	**32.5**	**27**	**32**	**35**	**38**	**6.1**

a. For each category the value under subtotal represents the average for all funds.

Table 3: Scoreboard for sovereign wealth funds (continued)

		Governance						Accountability & Transparency			
								Investment Strategy Implementation			
		Role of Government	Role of Managers	Decisions made by managers	Guidelines for Corporate Responsibility	Ethical Guidelines	Subtotal	Categories	Benchmarks	Credit Ratings	Mandates
NONPENSION FUNDS											
Algeria	Revenue Regulation Fund	1	1	0	0	0	2	0	0	0	1
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	1	1	1	0	0	3	1	1	1	1
Botswana	Pula Fund	1	1	1	0	0	3	1	1	1	0
Brunei Darussalam	Brunei Investment Agency	0	0	0	0	0	0	0	0	0	1
Canada (Alberta)	Alberta Heritage Savings Trust Fund	1	1	1	0	0	3	1	1	0.5	0
Chile	Economic and Social Stabilization Fund	1	1	1	0	0	3	1	1	1	1
China	China Investment Corporation	1	1	0	0.5	0	2.5	0.5	0.5	0	0
Hong Kong	Exchange Fund	1	1	0	0	0	2	1	1	1	0
Iran	Oil Stabilization Fund	0.5	0.5	0	0	0	1	0	0	0	1
Kazakhstan	National Fund for the Republic of Kazakhstan	1	1	1	0	0	3	0.5	1	1	0
Kiribati	Revenue Equalization Reserve Fund	1	1	1	0	0	3	0	0	0	0
Korea	Korea Investment Corporation	1	1	1	0	0	3	0.5	0.5	1	0
Kuwait	Kuwait Investment Authority	1	1	1	0	1	4	0	0.5	1	0
Malaysia	Khazanah Nasional	0.5	1	0.5	0.5	0	2.5	0.5	1	0	0
Mexico	Oil Income Stabilization Fund	0.5	0.5	0	0	0	1	0	0	0	0
Nigeria	Excess Crude Account	0.5	1	0	0	0	1.5	0	0	0	1
Norway	Government Pension Fund – Global	1	1	1	1	1	5	1	1	1	1
Oman	State General Reserve Fund	0	0	0	0	0	0	0	0	0	0
Qatar	Qatar Investment Authority	0	0	0	0	0	0	0	0	0	0
Russia	Reserve Fund and National Wealth Fund	1	1	0	0	0	2	1	0	1	1
São Tomé and Principe	National Oil Account	1	1	1	0	0	3	0.5	0	0	1
Singapore	Government of Singapore Investment Corporation	0.5	0.5	1	0	0	2	0.5	1	0.5	0
Singapore	Temasek Holdings	0	1	1	0.5	0	2.5	0.5	0.5	0	0
Sudan	Oil Revenue Stabilization Account	0	0	0	0	0	0	0	0	0	1
Timor-Leste	Petroleum Fund for Timor-Leste	1	1	0	0	0	2	1	0.5	1	1
Trinidad and Tobago	Heritage and Stabilization Fund	1	1	1	0	0	3	1	0.5	0	1
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	0	0	0	0	0	0	0.25	0.25	0	0
United Arab Emirates (Abu Dhabi)	Mubadala Development Company	0	0.5	0	0	0	0.5	0	0.5	0	0
United Arab Emirates (Dubai)	Istithmar World	0	0.5	0	0	0	0.5	0.25	0	0	0
United States (Alaska)	Alaska Permanent Fund	1	1	1	1	0	4	1	1	1	1
United States (New Mexico)	Severance Tax Permanent Fund	1	1	0.5	0	0	2.5	1	1	1	1
United States (Wyoming)	Permanent Mineral Trust Fund	1	1	1	0.5	1	4.5	1	1	1	1
Venezuela	Macroeconomic Stabilization Fund	0	0	0	0	0	0	0.5	0	0	1
Venezuela	National Development Fund	0	0	0	0	0	0	0.25	0	0	0
Total [a]		21.5	24.5	16	4	3	2.0	16.75	15.75	14	16
PENSION FUNDS											
Australia	Future Fund	1	1	1	1	0	4	1	1	0.5	1
Canada	Canada Pension Plan	1	1	1	1	1	5	1	1	1	1
Canada (Québec)	Caisse de dépôt et placement du Québec	1	1	1	1	1	5	1	1	0.5	1
Chile	Pension Reserve Fund	1	1	1	0	0	3	1	1	1	1
China	National Social Security Fund	1	1	0	0	0	2	1	1	1	1
France	Fonds de réserve pour les retraites	1	1	1	1	1	5	1	1	1	1
Ireland	National Pensions Reserve Fund	1	1	1	1	1	5	1	1	0	1
Japan	Government Pension Investment Fund	1	1	1	1	0.5	4.5	1	1	1	1
Netherlands	Stichting Pensioenfonds ABP	1	1	1	1	1	5	1	1	1	0
New Zealand	Superannuation Fund	1	1	1	1	1	5	1	1	1	1
Thailand	Government Pension Fund	1	1	1	1	1	5	1	1	1	1
United States (California)	California Public Employees' Retirement System	1	1	1	1	1	5	1	1	1	1
Total [a]		12	12	11	10	8.5	4.5	12	12	10	11
GRAND TOTAL [a]		33.5	36.5	27	14	11.5	2.7	28.75	27.75	24	27

a. For each category the value under subtotal represents the average for all funds.

Table 3: Scoreboard for sovereign wealth funds (continued)

		Investment Activities					Reports		Audit			
		Size	Returns	Location	Specific Investments	Currency Composition	Annual	Quarterly	Audited	Published	Independent	Subtotal
NONPENSION FUNDS												
Algeria	Revenue Regulation Fund	0.5	0	0	0	0	0	0	0	0	0	1.5
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	1	1	0.5	0	1	1	1	1	1	1	12.5
Botswana	Pula Fund	1	0	0	0	0	1	0.5	1	0	1	7.5
Brunei Darussalam	Brunei Investment Agency	0	0	0	0	0	0.5	0	1	0	1	3.5
Canada (Alberta)	Alberta Heritage Savings Trust Fund	1	1	1	0	0.5	1	1	1	1	1	11
Chile	Economic and Social Stabilization Fund	1	1	1	1	1	1	1	0.5	0	0.5	12
China	China Investment Corporation	1	0	0	0	0	0	0	0	0	0	2
Hong Kong	Exchange Fund	1	1	0.5	0	0.5	1	1	1	1	1	11
Iran	Oil Stabilization Fund	0.5	0.5	0	0	0	0.5	0	0	0	0	2.5
Kazakhstan	National Fund for the Republic of Kazakhstan	1	1	0.25	0	0.25	0.5	0.5	1	1	1	9
Kiribati	Revenue Equalization Reserve Fund	0	0	0	0	0	0.5	0.5	0	0	0	1
Korea	Korea Investment Corporation	1	0.25	0	0	0	0.5	0	1	0.5	1	6.25
Kuwait	Kuwait Investment Authority	1	0.5	0.25	0	0	0.5	0	1	0	1	5.75
Malaysia	Khazanah Nasional	1	1	1	0.5	0	0.5	0	1	0	0	6.5
Mexico	Oil Income Stabilization Fund	1	1	0	0	1	0.5	0.5	0.5	0.5	1	6
Nigeria	Excess Crude Account	0.5	0	0	0	0.5	0	0	0	0	0	2
Norway	Government Pension Fund – Global	1	1	1	1	1	1	1	1	1	1	14
Oman	State General Reserve Fund	0	0	0	0	0	0.5	0	1	0	1	2.5
Qatar	Qatar Investment Authority	0	0	0	0	0.25	0	0	0	0	0	0.25
Russia	Reserve Fund and National Wealth Fund	1	0.5	0.5	0	1	0.5	0.5	0	0	0	7
São Tomé and Príncipe	National Oil Account	0.5	0	0	0	0	0	0	1	0	1	4
Singapore	Government of Singapore Investment Corporation	0	0.25	0.25	0	0	0.5	0.5	1	0	1	5.5
Singapore	Temasek Holdings	1	1	1	0.5	0	1	0	1	1	1	8.5
Sudan	Oil Revenue Stabilization Account	1	0	0	0	0	0	0	0	0	0	2
Timor-Leste	Petroleum Fund for Timor-Leste	1	1	1	1	1	1	1	1	1	1	13.5
Trinidad and Tobago	Heritage and Stabilization Fund	1	0	0	0	0	0.5	0.5	1	0	1	6.5
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	0	0	0	0	0	0	0	0	0	0	0.5
United Arab Emirates (Abu Dhabi)	Mubadala Development Company	0	0	0	0.5	0	0	0	0	0	0	1
United Arab Emirates (Dubai)	Istithmar World	0.5	0	0.25	0	0	0	0	0	0	0	1
United States (Alaska)	Alaska Permanent Fund	1	1	1	1	1	1	1	1	1	1	14
United States (New Mexico)	Severance Tax Permanent Fund	1	1	0	0	1	1	1	1	1	1	12
United States (Wyoming)	Permanent Mineral Trust Fund	1	1	0	0	0.5	1	1	1	1	1	11.5
Venezuela	Macroeconomic Stabilization Fund	1	0	0	0	0	0	0	0	0	0	2.5
Venezuela	National Development Fund	1	0	0	0	0	1	0.5	1	0	0	3.75
Total [a]		24.5	15	9.5	5.5	10.5	18	13	21	11	19.5	6.2
PENSION FUNDS												
Australia	Future Fund	1	1	0	0	0	1	0	1	1	1	9.5
Canada	Canada Pension Plan	1	1	0.5	1	1	1	1	1	1	1	13.5
Canada (Québec)	Caisse de dépôt et placement du Québec	1	1	1	1	1	1	0	1	1	1	12.5
Chile	Pension Reserve Fund	1	1	1	1	1	1	1	0.5	0	0.5	12
China	National Social Security Fund	1	1	0.5	0	0	1	1	1	1	1	11.5
France	Fonds de réserve pour les retraites	1	1	0.5	0	1	1	1	1	1	1	12.5
Ireland	National Pensions Reserve Fund	1	1	1	1	0	1	1	1	1	1	12
Japan	Government Pension Investment Fund	1	1	0.25	0	0	1	1	1	1	1	11.25
Netherlands	Stichting Pensioenfonds ABP	1	1	0.5	1	1	1	0.5	1	1	1	12
New Zealand	Superannuation Fund	1	1	1	1	1	1	1	1	1	1	14
Thailand	Government Pension Fund	1	1	0.25	1	0	1	1	1	1	1	12.25
United States (California)	California Public Employees' Retirement System	1	1	0.5	1	1	1	1	1	1	1	13.5
Total [a]		12	12	7	8	7	12	9.5	11.5	11	11.5	12.2
GRAND TOTAL [a]		36.5	27	16.5	13.5	17.5	30	22.5	32.5	22	31	7.8

a. For each category the value under subtotal represents the average for all funds.

Table 3: Scoreboard for sovereign wealth funds (continued)

		Behavior							Grand Total
						Derivatives			
		Portfolio Adjustment	Limits on Stakes	No Controlling Stakes	Policy on Leverage	Policy on Derivatives	For Hedging Only	Subtotal	
NONPENSION FUNDS									
Algeria	Revenue Regulation Fund	0	0	1	0	0	0	**1**	**9**
Azerbaijan	State Oil Fund of the Republic of Azerbaijan	0	0	1	0	1	1	**3**	**25.5**
Botswana	Pula Fund	0	0	1	0	1	0	**2**	**18**
Brunei Darussalam	Brunei Investment Agency	0	0	0	0	0	0	**0**	**6**
Canada (Alberta)	Alberta Heritage Savings Trust Fund	0	0	0	1	1	1	**3**	**24.5**
Chile	Economic and Social Stabilization Fund	0	0	1	0	0	0	**1**	**23.5**
China	China Investment Corporation	0	0	1	0	0	0	**1**	**9.5**
Hong Kong	Exchange Fund	0	0	0	0	1	1	**2**	**22**
Iran	Oil Stabilization Fund	0	0	0	0	0	0	**0**	**7.5**
Kazakhstan	National Fund for the Republic of Kazakhstan	0	0	0	0	1	1	**2**	**21**
Kiribati	Revenue Equalization Reserve Fund	0	0	0	0	0	0	**0**	**9.5**
Korea	Korea Investment Corporation	0.5	0	0	0	1	0	**1.5**	**18.75**
Kuwait	Kuwait Investment Authority	0	0	0	0	0	0	**0**	**16.75**
Malaysia	Khazanah Nasional	0	0	0	0	0	0	**0**	**12.5**
Mexico	Oil Income Stabilization Fund	0	0	1	0	1	1	**3**	**15.5**
Nigeria	Excess Crude Account	0	0	1	0	0	0	**1**	**8.5**
Norway	Government Pension Fund – Global	1	1	1	0.5	0.5	0	**4**	**30.5**
Oman	State General Reserve Fund	0	0	0	0	0	0	**0**	**6.5**
Qatar	Qatar Investment Authority	0	0	0	0	0	0	**0**	**3**
Russia	Reserve Fund and National Wealth Fund	0	1	1	0	0	0	**2**	**16.75**
São Tomé and Príncipe	National Oil Account	0	0	1	0	0	0	**1**	**16**
Singapore	Government of Singapore Investment Corporation	0	0	0.5	0	0.5	0	**1**	**13.5**
Singapore	Temasek Holdings	0	0	0	0	0	0	**0**	**15**
Sudan	Oil Revenue Stabilization Account	0	0	0	0	0	0	**0**	**6.5**
Timor-Leste	Petroleum Fund for Timor-Leste	0	0	1	0	1	1	**3**	**26.5**
Trinidad and Tobago	Heritage and Stabilization Fund	0	0	0	0	0	0	**0**	**17.5**
United Arab Emirates (Abu Dhabi)	Abu Dhabi Investment Authority and Council	0	0.25	0.25	0	0	0	**0.5**	**3**
United Arab Emirates (Abu Dhabi)	Mubadala Development Company	0	0	0	0	0	0	**0**	**5**
United Arab Emirates (Dubai)	Istithmar World	0	0	0	0	0	0	**0**	**4.5**
United States (Alaska)	Alaska Permanent Fund	0	1	1	1	1	1	**5**	**31**
United States (New Mexico)	Severance Tax Permanent Fund	1	1	1	1	1	1	**6**	**28.5**
United States (Wyoming)	Permanent Mineral Trust Fund	1	1	1	1	1	1	**6**	**30**
Venezuela	Macroeconomic Stabilization Fund	0	0	1	0	0	0	**1**	**7.5**
Venezuela	National Development Fund	0	0	0	0	0	0	**0**	**6.75**
Total [a]		**3.5**	**5.25**	**15.75**	**4.5**	**12**	**9**	**1.5**	**15.1**
PENSION FUNDS									
Australia	Future Fund	0	1	1	1	1	1	**5**	**26.5**
Canada	Canada Pension Plan	0	1	1	1	1	1	**5**	**31.5**
Canada (Québec)	Caisse de dépôt et placement du Québec	0	1	1	1	1	1	**5**	**30.5**
Chile	Pension Reserve Fund	0	0	1	0	0	0	**1**	**23.5**
China	National Social Security Fund	0	1	1	0	1	1	**4**	**25.5**
France	Fonds de réserve pour les retraites	1	1	1	0	1	1	**5**	**30.5**
Ireland	National Pensions Reserve Fund	0.5	0	1	0	1	1	**3.5**	**28.5**
Japan	Government Pension Investment Fund	1	1	1	0	1	1	**5**	**28.75**
Netherlands	Stichting Pensioenfonds ABP	1	0	0	0	1	1	**3**	**28**
New Zealand	Superannuation Fund	0	0.5	1	1	1	1	**4.5**	**31.5**
Thailand	Government Pension Fund	0	1	1	0	0.5	0	**2.5**	**27.75**
United States (California)	California Public Employees' Retirement System	1	0	0	1	1	1	**4**	**30.5**
Total [a]		**4.5**	**7.5**	**10**	**5**	**10.5**	**10**	**4.0**	**28.6**
GRAND TOTAL[a]		**8**	**12.75**	**25.75**	**9.5**	**22.5**	**19**	**2.1**	**18.6**

a. For each category the value under subtotal represents the average for all funds.

