

White Whale or Red Herring? – Assessing Sovereign Wealth Funds

Glasshouse Forum

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Glasshouse Forum's Executive Summary

The world became fully aware of sovereign wealth funds when they helped to stabilize the American bank crisis. Many of these state funds represent authoritarian regimes.

Glasshouse Forum asked Professor Daniel W. Drezner at Tufts University to write a report examining the performance of sovereign wealth funds to date, and to place them in relation to the issue in the project "The return of the capitalist-authoritarian great powers". If the hypothesis of the return of the authoritarian great powers is correct, will sovereign wealth funds be playing a part in this development?

In his report "White Whale or Red Herring? – Assessing Sovereign Wealth Funds" Drezner establishes that the apprehensions about sovereign wealth funds have so far proved to be unfounded. As regards corporate governance and market uncertainty, it is difficult to prove significant negative effects from these funds. Attempts to use them for political pressure are impeded by the fact that the dependence between them and Japan, the USA and the EU is mutual. These great economies can to a considerable extent dictate the rules for sovereign wealth funds.

Drezner distinguishes the following possible risks from sovereign wealth funds in the future. They can amplify protectionist tendencies in the OECD countries. A general distrust of foreign investors is intensified by the fact that here it is a question of foreign governments. What is more, they can create problems either by failing disastrously or by being hugely successful. As counterparty surveillance of them is imperfect in authoritarian states, they can commit major errors as regards riskier investments.

Successful sovereign wealth funds can on the other hand contribute to the stability and attraction of authoritarian regimes. They can act as buffers vis-à-vis the vicissitudes of the market economy, mitigate crises and challenge the view that the market is the best allocation of resources. In this way, they can strengthen the position of the authoritarian states as an alternative to the liberal capitalist model.