



Sovereign Wealth Funds and Infrastructure: A Perspective for Latin America

Seminar on Infrastructure Financing in Latin America
CAF-IFC-OECD

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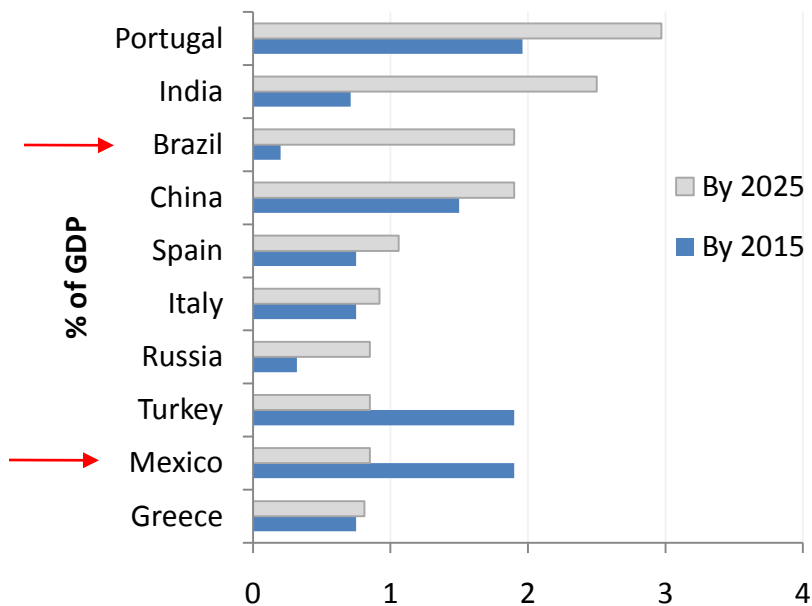
■ 14 May 2010 – Bogotá ■



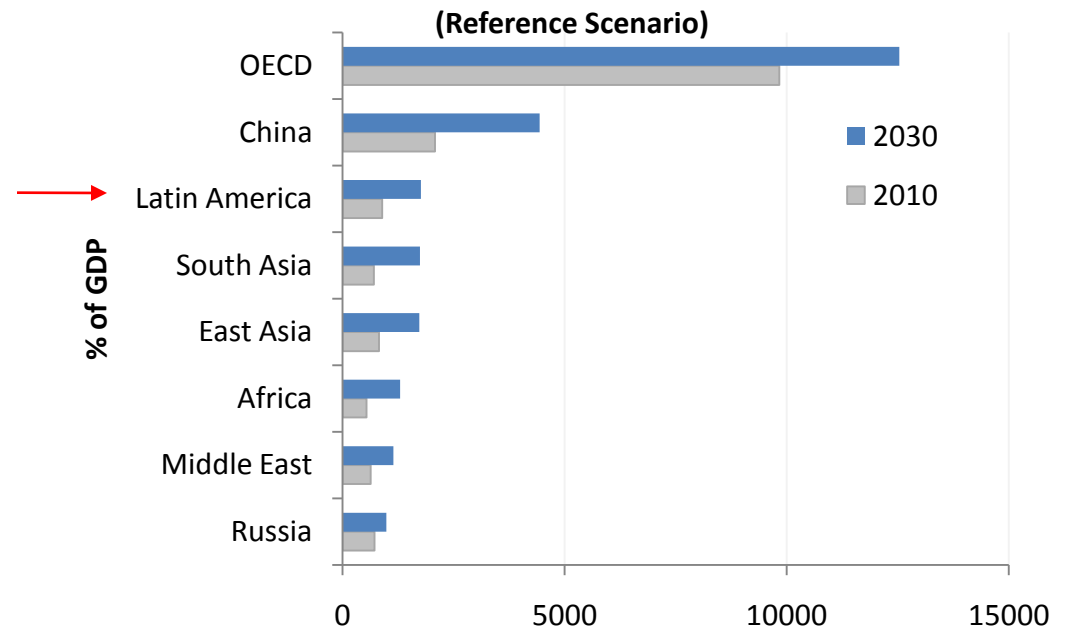
- 1 **Latin America's Infrastructure needs in the long run**
- 2 Sovereign Wealth Funds: New Investment Drivers
- 3 Looking and Emerging Economies: Infrastructure and Commodities

Infrastructure investment in Latin America : long-term prospects for 2030

Projected expenditure on water infrastructure



Final Electricity consumption by region (TWh)

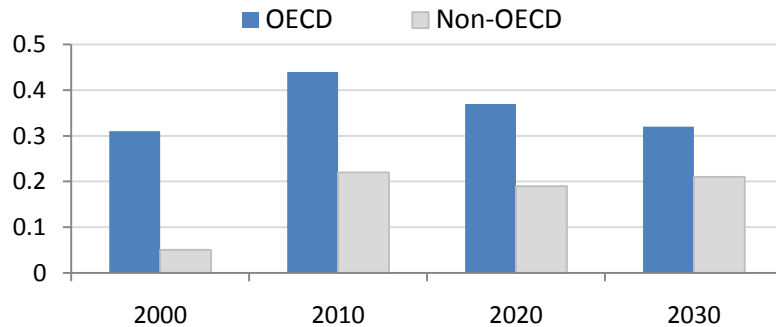


Source: Infrastructure in 2030. Telecom, land, transport and electricity. OECD 2007.

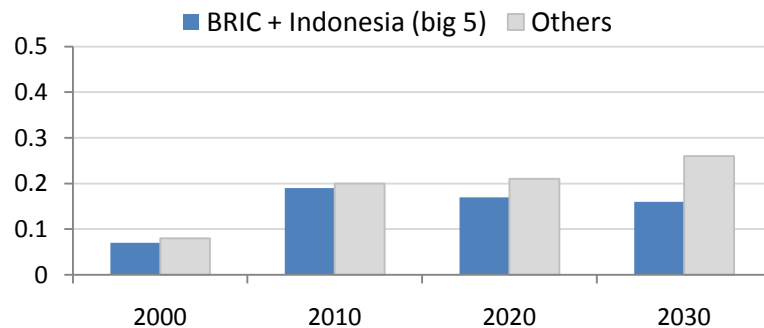
Infrastructure requirements in the long run: Similar needs in EM and OECD

