THE BROOKINGS INSTITUTION

REBUILDING AMERICA:
THE ROLE OF FOREIGN CAPITAL, SOVEREIGN WEALTH FUNDS AND GLOBAL PUBLIC INVESTORS

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P R O C E E D I N G S

MR. WEST: Good morning. I'm Darrell West, vice president of Governance Studies at The Brookings Institution, and I'd like to welcome you to our forum entitled "Rebuilding America: The Role of Foreign Capital and Global Public Investors."

Foreign investors link to the public sector, and various countries control trillions of dollars in financial assets. Sovereign wealth funds have an estimated $4 trillion under management while other entities, such as foreign pension funds, state-owned enterprises, and government currency reserve funds, have substantial holdings as well. These entities we call global public investors represent major sources of foreign capital, yet many American policymakers, political leaders, and members of the general public in the United States have only a partial understanding of how these foreign funds and foreign investors operate. What are their investing practices? What motivates them? And what are their political and regulatory implications?

To look at these issues, we launched a project at Brookings two years ago to understand how global public investors define their objectives. We interviewed senior investment professionals from sovereign wealth funds and other global public investors; we talked to public policy researchers who track the activities of these investors; we held off-the-record conversations with former senior U.S. government officials; and we analyzed data, academic reports, and articles about foreign investors.

Today we're releasing a paper on "Rebuilding America: The Role of Foreign Capital and Global Public Investors," and it presents the results of our research and makes recommendations for moving forward. If you have not yet gotten a copy, there are copies available out in the hallway and you can pick one up afterward.

In general, we argue that the United States needs to improve its climate for foreign direct investment, and we need to improve our understanding of foreign capital. America obviously faces many budgetary and financial challenges. We have a $1.5 trillion federal budget deficit and 13.5 trillion in long-term debt. In this fiscal situation, foreign capital can play a constructive role. We understand that there is sensitivity in certain sectors, such as the military and defense industries as well as selective natural resource areas. But we believe that there are certain areas, especially infrastructure and clean technology, that represent sectors where both U.S. and foreign investors could benefit. So, we'll talk a little bit more about those particular ideas in a minute.

To help us understand these issues related to foreign investment, we have brought together a set of distinguished speakers. Rick Kimball is managing director of Goldman Sachs. Vij Ramachandran is a senior fellow at the Center for Global Development. Daniel Zwirn is managing member of Zwirn Family Interests. Gordon Goldstein is senior vice president of Silver Lake. And Martin Baily is a senior fellow in Economic Studies at Brookings and holder of the Bernard Schwartz Chair in Economic Policy Development.

I want to note that each person is representing his or her own point of view and not the institutions which with he or she is affiliated.

Our format for this discussion this morning is going to be we're going to review the central findings and recommendations of our report, and then we will give Martin Baily, who was not affiliated with the report, a chance to offer his thoughts. And then we will open the floor to any questions and comments that you have.

So, we will start with Rick Kimball. And, you know, one of the things we did in this project was to look at investment objectives and practices of global public investors. How would you describe their investment objectives and practices?

MR. KIMBALL: Thanks, Darrell. Good morning, everybody.

So, as Darrell mentioned, there's about $4 trillion of assets in the sovereign wealth funds. To put that in context, there's $2 trillion in the entire hedge fund industry, so there's obviously a huge amount of capital, and this has grown significantly over the last 10 years, particularly with the uptick in oil prices. And as people forecast forward, there's various estimates that over the next 5 to 10 years, this body of capital may be as much as 7- to $12 trillion, so very large pool of capital. And so a key element of this is to understand how are these countries thinking about these funds? Why have they been established? How are they being used? And what are their practices? And that's going to inform what we think some of the key issues are as a political and economic matter.

You can break the sovereign wealth funds broadly into two categories. There are the commodity-based funds, generally oil based, so these are oil-producing countries -- the Middle East, of course, Norway -- where they have generally thought about these funds as a way to stabilize the government revenues and ultimately create a national endowment for a post-oil type of era. And then there is a series of more foreign exchange-oriented funds, and these are China, Singapore, where simply there's been very strong export-led economies that have developed very significant foreign exchange reserves, and these countries have put some of that wealth into these funds as a way to secure the economic security of these countries.

As a consequence of each of these categories, I would argue that these funds are effectively like pension funds. They are trying to secure the long-term wealth of these countries. As a consequence, it's one of their highest priorities to preserve capital. They want to have attractive, risk-adjusted returns. Generally because of their long-term orientation, they should be able to withstand price volatility or asset price volatility. But I'd argue that there are domestic political implications, as we saw in the 2008 timeframe when a number of these sovereign wealth funds invested in particularly the U.S. financial sector -- and then the group fell out of bed -- that created some political consternation in these countries.