APPENDIX
Scoreboard for Sovereign Wealth Funds

This appendix presents the elements of the scoreboard described in the testimony. For each of the 33 questions, if the answer is an unqualified yes, we score it as "1." If the answer is no, we score it as "0." However, partial scores of 0.25, 0.50, and 0.75 are recorded for many elements, indicated by (p) in the descriptions below.

The four categories in the scoreboard are listed below with subcategories where relevant. The words in bold are keyed to the results presented in table 3 for each SWF on each element.

Structure

1. Is the SWF's objective clearly communicated? (p)

Fiscal Treatment

2. Is the **source of** the SWF's **funding** clearly specified? (p)
3. Is nature of the subsequent **use of** the principal and earnings of the fund clearly stated? (p)
4. Are these elements of fiscal treatment **integrated with the budget**? (p)
5. Are the **guidelines** for fiscal treatment generally **followed** without frequent adjustment? (p)

Other Structural Elements

6. Is the overall **investment strategy** clearly communicated? (p)
7. Is the procedure for **changing the structure** of the SWF clear? (p)
8. Is the SWF **separate from** the country's **international reserves**?

Governance

9. Is the **role of the government** in setting the investment strategy of the SWF clearly established? (p)
10. Is the **role of the managers** in executing the investment strategy clearly established? (p)
11. Are **decisions** on specific investments made **by the managers**? (p)
12. Does the SWF have in place and publicly available **guidelines for corporate responsibility** that it follows? (p)
13. Does the SWF have **ethical guidelines** that it follows? (p)

Transparency and Accountability

Investment Strategy Implementation

14. Do regular reports on investments by the SWF include information on the **categories** of investments? (p)
15. Does the strategy use **benchmarks**? (p)
16. Does the strategy limit investments based on **credit ratings**? (p)
17. Are the holders of investment **mandates** identified?

Investment Activities

18. Do regular reports on the investments by the SWF include the **size of** the **fund**? (p)
19. Do regular reports on the investments by the SWF include information on its **returns**? (p)
20. Do regular reports on the investments by the SWF include information on the geographic **location** of investments? (p)
21. Do regular reports on the investments by the SWF include information on the **specific** investments? (p)
22. Do regular reports on the investments by the SWF include information on the **currency composition** of investments? (p)

Reports

23. Does the SWF provide at least an **annual report** on its activities and results? (p)
24. Does the SWF provide **quarterly reports**? (p)

Audits

25. Is the SWF subjected to a **regular** annual **audit**? (p)
26. Is the audit **published** promptly? (p)
27. Is the audit **independent**? (p)

Behavior

28. Does the SWF indicate the nature and **speed of adjustment** in its portfolio? (p)
29. Does the SWF have limits on the **size of** its **stakes**? (p)
30. Does the SWF not take **controlling stakes**? (p)
31. Does the SWF have a policy on the use of **leverage**? (p)
32. Does the SWF have a policy on the use of **derivatives**? (p)
33. Are derivatives used primarily for **hedging**?

Chairman BERMAN. Thank you, Dr. Truman.

Dr. Luft?

STATEMENT OF GAL LUFT, PH.D., EXECUTIVE DIRECTOR, INSTITUTE FOR THE ANALYSIS OF GLOBAL SECURITY

Mr. LUFT. Thank you, Mr. Chairman. Less than a decade ago, Washington was consumed by debate about what to do with our Federal surplus. The least-popular policy, by far, at the time was for the government to invest in private sector financial markets. Alan Greenspan testified, in 2001, saying that "[t]he Federal Government should eschew private asset accumulation because it would be exceptionally difficult to insulate the government's investment decisions from political pressures."

These words are worth remembering today, as we are again facing a similar dilemma about what to do with government surpluses, just, at this time, it is not our own government surplus that knocks on the doors of our financial system but that of some of the world's least-democratic, least-transparent, and least-friendly governments.

So, from an international relations perspective, most of the concerns raised about sovereign wealth funds only really matter if, in the years to come, the relations between the United States and the investing countries were to deteriorate. If tension between the United States and the Muslim world subsided, and if China maintained its peaceful rise, there would hardly be any reason for concern. But if the opposite occurs, then indulging on Arab or Chinese wealth could be outright dangerous.

The best example here is CITGO. You may remember that PDVSa's acquisition of CITGO in 1990 triggered very few concerns at the time. Just imagine to yourself that if such an acquisition would have happened today with Hugo Chavez.

Therefore, our discussion of foreign investment should not be dominated only by the question of what is happening today but also in view of where we are headed. Considering the trajectories and patterns we can already begin to observe, the most important of which are the unabated rise in oil prices combined with questionable international behavior of some of the major oil-producing countries.

Just to keep things in perspective, and I refer to page 5 in my testimony to the graph there, the value of OPEC's proven oil and gas resources, using today's prices, is roughly equivalent to the world's total financial assets. Saudi Arabia's oil and gas alone is worth 10 times the total value of all of the companies traded on the London Stock Exchange. Such monumental wealth potential would enable tremendous buying power.

For demonstration's sake, at $200 a barrel, and today we are just at $140 this morning, OPEC could potentially buy General Motors in just 3 days of production. It would take less than 2 years of production for OPEC to own a voting bloc in every S&P 500 company. This is what we are dealing with here.

I would like to talk about some vulnerable sectors that do not get much attention because we have been focusing mainly on the financial sector, but, as populations in Western countries age and dwindle, it is only a matter of time before the underfunded health care

and retirement systems will begin to face similar liquidity problems.

Foreign governments have already put their sight on the auto manufacturers, and I think our auto manufacturers are not doing too well. We need to view what are the implications of sovereign wealth funds getting into this sector.

Media organizations are another sector worthy of attention, just to remind the committee that, in September 2006, information ministers of the Organization of the Islamic Conference gathered in Saudi Arabia, where they were instructed to buy stakes in Western media outlets.

Another danger that is, I think, worthy of attention is that, through their investments, sovereign wealth funds can shape market conditions in sectors where the governments have economic interests. In recent months, commodity futures have increased dramatically, largely due to astronomical growth in the speculation and bidding up of prices while actually deliveries are far behind. Commodity markets are easily manipulated, and the impact of such manipulations could often reverberate throughout the world, as the current food crisis shows.

While U.S. companies are not allowed to buy their own products and create shortages to increase revenues, foreign governments with economic interest in a particular commodity face no similar restrictions.

One of the two things that I think Congress should focus on, most of all, is the issue of reciprocity. We know that while enjoying almost unlimited access to investment opportunities in the West, oil-rich governments do not feel the need to reciprocate by opening their economies to foreign investment. The opposite is true: They obstruct international companies from investing in their midst, limiting them, at best, to minority shares.

The least we can do is demand that foreigners treat us as we treat them. Despite being the lead violator of free trade, 3 years ago, with the United States' support, the Saudis were admitted to the World Trade Organization. This was a mistake. Since the admission, the world's generosity toward the Saudis was rewarded by nothing but continuous manipulation of oil prices and behavior that can only be described as antithetical to free trade.

Enjoying the benefits of free trade is an earned privilege, not an entitlement, and foreign governments wishing to acquire assets in the West should be obliged only if they show similar hospitality to Western companies.

There are currently four OPEC members waiting to accede to the World Trade Organization: Algeria, Iran, Iraq, and Libya. Oil-producing countries with sovereign wealth funds, like Russia, Kazakhstan, and Azerbaijan, are also on the waiting list. These countries' admittance to the organization should be contingent on an unequivocal commitment to refrain from noncompetitive behavior and antimarket activities. You cannot seek a seat at the World Trade Organization and, at the same time, promote a gas cartel.

Speaking of a cartel, my final point is that if we really want to deal with foreign investment, including sovereign wealth funds, we must bring down the price of oil, and this cannot be done as long as we continue to put on the roads cars that can run on nothing

but petroleum. Every year, 17 million new cars roll onto America's roads. Each of these cars will have a life span of nearly 17 years. If we allow these cars to be gasoline-only, we are locking ourselves into the future of petroleum, which is very bleak.

So if we want to address the challenge of sovereign wealth funds and increase foreign-investment control over our economy, we must focus on policies that can empower countries that share our values rather than the petro-dictators of the world. We must bring down the price of oil before it hits a critical point beyond which sovereignty laws become inevitable. Thank you.

[The prepared statement of Mr. Luft follows:]

PREPARED STATEMENT OF GAL LUFT, PH.D., EXECUTIVE DIRECTOR, INSTITUTE FOR THE ANALYSIS OF GLOBAL SECURITY

SOVEREIGN WEALTH FUNDS, OIL AND THE NEW WORLD ECONOMIC ORDER

Mr. Chairman, members of the Committee, less than a decade ago Washington was consumed by a debate on what would be the best policy to absorb the then multi-billion dollar federal surplus. Reductions in outstanding debt, tax cuts and spending increases were the most touted solutions. The least popular policy was for the government to invest the accumulated excess balances in private-sector financial markets. Former Office of Management and Budget (OMB) Director Alice Rivlin wrote in 1992, "No good would come of making the government a big shareholder in private companies or the principal owner of state and local bonds." Fed Chairman Alan Greenspan said in a 1999 testimony that federal investment in the private sector "would arguably put at risk the efficiency of our capital markets and thus our economy." Two years later, on January 25, 2001, he underscored this point at a Senate Budget Committee hearing: "The federal government should eschew private asset accumulation because it would be exceptionally difficult to insulate the government's investment decisions from political pressures. Thus, over time, having the federal government hold significant amounts of private assets would risk sub-optimal performance by our capital markets, diminished economic efficiency, and lower overall standards of living than would be achieved otherwise." These words are worth remembering today as we are again facing a similar dilemma about what to do with government surpluses just that this time it is not our own government's surplus that knocks on the door of our financial system but that of some of the world's least democratic, least transparent and least friendly governments.

The rise of sovereign wealth funds (SWF) as new power brokers in the world economy should not be looked at as a singular phenomenon but rather as part of what can be defined a new economic world order. This new order has been enabled by several mega-trends which operate in a self-reinforcing manner, among them the meteoric rise of developing Asia, accelerated globalization, the rapid flow of information and the sharp increase in the price of oil by a delta of over $100 per barrel in just six years which has enabled Russia and OPEC members to accumulate unprecedented wealth and elevate themselves to the position of supreme economic powers. Oil-rich countries of OPEC and Russia have more than quadrupled their revenues, raking some $1.2 trillion in revenues last year alone. At $125 a barrel oil they are expected to earn close to $2 trillion dollars in 2008.

The resulting transfer of wealth from consumers to exporters has already caused the following macroeconomic trends:

1. *Regressive tax on the world economy.* As a result in the rise in oil prices consuming countries face economic dislocations such as swollen trade deficits, loss of jobs, sluggish economic growth, inflation and, if prices continue to soar, inevitable recessions. The impact on developing countries, many which still carry debts from the previous oil shocks of the 1970s, is the most severe. Three-digit-oil will undoubtedly slow down their economic growth and exacerbate existing social illnesses; it would also make them economically and politically dependent on some of the world's most nasty petro-regimes.
2. *Change in the direction of the flow of capital.* Historically the flow of capital has always been from industrialized countries to the developing ones. The rise in oil prices coupled with growing dependence on oil and other commodities by the industrialized world have reversed this course and today it is the developing world which feeds the industrialized world with capital.

3. *Change in ownership patterns.* During the post-Cold War era, there has been a decline in direct state ownership of business and a significant strengthening of the private sector. Throughout the world private businesses took ownership over what were once state-owned companies. In some cases, like Russia, such privatization happened too fast, leading to various socio-economic problems. The tide is now turning against the private sector as governments accumulate unprecedented wealth which allows them to buy stakes in what were once purely private companies.

In this context, we should view SWF as *enablers* of the new economic order. SWF are pouring billions into hedge funds, private equity funds, real estate, natural resources and other nodes of the West's economy. No one knows precisely how much money is held by SWF but it is estimated that they currently own $3.5 trillion in assets and within one decade they could balloon to $10–15 trillion, equivalent to America's gross domestic product. While much of the economic activity is generated by the Asian funds, particularly China's and Singapore's, I will focus my testimony on the activities of the SWF from oil producing countries primarily the five Persian Gulf states that account for nearly half of the world SWF assets—Abu Dhabi, Dubai, Qatar, Kuwait and Saudi Arabia—as well as SWF owned by oil producing countries like Nigeria, Oman, Kazakhstan, Angola and Russia which have been among the fastest-growing over the last five years.

Before I delve into the specific issues related to SWF, I would like to remind the Committee that those funds are not the only way states can exert influence in global financial markets. High net worth individuals, government controlled companies and central banks are just as important in this context. Each one of the governments which are concentrating wealth has a different portfolio of investment instruments. Saudi Arabia, for example, accounts for roughly half of the GCC's private foreign wealth yet, unlike the UAE, where SWF control foreign assets, most Saudi foreign wealth is in the hands of private investors who are mostly members of the royal family. Only recently the Kingdom announced its intention to create a large SWF. While I applaud the Committee for holding this hearing on this important topic, we should realize that SWF are only part of a much bigger problem.

The second thing to bear in mind is that to date there has been little evidence that SWF attempt to assume control of firms they invest in or use their wealth to advance political ends. This is perhaps why so many experts dismiss the fear of foreign money acquiring portions of Western economies as a new form of jingoism, deriding the "fear mongers" as disciples of those who propelled the "Japanese-are-coming" hysteria of the 1980s. I do not share their dismissive view. The key issue to understand is that there is a fundamental difference between state vs. private ownership, and that because governments operate differently from other private sector players, their investments should be governed by rules designed accordingly. Unlike ordinary shareholders and high net wealth private investors who are motivated solely by the desire to maximize the value of their shares, governments have a broader agenda—to maximize their geopolitical influence and sometime to promote ideologies that are in essence anti-Western. Non-democratic and non-transparent governments can allow the use of their intelligence agencies and other covert as well as overt instruments of power to acquire valuable commercial information. Unlike pure commercial enterprises, state owned investment funds can leverage the political and financial power of their governments to promote their business interests. Governments may enter certain transactions in order to extract a certain technology or alternatively in order to 'kill' a competing one. The reason the Japan analogy is incorrect is that Mitsubishi Estate, the Japanese company that bought the Rockefeller Center in 1989 was not Tokyo's handmaid and Japan was—and still is—an American ally. This can hardly be said about Russia, Communist China or OPEC members some of whom use their revenues to fund the proliferation of an anti-Western agenda, develop nuclear capabilities, fan the flames of the Arab-Israeli conflict and serially violate human rights. As it is now known to all, for decades the de facto leader of OPEC, Saudi Arabia, has been actively involved in the promotion of Wahhabism, the most puritan form of Islam, and its charities and other governmental and non-governmental institutions have been bankrolling terrorist organizations and Islamic fundamentalism. To this day, the Kingdom's petrodollars pay for a hateful education system and fuel conflicts from the Balkans to Pakistan. With a little over one percent of the world's Muslim population, Saudi petrodollars support today 90 percent of the expenses of the entire faith. U.S. Undersecretary of the Treasury in charge of fighting terrorist financing Stuart Levey recently said in an interview: "If I could snap my fingers and cut off the funding from one country, it would be Saudi Arabia."