Road new construction requirements

Highly Industrialised Countries

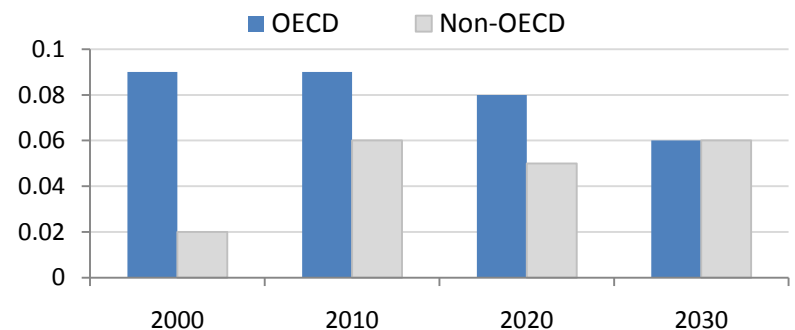


Developing and Emerging Countries

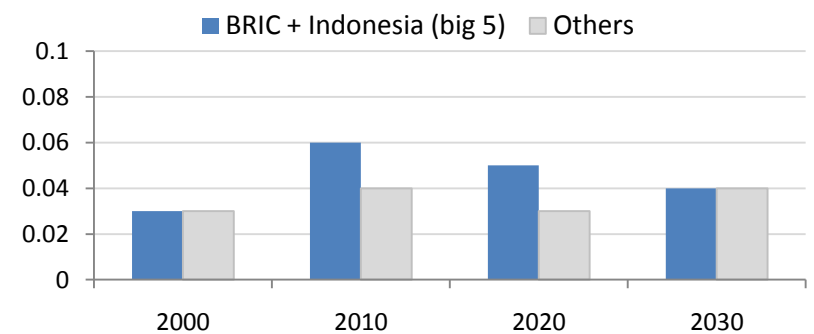


Rail new construction requirements

Highly Industrialised Countries



Developing and Emerging Countries

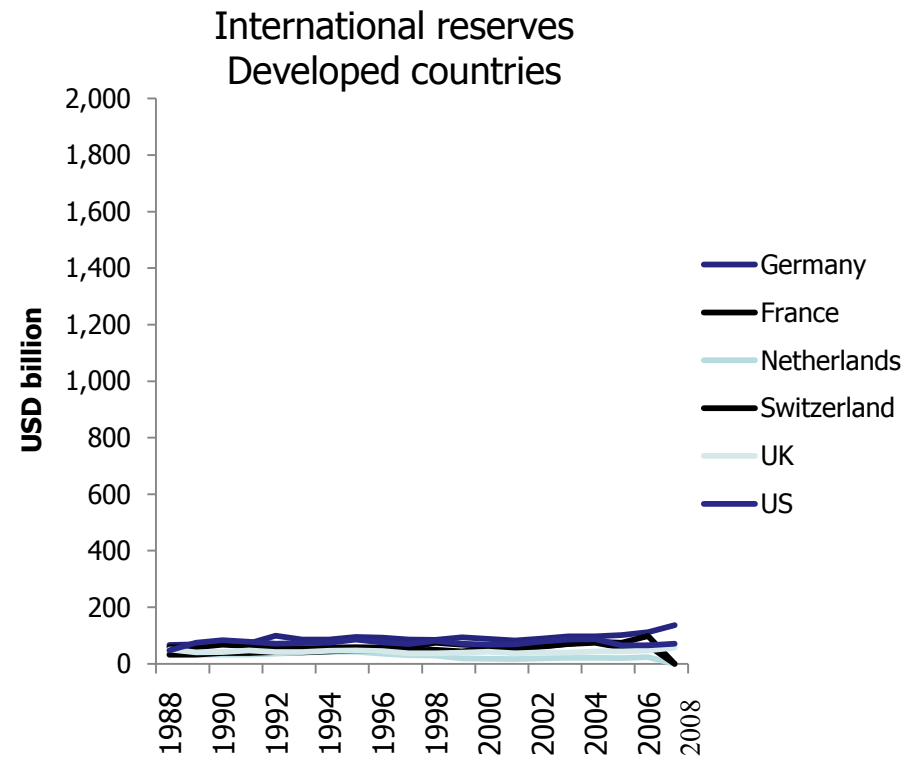
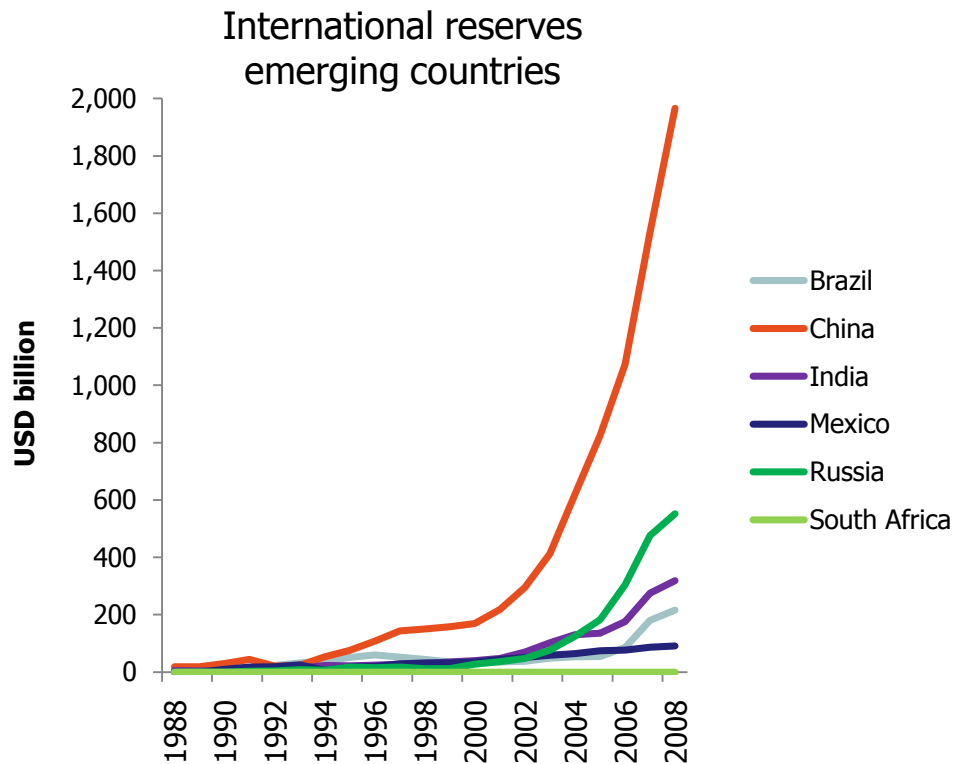


Source: Infrastructure in 2030. Telecom, land, transport and electricity. OECD 2007.



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Emerging economies accumulated foreign reserves in the last decade



Source: OECD Development Centre, based on Economist Intelligence Unit. 2010.

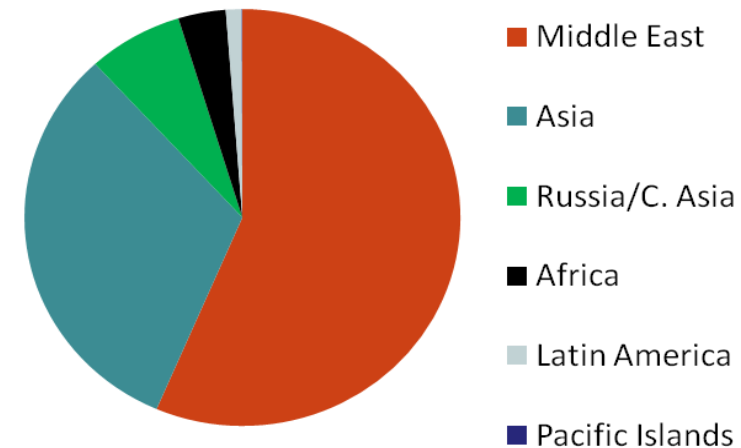
Where are the Sovereign Wealth Funds?

Sovereign Wealth Funds (SWFs) - 2009

	Number	Total assets (USD bn)
Middle East	7	1533
Asia	9	867
OECD	10	489
Russia & Central Asia	4	177
Africa	7	109
Latin America	4	23
Pacific islands	6	1.2
Total	47	3,194

Source: OECD Development Centre, estimation based on Dealogic, Deutsche Bank, and SWF Institute.