Well, one of the key issues here, as you all know, are these funds being used for political purposes of these countries? And I think it's fair to say that a number of these countries have been buying assets around the world for political or domestic reasons, particularly the Chinese buying mining and mineral interests. But most of that is really being done through state-owned enterprises, so the national oil company in China looking to buy Unocal, for instance, as opposed to the sovereign wealth funds looking to take these interests.

And I think importantly, increasingly these funds are really being managed by Western-trained investment professionals. As effectively, pension funds across a whole variety of asset categories, and I think most of these funds would prefer to actually use third-party managers to manage these assets. In fact, most of the private equity investments are actually being intermediated through the large private equity firms, the KKRs, and Blackstone's TPGs of the world.

I think a key issue here is these funds really do want to preserve capital and maximize returns, and as we think about how to use this capital productively in the United States, we need to really think about how do we think about investment alternatives that fit with the investment themes of these institutions. So, while certainly more needs to be done in the area of transparency -- and we'll talk about that -- I'd argue that these funds have really been set up as traditional investment managers, and we can think about them quite similar to pension funds.

MR. WEST: Okay, thank you very much, Rick.

And Vij, the United States faces a variety of fiscal pressures and infrastructure challenges. How would you describe our current situation, and what do you think the implications are for global public investors?

MS. RAMACHANDRAN: Okay. Thanks, Darrell. I think the current situation is particularly interesting to review in light of what Rick just said. I think what we're trying to do in this report is marry some of these facts about sovereign wealth funds to the needs of the United States, particularly when it comes to infrastructure-related investments. I think there's no question we can all agree that the public sector is facing a drastic shortage of capital. Our aggregate public debt is now at about 94 percent of GDP. We have suffered from decades of underinvestment in infrastructure. The available evidence suggests that about 3 percent of GDP is currently allocated to infrastructure versus, you know, 5, 6, or 7 percent in other parts of the developed world. We also know that about a quarter of America's bridges are judged to be structurally deficiently or functionally obsolete, and the report points out that in Pennsylvania alone there are about 6,000 bridges that are judged to be structurally deficient. The average life span of bridges, for example, is about 50 years in the U.S., and most of the bridges in the U.S. are around -- the average is around 43 years, so we're currently facing -- we're looking at, I think, a very, very large shortage of capital with which to renovate and increase investment in existing infrastructure and new infrastructure.

At the same time, municipal debt markets which have largely been the source of capital for infrastructure-related investments in the U.S. are also not what they used to be. Total municipal debt is now at about $2.5 trillion. Bond markets are getting softer. We've seen some exit of investors in recent months, and we know that most states are looking at acute budget deficits. And so there clearly is a desperate need for alternative sources of capital with which to fund infrastructure and other activities at the state and federal level I think it's fair to say.

Anyway, on a more positive note, a paradigm shift has emerged. Many agencies of state and municipal governments are now looking at different types of ways to raise capital, new ways rather than rely on their own funds. They have begun to explore partnerships. And in particular I think a number of agencies are looking at private-public partnerships which have been the vehicle for infrastructure investment in the U.K., in Australia, in Canada, and of course in much of the developing world where PPPs are the main source of infrastructure-related investments. So, I think our report and the consultations we had -- and I particularly want to mention Jewel Mozo, who was very instrumental in helping us think through these things and, as a co-author on our report, it was really useful, I think, for us to review the evidence and think about how we might explore these new partnerships for infrastructure investments, how we can best leverage private capital as we look at these acute budget shortages.

So, with those comments, I'll turn it over to Dan, who will go into some detail on some of the vehicles we explore in the report.

MR. ZWIRN: You know, as Vij said, there's obviously an acute need, and one of the things that we tried to think about was, you know, how can sovereign wealth investors, or GPIs generally, who want to involve themselves in the U.S.-related investments meet a need? And obviously within municipal infrastructure and infrastructure broadly defined there's a great need.

Inherently, there should be a very good match. When you take the pension-like characteristics of sovereign wealth entities that Rick mentioned and the vast need of municipalities that have the ability to raise revenue contractually from their citizens, there should be a wonderful opportunity for there to be a good two-way trade between investors looking for good, long-term contracted cash flows in the form of sovereign wealth funds and municipalities that are in great need of infrastructure redevelopment.