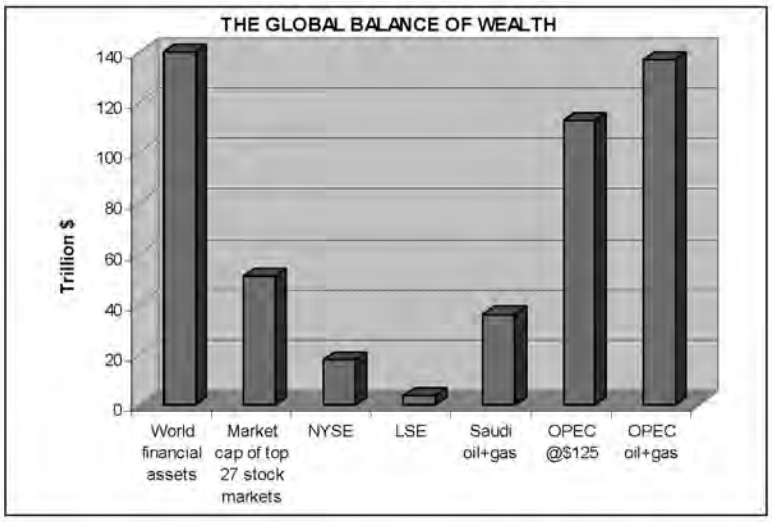
Mr. Chairman, from an international relations perspective most of the concerns raised about SWF only really matter if in the years to come the relations between the U.S. and the investing countries were to deteriorate. If tension between the U.S. and the Muslim world subsided and if China maintained its peaceful rise without undermining U.S. strategic interests there would hardly be a reason for concern; if the opposite occur, then indulging on Arab or Chinese wealth could be outright dangerous. The best example here is CITGO. PDVSa's successful acquisition of CITGO in the U.S. (50 percent in 1986, the remainder in 1990) triggered very few concerns at the time. But if such a takeover were attempted by Hugo Chavez today, when U.S.-Venezuela relations are acrimonious, the public outcry would be huge. Therefore, our discussion on foreign investment should not be dominated only by "what is happening today" but also in view of "where we are headed" considering the trajectories and patterns we can already begin to observe, the most important of which are the unabated rise in oil prices combined with questionable international behavior of some of the major oil producing countries.

Despite the attention given to SWF, they are still relatively small players in the global economic system. Their assets exceed the $1.4 trillion managed by hedge funds but they are far below the $15 trillion managed by pension funds, the $16 trillion managed by insurance companies or the $21 trillion managed by investment companies. Here again it is more important to look at the trend rather than the present situation. At their current growth rate of 24 percent a year SWF are beginning to present tough competition to other institutional investors over access to investment opportunities. To understand the anatomy of the competition between government entities and commercial firms one needs only to observe the process in which International Oil Companies (IOC) have gradually lost their competitive edge vis-à-vis National Oil companies (NOC). IOCs find themselves unable to compete against the deep-pocketed NOCs which do not face the same regulatory limitations, do not have to provide the same measures of transparency and do not have to abide by stringent environmental and humanitarian constraints. As SWF gain strength and volume they could sideline other players vying for investments. Unlike pension funds and other institutional investors who are slow in their decision making process, following strict timelines set by their investment committees, SWF are agile. They have the in-house structure and the resources to make investment decisions quickly.

NEW ECONOMIC BALANCE OF POWER

No doubt perpetual high oil prices will shift the economic balance between OPEC and the West in the direction of those who own the precious commodity. As Robert Zubrin points out in his book *Energy Victory*, in 1972 the U.S. spent $4 billion on oil imports, an amount that equaled to 1.2% of our defense budget. In 2006, it paid $260 billion which equals to half of our defense budget. In 2008, it is likely to pay over $500 billion which is equivalent to our full defense budget. Over the same period, Saudi oil revenues grew from $2.7 billion to roughly $400 billion and with it their ability to fund radical Islam. In the years to come this economic imbalance will grow by leaps and bounds. To understand the degree of the forces in play it is instructive to visualize the scale of OPEC's wealth in comparison to the consuming countries. The value of OPEC's proven oil and gas resources using today's prices is $137 trillion. This is roughly equivalent to the world's total financial assets—stocks, bonds, other equities, government and corporate debt securities, and bank deposits—or almost three times the market capitalization of all the companies traded in the world's top 27 stock markets. Saudi Arabia's oil and gas alone is worth $36 trillion, 10 times the total value of all the companies traded in the London Stock Exchange. If one adds the additional oil and gas reserves that have not yet been discovered, OPEC's wealth more than doubles. If oil prices climb to $200, as OPEC's president Chakib Khelil recently warned, the wealth nearly doubles again. In an economic system of $200 barrel oil we can expect the value of financial institutions to shrink while the transfer of wealth to the oil producing countries increases in velocity. Such monumental wealth potential will enable buying power of the oil countries that far exceeds that of the West. For demonstration sake, at $200 oil OPEC could potentially buy Bank of America in one month worth of production, Apple Computers in a week and General Motors in just 3 days. It would take less than two years of production for OPEC to own a 20 percent stake (which essentially ensures a voting block in most corporations) in every S&P 500 company. Of course, takeovers of such magnitude are unlikely, but $200 oil and additional trillions of dollars in search of a parking spot are very likely. What is clear about the new economic reality is that while the economic power of America and its allies is con-

stantly eroding, OPEC's 'share' price is on a solid upward trajectory and with it an ever-growing foreign ownership over our economy.



Vulnerable sectors. SWF have lost $25 billion on their recent investments in struggling banks and securities firms worldwide. In the near future, they are not likely to be as enthusiastic to bail out additional financial institutions. But with high oil prices here to stay and with the International Energy Agency projecting that "we are ending up with 95 percent of the world relying for its economic well being on decisions made by five or six countries in the Middle East," it is hard to see how OPEC's massive buying power would not upset the West's economic and political sovereignty. This is particularly true in light of the prospects of potential future bailouts in sectors other than banking should the U.S. economy continue to decline. As populations in Western countries age and dwindle, it is only a matter of time before the under funded healthcare and retirement systems begin to face similar liquidity problems. Foreign governments have already put their sight on auto manufacturers, buying stakes in companies like Ferrari and Daimler. In 2004, Abu Dhabi attempted to buy 25 percent of Volkswagen's shares after the German automakers profits fell sharply. The danger here is that SWF might be the first to step in to save the ailing U.S. auto industry from its pension obligations if the industry continues to under perform. What would this mean for the effort to make our cars less dependent on petroleum is a question policymakers should think about before such crisis occurs.

Media organizations are another sector worthy of attention. In September 2006, with mainstream news organizations in the U.S. reporting falling earnings and downbeat financial assessments, information ministers, tycoons and other officials of the 57-nation Organization of the Islamic Conference (OIC) gathered in Saudi Arabia where OIC Secretary General Ekmeleddin Ihsanoglu urged them to buy stakes in Western media outlets to help correct what he views as misconceptions on Islam around the world. To date, though private investors from the Middle East have made substantial acquisitions of global media, SWF have not bought holdings in this sector. A change in SWF behavior which leads to attempts to gain control over media organizations could lead to an erosion in freedom of speech and freedom of information. Pervasive influence of Saudi money in the publishing world coupled with growing number of litigations against scholars critical of Saudi Arabia is shielding from public scrutiny the one country that is most responsible for the proliferation of radical Islam.

Opaque investment patterns and the risk of predatory behavior. When it comes to governance, transparency and accountability SWF are not cut from the same cloth. There is a profound difference between SWF of democratic countries like Norway and the U.S. and those of non-democratic regimes. In some of the latter countries, like Kuwait, SWF are barred by the country's laws from revealing their assets. The Linaburg-Maduell Transparency Index which was developed at the Sovereign

Wealth Funds Institute shows significantly lower SWF transparency ranking among non-democratic countries as opposed to democratic ones. Not surprisingly, nine out of the ten worst ranked funds are those of oil producing nations. Lack of transparency and accountability among those SWF makes them a disruptive factor in our overall highly transparent market economy. To avoid scrutiny, SWFs have fostered new alliances with private equity funds which offer a culture of secrecy. SWF already account for approximately 10 percent of private equity investments globally and this number will grow further in the coming years. Last year, Chinese entities bought the largest external stake in Blackstone that, indirectly through its holdings, is one of the largest employers in the U.S. Carlyle Group sold 7.5 percent stake to a fund owned by Abu Dhabi which also bought 9 percent of Apollo Management. The situation is similar in hedge funds. One of the dangers here is that through their investments SWF can shape market conditions in sectors where their governments have economic and/or political interests or where they enjoy comparative advantage. In recent months, for example, commodity futures have increased dramatically largely due to astronomical growth in speculation and bidding up of prices while actual deliveries are far behind. Commodity markets are easily manipulated and the impact of such manipulations could often reverberate throughout the world as the current food crisis shows. While U.S. companies are not allowed to buy their own products and create shortage to increase revenues, foreign governments with economic interest in a particular commodity face no similar restrictions bidding on it, via their proxies, in the commodity market. Under the current system, oil countries can, via their SWF as well as other investment vehicles that receive investment from SWF, long future contracts and commodity derivatives and hence affect oil futures in a way that benefits them. This would be tantamount to the U.S. government using its position as the world's largest exporter of corn to bid up corn futures.

Country	Fund Name	Assets $Billion	Inception	Origin	Linaburg-Maduell Transparency Index
UAE - Abu Dhabi	Abu Dhabi Investment Council	$875	1976	Oil	3
Norway	Government Pension Fund – Global	$380	1990	Oil	10
Singapore	Government of Singapore Investment Corporation	$330	1981	Non-Commodity	6
China	SAFE Investment Company	$311		Non-Commodity	2
Saudi Arabia	SAMA Foreign Holdings	$300	n/a	Oil	4
Kuwait	Kuwait Investment Authority	$250	1953	Oil	6
China	China Investment Corporation	$200	2007	Non-Commodity	2
China - Hong Kong	Hong Kong Monetary Authority Investment Portfolio	$163	1998	Non-Commodity	7
Russia	National Welfare Fund	$162	2008	Oil	4
Singapore	Temasek Holdings	$159	1974	Non-Commodity	7
Australia	Australian Future Fund	$61	2004	Non-Commodity	9
Qatar	Qatar Investment Authority	$60	2000	Oil	1
Libya	Libyan Arab Foreign Investment Company	$50	1981	Oil	1
Algeria	Revenue Regulation Fund	$43	2000	Oil	1
UAE - Dubai	Investment Corporation of Dubai	X	2006	Oil	5
UAE - Federal	Emirates Investment Authority	X	2007	Oil	1

Source: Sovereign Wealth Funds Institute

Boardroom presence. To date, the influx of petrodollars has not translated into overbearing presence of government agents in corporate boardrooms. In fact, many of the SWF buy holdings under the 5 percent benchmark that triggers regulatory scrutiny and forego board seats. But at the current rate of investment and many more years of three-digit-oil combined with deepening geopolitical tensions, foreign governments might be more willing to translate their wealth into power, dictating business practices, vetoing deals, appointing officers sympathetic to their governments and dismissing those who are critical of them. Direct influence of foreign government could lead to inefficiencies, capital misallocations and political interference in business decisions. This is why it is my view that SWF acquisitions should be restricted to non-voting stakes.

The rise of Sharia finance. The gradual penetration of Shariah (Islamic Law) into West's corporate world is another characteristic of the new geo-economic order. Islamic countries operating on the basis of compliance with Shariah have strict guidelines of economic conduct. Banks and investment houses gradually employ a new breed of executive—the Chief Shariah Officer (CSO)—whose sole job is to ensure compliance with Islamic law and hence attract more business from the Muslim investors. Over time, such compliance could put pressure on companies not consistent with Islamic principles to become more "Islamic." Imams sitting on Shariah boards could be pressured to withhold their approval of any business dealing directly or indirectly connected with countries or institutions that are offensive to Islam. One can only guess what this would mean for publishing houses, Hollywood movie studios, the alcohol and gambling industries. A sure casualty of the Islamization of the corporate world would be Israel, which has for years been subjected to the Arab boycott. According to the U.S. Department of Commerce, last year, American companies reported no fewer than 486 requests from UAE companies alone to boycott Israel.

BUILDING A FIRELESS FIREWALL

None of the potential risks to which I alluded entails lifting the drawbridge and becoming economic hermits. America's commitment to open markets has been a source of respect and admiration around the world and reversing it through investment protectionism would only hurt U.S. prestige while undermining economic growth and job creation at home. To arrest the current economic trend and to hedge the risk of sovereignty loss the U.S. should apply a healthy dosage of vigilance and develop a system of indicators to determine and examine when SWF pursue different approaches from other institutional investors. Willingness to pay above market prices, use government assets to back up financial deals or manipulate prices to increase returns should all be red flags that trigger response. The U.S. already has a rigorous safeguard mechanisms against undesirable foreign investors. The Committee on Foreign Investment in the U.S. (CFIUS) protects national security assets in sectors such as telecommunications, broadcasting, transportation, energy and minerals in which there is a clear potential danger to national security. I am delighted that many of the concerns about foreign investments have already been addressed in the CFIUS reform legislation entitled the Foreign Investment and National Security Act of 2007. The range of regulatory and supervisory tools available to the Federal Reserve Board as described in the Federal Reserve Act are quite satisfactory for the case SWF make an investment in a U.S. banking organization that triggers one of the Fed's thresholds. But in order to protect ourselves against sovereignty loss more safeguards are needed.

Reciprocity. While enjoying almost unlimited access to investment opportunities in the West, oil rich governments do not feel the need to reciprocate by opening their economies to foreign investment. The opposite is true: they obstruct international companies from investing in their midst limiting them to, at best, minority share. This is the root cause of insufficient production of new oil. Oil countries, together owning 80 percent of the world's reserves, practice resource nationalism, stick to quotas, refuse to provide transparency of oil activities including reserve studies and terms of contract with their own national oil companies and they are riddled with corruption and cronyism.

The least we can do is demand that foreigners treat us as we treat them. Despite being the lead violator of free trade by dint of its leadership of the OPEC cartel, three years ago, with U.S. support, the Saudis were admitted to the World Trade Organization (WTO). This was a terrible mistake. Since the admission, the world's generosity toward the Saudis was rewarded with nothing but continuous manipulation of oil prices and behavior that can only be described as antithetical to free trade. Enjoying the benefits of free trade is an earned privilege not an entitlement, and foreign governments wishing to acquire assets in the West should be obliged only if they show similar hospitality to Western companies. We should not be shy

to use retaliatory measures against serial violators of free trade principles. There are currently four OPEC members in waiting to accede to the WTO—Algeria, Iran, Iraq, and Libya. Oil producing countries with growing SWF like Russia, Kazakhstan and Azerbaijan are also on the waiting list. These countries' admittance to the organization should be contingent on compliance with those principles and on an unequivocal commitment to refrain from non-competitive behavior and anti-market activities. You cannot seek a seat at the WTO and at the same time promote a natural gas cartel.

Increase transparency. The scope and growth rate of SWF are so vast that their actions can have far-reaching influence on world financial markets whether intentionally or mistakenly. This begs for the introduction of intermediary asset managers and the creation of disclosure standards for SWF as well as other foreign institutional investors that are at least as stringent as those applied to other regulated investors. However, any go-it-alone effort to force SWF to adopt higher transparency standards would be unworkable and easy to circumvent. The guidelines of working with SWF should therefore be drawn in collaboration with the EU and other countries on the receiving end of sovereign money.

Break the oil cartel. In the long run, the only way to roll back the new economic order and restrain OPEC's control over the world economy is to reduce the inherent value of its commodity. This cannot be done as long as we continue to put on our roads cars that can run on nothing but petroleum. Every year 17 million new cars roll onto America's roads. Each of these cars will have a lifespan of nearly 17 years. In the next Congressional session 35 million new cars will be added. If the next president presides for two terms he or she will preside over the introduction of 150 million new cars. If we allow all those cars to be gasoline only we are locking our future to petroleum for decades to come. I cannot think of something more detrimental to America's security than Congress allowing this to happen. Congress can break OPEC's monopoly over the transportation sector by instituting fuel choice. The cheapest, easiest and most immediate step should be a federal Open Fuel Standard, requiring that every new car put on the road be a flex fuel car, which looks and operates exactly like a gasoline car but has a $100 feature which enables it to run on any combination of gasoline and alcohol. Millions of flex fuel cars will begin to roll back oil's influence by igniting a boom of innovation and investment in alternative fuel technologies. The West is not rich in oil, but it is blessed with a wealth of other energy sources from which alcohol fuels—such as ethanol and methanol—capable of powering flexible fuel vehicles, can be affordably and cleanly generated. Among them: vast rich farmland, hundreds of years' worth of coal reserves, and billions of tons a year of agricultural, industrial and municipal waste. Even better: in an alcohol economy, scores of poor developing countries which right now struggle under the heavy economic burden caused by high oil prices would be able to become net energy exporters. With hot climate and long rainy seasons countries in south Asia, Africa and Latin America enjoy the perfect conditions for the production of sugarcane ethanol, which costs roughly half the price and is five times more efficient than corn ethanol. Hence, a shift to alcohol enabled cars will enable developing countries to generate revenues and emerge as a powerful force that could break OPEC's dominance over the global transportation sector.