SWFs by asset size

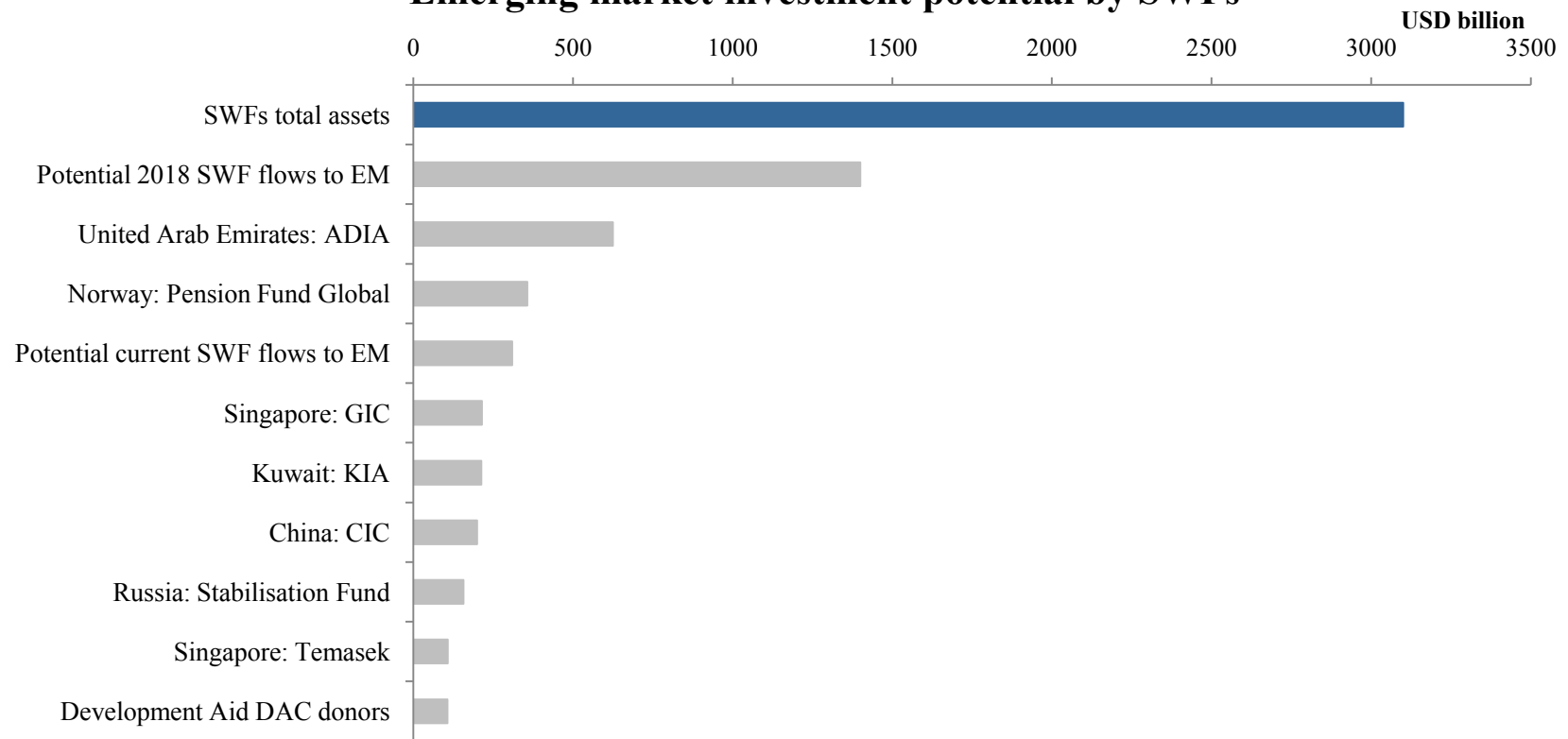


SWFs: "Special-purpose investment funds or arrangements owned by the general government, with the mandate to hold, manage, or administer assets to achieve financial objectives", GAPP 2008.



SWFs: A potential to reach USD 1.4 trillion to emerging markets over the coming decade

Emerging market investment potential by SWFs



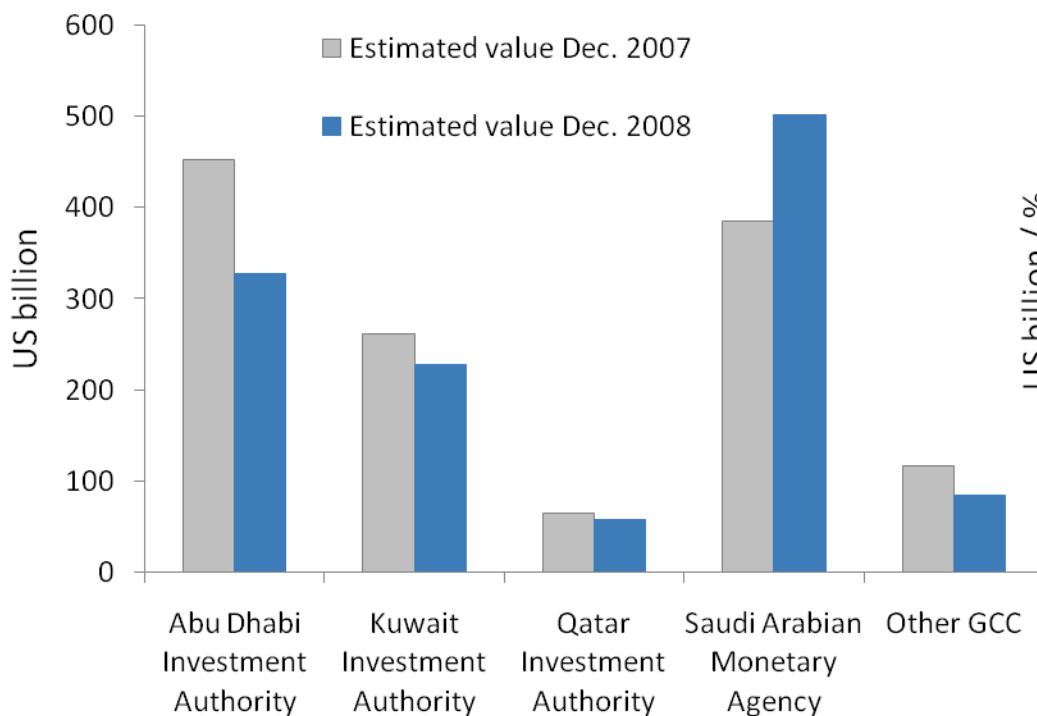
Source: Country reports, Deutsche Bank, and SWF Institute, 2009.