Certainly we do point out that there isn't an Obama-backed idea for an infrastructure bank. The infrastructure investment vehicle that we would advocate would focus on a structure where there was no specific individual sovereign wealth decision-maker, so we advocate a pooling of sovereign wealth entities investing in these projects in order not to drive a direct relationship between a given municipality and a given sovereign wealth fund that could create political issues.

There are great opportunities for the U.S. to provide incentives for this investment to occur in terms of tax breaks and potential loan guarantees. In addition, you know, thinking through the benefits for each side, the benefits to the sovereign wealth fund investors, in addition to just simply returns, could potentially be connected to the familiarity with which the U.S. municipality specifically would have with those institutions, so they said that they want to be increasingly active in their overall investment activities in the U.S. and also, frankly, may allow them to put very large pools of capital to work, you know, in a world where particularly today there may not be as many risk-adjusted opportunities for funds that have hundreds of billions of dollars to put to work as they would otherwise prefer.

From the point of view of the U.S., the ability to have -- well, first is conventional, privately raised infrastructure funds -- the ability to have larger pools that may not be constrained in terms of diversity so that larger projects with potentially longer payoff horizons could be attacked would be very compelling. And at the same time, the ability to, again, develop broader and deeper ties with these institutions that have capital may allow them to entice sovereign wealth investors into a broader group of projects than they otherwise would have.

Connected to the infrastructure investment policies that we looked at in the paper, we also discussed incentives for green financing, and again we tried to stay within the realm of commercial reality and think about needs that need to be met, and when you look at the landscape in green finance, there's a good amount of early-stage venture capital focused on the area, and there's relatively available project finance for absolutely commercially viable, already financed projects out there.

However, in that middle zone between the early-stage venture world and project finance world, there's very little, and so what we talk about is the opportunity for green finance in the kind of mezzanine part of the financing structure to be met through potential interaction with sovereign wealth entities with a view toward creating an SBIC-type relationship where the investments are subsidized so that, effectively, people taking inherently debt-like returns are getting equity-like returns off that mezzanine-type risk.

MR. WEST: Okay, thank you, Dan.

MR. ZWIRN: Sure.

MR. WEST: Gordon, in our report we talked a little bit about best practices and the need for better understanding of global public investors. What do you think are the most important things we can do to improve mutual understanding between

American policymakers on the one hand and global public investors?

MR. GOLDSTEIN: Is this working? Okay.

So, our report coincided with a really interesting historical period here in the United States. The bulk of our conversations occurred over the past 18 months, and as you all well know that recent history corresponds to a period of enormous volatility in our political system, and a period of very pronounced, populace anger, antipathy in the political environment, a hostility to Wall Street generally, and skepticism about the business community specifically, creating what to many in the private sector was perceived to be a hostile public policy environment. This also coincided with a period of great regulatory activism in the Congress.

So what we discovered in our conversations with global public investors, and in off-the-record exchanges with them, was a great and pronounced discernible sense of uncertainty about how our system was going to operate and the decision-making, rule-making, policy-making process in Washington. And that uncertainty, as you know, contributes to a great apprehension about making investment decisions. Nothing is more chilling to investment than the uncertainty of the shadow of the future. And this thing came through loud and clear in varied and diverse conversations that we had.

For these global public investors, the turbulence of the political environment, the rapidly shifting game board of regulatory change, the activism in Congress, all exacerbated a general lack of transparency from their perspective on how to understand the rulemaking process here in the United States. Adding to that ultimately was the mid-term elections where we saw the biggest swing in the composition of the Congress in 74 years.

So, if you're a global public investor looking at investment in the United

States and you're evaluating risk, you're looking at political risk and regulatory risk. And you observe that the United States has gone through really a historic period of turbulence and uncertainty, and that is a pronounced disincentive to investment here and we believe is the thesis of this report, to quote my colleague, Dan Zwirn, "in today's integrated global economy, global capital will inevitably and inexorably find its highest and best use."

So, we are competing for global capital. We are competing for investment in the United States. And unless we can create an environment which is predictable and transparent and ultimately hospitable to global capital, it's going to go elsewhere, and the benefits of that global investment will be enjoyed by other countries competitive with the United States.

So, one of the proposals that we have come up with we believe is particularly constructive but also quite actionable, and that is to structure a more regular, substantive, and continuing dialogue between global public investors on the one hand and the American political and policy-making community on the other hand.