In addition to alcohols, coal, nuclear power, solar and wind energy can make electricity to power pure electric and plug-in hybrid cars. The latter have an internal combustion engine and fuel tank, and thus are not limited in size, power, or range, but also have a battery that can be charged from an electric socket and can power 20–40 miles of driving, giving the consumer the choice of driving on electricity or liquid fuel. Only 2% of U.S. electricity is generated from oil today. While plug-in hybrids have unlimited range and a cost premium of several thousand dollars, pure electric cars are planned to be sold at competitive prices in several countries, including the U.S. and Japan, as early as 2010. Because pure electric cars have a range limitation—at least two countries, Israel and Denmark, are now in the process of developing an infrastructure for battery replacement to address this problem—they may not satisfy the needs of many Americans. But electric cars can easily serve as a second or third family car. This "niche market" is roughly two thirds of America. Thirty one percent of America's households own two cars and an additional 35 percent own three or more vehicles. These are not the cars a family would use to visit grandma out of town but cars that drive routinely well below the full battery range. There are over 75 million households in the U.S. that own more than one vehicle and that can potential replace one or more gasoline only cars with cars with cars powered by made-in-America electricity.

Mr. Chairman, the new economic order is shaping up right before our eyes increasingly invalidating much of the economic paradigm to which we have been accustomed. For America, a continuation of the petroleum standard guarantees eco-

nomic decline and perpetual economic and political enslavement to the OPEC cartel and its whims. If we want to address the challenge of SWF and increased foreign government control over our economy we must focus on policies that can empower countries that share our values rather than the petro-dictators of the world. We must bring down the price of oil before it hits a critical point beyond which sovereignty loss becomes inevitable.

Chairman BERMAN. I thank all of you. I recommend to my colleagues on the committee the entire statements of these witnesses, just filled with information. I yield myself 5 minutes to open the questioning.

My first question is, not that the papers do not touch on it, but the testimony did not really focus on this: When you talk about transparency, what are you talking about? Are you talking about what is the money that came into these sovereign wealth funds?

Are we talking about what investment these sovereign wealth funds are making, or are we talking about how decisions to invest are made, and how possibly do you create a real transparency with respect to that? You could have millions of board meetings and not learn anything about the real motivations of investment decisions.

So I am wondering if any of you could just quickly sum up. I would like to ask one other question, in addition to that, on this round, but quickly sum up a few specifics about what you think of when you think about transparency.

Go ahead, Dr. Lyons.

Mr. LYONS. My colleagues will probably want to add something, but maybe if I can just start.

If one looks at the sovereign wealth funds at the moment, as Dr. Truman said, there is a whole spectrum of these funds, some of them very open and transparent. I would cite Norway, Singapore, and Alaska, actually. They are transparent in terms of providing detailed information on their size, on their returns, on their portfolio composition. But I think transparency embraces lots of areas, and I think a code of conduct should very much focus on this.

It is a need for transparency in terms of the objectives and the investment strategies of these funds, i.e., are they purely going to be commercially driven?

I think we need to also look for best practice in terms of corporate governance and accountability because this has important implications for other shareholders and investors. A fiduciary responsibility is very important here.

Also, I think there is a need for greater transparency regarding transactions.

So, basically, in answer to your question, I would almost argue it is the whole gamit, shall we say? There is a whole number of areas, and I think, in arguing for greater transparency, it will basically ease fears about what these funds are up to. The very fact that some of these funds can carry out their business by being open and transparent, in my mind, argues that the whole range of funds should be more open and transparent.

The final point is that, speaking to some funds in the Middle East, they would argue that, in private, they carry out everything that people ask them for. Therefore, they also would argue, it is their money. Why should they become more transparent? Judge them by their behavior and their actions.

I think that the scale of these funds, in terms of the investments that they make, not just the Middle East but globally, suggests that we do need to have a code of conduct that incorporates some of these areas, even though, in the past, many of these funds behaved above board. Thank you.

Chairman BERMAN. Dr. Truman and Dr. Luft, do you have anything to add to that?

Mr. TRUMAN. Yes. I would like to. The basic issue is less one of transparency, per se, than one of accountability. These funds need to be accountable to their own citizens and to our citizens and to the financial markets, in general, and transparency is a means to that end.

So the issue is a question of accountability, and, therefore, as Gerard Lyons said, it includes all three elements: How much money you have, what you are doing with it, and how you make your decisions—how a fund behaves in terms of those processes.

It so happens that in my scoreboard ranking funds by the category of accountability and transparency produces roughly the same ranking as overall, which includes elements of structure and governance.

Chairman BERMAN. Let me just draw a finer point to this. Dr. Luft mentioned that sovereign wealth funds from Middle East states decide to invest in auto companies perhaps more with the agenda of slowing down efforts to improve fuel efficiency or look for alternatives than for purposes of simple commercial profit. Is there anything about transparency or accountability which reveals intentions? Should we care? Is this something we can possibly deal with in any fashion?

Mr. TRUMAN. Well, I think, at one level, you can because, to the extent that they tell you where they are investing, then you know, you can interpret some——

Chairman BERMAN. Well——

Mr. TRUMAN. If they do not report how much in the way of auto stocks they own, then you are not going to know anything. So, at a first level, a certain amount, you will learn something from where they invest. If they do not tell you what they are buying, then you cannot intuit this kind of thing.

However, I think the problem is that it is very difficult to read motivation into those investments in some cases. That is true of all investors, and I think that is the challenge that we face.

Chairman BERMAN. All right. My time has expired, as much as I would love to hear everybody just answer my questions. So I recognize Mr. Manzullo for 5 minutes.

Mr. MANZULLO. Thank you, Mr. Chairman. I have one question for the three of you, and I guess I gave you a preview of what I was going to ask before the hearing started.

There is a big concern on the part of this Congress and the prior Congress, regardless of who is in the majority, of taxing foreign direct investment, and, obviously, sovereign wealth fund is a subset for foreign direct investment. For example, 3 or 4 years ago, there was a big war that went on with the foreign sales corporation extraterritorial income tax proposal that would place a special tax on foreign direct investment. That was under the Republicans.

Then, this past year, under the Democrats, with the Farm Bill, there was almost a $2 billion tax on foreign direct investment in the House bill, and, even with a very heavy agriculture district, I voted against that because of the impact that that would have on foreign direct investment.

My question to the three of you, as economists, is: Is there a chilling effect on foreign direct investment where foreign investors have to watch what Congress does, regardless of who is in power, because of the front door tax that could be placed and thus penalize foreign direct investment.

Mr. TRUMAN. Maybe you should let Dr. Luft start.

Mr. MANZULLO. Dr. Luft?

Mr. LUFT. I think that it will have a chilling effect, and it will have a deterring effect among governments that have a choice. Those governments have a choice. We are not the only game in town. I think that before we go into these kinds of policies, there are some much more basic, universal requirements from those actors that we should focus on, and I think that those issues of reciprocity and accountability should be much higher on our priority list.

I do think, however, that we have to be quite realistic in asking governments that do not provide accountability and transparency to their own people to provide accountability and transparency to our people. I do not think it is a realistic proposal that we ask those governments to be more transparent to us than to their own people.

Mr. MANZULLO. Dr. Truman?

Mr. TRUMAN. I think I agree that a unilateral tax on a particular inflow is going to have a chilling effect, for example, on foreign direct investment. That, I think, is clear.

We need to worry about national treatment in this area. In that respect, we have a problem because our corporate income tax system is very complex, and it does not mesh with those of the rest of the world. Therefore, aligning our corporate tax system with the rest of the world in a national treatment framework is very difficult. But I think the basic answer to your question is, yes, there are issues there, and if you single out foreign direct investment for special taxation, you will discourage foreign direct investment.

Mr. MANZULLO. Dr. Lyons?

Mr. LYONS. I would reiterate that. I think, in the whole debate, the word "reciprocity" has been mentioned. I think it is important to argue for level playing fields rather than to demand reciprocity, and that is in terms of looking at sovereign wealth fund countries.

In terms of your specific question, I think the level-playing-field approach should apply to investment here in the U.S. Clearly, any increase in tax on foreign direct investment, I think, would be counterproductive.

When one looks at the U.S. in the global perspective, it is the same as the U.K. We need to compete. You can either compete on price or compete on value. The reality of it, though, is that the pace and scale of change in China and the catch-up potential in India mean it is very hard to compete just on price. People in the U.S., like the U.K., they do not want the low-priced jobs.

So I think we need to encourage both our own investment at home, which begs the question, of course, why we cannot have more investment at home, but also we need to encourage foreign direct investment, whether it is into the U.K. or, indeed, into the U.S. itself, because I think that is positive for growth, positive for jobs, and I think the important thing is to try and encourage the Western world. There is an underlying assumption that high-value-added jobs will stay in the West; low-cost jobs will go to the East. I think that is fundamentally wrong.

We are seeing economies across Asia and elsewhere trying to move up the value curve very quickly, and, therefore, I think the important thing is to make the U.S., like the U.K., as competitive as possible and no tax on foreign investment.

Mr. MANZULLO. Thank you.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from California, Mr. Sherman, is recognized for 5 minutes.

Mr. SHERMAN. First, a few observations about Dr. Luft's testimony. First, I want to thank you for reprising the funniest moment I ever had in Congress, which was listening to Alan Greenspan worry about the future date when we were going to pay off the entire national debt, and had he worried, in his testimony about alien abduction, it would have been a more realistic concern.

You have also observed that our cars are all made to run on petroleum. I am not sure it would be a huge step forward to require them to run on a variety of different liquid hydrocarbons. I am not sure that grain ethanol is a sufficient answer.

And then, finally, you point out that we should not expect these funds to be more open with us or disclose information relevant to us if they will not be fair and open and transparent to their own people. I think that is a morally correct statement but not one that is practically correct; that is to say, their own people could overthrow them and kill them if they do not like what is disclosed to them, whereas if those same funds were simply to disclose to U.S. regulators, that they have gone from 5 percent ownership to 6 percent ownership in one of our corporations, that might cause a little consternation on page 7 of the Wall Street Journal but does not pose any practical threat to the health and security of the ultimate owners of these funds, which are often the monarchs.

All of the testimony here seems to be based on the idea that these sovereign wealth funds will follow the laws and that the Anglo-Saxon view that people with money behave like gentlemen. My concern is the theft of corporate assets.

Now, in a gentlemanly society, theft is only committed by the lower classes, but we know that not to be true. Now, in the old days, we had a lot of protection on the theft of corporate assets because corporate assets were physical, and if you stole them, you had them, and then we could enforce laws against you.

But take this situation: A Chinese sovereign wealth fund acquires 5, 10, 15, 20 percent of a United States corporation that is high-tech. Its corporate assets are intellectual. The wealth fund demands access to the technical information. What corporate executive is going to say no to a 15-percent owner who could sell out the

company, agree to a hostile takeover, et cetera, cancel the stock options, or, at least, not issue any new ones.

Once that intellectual property is in the hands of one entity of the Chinese Government, it can be transferred to any other entity, far distant in location from one Chinese city to the other. Should we allow these funds to acquire more than a 5-percent interest in any U.S. company that has valuable technology, and, if so, how would we prevent this from being the easiest case of a technology theft and piracy other than relying on the gentlemanliness of all of those with capital? I will ask whichever witness would like to respond. Dr. Truman?

Mr. TRUMAN. Well, it is a complicated question you raise. I think the answer is you do not want to say to the sovereign wealth funds or, more relevantly, as Dr. Lyons said, to any foreign investor, "You shall not buy more than 5 percent of the stock of any U.S. corporation." I think that is probably too blunt an instrument to apply.

Mr. SHERMAN. On the other hand, if we lose all of our technological advantage——

Mr. TRUMAN. The question is whether we have devices, of which we have many, starting with the CFIUS process, and a variety of other devices in our Defense Production Act, and so forth and so on, to protect our intellectual property.

Mr. SHERMAN. Does CFIUS apply to all companies with intellectual property or just a few strategic——

Mr. TRUMAN. It applies to all controlling investments. Now, you are raising the question, which I think is very relevant, about noncontrolling investments and an investor that has—the phrase I have used is "undue influence" over the corporation. I think that is a very complicated area, and it is difficult maybe to rely on gentlemanly behavior.

But we do have devices that can investigate the kind of activity, whether it is insider trading or a variety of other kinds of activities, and if a country, through a sovereign wealth fund or other investment, actually establishes a pattern of misbehavior, then I think the question will become whether one should implement something in terms of that pattern of misbehavior.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from Colorado, Mr. Tancredo, is recognized for 5 minutes.

Mr. TANCREDO. Thank you, Mr. Chairman. I have only one question for all of the panelists, and that is, let us assume, for a moment, that all of the dangers that we have identified with a lack of transparency in sovereign wealth funds, a lack of reciprocity, are accurate and that they really do pose a threat to the economy and to the security of the United States, from the standpoint of one of the panelists. What exactly can we do about that?

The fact is that I guess I need to know, do we really know how much of the entire capital that is represented by sovereign wealth funds throughout the world is invested here so that any action we take unilaterally can actually affect the behavior of the sovereign wealth funds, or is any action that would elicit that kind of change in behavior only going to come about as a result of some international action, Western nations acting in conjunction with each other, and what do you think the possibilities of that would be, and

what actions would they actually be? What actions would we have to take, in very specific terms?

Mr. LUFT. I do not believe in a go-alone approach, and I think that, to the degree that we can, we need to collaborate on this with other major pools of investment in order to create those uniform standards. However, there is one thing that we can do, even if we have to do it unilaterally, and that is to restrict the presence of government agents in our boardrooms.

I think that, this way, you do not restrict investment itself that can buy equity and stakes, but I do not think those funds should have representatives' voting rights in boardrooms of major entities, major corporations, and that is a way to sort of separate, like a clutch that enables them to invest and, at the same time, does not enable them to control.

Mr. TANCREDO. Mr. Truman?

Mr. TRUMAN. In answer to your question, if worse came to the worst, an immediate reaction probably would be for sovereign funds to withdraw money from the U.S. and to invest their future money outside of the U.S., and that is not good for markets, and it is not good for the dollar. That is a worst-case scenario.

I do not think anyone really anticipates it coming to that, and it is in no one's best interest for it to come to that, either the investors or, indeed, the recipient countries like the U.S. or the U.K. That is why I think it is vitally important that both sides work together.

I am encouraged by the fact that, since last summer, many sovereign funds never previously said anything or did anything publicly and now, either directly or indirectly, they are being forced to engage in the debate. I think, therefore, code of conduct is vitally important. Of course, what countries do not adhere to the code of conduct? That is a difficult aspect.

They had a follow-up, and part of the debate since last summer has been whether sovereign funds should be encouraged to be active or passive investors in companies, and maybe that links into the question that came up for Mr. Sherman before about intellectual property rights. I think there is lots of why to issues, but, basically, worst-case scenario, I think we can all envisage what would happen, but I do not think, because of that, it will happen. I think it is important that both sides, the sovereign funds as well as recipient countries, do work together. I strongly argue for a code of conduct.

Mr. TRUMAN. I think a code of conduct is the place to start and common international action is the way to proceed. Just as I commented about the 5-percent limit, you have the same problem with respect to the boardroom, quite frankly. I wish it was as easy as to say, "You cannot be on the board." But if you still own 7 percent of the stock, you are going to be listened to, and if your objective is to steal secrets, you are going to steal secrets.

I want to comment on one aspect of your question, Congressman Tancredo. We actually do not know the numbers. It is a fact that we and the rest of the world do not collect our data based generally on government ownership or nongovernment ownership. This is a complicated process. It costs money, in the budget and so forth and

so on, if we wanted to do that, but the fact of the matter is we cannot say what share of the U.S. economy is owned by governments.