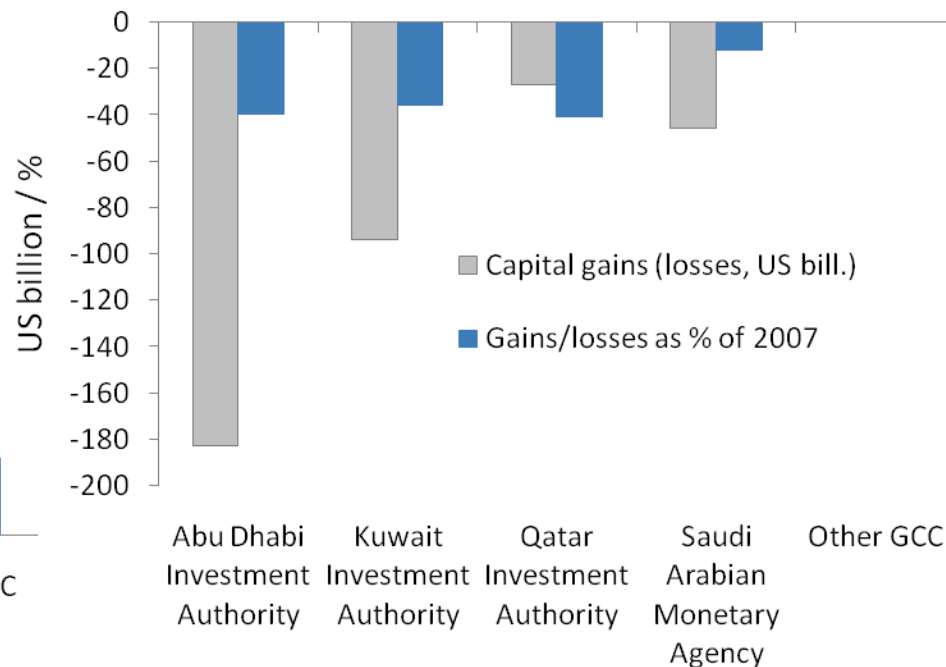
SWF after the crisis

GCC funds in 2009 and the Reversal of fortune

Fall in Value for GCC funds



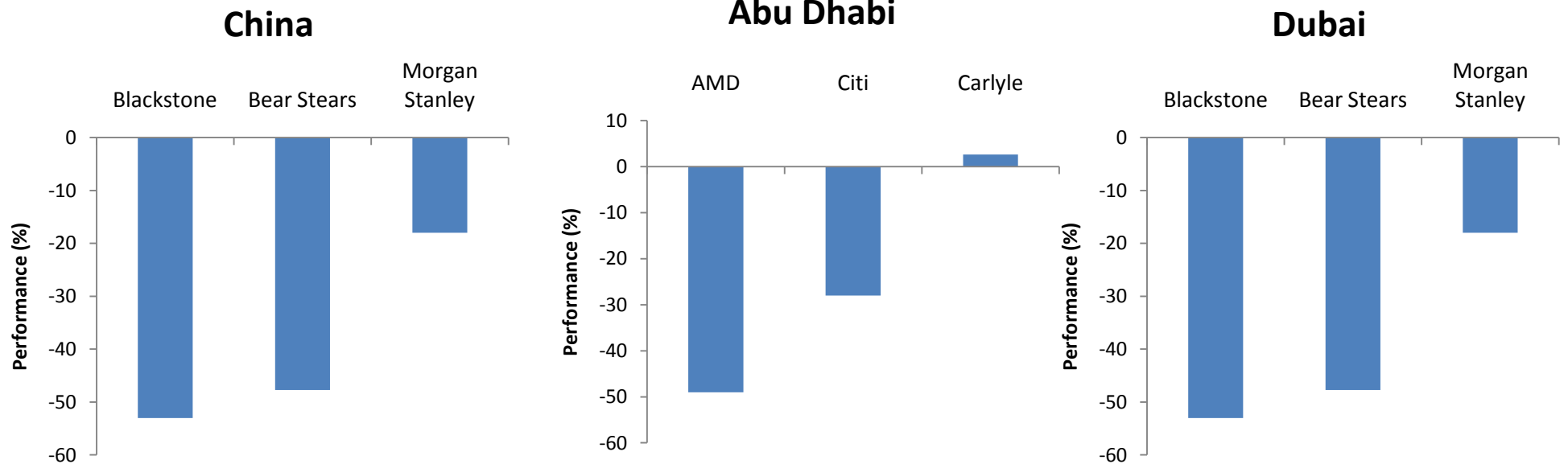
Losses as share of 2008



Source: OECD Development Centre, 2009. Based on Setser and Ziemba "GCC Sovereign Funds: Reversal of Fortune". WP Council for Foreign Relations, 2009.

Large stakes in the “developed” financial sector: A good strategy?

Performance of Notable Sovereign Funds Investments



Source: Financial Times, March 2009.



Moving forward in the Regulatory agenda

OCDE Guidelines

1. Recipient countries should not erect protectionist barriers to foreign investment.
2. Recipient countries **should not discriminate** among investors in like circumstances. Only legitimate national security concerns.
3. Where national security concerns do arise, investment safeguards should be:
 - Transparent and predictable,
 - Proportional to clearly-identified national security risks, and
 - Subject to accountability in their application.

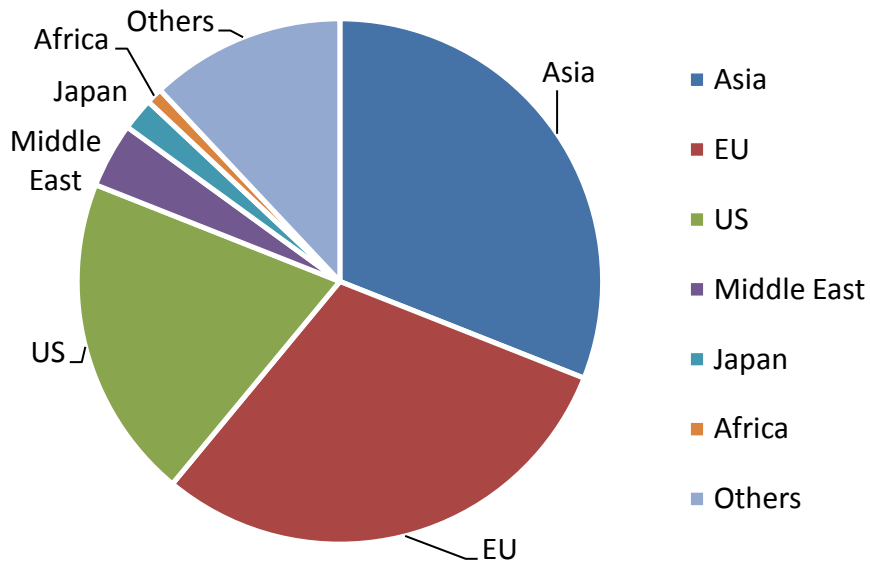
Santiago Guidelines

- 1. Legal framework:** ensuring recipient regulatory requirements.
- 2. Appropriate governance:** transparent and sound governance structures for adequate operational controls.
- 3. Accountability:** public disclosures in a variety of areas, although mindful of SWFs' competitive position
- 4. Prudent investment practices:** invest only on the basis of economic and risk and return, contribute to stable financial markets.



SWF regional allocations: room for future investment

SWF investments by region



- Asia and EU remain preferred targets for SWF investments.
- An interest to diversify from dominating currencies (EUR, JPY)
- Asian investment reflects long-term growth potential
- Latin America lags behind other emerging regions

Note: Covers public transactions for the period 1995-2009

Source: Dealogic.

Sovereign Wealth Funds and Infrastructure investment potential (i)

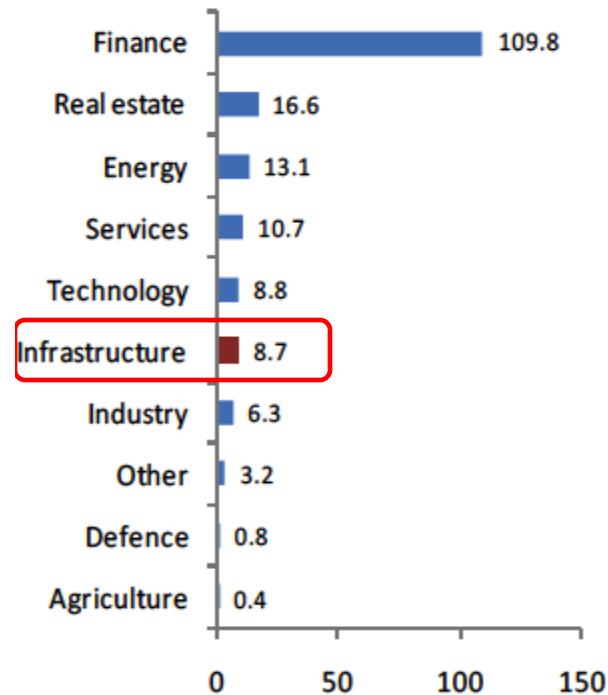
Investment perspective for SWFs:

- Freedom in asset choice
- Diversify resource allocation
- Longer-term investment horizon
- Higher return perspective

Infrastructure investment

- A “safe” investment
- Countercyclical tool for governments

Sovereign Wealth Funds investments by sector
Estimation 1995-2008



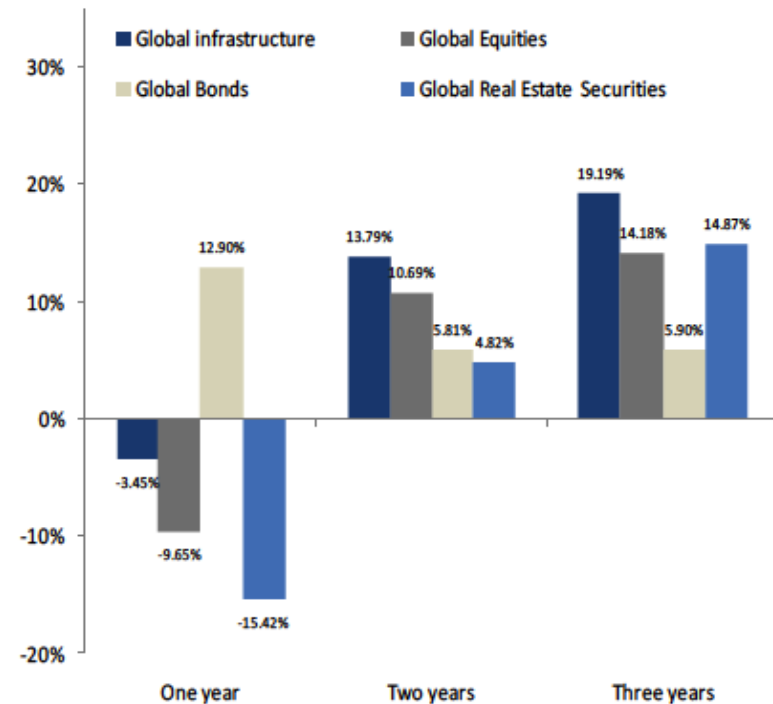
Source: Factset. Thomson financial and Dealogic, 2009.