What we would propose is the creation of what we call in our report the Global Public Investor Roundtable, which would be a series of periodic, structured, substantive discussions between these two constituencies; global investors from China, from Singapore, from the Persian Gulf, from the Middle East, from Europe, increasingly South America, which has a rising class of new sovereign wealth funds, who are going to look at our marketplace, are look at the possibility of foreign direct investment in the United States, and will want clarity and transparency on the legislative environment and the regulatory environment in particular. And we would propose that they engage in dialogue with the constituencies in Washington. We're going to set the rules, and we're going to define the environment for foreign investment. Representatives from the White

House, from Treasury, from State, from Commerce, and, most importantly, from Congress, the relevant committees on the Hill that, on a day-to-day basis, really are rule makers.

We think that a dialogue that could bring these constituencies together would, at the very least, contribute to greater understanding, an exchange of information, and greater clarity and hopefully greater certainty from the prospective investors who are considering foreign direct investment in the United States.

At its best, this dialogue could explore ways in which the United States can try to become that competitive magnet for global capital investment in the United States to perpetuate, to create a more competitive dynamic here to attract those investment dollars, particularly now during a period where for the foreseeable future we're going to be grappling with chronic budget deficits and acute public needs and an enormous disparity been our ability to fund those needs.

So, in that sense, we think the Global Public Investors Roundtable could constitute a small but meaningful contribution to making the United States competitive in the competition for global capital.

MR. WEST: Okay, thank you.

Martin, you were not involved in writing the report, but you do have lots of expertise in financial markets and the investment climate. What is your view of the role of foreign capital and global public investors?

MR. BAILY: Well, let me say that I thought this was a terrific piece of work. I want to congratulate the authors. I agree with a huge amount of what's in here. I'm sort of the non-author and, therefore, the discussant, if you like, of this, so I'm going to raise some skeptical questions, but I don't want that to obscure my enthusiasm for the overall message, which I think is exactly right, which is that we want to encourage -- we want to deal with some of the regulatory issues, and we want to encourage availability of foreign capital and sovereign wealth funds in order to help us meet our infrastructure needs.

Okay, so some of my skepticism. Number one, how big is the infrastructure need? How much infrastructure do we really need here in the United States? We clearly need some. We've obviously got some bridges that are falling down. We've got some potholes in the road. You could spend quite a bit just filling in the effects of last night's rain for example. We do need much better maintenance of the existing infrastructure, and so that's certainly a critical issue.

I think we also need infrastructure in the sense that our power grid is in some respects a third-world power grid. I speak as a resident of Montgomery County, one of the most affluent counties in the world, and I actually thought of bringing in some pictures of the sort of wires hanging off the poles and, you know, every time we have a storm the power goes out. This is sort of really appalling that we do not have -- we also have a lack of coordination across jurisdictions in a way that's needed. So, we certainly need to transform our power grid, not just because it's unreliable but because it's very heavily carbon oriented and we need eventually or maybe even quickly to move in the direction of a lower carbon infrastructure.

I think there is a serious problem with urban congestion, urban transportation. I'm not convinced that that's an infrastructure problem. I mean, clearly it is, but it's more on how badly we use our existing infrastructure than it is we necessarily need to build a lot more roads.

So, I'll stop there. I'm not an engineer. And I do think that we do have some infrastructure needs. I'm a little bit skeptical at some of the very large estimates of what are needed. I'm impressed, actually, how well the U.S. infrastructure functions in many ways. It's very easy to get around in the United States. It's very easy to ship goods in the United States, and so I think there's some extravagant claims sometimes of how much productivity and competitiveness could realistically be augmented by additional infrastructure spending. But as I said, we certainly need some.

The next issue of skepticism I have is around federal guarantees, and none of the speakers mentioned that, but it is mentioned in the text and it's certainly talked about a lot with respect to an infrastructure bank or a green bank.

Federal guarantees for this infrastructure bank or green bank? I'm against them. I'm against them. I think the federal government is maxed out on its credit and should not be offering additional guarantees.

Now, the argument is that we need those guarantees because otherwise we won't attract the capital. It seems to me we have to provide sound sources of revenue behind these capital investments, and then the investment will come in. I don't think we should short circuit that process by getting federal guarantees, because I just think the federal government can't do it. By the time we've dealt with our deficits, with Medicare, with Social Security, with defense, with the interest on the debt -- and, by the way, if our debt goes up to 100 percent of GDP, which it seems like it will, and interest rates go up to, say, 4 percent, then just servicing the debt is going to be 4 percent of GDP. So, this is just we really are maxed out.

I was on a panel with Doug Holtz-Eakin, and somebody asked a question -- well, you know, if everything you say about the precarious nature of the finances of the federal government is true, how come interest rates are so low? Aren't the markets indicating that this is still -- there's no risk involved in that? Well, I think that is somewhat of a puzzle. I think Doug Holtz-Eakins' answer was better than mine. He said well, just because we're the favorite horse in the glue factory doesn't mean that we can take the steed for a long ride. (Laughter) You know, we are -- I think there is a danger in maxing out something that's already maxed out. So, I would like to see funding mechanisms that are associated with secure revenue sources.