We know some of it, but we do not actually collect our data on foreign direct investment, for example, in that form. So it is an interesting question to see how difficult it would be. In principle, we could do it, but it is one more burden on all of the parties, but the facts are that we do not have all of the facts.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from New Jersey, Mr. Sires.

Mr. SIRES. Thank you, Mr. Chairman. A very interesting hearing. Thank you for being here.

I have a concern. I see the scale of the surpluses for some of these countries. I see China, I see Russia, and I see their investment in South America, Africa. Obviously, they are doing it for a reason, to meet their needs, but also to enlarge their sphere of influence.

I do not think these countries do it with a real gentlemanly behavior in some of these places. How can we encourage them to be more responsive in some of these countries where they make these investments? I know we have this conduct, but, for me, to think that they are going to behave when I have not seen that.

Mr. TRUMAN. I think the cases of both Singapore and the United Arab Emirates are instructive in this area. Singapore, which was referred to earlier, has two sovereign wealth funds that 2 or 3 years ago, were completely opaque. Temasek now ranks not at the top, as Dr. Lyons said, but is in the middle of my scoreboard.

When I did my scoring last summer for the GIC, the Government Investment Corporation, it was at the bottom. It has completely changed its approach, and it is changing further. The United Arab Emirates is, too.

These countries have different systems than ours. You are absolutely right. The question is, How do we trust them? The answer is you are very uneasy, and both of those can sleep uneasily at night about that, but they are integrating with the global and the U.S. economy and financial system, and if they are going to do that, if they are going to invest their wealth outside their country, they are going to have to behave more like the mores and structures of the countries in which they invest.

I think we have to rely on, at least as a first approximation, as a first step, that process of integration of these countries with the U.S. and the global economy in order to ensure that they will, in general, behave reasonably.

Mr. LYONS. I think your question touches on a very key area, and I think it is linked into the way the global balance of trade is changing. I call it "new trade corridors." We are seeing increased flows of goods, of commodities, of people, remittances, and of capital between what would previously have called south-south countries: Asia-Africa, Asia-Middle East, Asia-Latin America. Trade flows: for instance, China-Latin American trade is over $100 billion now. That is roughly a third of China-United States trade.

I think it is very linked into commodity demand and commodity needs, particularly in terms of China. China's investment in Africa is not through its sovereign wealth fund; it is through Chinese companies. China-Africa relations have gone through a pendulum.

They have swung good, and then they have swung back, bad, and now they are swinging good again.

Now, the important thing is to engage these regions of the world and to actually help them develop their capital markets. The OECD, for instance, claims, or has worked out, that if sovereign wealth funds "allocate 10 percent of their portfolio to emerging and developing economies over the next decade, this would generate inflows of $1,400 billion, more than all OECD countries' aid to developing economies put together."

Now, one of the issues I have, at the moment, is that there are countries in Africa that do not have access or easy access to capital markets. Therefore, they are going to accept the money from countries who give them the money, and if it is China, now they will take the money. Now, does this, in the future, bind them closer together? I think it is a problem.

So the challenge for us in the West is to engage these regions more and to actually try and get these countries in those regions access to Western capital, not just capital from the East, shall we say?

Mr. SIRES. Dr. Lyons, I have a problem identifying Chinese companies separate from the Chinese Government. So when you say Chinese companies are investing in Africa, to me, it is the Chinese Government. But beyond that, are we in danger of losing South America and Central America to the investment of all of these countries?

Mr. LYONS. In answer to your second point about are you in danger of losing South America, I do not know, is the answer. I would be surprised, actually, given the U.S. is still the world's biggest economy. Yet the linkages between Asia and Latin America are very important.

Getting back to your first point, I think you are right. It is the corporate governance and structure of companies in other countries. One of the reasons why sovereign wealth funds, in my mind, have come to the front page, shall we say, of newspapers, even though many of them have been around for 50 years, is not just the fact that the amounts at their disposal are increasing, and the amounts of their targets more controversial. It is the very fact that Russia and China now have these funds. That is the issue.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from California, Mr. Royce, is recognized for 5 minutes.

Mr. ROYCE. Thank you, Mr. Chairman. Let me ask, first, Dr. Lyons, why is it that the wealth in these countries is not in the hands of the Chinese people or not in the hands of Saudi citizens? It is in the hands of the government. I think I know the answer to this, but I wanted to hear your comments. I think you would agree that the ideal would be if those systems had the wealth in the hands of the populace. Dr. Lyons?

Mr. LYONS. I completely agree that that would be a nice situation. The reality is that China is still a developing economy, and I think the important thing is to try and encourage China and, indeed, other economies to open up their markets further. I think you know the answer to the question, in a sense.

Mr. ROYCE. Then let me ask you another question. Mike McConnell is the director of national intelligence. He testified here.

Among his top concerns are "the financial capabilities of Russia, China, and the OPEC countries and the potential use of their market access to exert financial leverage to achieve political ends." That was his quote. Do you believe he was specifically talking here about sovereign wealth funds, and are those concerns well placed?

Mr. LYONS. Well, I do not know what he was specifically talking about, but, in terms of sovereign wealth funds, if you had the range of them here in front of you, the ones from the Middle East, quite frankly, have been around for a long time and have records that they have behaved well in the past. Now, of course, we want them to continue to behave well in the future.

In terms of China's and Russia's funds, Russia's fund is, on the face of it, rather simply transparent, but companies like Gazprom people have a bigger concern with. Regarding China's fund, Lou Jiwee, who runs it turned up in London last November–December. He gave a talk, and, quite frankly, he ticked every box in terms of what the audience wanted to hear, but the concern might not be about China's fund; it might be, as the previous Congressman asked, it might be more about Chinese companies that come under government influence rather than the sovereign wealth fund themselves.

Mr. ROYCE. Let me ask Mr. Luft about this because if we are weighing up China now, we could look at Africa, with respect to Chinese conduct there. I chaired the Africa Subcommittee for 8 years, and I have watched with concern the intensification of Chinese engagement in Africa. But, specifically, we look at Zimbabwe; Beijing is backing the dictator, Mugabe. If we look at Sudan, China has backed the government carrying out genocide in Darfur.

At least, there is the possibility here that more sovereign wealth, as you point out, will be going to developing countries, such as China, and those countries do not distinguish between economics and politics abroad. It is one in the same. It is aimed at increasing the Chinese Government influence, and, in Africa's case, this is not for the good of Africa, from what I have seen.

So I would like to hear your views on the connection between Chinese investment and political goals in Africa. We just saw that ship try to carry Chinese weaponry in, you know, for Mugabe. Dr. Luft, your observations on that, please.

Mr. LUFT. You are absolutely right. All of this talk about a code of conduct; we have a code of conduct for human rights. We have it. It has been around for decades, and yet, if you look at the roster of countries that have the biggest sovereign wealth funds, they have the worst records on human rights. The United Arab Emirates are just one notch under Saudi Arabia in terms of human rights. So these are not Jeffersonian democracies, and there is no reason to believe why they would adhere to a code of conduct when it comes to investment.

Mr. ROYCE. Let me stop you there. The ideal is not to see the growth of these funds. That is the point. They are not pro-market. They are about state control.

Mr. LUFT. Absolutely, and that is not going to change anytime soon. Africa, for example, is a very instructive example because look what happened to our own oil companies, the international oil companies in Africa. They have been losing every single bid be-

cause they have to compete against deep-pocketed Chinese companies that can afford not only the money for the deal but also major, multibillion-dollar, development projects, and that goes into the whole issue of competitiveness.

I think, if you apply the same analogy to institutional investors, you would see that our institutional investors are losing their competitive edge when they compete against a growing government investor, and I think we are only at the beginning of this, but we need to sort of think about the future and take the analogy of what happened to oil companies versus national oil companies, and I do not think that we will see different results.

Chairman BERMAN. China could not be doing that. They are in the WTO. Never mind.

The gentleman from Texas, Mr. Hinojosa, is recognized for 5 minutes.

Mr. HINOJOSA. Thank you, Mr. Chairman. I want to thank the witnesses for their presentations and most interesting information that you are sharing with us.

My question is to Dr. Luft. I find your presentation and testimony extremely interesting, and I want to talk about this overview of investment approach and transparency. I want to talk about the chart on page 5 that talks about the global balance of wealth.

It is of great concern to me that Members of Congress have no idea that when you look at page 5, and you look at the strength of the New York Stock Exchange and the London Exchange combined would be smaller than Saudi Arabia's wealth in oil and gas, and when you look at the total OPEC oil and gas strength of over $135 trillion, we are poorly informed in Congress, and we possibly should be thinking very carefully about what priorities on how we should spend our financial assets and human assets that have given us the lead in global leaders, and that is because of our education, our production of stem careers, many college graduates in education that have given us that kind of information technology and engineering prowess.

And yet it seems like that states that are producing the airplanes and the jets, like Washington State, sending so many—in fact, they are number one with exports, the United States exports to the United Arab Emirates with their airplanes. We are constantly trying to increase our exports. So much of our strength is based on what I just mentioned to you, and yet we are not producing additional college graduates to replace those who are passing away or who are retiring.

Tell me, what should we be doing in Congress to be able to deal with this prowess of the OPEC countries of $135 trillion versus ours, which is a measly less than $20 trillion? That concerns me. Talk to me about what your thoughts are.

Mr. LUFT. The single most important thing that Congress can do today, tomorrow, this week, is to begin the process of turning oil from a strategic commodity, one that underlies the global economy, to just another commodity. Tomorrow, there will be a hearing here that will go into more details, and I recommend that you all attend this hearing. But I think that this is the main task. If we do not do that, we will meet here next year, and the net wealth of OPEC will be much higher.

Just today, oil prices went up to $140 a barrel. I did this graph on 125, and that is, by the way, only proven reserves. There is much more that is not yet discovered. So the real disparity in wealth is much bigger.

To begin to roll back the influence of oil in world politics, you have got to introduce competition to the transportation fuel market, you have got to electrify our automobiles, you have to bring in alternative fuels, and you have to introduce a requirement that every new car sold in America must be able to run on gasoline and something else.

I want to impress upon you, what are the implications of not doing it? In the next session of Congress, the 111th session of Congress, there will be 35 million new cars running on petroleum only. If you do not change this, then we are locked, we are married to these countries for as long as the eye can see. So we have got to begin to break this dependence by introducing competition, by introducing an open fuel standard in the transportation sector. That is the lowest-hanging fruit. It costs only $100 per car to do it.

I just gave an example a few weeks ago in an op-ed. If we do a flex-fuel requirement, and let us suppose that taxpayers fund it, that would be $20 billion. That is less than what the Fed forked in 1 weekend to save Bear Stearns.

Chairman BERMAN. Dr. Luft——

Mr. HINOJOSA. Thank you, Mr. Chairman. I think that this is very interesting. If you did it at $120 or $140 a barrel, it scares me that on page 4, on the demonstration of what happens at $200 oil per barrel. Thank you, Mr. Chairman.

Chairman BERMAN. The time of the gentleman has expired.

Let me use the chairman's prerogative just to reveal my ignorance. The chart that Mr. Hinojosa referred to says, "World Financial Assets, 140; OPEC Oil and Gas." Do you mean the value of the world's assets, or are financial assets somehow different than reserves of oil and gas in OPEC countries, because if they are not, the chart does not make sense to me?

Mr. LUFT. No. Of course, they are not included.

Chairman BERMAN. All right. They are not included. You are essentially saying they are equal to all of the rest of the——

Mr. LUFT. Oh, yes. Not included, of course, yes.

Chairman BERMAN. Okay. The gentleman from South Carolina, Mr. Wilson, is recognized for 5 minutes.

Mr. WILSON. Thank you, Mr. Chairman, and thank you all for being here today on this very important issue.

Many policymakers, and this is for anyone who would like to answer the question, many policymakers are concerned that sovereign wealth funds may use their funds' investments as a tool to achieve political or economic goals other than securing a higher rate of return on their investments. Do you think this is a serious risk? If so, what would you recommend be done to mitigate this risk?

Mr. TRUMAN. If I could jump in first for that one—you will want to hear from each of us. I think we need to distinguish a little more clearly about political-economic goals which are achieved through sovereign wealth funds, which is a sort of secondary process, and those might be achieved through foreign direct investment itself. Right?

Government investments are part of a continuum. It is all government, but the sovereign wealth fund is managed separately, and the question is, How separately from the government?

So if you were a foreign government, and you wanted to steal U.S. secrets, you would not set up a sovereign wealth fund in order to do that. You would form a corporation that was called the Stealing U.S. Secrets Corporation, and you would do it a lot more directly.

That is the first part of my answer. Then we have the CFIUS process, and you have just strengthened that through FINSA, and the Congress, I think, did a very nice job there to try to limit the capacity for this to happen. That is what I would say to answer your question.

Mr. WILSON. Thank you.

Mr. LUFT. I think, to add, one of the dangers with involving government in corporations, let us not forget that governments, particularly those governments, have a very robust, intelligence apparatus. The question is, How do you prevent those governments to use their intelligence apparatuses to improve their access to information? Imagine to yourself, the U.S. Government is using the CIA to acquire information about corporations that the U.S. has some financial interest in.

So I think that it is very difficult now to pinpoint that these kinds of things happen, but that is one of those issues that sort of comes to mind when you talk about the nexus between government and business.

Mr. LYONS. I would reinforce Dr. Truman's comment about the need to differentiate between sovereign wealth funds and foreign direct investment. In terms of foreign direct investment, I think one needs to ensure that, if one looks at it from the viewpoint of the consumer, it adheres to competition policy, it adheres to regulation policy, and then, if necessary, I think it is important to safeguard sensitive sectors. People accept those in terms of defense. People might accept them in terms of media.

Over and above that, I think there is still a black hole, in my mind, in terms of intellectual property rights. I think we need to have global standards on patent and intellectual property rights because this is important because the economies in poorer parts of the world will want to move up the value curve very quickly, in economic and maybe political terms.

Finally, in terms of sovereign wealth funds, I would argue very strongly for a code of conduct and enforceability if people do not play by the new rules of the game. Obviously, to get the rules of the game, you need to have active discussion ahead of that code of conduct.

Mr. WILSON. Thank you, all. Indeed, in my home state, we have benefitted extraordinarily from foreign direct investment, with BMW, with Michelin, with Hier from China, and so we have seen the positive side.

Indeed, Dr. Lyons, a follow-up question: Do you support financial disclosure requirements for sovereign wealth funds? If so, what kinds of additional disclosures would be appropriate?

Mr. LYONS. In terms of the recent paper I gave, I was outlining what I thought should be included in terms of a code of conduct.

I am not sure about how far we need to go, but there needs to be more clarity in terms of investment strategy. There should be annual reports. I think we should actually be able to see, at face value, how much the funds have and in what companies, and, indeed, what is sensible in terms of a reporting requirement.

I think there needs to be more clarity, more transparency, partly because I think that will alleviate fears, as well as expose any, shall we say, any bad practices.

Mr. WILSON. Without penalizing foreign investment, I look forward to working with the chairman on any legislation that may promote transparency, indeed, to encourage more foreign investment. I yield the balance of my time.

Chairman BERMAN. The gentleman's time has expired. The gentleman from California, Mr. Costa, is recognized for 5 minutes.

Mr. COSTA. Thank you very much, Mr. Chairman. I would like to explore with the panel here the economic considerations regarding sovereign wealth funds. We have talked about a code of conduct, and we have talked about the impacts on intellectual property rights. Actually, where is the forum—if there is a forum—that exists today where all of these countries that are taking place in sovereign wealth funds sit to discuss whether or not there should be a code of conduct or whether or not there is a process that is being developed?

Then I would like to ask you each whether or not you regard these sovereign wealth funds as an overall source of market stability or instability, given the current way they are structured.

Mr. TRUMAN. Briefly, the effort that is underway to develop a code of conduct or best practices is being sponsored by the International Monetary Fund. They have set up a committee involving the countries with sovereign wealth funds, which includes countries like the United States, since we have some sovereign wealth funds ourselves, and that is the way the effort is. They are sitting together.

Mr. COSTA. And all of the countries on this graph are participating.