Infrastructure investment potential (ii)

Attracting SWFs to Infrastructure:

- Potentially high historical returns
- Low correlation with other asset classes
- Revenues implicitly linked to inflation
- Stability of cash flows
- Monopolistic or quasi-monopolistic activities

Historical Return by Asset Class



Source: Brookfield Redding/ Dow Jones, 2009.

Looking at the data: SWFs and other Institutional investors

- Using data on equity holdings for a set of SWFs, we compare their investments to private mutual funds (index and actively managed).
- Source: FactSet and Thomson Financial on portfolio holdings of institutional and private funds. Mandatory filings with national regulatory agencies (e.g. 13 filings with SEC, share register with UK), annual reports and primary sources.
- SWFs: 22 funds – 14.000 holdings
- Mutual funds: 25 largest US funds – 11.600 holdings
- Period studied: 2006-2009

An investment benchmark for SWFs?

Example of disclosed Benchmarks for selected Sovereign Wealth Funds

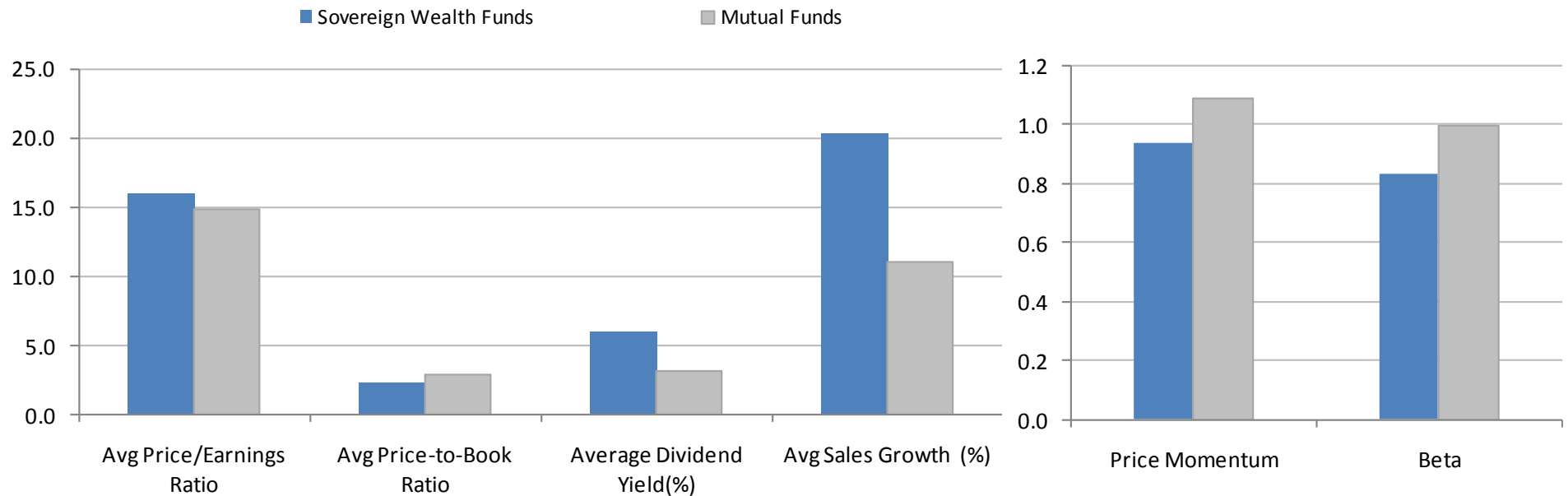
Sovereign Wealth Fund	Equities	Fixed income
China Investment Corporation	Return net-of-fees 300 bps above MSCI All country Index for global equities 200 bps above EAFE 300 bps above MSCI EM Asia ex-Japan, benchmark to be suggested by manager seek in the mandate.	150 bps above the JP Morgan EMBI Global
Kuwait	Outperform MSCI Global Index	
Norway	FTSE large and mid-cap equity indices for the countries where it invests.	
Saudi Arabia	S&P 500, MSCI (Europe and Global), TSE (Japan)	JPM Global Bond Index, 3-month Libor (cash/deposits)
Korea	MSCI world equity.	Lehman global bond index (now Barclays)
GIC Singapore	MSCI World equity	Lehman global bond indices.
Kazakhstan	MSCI World Equity	Merrill Lynch 6-month T-bill index, Salomon World Government Bond Index
Alaska	S&P 500, Russell 1000, Russell 2000, MSCI EAFE, EM	
Alberta	Standard & Poor's/ TSX Composite Index (Canada), Standard & Poor's 1500 Index (US), MSCI EAFE	Scotia Capital Universe Bond Index

- Overall portfolio benchmarks (index or total return)
- Separate benchmarks for each asset class
- Most benchmarks based on market indices are customised.

Note: Benchmarks for 2008-2009
Source: Ziembra, 2009.

SWFs' Portfolio Characteristics: Not radically different from other investors

Average Portfolio Characteristics for SWFs and Mutual Funds



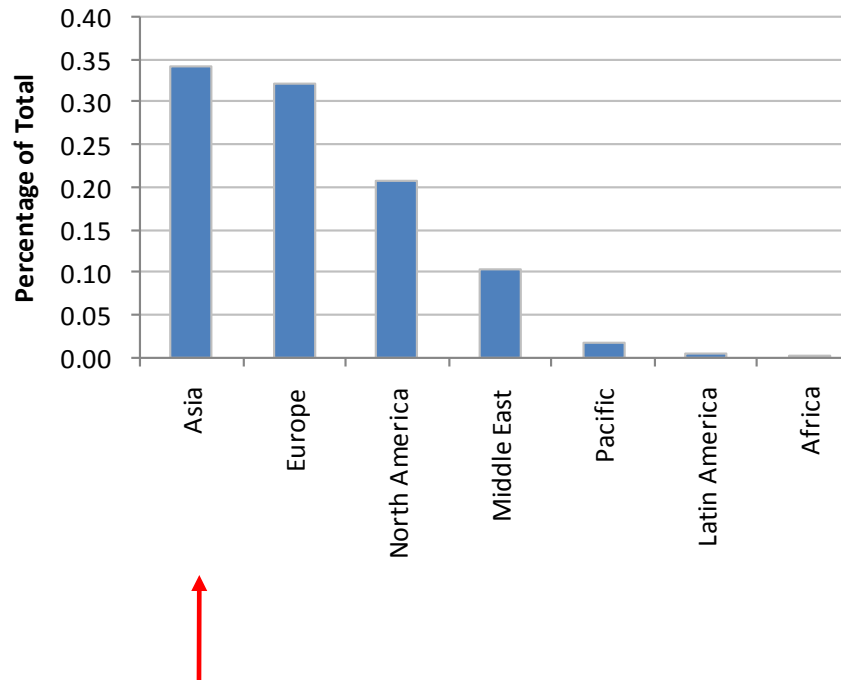
Sources: Avendano and Santiso (2009), based on FactSet and Thomson Financial, 2009.



