

# Pounding the pound

## The role of sovereign wealth funds

Going abroad has become expensive for British people. Even the British Prime Minister could not afford it. He had to make do with a holiday in Britain. The decline in sterling, which began a few months ago, has become a rout. It has lost a sixth of its value against Euro. Against the US dollar, it has lost 13 per cent of its value. Thanks to a downbeat medium-term assessment from Alistair Darling, chancellor of the exchequer, fortunes of UK home owners have tumbled not only due to the fall of 12% in house prices but in addition a sudden fall of almost 13% in exchange rate.

A feeble package to reflate the housing market as recently announced will only further reduce confidence in the pound. Its slide and the slide of the housing market is inevitable. Both had been overvalued for a long while. UK has been living a life of luxury on others' money as the financial hub of the world. UK public must now contend with rising import costs. All else being equal, the weakness of sterling means the Bank of England will need tighter monetary policy than would otherwise be necessary to bring inflation back down to the target of 2 per cent from its August level of 4.4 per cent.

There is however good news elsewhere. The spotlight is back on sovereign wealth funds. While Qataris have bought into Barclays, Abu Dhabi is investing in an English Premier Football club. The emirate has set out plans to become one of the world's largest film producers, with \$1bn to invest in productions to be made in Hollywood, Bollywood and beyond.

Further good news is that the SWFs have come up with a voluntary code of conduct supported by countries as diverse as China, East Timor, Libya, Norway, Russia, the US and the United Arab Emirates. This is a step in the right direction and a new hope to a dematerialised growth that I talked about in the last issue of this journal. Thanks to high commodity prices and global imbalances, sovereign wealth funds now control at least \$2,000bn in assets. It is widely accepted that the scale of their activities is far too important to ignore. One is acutely reminded of the resistance to investments by Gazprom in the UK and by CIC (China Investment Corporation), China's sovereign wealth fund. Last year Gao Xiqing, the president of China Investment Corporation, frustrated at the opposition to its investment in US said "Fortunately there are more than 200 countries in the world. And fortunately there are many countries who are happy with us."

This does not mean we dilute our principled approach to investments. Faced with one of the worst financial crunches in history we simply need to be more realist. The purchase of a soccer club hardly compromises national security. Like US we are reaching an uneasy relationship with our creditors. Time has come to review the contribution SWFs to help UK and the world get out of the financial crisis. Of course we cant make the same mistake as we did with hedge funds. We have to ensure a measure of transparency and make them accountable.

Effective Mobilisation of Sovereign Wealth Funds should go to the top of global agenda. It will be beneficial to all parties including the emerging countries who are all dressed up with bagful of dollars but no strategies where to go. This is one area that should occupy the world nations next only to climate change. The Santiago meet heightened attention to the growing role of these state-owned funds in the global financial system.

The world recognises the stability that SWFs investments in UBS, Merrill Lynch and Citigroup have provided to the world financial system. Funds from Singapore and Abu Dhabi have helped to keep US financial markets afloat during the credit squeeze. The decisions, at the conclusion of the two-day Santiago summit on a voluntary code of conduct that followed months of discussions supported by the International Monetary Fund could not have come at a better time.

The code of conduct agreed in Santiago, covers a set of 24 principles. All sides agree that the SWFs are long term and are diversely invested. The concern is only when they try to take controlling stakes in strategic companies. The voluntary code provides a benchmark for market participants to judge. It will go a long way towards increasing transparency in the governance structure and investment strategies of SWFs thereby fuelling growth and true internationalisation of the shrinking world economy.