Mr. TRUMAN. Yes, essentially. There are 25 countries that are involved in that process. I am not sure whether the committee is all of the ones on the graph, but most of them, yes.

That is where the process is. The results are supposed to come out at the end of the summer, in October, and I think the question will be, as I outline in my testimony, how robust that code of conduct will be, whether it covers all of the kinds of issues that I have outlined, whether the countries all sign up to it, and then whether it is enforceable, at least to the extent that you and I can tell whether countries are obeying that code of conduct.

Mr. COSTA. Are there any current examples of those that are on here that are not participating?

Mr. TRUMAN. I think I can handle this bilaterally. I have a list of the countries, but I do not think you want to spend the committee's time on that point.

Mr. COSTA. All right. My time is evaporating here. How about the questions of stability or instability in world markets?

Mr. LYONS. Basically, the global financial sector is still in turmoil, and the credit crunch is clearly going from one stage to an-

other stage. So far, the injection of capital has been a source of stability because financial firms in the West, particularly in the States but primarily in Europe and the States, were short of liquidity, short of capital, so we have had a capital injection.

The issue raised is, of course, should these funds be more active or less active in terms of having put that capital in? Should they be encouraged to take a seat at the table, or should they just invest passively?

Mr. COSTA. Some of my colleagues inferred, in some of their questions, that potentially this could be a source of instability in the future. Could you foresee a set of circumstances where that could happen?

Mr. TRUMAN. The next stage of the instability could be that if we have the problems spreading to the greater economy, and financial firms get into more trouble, and they become short of liquidity of capital, and they do not get the provision of capital that they had previously, the only way in which, looking at your question in different ways, whether that capital is withdrawn in the future. So that, in itself, could be a sort of instability.

Mr. COSTA. Political reasons.

Mr. TRUMAN. Most of the countries with sovereign wealth funds have actually put money in, properly you might regard as being politically friendly to the States, in that respect.

So, in answer, yes, it is possible to envisage the situation. Would it happen? I am not sure.

Mr. COSTA. Mr. Luft, you talked about, in essence, a political-socioeconomic conscience of the cost of energy being a regressive tax. I would add to your comment, I guess, that it also, as we look at $120-and-up a barrel for oil, that we are financing both sides of the War on Terror.

This regressive tax on the world economy that you speak of brings to mind an issue that, I think, World Bank President Robert Zoellick raised in terms of proposing the use of sovereign wealth funds as a small increment on the interest of them to deal with some of the questions of the lack of food in sub-Saharan Africa and other places. The silence has been deafening after he raised that proposal. Would you care to comment?

Mr. LUFT. Well, that goes into my earlier comment about the influence of government money on commodity prizes. I referred mainly to oil, but I think that the same mechanism applies to other commodities, including food commodities. If we just look at some of the food commodities, we have seen, within just less than 3 years, doubling the number of contracts, whereas deliveries remained about the same.

So I think that the problem is that we have more and more sovereign wealth going into private equity funds, hedge funds, and that becomes very murky when you have this massive laundromat where the money sort of goes into other institutional investments.

Chairman BERMAN. Dr. Luft, I am sorry. The time has expired. Assuming floor votes will not kill us, I do intend for there to be a second round, not just for me.

The gentleman from Tennessee, Mr. Tanner, is recognized for 5 minutes.

Mr. TANNER. Thank you very much, Mr. Chairman, and I want to thank the chair for holding this hearing.

I personally believe that this is a far greater problem than I have heard today, that, Dr. Luft, you, in your paper, have pointed out. I want to ask a slightly different version.

This country is addicted not only to foreign oil but to foreign capital. During the last 72 months, this administration and the Congress have borrowed more money from foreign sources than all 42 administrations before it combined. Now, as we see sovereign wealth funds begin to, as you just described it, murkily get into not only the equities that are here in the United States but financing our debt.

Ed Royce said it well a while ago when he said, when you get into sovereign wealth funds, there is not always the economic principles at work, but there is also a geopolitical aim that some of these governments have that does not have anything to do with a traditional profit motive or with economics, as we know it.

I think that is approaching a national security issue, if it is not one already, and I, frankly, would like to hear your comments as to our inability to basically pay our own bills, to rely on foreign investment to finance the operation of the Government of the United States of America.

Mr. TRUMAN. Let me start here. I, 100 percent, agree with you and the fact that we are running a deficit, both in our external accounts and in our fiscal accounts, is a big problem. It increases our reliance on foreign investment.

I would point out another two things. We have $13 trillion of foreign investment, and there is $16 trillion here in the United States. So we are engaged in the international financial system. Even if we are in balance-of-payments surplus, current-accounts surplus, and budget surplus, you still would have a problem with sovereign wealth funds. Sovereign wealth funds are investing in Germany, which has a current-accounts surplus; investing in Switzerland, which has a huge current-accounts surplus.

So the problem we point to about our reliance on foreign investment, net reliance on foreign investment, is very real, but I think it is a problem to conflate that issue with sovereign wealth funds. The sovereign wealth fund will be there anyhow because of the very fact that we have a big deficit, but we are putting private wealth, $13 trillion, in the rest of the world.

Mr. TANNER. We have a saying in Tennessee that "there is a fine line between you owning the bank and the bank owning you," and it cannot be a good thing for this country to continue to rely on foreign investment to finance the operations of our Government, in my judgment.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from New York, Mr. Meeks, is recognized for 5 minutes.

Mr. MEEKS. Thank you, Mr. Chairman. More than ever, the United States is deeply immersed in a more global and a more singular economy. With the integration of the swift changes that come with globalization, we are experiencing a period of trepidation, and even doubt, about our future. Sovereign wealth funds are not a new phenomenon, but when linked to the anxiety that accompanies the

global economy and the geopolitical challenges, these funds have become far more visible and far more controversial.

The fact is, when a government owns and controls investment, there is an inherent concern that there may be political, rather than business, motives. The sheer enormity of these investment funds presents both economic growth opportunities and challenges.

Now, from my perspective, with globalization, it is important, I think. I have often said that they basically, over a period of time, there have been two basic forms of relationships that governments have had. One is where you trade or work with one and invest and one, creating more interdependency, and the other is where you go to war. You just want to take over a country, or something of that nature, to take its wealth, et cetera.

From my perspective, it is better if we become more interdependent, more trading and investing with one another, because I think that makes us all safer on the planet that we share that is increasingly becoming much smaller. I know that we do have to look and make sure that we have processes in place so that we can assure that someone else is not going to want to go to the tactic of war to just take wealth.

But it just seems to me, first of all, we are on the Foreign Affairs Committee, so one of the questions that I think that I want to ask, first, to Dr. Truman is, I am always concerned that we tell other people to do something, and we do not do the same thing ourselves. I do not know, in this instance, but I have seen, in your testimony, that you talk about the $3 trillion that we have in sovereign wealth funds, and I believe that we are transparent, so I think that we are good to ask others to be transparent.

But some of the things that we are asking sovereign wealth funds that are investing in the United States; are we doing those things now in the countries in the areas where we are investing sovereign wealth funds?

Mr. TRUMAN. That is a good question. I appreciate it. I think that my studies of the U.S. sovereign wealth funds, per se, are very transparent in that sense, that we do follow the practices that we would like the rest of the world to follow, and I think you are very right to point out that this is a double-edged sword, and we need to expect other countries to do what we are doing.

We do not do this in all cases, but I think that this area is one where we, the United States, through a variety of our own political processes, the government ownership of wealth is quite transparent, and I think that is, picking up on the first part of your question, that is the kind of doctrine, if you want to put it that way, that we want to project onto the rest of the world, and this code of conduct, best practices, is one way to bring the rest of the world up to our standard, and it will be a long and prolonged process, but I am an optimist.

Mr. MEEKS. Let me ask this question, because the other thing is I am always trying to find how we do something and pull something for the greater good. There was a recent proposal by the chair of the World Bank, Mr. Zoellick, that said that one way that maybe we can do good and create greater confidence in sovereign wealth funds is if the profits that the sovereign wealth funds receive, 1 percent of it would be dedicated to the poorest continent

on the planet, Africa, that would then help create other private investments, et cetera, and bring that continent up to modern-day standards. What is your feeling on that?

Mr. TRUMAN. I think, actually, that illustrates precisely the problem we have here. President Zoellick says, "Devote 1 percent of your profits to Africa." That is good. The problem is that he is also is saying, We want these sovereign wealth funds to act politically by devoting some of their money to Africa.

So you and I might agree that it is a good idea for corporations, if you want to put it that way, to do a certain amount of charitable activity. But in this case, we are combining politics with finance, and one of the issues is that we want to separate politics from finance.

I do not want to comment particularly on the merits, in some sense, but I think it illustrates the problem that where you have governments handling large amounts of money, you are going to have governmental motives involved in the use of that money when you would prefer, as Congressman Royce said, to have it essentially be in private hands.

Chairman BERMAN. The time of the gentleman has expired. I yield myself 5 minutes for questions. I want to follow up on two issues that Mr. Meeks raised, and your last comment leads right into it.

For me, right now, a big priority is how do we get this regime in Iran to stop developing a nuclear weapon? Why don't I want our Government to persuade the sovereign wealth to make sure that the government-controlled sovereign wealth funds of certain countries that may very well be investing in Iran's energy sector, or in any company in Iran, and the relationship of the Government of Iran, the wealth of Iran to those investments? There is a relationship.

I have a political agenda. Those sovereign wealth funds are one way to achieve my agenda. I want our Government to be doing that.

So, I take it, in this whole notion of codes of conduct and transparency, none of this involves pushing companies to subscribe, pushing sovereign wealth funds to subscribe, to the notion of your investments have to be commercially based rather than political- or governmental-policy based. The codes of conduct being discussed do not cover that.

In other words, it gets back to Congressman Meeks' point: Do we want to stop others from doing things that we would like to have the leverage to do? And then the second part of this, and then I will quit: Conflation here. Mr. Meeks sort of assumed we have sovereign wealth funds because we have pension funds that make investments.

Is it right to think of those many different pension funds which, presumably, are governed by boards, some of whom represent employees who have contributed money into that and who do have a high commercial profit agenda in terms of the funds investments, to think of them as pretty much the same as sovereign wealth funds?

Those would be the two issues that I would like you to explore here.

Mr. LYONS. In terms of your first aspect, I think that whether one has a code of conduct or not, I think there is a need for clarity of objectives and of investment strategies of sovereign wealth funds. Within that, I think sovereign wealth funds should have a clear mandate set around commercial objectives, and the investment practices of the funds should be made public.

Chairman BERMAN. Why would we believe what they say? They say, "We are interested in commercial, profit-making, economically driven investments, but—"

Mr. LYONS. Well, that comes out as the undercurrent of the comments this morning. There are two different sides to this. Many of the funds would say, "Hands up. We have behaved well in the past." Of course, we want to be reassured that if they have behaved well in the past that they behave well in the future.

But then the other aspect to that is that, as we have talked about, there is the state capitalist aspect, whether it is referring to aspects of these funds or, indeed, to nonsovereign wealth funds but foreign direct investment by the likes of whether it is Russia or China. In that aspect, in answer to your question, can we believe them, well, it is difficult to say. You can only hope that they will adhere to best practice, but I think the important thing is that both sides work together on this.

In terms of the aspect about Iran, I would not want to go into that particular case, but I think, going back to your comment, is the state capitalist aspect of this, and, as Dr. Truman said in the answer to the last question, the important aspect here is to differentiate between the commercial and the sort of government or the strategic versus commercial aspect here.

Mr. TRUMAN. Could I just answer the second part of your question? I think it is reasonable to make that comparison. There are differences between pension funds, government-run and -managed pension funds and commonwealth funds, if you want to put it that way, nonpension, but I think that the code of conduct that is involved, and the reason why you want a code of conduct involved, both for the employees, if you want to put it that way, and the citizens is exactly the same.

So the same standards should apply to pension funds, sovereign wealth fund pension funds, if you want to put it that way, and nonpension funds. That is why I have included them for comparison purposes in my scoreboard, and I will point out that the pension funds do very well, but a number of sovereign wealth funds do very well, too. So it is not impossible to say the sovereign wealth funds can live up to the same standards as the pension funds.

Chairman BERMAN. My time has expired. The gentleman from Illinois, Mr. Manzullo.

Mr. MANZULLO. This is a fascinating hearing, with three economists that are exquisitely clear. I commend each of you. Your testimony is very easy to follow, and I thank you for that.

As I have been following the stream here, it gets more frightening as the price of oil goes up per barrel, the less money there is in the United States and the more we have to rely upon foreign capital. Is that correct?

Mr. LUFT. Absolutely. This year, we are going to export $.5 trillion of our money in exchange for foreign oil, which is about the

size of our defense budget. So, of course, the less money we have and the more money we have to ship overseas ends up in the hands of a cartel that is doing nothing.

Mr. MANZULLO. There is a follow-up. If taxes are increased in the United States, that is less liquidity here, and that means we have to rely more upon foreign direct investment. Is that correct also?

Mr. LYONS. Could I come back on this?

Mr. MANZULLO. Of course.

Mr. LYONS. This is not a static situation. If we look at the Middle East, the economies in the Middle East are a spectrum, but I tend to say that the best way to think about them, allowing for that, is what I call the "three Ds": Demographics, diversification, and the dollar. These countries have very young populations. Therefore, they need to diversify. Energy is always going to dominate the region, but they need to diversify as much as they can to generate jobs because energy-intensive areas do not generate the jobs they need.

On top of that, they need a monetary policy best suited. They are importing inflation at the moment because they are tied to a U.S. monetary policy. Now, in a static situation, it looks terrible. You are an oil importer, and you are exporting to the U.S., as you said from your question. Your money is going to this region. But the reality is that it is a dynamic situation.

In the past, we had oil price booms and busts. They got the money. They spent it. Hey, presto, they had a good time, but they did not have anything to show for it. What we are trying to get these countries to do now is to diversify and invest at home. Now, if they do that, then their economies start to become more service economies, their economies start to demand goods and services that we, in the States, we, in Western Europe, produce, and if they start to develop their financial markets, then you can have United States investment firms, doing more business there.

So I think the important thing is to get them to say——

Mr. MANZULLO. UAE is building a city for 50,000 people that will be entirely run on alternative energy. My question here is that the higher our taxes are in this country, the less money we have to invest in our own companies, and the more we have to rely upon foreign direct investment. Is there agreement on that?

Mr. LYONS. If I could just conclude and pass on, if you go to China, what is interesting is it is United States companies who are some of the biggest exporters from China. U.S. companies, for their own commercial reasons, have chosen, in recent years, to invest outside of the States. Therefore, the U.S., like the U.K., we need to make ourselves competitive at home to encourage those companies to invest at home. The Western companies are making their own commercial decisions.

Mr. MANZULLO. Right, but one of the ways you become more competitive is buying the best machine tools, and you cannot do that if you do not have the money.

Mr. TRUMAN. I do not want to get too partisan here—taxes are only part of the equation. Right? Taxes are raised to fund public expenditures. You could argue about whether you want to have those public expenditures. It is the balance that actually takes money out of the pocket, the fact that government dissaves means

that savings will not go to corporations that need to invest, and that, I think, is the best way to think about it.

So whether it is on the tax being too high or the expenditures side being too high, you have to reach some balance, and that is what you people here in Congress are worrying about. Sure, if the rate of taxes were zero, then you would have to have no government expenditures as well, and the question is that balance. When it gets imbalanced—right?—when you have taxes too high relative to——

Mr. MANZULLO. If taxes are going up, and the price of oil is going up, that means the United States has to become more dependent upon foreign investors to build our own infrastructure here and to build our own factories.

Mr. TRUMAN. It is the fact that we have to issue debt, and the foreigners buy our debt——

Mr. MANZULLO. Right.

Mr. TRUMAN [continuing]. Associated with the imbalance between taxes and expenditures.

Mr. MANZULLO. Okay. Thank you.

Chairman BERMAN. We have seen the enemy, and it is us.

The gentleman from New York, Mr. Meeks.