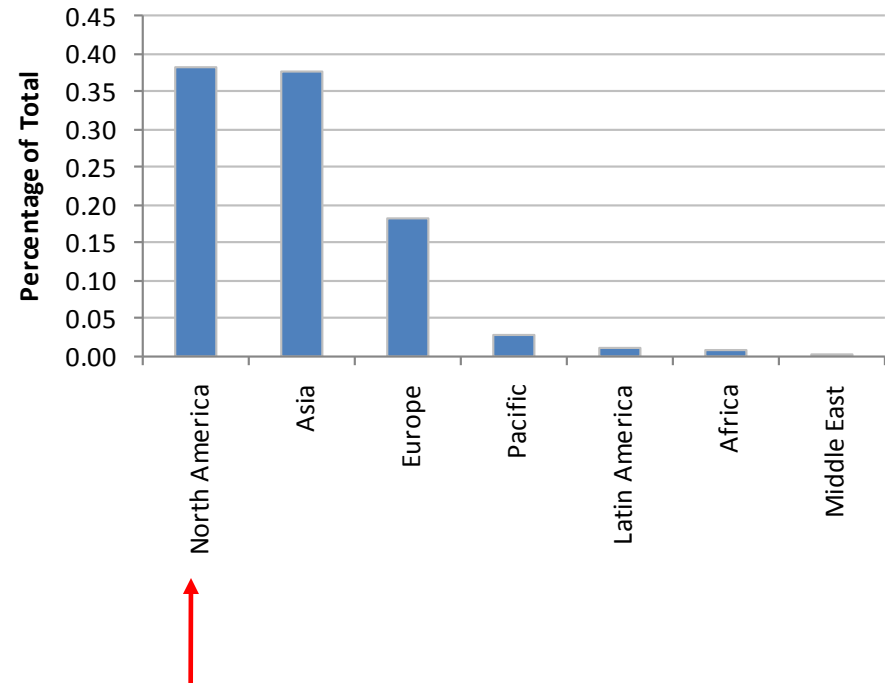
Regional destinations: Asia and US targets

Distribution of Fund Holdings – Regions

SWFs



Mutual Funds

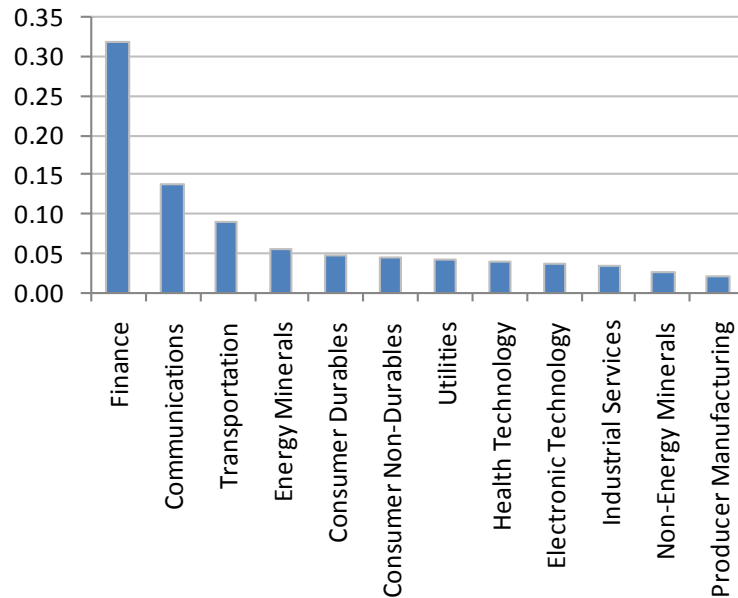


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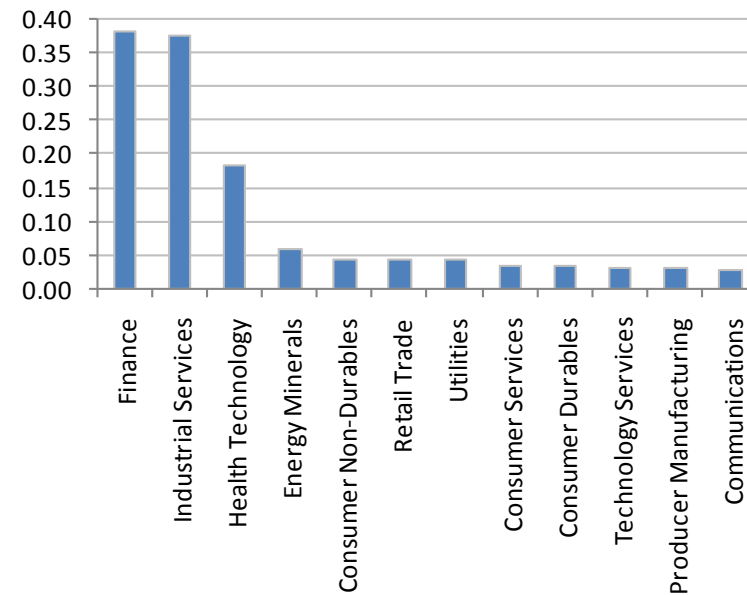
Sector distribution: critical sectors are different across groups

Distribution of Fund Holdings – Sectors

SWFs



Mutual Funds

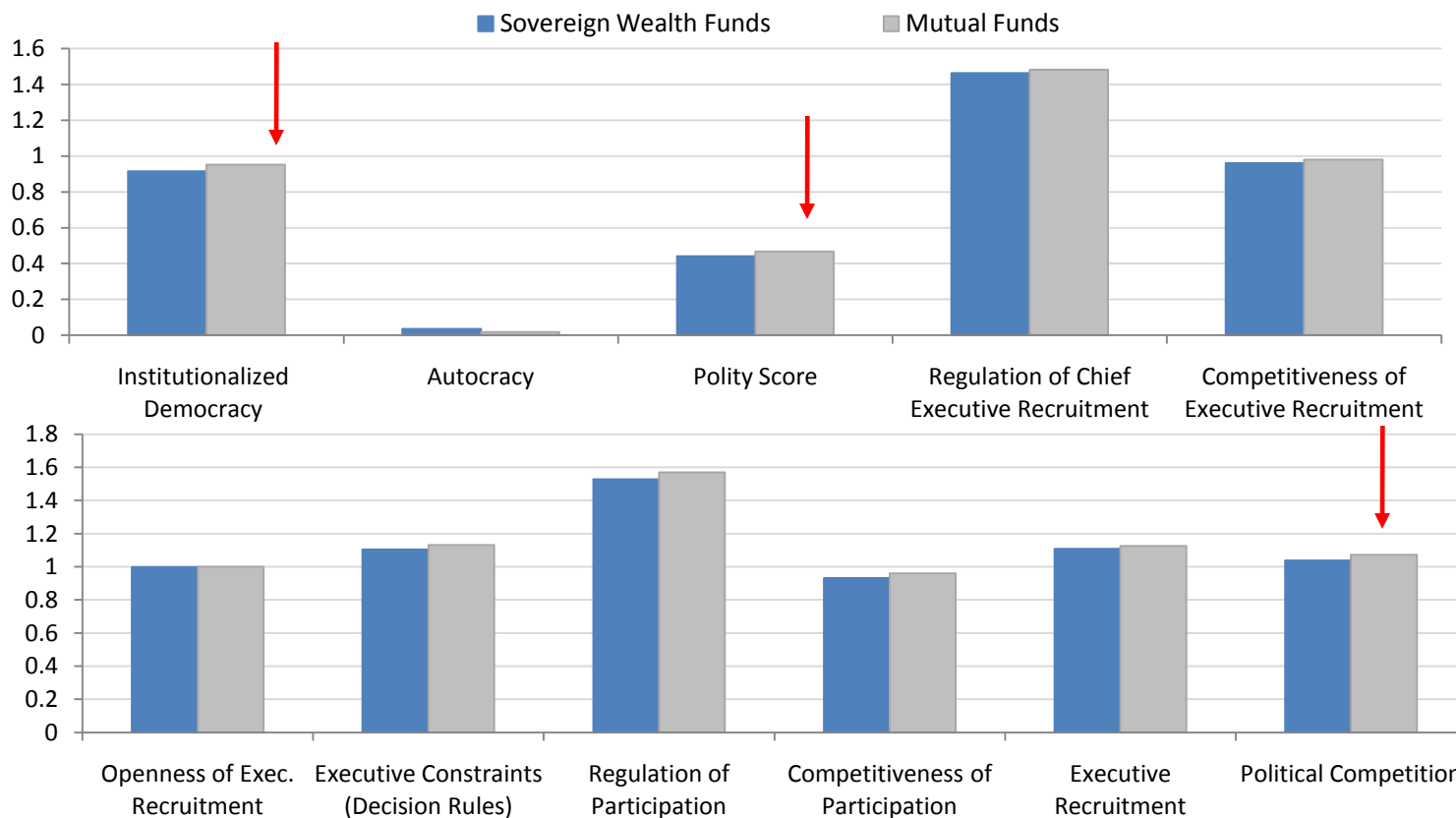


Sources: Avendano and Santiso (2009), based on FactSet and Thomson Financial, 2009.



Political regimes in recipient countries: SWFs and mutual funds act alike

Political regimes and governance in (investment) recipient countries: SWFs vs. Mutual funds



Note: Scores weighted by holding amounts.

Sources: Avendano and Santiso (2009), based on FactSet, Thomson Financial, and Polity IV Project, 2009.

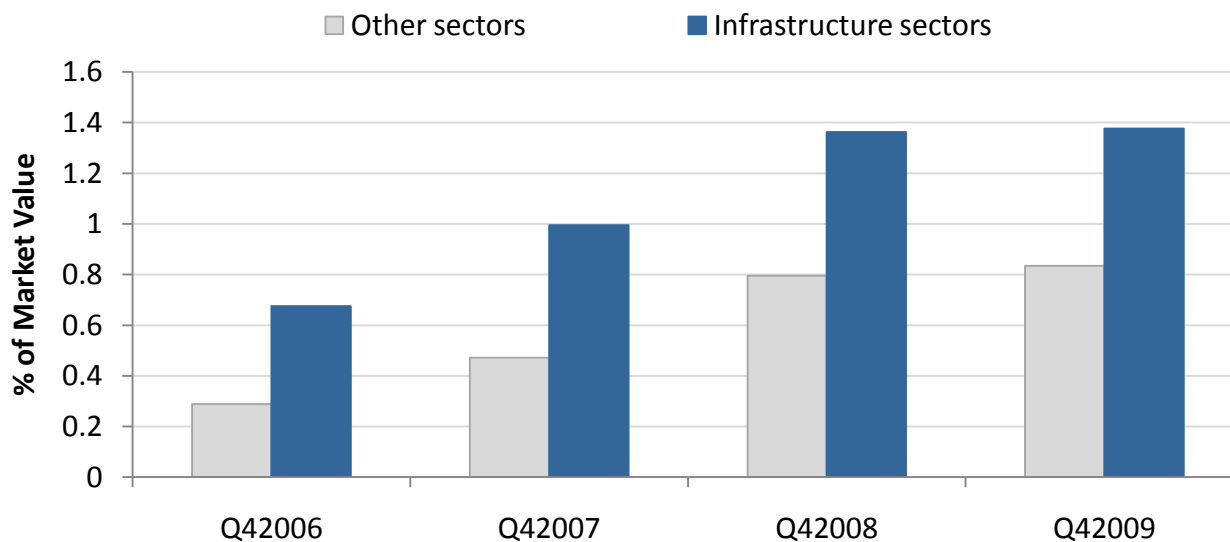


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Sovereign Wealth Funds: Public investment in Infrastructure

Average SWF investment in Infrastructure Firms Share of Market Value



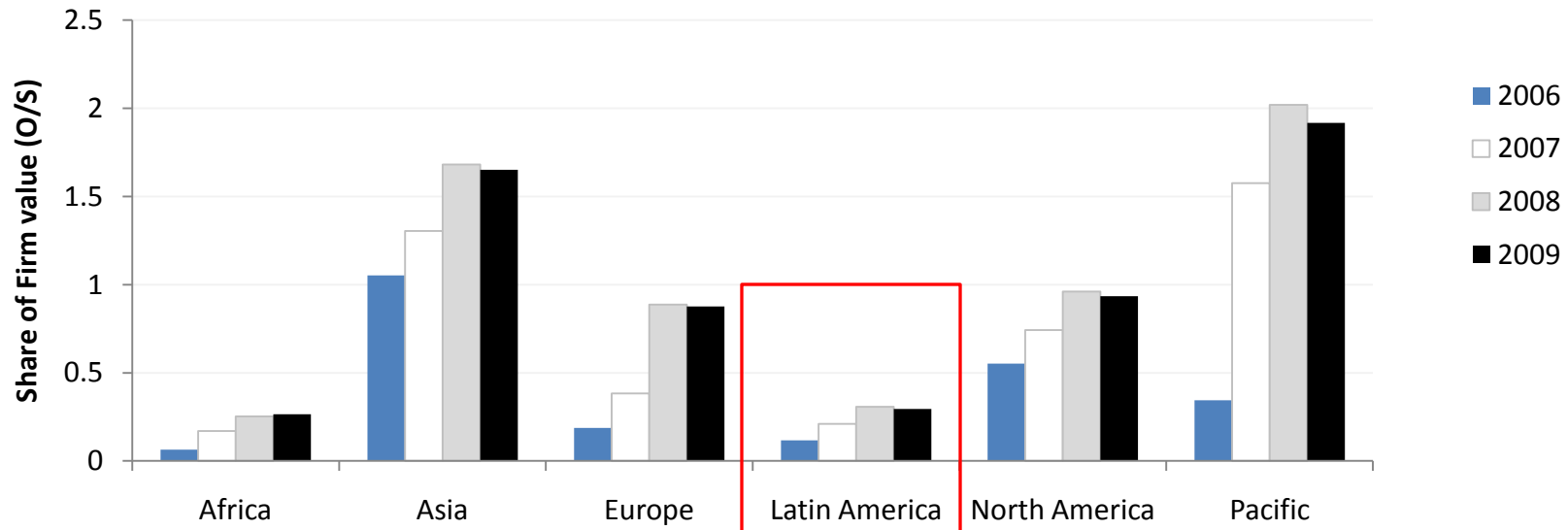
Note: Data comprises SWF public equity investments.

Source: Avendano and Santiso (2010), based on Thomson Financial and Lionshares.



SWF Investments in infrastructure: Regional differences

SWF equity investments in infrastructure Share of Market Value



Note: Data comprises SWF public equity investments.

Source: Avendano and Santiso (2010), based on Thomson Financial and Lionshares.