Mr. MEEKS. I think that you just touched on a point that I think is important to mention, that there is a difference between investment and debt. Those are not the same thing. If you are buying debt, that is one thing. If you are investing, I believe that is a whole other issue. That is a whole other thing, and we cannot confuse the two because then you would think that we are giving away our country in that regard.

In fact, often I think just the contrary. When I look at the municipality of New York City, if I want to keep taxes kind of consistent, then if I did have sovereign wealth fund or other investments to help do it, as opposed to the taxpayers building it, then we could do a couple of things. I think it makes us more interdependent also.

Let me go back to where I ended before because I agree and understand the principle of whether or not we are getting political when we try to tell individuals this. I understand Mr. Berman's position because I agree. However, I think that I am trying to come from a different position.

One of the things that the way I am coming from is charity, and I think that charity is a good benefit for all. I know everybody has different religious beliefs and everything, so I do not want to impose mine, but I would just use mine as an example, where, in church, you are required to make sure you set aside a certain amount of money for the church, called "tithing." That is charity, and, basically, what I was getting at was maybe the money could go to the World Bank or something of that nature.

When we see that we have other people in the world who are suffering, the poorest continent in the world, if, in fact, we have the individuals that have and to make sure that we are making it so that it is good or better for all of us, that if a certain percentage is put into the World Bank so that it could be investment or charity that is given to the World Bank, if you will, and the World Bank is required to put that into infrastructure or other items on

the continent of Africa, that seems to me—those who give charity, we look at them as good people. I know some of us, politically; they look at how much we give, based upon how much money. If you do not give, they say, "Hey, you are a greedy person." If you give, you are better off.

So that is the concept that I am looking at, and I think that Ambassador Zoellick was looking at. What do you think of that?

Mr. TRUMAN. I did not want to come out against charity. That is why I answered the question the way I did, and I think there is a role for charity, including by corporations, as well as individuals, but I was using it to illustrate the problem between the mix of politics and economics in this case, but I will defer.

Mr. MEEKS. I am anxious to hear Mr. Luft because, you know, I am intrigued by your testimony and reading it also because I do think that part of our problem is we can resolve it ourselves, and that is finding the alternative fuels, finding other mechanisms other than fossil fuels, and quenching our thirst on that can make a difference. I would just be interested in your response, Dr. Luft.

Mr. LUFT. On charity, look, it would be nice, but if you look at the different patterns of Saudi Arabia, Dubai, all of these countries that are having quite a jolly time at the moment, we have not seen a dramatic increase, nothing in relation to their increase in revenue, when it comes to their foreign aid, including, by the way, two Muslim countries. The Palestinian brothers, the African brothers, the tsunami victims in Indonesia who are mostly Muslims; we have not seen that kind of generosity coming out of those people who are making a lot of money at the moment.

So I think that it would be nice, but it is not happening in the——

Mr. MEEKS. But, at the same time, because the problem that I am seeing is if they did, like we talk about China investing in Africa, et cetera, then we are concerned about their investing being not then charity, but they are doing it for some other strategic advantage, something of that nature. So what happens is if you cannot do it one way, nor do you want to do it the other way, then we are still leaving this continent barren, without anybody really contributing.

We are trying to do the best that we can, to some degree, from the United States. We are probably not doing as much as we can, or should be doing, but it should be, I think, a collaborative, and that would then help us. You know, I do not see any other way around this thing.

Mr. LUFT. Mr. Berman, I think that it boils down to the point that you made before. Look, we all engage in the relations between politics and money and the relations between foreign relations and investments, and we are not going to be able to divorce the two. History is full of examples of economic warfare. Our own country used it against South Africa. We are using it now against Iran. That is how it is going to be.

So I think there needs to be a dose of political realism that what was the case will continue to be, and, therefore, this is a budding issue, so I think eternal vigilance is the important issue here, and it is a moving target. The committee is doing good for shedding light on it, but it is definitely the beginning of something much big-

ger that, in my view, boils into who is going to control the world economy in the 21st century.

Chairman BERMAN. The time of the gentleman has expired. The gentleman from California, Mr. Royce.

Mr. ROYCE. Thank you, Mr. Chairman. Dr. Luft, getting back to your point on eternal vigilance, a lot of these issues that we are discussing today are really dependent upon a robust CFIUS process actually working, if we are going to alleviate some of these concerns, and I would ask maybe Dr. Truman and Dr. Luft, how confident are you in the CFIUS process to weed out the troublesome investments that concern us?

You know, it is a complex world, and I wonder if our Government really is as cognizant as we would like to think it is about this.

We had a hearing yesterday in the Nonproliferation Subcommittee, and we heard testimony regarding the Commerce Department, Bureau of Industry and Securities, validate an end-user program, and what this was supposed to do was allow selected companies to receive dual-use items without export licenses, and, of course, what we found out was that two of the first five Chinese companies designated in the program, were closely linked to China's military industrial complex and to Chinese proliferators that were sanctioned by the United States.

Now, this Commerce program that I am talking about is not CFIUS, but it does raise questions about the U.S. Government's ability to vet foreign institutions, and I would like your evaluation on that, given what we learned yesterday. Dr. Luft?

Mr. LUFT. I am much more comfortable with CFIUS after the reform, and I applaud Congress for improving this system.

I think that the biggest weakness now of CFIUS is that it is a little bit too vague on what constitutes national security. It is too much of a gray area. My concern is not so much on the sort of traditional national security hardware issues—these are going to be okay—but more vague issues.

When foreign governments buy major media outlets, is that national security? We talked before about the autos.

The problem is more with the gray area there. What falls under the category of national security?; that is something that CFIUS does not define very clearly.

Mr. ROYCE. Thank you. Dr. Truman?

Mr. TRUMAN. I am optimistic. Let me put it this way. I do not think you can be 100 percent certain. There is no sure thing in this world. I think the CFIUS process has been strengthened. Particularly in the area of providing information it has been strengthened. The interaction with other programs has been strengthened. In particular, I would note that the CFIUS law applies where other U.S. laws do not already apply. So it actually is on top of the Commerce Department rules that you just described.

So I am as confident as you can be, in an uncertain world, about how that process will be able to protect us fundamentally. There will be, no doubt, some problems in between.

I worry about our going down the road of walling off big sectors of our economy, quite frankly, because I think everybody thinks something is important, if I may put it that way. You know, one might argue—I will probably get a lot of bad e-mail from this—that

Disneyland is part of our national security, and, therefore, we should not let the foreigners buy Disneyland because it is a national asset. It certainly is associated with America. That is an extreme example, but it illustrates the problem if we start saying, "You cannot go here; you cannot go there."

When you end up doing that, you will end up excluding, for one reason or another, 85 percent of the U.S. economy, and I do not think that is where you want to go. I think you have to live with this gray area, and certainly the use of CFIUS since 9/11—there are two ways to look at it—it has been vastly increased, and so there is a vastly increased amount of scrutiny that is now being applied to these kinds of investments in the United States than there was 10 years ago, when I actually was involved in the process.

Mr. ROYCE. Thank you, Dr. Truman.

Chairman BERMAN. If I can get unanimous consent to recognize the gentleman from Virginia, who was, as I understand it, a co-chair of this sovereign fund working group with Mr. Moran, and if he had any questions, we would be happy to yield him 5 minutes.

Mr. DAVIS. Thank you, Mr. Chairman. Thank you very much.

As a country, we want to continue to attract capital, not to wall it off and chase it away. This investment is going to go somewhere. You could argue that some of this is our money. It was spent on fuel prices from Americans and transferred to other areas.

I will start with you, Dr. Luft, because I think you have been the most skeptical one on the panel. This is not outsourcing; this is really insourcing in terms of bringing foreign capital investment to this country.

We allow governments to buy U.S. Treasuries. That, in some ways, almost allows them to undermine us in a way that buying companies and buildings would not. Would you feel the same way about foreign countries buying U.S. Treasuries?

Mr. LUFT. These kinds of questions cannot generalize here. We have to look at this on a case-by-case. Foreign governments are different, and I think that the instruments they are investing in are different, and also, if you sort of look at it more broadly, it is not only sovereign wealth funds. You have got to look at the entire package of investments, which includes central banks, high-net-wealth individuals, government-owned private investment firms. So we have got to look at the entire picture.

The danger here is that we try to tailor a suit for everybody, and it is never going to work well. If we were to do something right to introduce the mechanisms that would allow us to look at each case, vet it properly, and deliver the recommendations, whether on the ballots it is a net gain or a net loss, looking, as I said before, at the future trajectories and looking at the behaviors of these countries over a long period of time and making——

Mr. DAVIS. So you apply a political-correctness test, basically.

Mr. LUFT. Pardon?

Mr. DAVIS. You would apply, like, a political-correctness test to countries whose sovereign wealth funds would be invested. Either they were behaving appropriately, or they were seen as a threat.

Mr. LUFT. I think that there will have to be a grading system, so to say, to each country to figure out what is the level of risk associated. I am not in favor of sort of removing all of the barriers

and giving every country full access to the financial system, and I think that these countries are doing the same to us, quite frankly. If you look at those countries' approach toward foreign investors that try to invest in their midst——

Mr. DAVIS. It is not a two-way street.

Mr. LUFT. Yes.

Mr. DAVIS. But you want to find a way where it is not case by case, or no one is going to invest here. You have to have a certain predictability and constancy to this really to be effective. My gut was this is in the long-term interests of the country to be able to attract capital from throughout the globe. Let me just ask Dr. Lyons and Dr. Truman how they feel about this.

Mr. LYONS. Certainly, one size is not going to fit all for most things, but what we clearly need is broad parameters, rules of the game.

Sovereign funds may well go from buying debt to now buying equity. I think, as we have discussed earlier, it is in the United States remit, as it is in France and other countries' remit, to protect sensitive areas. One can define "sensitive areas" as one wishes in international terms. I think that provides some clarity as to sectors that overseas investors cannot go into.

I do think you want to have a clear, predictable framework. I am a strong advocate of a code of conduct. I think it needs to be enforceable, and if, at the end of the day, people do not want to play by those rules, then you might say, well, you do not want their money, and it is up to them to put their money elsewhere.

Once we start trying to have specific rules for specific people at specific times, we are going to get bogged down. Reciprocity, things like this, you get bogged down. I think we want level playing fields and clear, predictable rules.

I think, finally, it is encouraging. It was only last October, for the first time, at the IMF meetings, that there was an outreach dinner hosted, as I believe, by the U.S. Treasury with eight sovereign funds. I think, given where we have come from in such a short space of time, it shows that engagement, putting our cards on the table, does actually force a more open debate, and I think both sides are moving, and, therefore, that is encouraging.

Mr. TRUMAN. I agree. I would add that in general, you want to be open, and then you want to be careful in certain areas, and I think that is the only way you can do it.

The case-by-case, if you think about the fact that we now have $16 trillion invested in foreign investment in the United States, if we had to put each one of those dollars through a fine sieve, based upon our views of the country from which the investment comes today, as opposed to yesterday or tomorrow, and our views do change over time—some of our old friends are now our enemies and vice versa—I think it would be a cumbersome process and would wall us off from the world.

So I think we need to think about trying to be proactive in this area, but the answer, I think, is not—I do not agree with Dr. Luft—is not a case-by-case on each investor. You do not want to say, "Central Bank A can buy U.S. Treasuries, and Central Bank B cannot buy U.S. Treasuries." I just think that is not practical or appropriate in the world today.

Chairman BERMAN. The time of the gentleman has expired. The gentlelady from Texas, Ms. Sheila Jackson Lee, is recognized for 5 minutes.

Ms. JACKSON LEE. Mr. Chairman, thank you very much, and my apologies to the witnesses. We were, interestingly enough, in a Homeland Security hearing. I believe that the hearing here today has some impact on homeland security and the security of our nation and the use of sovereign wealth funds.

We typically think of security by bodily harm, and intelligence gathering to keep out terrorists that would bring down airplanes or interrupt rail transit, and, by no means, am I trying to have a complete comparison, but we are diligent about those aspects of our society.

This issue, dealing with sovereign wealth of another country, is not a new phenomenon because, I believe, if I recall correctly, there was a great deal of enthusiasm, for example, when Japanese businesspersons bought up a lot of real estate in Hawaii for a period of time. I think the market went bust, but we were welcoming individuals to spend their wealth.

In this instance, I am particularly concerned because the financial sector is an infrastructure. It is something that can clearly be undermined or pulled, and, in the plight that this present administration has put us in, with enormous paper debt, certainly the ability to buy up that debt, I think, is a question of security.

So I am going to start—there may be differences of opinion—I am going to start with Dr. Lyons and just go down the row, and tell me whether or not the use of sovereign wealth in investment can be a question of security, and can it undermine the financial system of this nation?

Mr. LYONS. I think it is an issue because sovereign funds can buy into sensitive areas and strategic areas, but, therefore, it is important for the U.S. and, indeed, other countries in the West to make safeguards to protect those sensitive or strategic areas.

I think the key aspect is for the U.S. economy to move back to a more balanced economy. We have a very imbalanced global economy, and that is why the issue of sovereign funds, and maybe some of the issues you have touched on, have come to importance at the moment.

To get to a balanced global economy, one needs to see a period of weaker U.S. growth, and we are seeing this, and currency adjustment. One needs to see Europe and Japan pick up some of the slack. But, very importantly, one needs to see surplus or saving countries around the world, and this is many of the countries from which these sovereign funds emanate, whether it is in the Middle East or in Asia, one needs to see those countries try and switch their high savings into increased domestic demand.

So what one needs to do, from the U.S. perspective, I think, is twofold: One, to protect your sensitive strategic areas, not by a protectionist route but, as we have talked about this morning, clear, predictable rules. Also, at the same time, I think the U.S. should be encouraging sovereign wealth fund countries, countries from which these funds emanate, to actually basically try and contribute to a more balanced global growth by deepening, broadening, opening up their financial sectors.

Ms. JACKSON LEE. Dr. Truman?

Mr. TRUMAN. On your first question, I think the answer is yes. Sovereign wealth could be a security issue; however, I think we have adequate means to deal with that in general.

Ms. JACKSON LEE. Just quickly, what adequate means are you speaking of?

Mr. TRUMAN. I am talking about the CFIUS process. Let me come to the second part of your question, the financial system.

We have the CFIUS process, which applies to all investments in the United States, and we have special rules, in terms of the financial sector, and the Federal Reserve, where I used to work for many years, has rules that are tighter and allow us to look at investments by foreign entities, any foreign entity, including sovereign wealth funds, in U.S. financial institutions, and I think there are special issues there because they are more easily looted than almost any other kind of investment.

I am reason why confident that those rules are strong at the moment. I do worry a bit whether the Federal Reserve and the other financial regulators need to think a little bit harder about what I call the "issue of undue influence." I think that is an issue of supervisory practice. It is not an issue of rules. You cannot define what "undue influence" is. You can define what "control" is. You can come close to it. I think you need to worry a bit about that.

We have rules that say, if you are a big shareholder, you cannot lend money to your friends and relations and so forth and so on. So there are rules in place, but I think one needs to think about them again, and I know the Federal Reserve is doing it. They have testified twice before Congress already on this subject, thinking about how those rules apply in the current circumstances.

Chairman BERMAN. The time of the gentlelady has expired. I yield myself 5 minutes, and we do intend to get you out for lunch.

Let me challenge my earlier line of thinking in this debate with myself. Let us not worry about motivations because they are complicated and hard to evaluate, and we have put together a package of transparency and accountability, and we have CFIUS, and then, on things like sovereign fund investments in the automobile industry, and instead of focusing on the danger of that, we focus on national policy.

What do we want to do about reliance on fossil fuels? We have focused regulation to serve our goals there and effective enforcement, which, in the end, that plus profit-motive competition, people able to make more people by not dawdling on this issue because the economics of researching and then implementing meaningful alternative energy sources is going to trample on the company that is going slow and trying to hide the ball because of the agenda of one of its investors, and, with respect to something like Iran, do not focus on sovereign wealth funds.

There is no greater danger from the investment of a sovereign wealth fund in Iran than a huge number of companies in Germany having bilateral trade and investment dealings with Iran, and you work to get policies that apply to all sources of investment and do not get into the motivations of the investor.

I am curious, which argument is better?