SWFs and Commodities: A new Investment space

SWF investments - 2009: Commodities Sector Deals - Example

•China Investment Corporation:

Kazakhstan – Astana (gas)

Indonesia – PT Bumi (coal)

Russia – Noble Oil (oil supplier)

Mongolia – Iron Mining Int. (mining)

Canada – Teck Resources (mining)

•Temasek Singapore :

Olam international (agriculture)

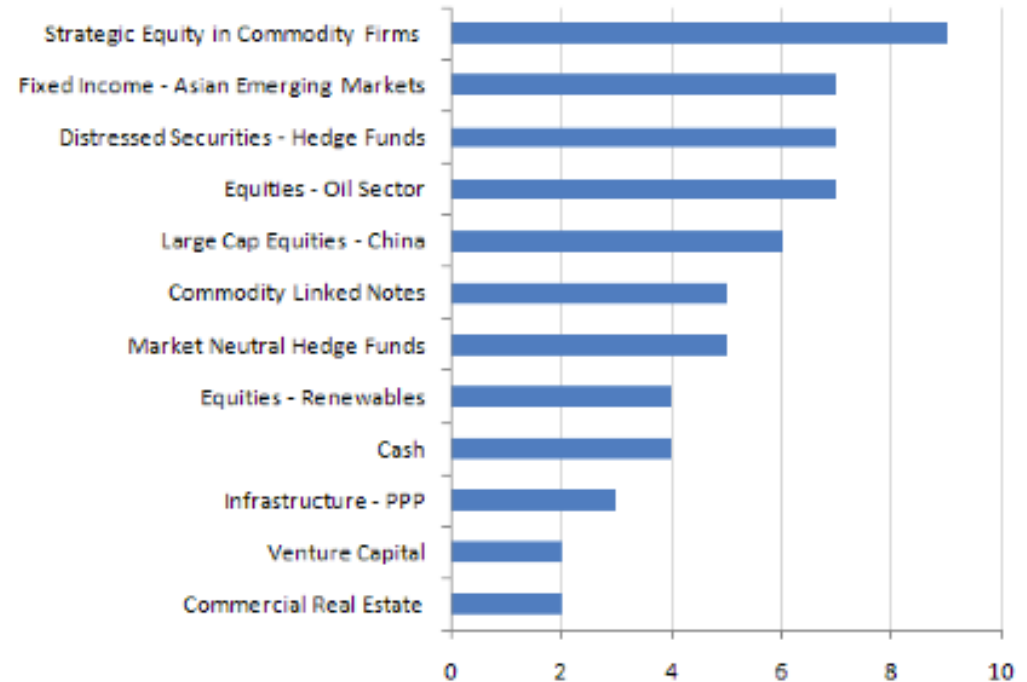
•Joint investments:

1Malaysia Development (Malaysia) – PetroSaudi

(S. Arabia)

Islamic Development Bank – Qatar Investment Authority

Estimated SWF Demand for assets – Q4 2009



Source: SWF Institute, based on annual reports.



SWFs in Latin America: Brazil is dominant in Infrastructure sectors

Sector	Firm	Country	% O/S
Communications	Brasil Telecom Participacoes Sa Ord	Brazil	0.387
	Brasil Telecom Sa Ord	Brazil	0.083
	Gvt Holding Sa Ord	Brazil	0.021
	Tele Norte Leste Part Ord	Brazil	1.006
	Telemar Norte Leste Sa Ord	Brazil	0.153
Electronic Technology	Embraer (Emp Brasil Aero) Ord	Brazil	0.021
Energy Minerals	Petrobras Energia Sa Adr B	Argentina	0
	Ultrapar Participacoes Sa Pfd	Brazil	0
Non-Energy Minerals	Cia Siderurgica Nacional (Csn) Ord	Brazil	0.33
	Confab Industrial Sa Pfd	Brazil	0
	Metalurgica Gerdau Sa Ord	Brazil	0.994
	Mmx Mineracao E Metalicos Ord	Brazil	0.197
	Usiminas (Minas Gerais) Pfd A	Brazil	0
	Vale Sa Adr	Brazil	0
	Cia Acero Del Pacifico (Cap Sa) Ord	Chile	0.404
	Cia De Minas Buenaventura Ord	Peru	0.321
	Sociedad Minera Cerro Verde Ord	Peru	0.017
	Southern Copper Corp Com	Peru	0.124
Volcan Compania Minera Sa Ord A	Peru	0.063	

Sector	Firm	Country	% O/S
Transportation	Mercadolibre Inc Com	Argentina	0.773
	Totvs Sa Ord	Brazil	0.399
	Empresas La Polar Sa Ord	Chile	1.073
	All America Latina Log Ord	Brazil	0.03
	Cia De Concessoes Rodoviaras Or	Brazil	0.356
	Gol Linhas Aereas Intel Pfd	Brazil	0.193
	Llx Logistica Sa Ord	Brazil	0.083
	Santos Brasil Part Sa Unit 4Pfd/Or	Brazil	0
	Cia Sudamericana De Vapores Ord	Chile	0.153
	Lan Airlines Sa Ord	Chile	0.215
	Aes Tiete Sa Ord	Brazil	0.588
Utilities	Cia Paranaense Ener/Copel Ord Pfi	Brazil	0
	Cia Saneamento Minas Gerais Ord	Brazil	0.235
	Cia Transmissao Energia Paulista P	Brazil	0
	Cpfl Energia Sa Ord	Brazil	0.004
	Eletrobras Ord Pfd B	Brazil	0
	Eletropaulo Metropolitana Ord	Brazil	0
	Energetica Sao Paulo (Cesp) Ord	Brazil	1.262
	Energias Do Brasil Sa Ord	Brazil	0.17
	Light Sa Ord	Brazil	0.276
	Mpx Energia Sa Ord	Brazil	0.118
	Sabesp (Saneamento Basico) Ord	Brazil	0.795
	Tractebel Energia Sa Ord	Brazil	0.261
	Transmissora Alianca (Terna) Ord	Brazil	0
	Colbun Sa Ord	Chile	0.233
Endesa (Empresa Nac Elec) Ord	Chile	0.258	
Enersis Sa Ord	Chile	0.245	

SWF investments: firm determinants and natural endowments

SWF investments – Three dimensions

- Source: Commodity/non-commodity
- Peer effect: OECD/ non-OECD
- Foreign vs domestic investments

SWF investments - Firm factors

- Size
- Liquidity (turnover)
- Cross listed
- Cash Holdings
- Foreign Sales
- R&D

Gravity Model: Natural endowments

- Fuel exports (%) merchandise exports
- Agricultural raw material exports
- Arable land (% of land area)
- Forest area (%)
- Energy imports net (% of energy use)

SWF investments: firm determinants and natural endowments

- Non-commodity funds favour firms with more foreign activity and higher turnover, in contrast to commodity-funds.
- OECD-based funds privilege firms with lower leverage levels, whereas non-OECD funds have a preference for profitable (i.e. high ROE) and international (i.e. high foreign sales) firms.
- SWF foreign investments are oriented towards large and highly leveraged firms, in contrast with their domestic (and low leveraged) investments.
- Specific sectors, such as R&D, tend to attract foreign investments.
- Natural endowments explain large shifts towards commodity-related sectors.



SWF participation in infrastructure: Different needs, different schemes

Concessional loans

- China Exim bank

Equity Development Fund

- China-Africa Development Fund

Partnership with financial entity

- Abu Dhabi Investment Authority and UBS

Direct investment

- Libya Investment authority

Regional Network

- Arab Fund for Economic and Social Development



Concluding remarks

- Differences in geographic/sector allocation between SWFs and other institutional investors (mutual funds) are modest.
- The political regime. No differentiation for (investment) recipient countries
- Santiago and OECD Guidelines: More transparent and diversified investments. Double standards to regulate should be avoided
- The determinants of SWF investments: firm characteristics and natural endowments. Large heterogeneity across fund types and targeted sectors



Concluding remarks

- Financial crisis in 2008 allowed SWFs to re-consider their mandates and re-direct their investments: “Flight to Quality” vs “Frontier Markets”
- Traditional arguments to attract investment in infrastructure remain valid for SWFs:
 - Long term horizon
 - High returns
 - Diversified asset class
- SWF investments in Latin America’s infrastructure are modest, compared to other regions. Between 2006-2009, the trend is increasing.
- SWFs, as other investors, want to reduce PPP-related risks



Gracias

www.oecd.org/dev