Mr. TRUMAN. I think that your argument is probably an accurate description, Mr. Chairman. You cannot stop being involved in motivations. When governments are involved, governments, by definition, have different motivations, or different motivations get read into their acts, and that, I think, is the fundamental problem we are facing.

So it could be a country in which the motivations are completely clear. A good example is when the Norwegian Sovereign Wealth Fund sold Icelandic bonds. It was a commercial decision, but it was read in Iceland as a political decision. That illustrates the tension——

Chairman BERMAN. The politics of Norway's decision to sell its Icelandic bonds escapes me. What is going on in that part of the world?

Mr. TRUMAN. Norway's fund owned Icelandic bonds. They looked at the Icelandic economy, and they thought it was weakening. They said, We need to sell those bonds because——

Chairman BERMAN. Why is that a——

Mr. TRUMAN. Because it was a Norwegian Government entity.

Chairman BERMAN. But it was a commercial decision.

Mr. TRUMAN. Yes, but the point is, the Icelandic Government, because it was a Norwegian Government entity, read into the motivation something political. I think that illustrates precisely the tension that you very accurately have described.

Mr. LYONS. I do not know the details of that, but it was covered—actually, Larry Summers talked about this at Davos. I think there was a binding agreement as well between the countries as well, in terms of financial stability, that led to noncommercial aspects to come into the decision.

Chairman BERMAN. So the original motivation to invest was not commercial; it was about a bilateral relationship using——

Mr. LYONS. When they came to sell, I think, some of the noncommercial aspects came in, but I need to look back at it in detail.

It comes to the heart of what we have been saying about the commercial versus noncommercial aspects of this.

I think, just coming back to your comment, you have thrown lots of issues together. I think it is important that we try, as I was saying at the beginning, to have rules for the sovereign wealth funds. We need to also accept the problems with state capitalism. But also there is this macroeconomic picture.

The world is changing. Energy dependency, resource dependency is changing, so some of these issues are going to be with us for a long time. That is why I think we do need to have broad rules that bind us all together.

Mr. LUFT. I just want to touch upon the automakers because, to me, that is a place where it could be very, very attractive to some of those countries.

In 2004, Volkswagen had run into tremendous economic difficulties. Abu Dhabi came up and offered to buy 25 percent of the company.

Chairman BERMAN. Which company?

Mr. LUFT. Abu Dhabi offered to buy 25 percent of Volkswagen, a major German automaker. The reason that the deal did not go through was not because of politics. It was not because of CFIUS-

like issues. It was just because they could not agree on the fine print.

But it tells you what kinds of challenges we can face when, one day, GM will be approached by a country that is willing to take the pension obligations, and, at that point, I am sure that there will be hearings in many committees in the House and the Senate about the viability of such a transaction, and that is going to put to test some of those premises of, you know, freedom of this, freedom of that, but it is all good until you actually have to sort of approve it or not, and, at that point, you can make the case that there is an interest beyond just commercial interests, you know. You want to own a major automaker, and that will help you to perpetuate the oil economy, which is basically the goose that lays the golden eggs on which you thrive.

Chairman BERMAN. My time has expired. Does anybody else want to?

You have been a great group of witnesses. We really appreciate it. You have given us a lot, even including your entire statements and charts, and I thank you very much, and this hearing is adjourned.

Mr. TRUMAN. On behalf of the economic profession, we thank you for the compliment.

[Whereupon, at 11:57 a.m., the committee was adjourned.]

APPENDIX

MATERIAL SUBMITTED FOR THE HEARING RECORD

PREPARED STATEMENT OF THE HONORABLE GENE GREEN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Thank you, Mr. Chairman, for holding this hearing, and I would like to welcome our witnesses.

We are here today to discuss sovereign wealth funds—an issue that might not have deemed a hearing this time last year.

But during the second half 2007, Asian and Middle Eastern sovereign wealth funds invested large sums of capital in the United States and other developed countries due to surging foreign exchange reserves and commodity prices.

Analysts predict that these funds will grow to over $12 trillion by 2012 up from a current estimate of between $1.9 and $2.9 trillion.

According to Dealogic, a financial data provider, sovereign wealth funds invested $37.9 billion alone in U.S. financial institutions in 2007 as a result of the sub-prime mortgage crisis.

Currently, the Committee on Foreign Investment in the United States (CFIUS) monitors incoming foreign investment and recommends to the President if he should block an investment on the grounds of national security.

Now, this has become more difficult as we have broadened our definition of national security to include infrastructure, energy, and technology, but the data shows that CFIUS has adapted; they have increased the number of reviews they conduct as well as utilizing more mitigation agreements.

Therefore, I am curious as to how or whether our witnesses suggest Congress play a more effective role in safeguarding U.S. interests.

There is also an international consensus building in favor of a voluntary code of conduct for sovereign wealth funds, and the International Monetary Fund and the Organization for Economic Cooperation and Development are working on this.

In fact, both Abu Dhabi and Singapore, owners of some of the largest SWFs in the world, have already agreed in principle to a code of conduct.

How can we encourage increased transparency internationally when we do not have any control over how China and Russia choose to invest there money worldwide?

Again, I look forward to our panelists' insight on this issue and what recommendations they have for us.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF THE HONORABLE DONALD A. MANZULLO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Mr. Chairman, thank you for holding this important hearing on the impact of sovereign wealth funds on America's national security. In March of this year, the issue of sovereign wealth funds was examined in a Financial Services Committee hearing, of which I am also a senior member. I believe that the more attention this issue receives the better. In fact, I raised serious concerns about China's sovereign wealth fund as early as April 2007 during an Asia Subcommittee hearing. Thus, I commend your interest in this area of America's international economic relations.

Before I go further, let me begin by saying that I am honored to be filling in for my good friend Representative Ileana Ros-Lehtinen, the distinguished Ranking Member, who is with the President at the White House commemorating Cuba Solidarity Day.

Although sovereign wealth funds are not new to the world of finance and international business, surging trade surpluses in commodity-rich countries and large foreign exchange reserves have raised the influence of sovereign wealth funds worldwide. When combined with the lack of transparency that characterizes many sovereign wealth funds, Members of Congress and the American people have good cause for concern. In the past, the process for reviewing foreign investment through the Committee on Foreign Investment in the United States, better known as CFIUS, was not adequate enough to take into consideration the new clout of the sovereign wealth funds.

The enactment of the Foreign Investment and National Security Act of 2007 greatly strengthened the CFIUS review process and eliminated potential loopholes that allowed questionable investments to go forward. I worked closely with my colleagues in the Financial Services Committee to insert a provision into the final bill that boosts national security by scrutinizing acquisitions and investments made by foreign state-owned enterprises in the United States.

We all remember not too long ago that an oil company controlled by the Chinese government tried to purchase an American oil company. At the time, those in favor of the transaction argued that the American company being purchased was of insignificant scale to adversely affect national security. With oil costing over $126 a barrel, I would argue that those of us in Congress did the right thing by opposing the purchase. Otherwise in 2008 our dependence on foreign sources of oil would be even greater!

In America, the growing footprint of sovereign wealth is felt most directly in the banking sector, where turmoil in the subprime mortgage market and other credit derivatives caused huge losses for investment and commercial banks. Since the credit crunch first unfolded last year, funds from the Middle East and Asia have invested about $70 billion in recapitalizing the rich world's biggest investment banks.

In general, there is nothing particularly new or threatening when foreign investors, be private or state, seek investments in the U.S. in non-sensitive areas of the economy. Indeed, foreign investment is a boon to our economy: U.S. subsidiaries of foreign companies employ approximately 5.1 million Americans, of which 30 percent are in the manufacturing sector; have a payroll of $336 billion; and account for 19 percent of all U.S. exported goods. Foreign direct investment, including sovereign wealth funds, provide capital to purchase companies in the U.S. where there may be no domestic financing available, thereby saving thousands of U.S. jobs. Thus, when investments decisions are made based on market fundamentals the outcome is often a win-win scenario for everyone involved.

For example, foreign owned companies play a positive role in the northern Illinois district that I represent by providing significant jobs. In Rockford, Illinois, firms from Japan and Italy own T.H. Foods and Ingersoll Machine Milling; Atlas Cold Storage in Belvidere is owned by a Canadian company; Nissan Forklift is based in Marengo; Eisenmann Corporation is the American subsidiary of a German firm in Crystal Lake; and Cadbury-Schweppes, which owns the Adams confectionary plant in Loves Park, is a British firm. In fact, Illinois is fifth in the U.S. in terms of the number of employees supported by foreign subsidiaries per state.

Indeed, most sovereign wealth funds have proven they are beneficial vehicles for foreign investment. Norway, for example, is a close ally with transparent governance for its sovereign wealth fund, the second largest in the world. However, we must acknowledge that all sovereign wealth funds are not created equal. Sovereign wealth funds from China, the United Arab Emirates, and Qatar are troublingly secretive and appear to have political or strategic investment objectives.

These activities speak to the need for the U.S. to continue to be on guard against efforts by foreign government-owned and influenced entities to secure control over U.S. companies with sensitive technologies and other assets related to national security.

In this context, I applaud the Administration for issuing clarifying regulations concerning the 10 percent ownership threshold for CFIUS review. The acquisition agreement that governs how much management control any investors, whether a public or private, is of prime importance. By removing the presumed threshold of 10 percent, the U.S. Government is putting sovereign wealth funds on notice that non-economically driven decisions will be detected.

Congress should also examine the economic security risks associated with allowing sovereign wealth funds to invest large sums of money into our economic infrastructure. Appropriate risk management structures should be in place and sound management of assets should be guaranteed. We must ensure that fair investment strategies are the standard, and that a foreign government is not using its deep pockets to subsidize a company it owns, putting other potential private sector bidders at a distinct competitive disadvantage.

Furthermore, sovereign wealth funds investing in the U.S. should be encouraged to adopt "best practices" for sovereign wealth funds, a first draft of which will be put forward by the International Monetary Fund (IMF) in August of this year. The Organization for Economic Cooperation and Development (OECD) has additionally provided guidelines to recipient countries, and will release a final report in mid next year. All of these discussions are important considerations as the international community attempts to set standards for sovereign wealth fund activity.

Mr. Chairman, it is important that we strike the appropriate balance when it comes to foreign investments and America's national security. It is worth mentioning that keeping America open to positive, employment creating investment is in the interest of all Americans. Similarly, investments that pose a threat to our security must not be allowed to occur. Striking this balance will ensure that our economy continues to be competitive.

I look forward to hearing from our distinguished witnesses.

PREPARED STATEMENT OF THE HONORABLE JOE WILSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF SOUTH CAROLINA

Thank you, Chairman Berman, for holding this hearing on sovereign wealth funds (SWF).

We truly live in a global market where commerce and the exchange of large amounts of wealth and investment across borders has dramatically enhanced the economic dynamic the United States and other nations must prepare for. As someone who believes wholeheartedly in the tremendous positive power of a free market, I am supportive of this global trade. Investments between nations and between international companies break down barriers and build partnerships that can benefit the common good.

However, because it is speculated that the growth in SWFs may exceed as much as $12 trillion in a few short years, the United States has a strategic interest in ensuring SWFs and other foreign investment are built upon a foundation of greater transparency. Transparency benefits not only economic stability; it shines a greater light upon the strategic interests of a nation in regard to their SWFs and will better inform our economic and diplomatic approaches.

I look forward to the testimony from our witnesses today. I hope we can focus on determining how we balance our economic interests with a clear understanding of the strategic and political ramifications of this type of government investment. We can be cautious while not be isolationist.

Again, I wish to thank Chairman Berman and my fellow committee members for this opportunity.

PREPARED STATEMENT OF THE HONORABLE SHEILA JACKSON LEE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Thank you, Mr. Chairman, for convening today's important hearing. Both the number of sovereign wealth funds and the amount of money in them have ballooned over the past five years, and all indications suggest that these funds will play an important role in our collective financial future. I would like to welcome our distinguished panel of witnesses: Dr. Gerard Lyons, Chief Economist, Standard Chartered Bank; Dr. Edwin Truman, Senior Fellow, Peterson Institute for International Economics; and Dr. Gal Luft, Executive Director, Institute for the Analysis of Global Security. I look forward to your informative testimony.

As defined by the United States treasury, sovereign wealth funds, or SWFs, are government investment funds which are funded by foreign currency reserves but managed separately from official currency reserves. Foreign governments may invest these for profits, in practice often in foreign companies. In comparison to other ways countries hold money, SWFs typically seek riskier investments with a higher rate of return. In September 2007, the International Monetary Fund (IMF) estimated that sovereign wealth funds control as must as $3 trillion, and that this could jump to $12 trillion by 2012.

Sovereign wealth funds are positioned to be a major economic force in the future. According to estimates, they currently control double the assets of hedge funds worldwide; however, their holdings are dwarfed by the approximately $53 trillion managed by institutional investors, such as pension funds and endowments. Currently, the nations wielding the largest SWFs are the United Arab Emirates, Norway, Singapore, Kuwait, and China, with many experts predicting that the latter will soon move to the top of this list, on account of the nation's $1.3 trillion foreign exchange reserves. According to Dealogic, a financial data provider, sovereign

wealth funds invested $37.9 billion in U.S. financial institutions in 2007. This sum represents approximately 63% of their total activity.

As our witnesses today point out, the rise of sovereign wealth funds is indicative of larger economic trends in today's globalized world. International wealth is increasingly concentrated in developing nations, rather than the traditional industrialized financial giants, like the United States. And as Dr. Truman states in his written testimony, these newly wealthy nations are now part of an international financial system that they did not play a role in developing.

In theory, SWFs can invest in anything they want, and they do not generally disclose their investments to the public. In recent months, the governments of Singapore, Kuwait, and South Korea made headlines when, on January 15th, they provided most of the $21 billion extended to two banks hit hard by America's credit crisis: Citigroup and Merrill Lynch. This is not the first time this has happened: since last year's subprime-mortgage crisis, sovereign wealth funds have invested almost $70 billion in some of the world's largest investment banks.

While sometimes playing savior to Western banks, sovereign wealth funds have also given rise to a number of concerns in western nations, particularly surrounding transparency. The U.S. government and others have expressed major concern over SWFs' lack of disclosure of assets and trading activities, which could potentially be an attempt to conceal efforts to invest for political gain. Treasury Secretary Henry M. Paulson, Jr. has advocated the need for a code of "best practices" to encourage greater disclosure. While the International Monetary Fund has taken the lead in drawing up such a code, it remains to be seen whether investors and investees will agree.

Critics have questioned the motives of sovereign wealth funds, citing potential goals of stifling competition, protecting national business interests, or even engaging in geopolitical troublemaking. The managers of these funds are not accountable to regulators, shareholders, or voters.

According to some experts, the recent explosion of sovereign wealth funds demonstrates a fundamental shift in the reasons governments invest money. While governments traditionally sought to protect domestic currencies and banks from crisis through investment, SWFs are a consequence of the rapid growth in emerging market reserves, largely due to rising prices of oil and other strategic mineral commodities, and the accumulation of foreign reserves by several Asian economies.

Analysts have noted two major concerns about sovereign wealth funds. First, a distinct lack of transparency among SWFs, which has implications for the entire international economy; and second, the potential use of SWF capital by foreign nations for strategic and political purposes. With regards to the first concern, there are currently no supra-national regulations or disclosure requirements for SWFs, so they do not have to divulge their size, investment strategies, or holdings. They are not accountable to stockholders. This lack of accountability and transparency is of significant concern to policymakers, who note that the failure of sizeable SWFs could affect national or global markets.

Other analysts have noted that the investment decisions of SWFs may be motivated by non-commercial considerations. Citigroup, for one, notes that "some sovereign wealth funds invest purely to achieve financial returns and portfolio diversification while others have a broader economic or social agenda." Concerns have been raised about the use of SWFs to access other countries' natural resource industries or other politically sensitive sectors.

Mr. Chairman, Sovereign Wealth Funds are an increasingly prevalent component of the international financial picture. I thank you for calling this timely and important hearing, and I look forward to hearing the testimony of our panel of witnesses.

Thank you, Mr. Chairman. I yield back the balance of my time.

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