You know, we always sort of want to avoid the costs. We want better roads; we don't want to pay the tolls that we need to pay on them. We want a new electricity grid, but we don't want to pay higher rates for electricity. Electricity is very cheap in the United States. I think we may have to pay more if we want to convert to a low carbon. I think we should probably pay tolls on our roads. You know, in California they don't. They think tolls on roads? We never heard of that. Well, maybe they need tolls to deal with their budget situation.

Should sovereign wealth funds be the vehicle for providing some of this funding? Yes, I'm all in favor of that. Maybe there's some critical infrastructure things that we should not put in foreign hands, but I think even there there's a difference between ownership and operational control. I would not have had any particular problem with Dubai ports operating ports in the United States. Again, you can build in safeguards around that, and I don't see that as a big problem. So I'd be probably more lenient than most of the policymakers on that issue. I think sovereign wealth funds will generally be a good source of money for that.

I notice Ted Truman is one of our experts on best practices in sovereign wealth funds, so I think the Santiago rules -- and they're not rules, they're guidelines -- are good things, and we can deal with what issues might arise in that sovereign wealth fund. So, I'm supporting of that.

And then the last point I want to make is the macroeconomic point, and that is we are caught in a dilemma where we have been running large trade deficits chronically, and at the same time we are short of capital. Now, actually though, those are the other sides of the same coin -- two sides of the same coin. In other words, we are a trade deficit/current account deficit country because we are a low-saving economy and are bringing in a lot of capital. China, which chronically has been running surpluses -- not, apparently, in February but mostly it runs trade surpluses -- and that's because they're a very high-saving economy even though they're a high-investment economy, and so they have a surplus of saving.

So, borrowing from sovereign wealth funds is not going to solve this arithmetic. In other words, if we want to become more competitive in the sense that if we want to have more balanced trade going forward, then we need to raise the level of domestic saving so that there's no sort of free lunch on that. In other words, it would be great to bring in more money for our infrastructure, but let's also concentrate on reducing dis-saving dealing with budget deficit problems so that we become a higher-saving economy and therefore a smaller trade deficit economy.

Thank you.

MR. WEST: Thank you, Martin, and thank you for bringing humor to the issue of the subject of foreign investment.

You raised several interesting points, and I'd like to structure two or three questions based on comments that you've made for the panel, and anyone who wants to jump in can.

I think one question is a subject of federal guarantees, and in the paper we do talk about a variety of ways to build this intermediary connection between global public investors and particular needs within the United States. We recognize there are different ways to do it. Some people have proposed an infrastructure bank or a green bank. Others prefer more private approaches to this, and then some people suggest a need for public-private partnerships. So, I was just wondering if people on our panel could address the subject of what is the best way to structure these types of foreign investments in the United States.

MR. GOLDSTEIN: I the critical question is thinking about needs that aren't met and why they aren't met in the private sector. And so as an example with the infrastructure fund, as we mentioned, there are already conventional, smaller-sized infrastructure funds out there that sovereign wealth funds and other large pensions, etc. can partake in.

However, I do think that there's a place for, as an example, a federal guarantee in situations where there might otherwise be competitive risk-adjustment returns available but due to the structure's inherent and private market opportunities, needs -- the kind of greater needs of, in this case, municipalities are not met. So, as an example, there may be a very compelling project that could -- that might take, say, $2 billion of equity capital financed out to a total value of -- call it 8 billion. The largest of the infrastructure funds themselves are only -- call it 5 to 6 billion. So, you have a situation where, by virtue of their needs to be responsible fiduciaries for their investors and maintain a certain level of diversity, they may be capped at -- call it half a billion. And while it's not inconceivable that consortia of those types of investors may align themselves, there are clearly investments -- individual investments that either by size or potentially by investment horizon that again may make economic sense in a vacuum but, by virtue of the structures already out there, are not going to be met by the private sector. And so where that gap exists there could be places for guarantees to step in.

And I think there's a similar analog with what we recommend for the greenback initiative, which really is not a bank at all but rather a guarantee program along the lines of the SPIC, or again there's a very specific middle of the, if you will, the capital supply chain between venture and project finance that's not being met. It's in the greater interest of the country for that to be met. There's a pool of capital that otherwise might not, but for those guarantees, be willing to accept, you know, what arguably is a compelling but potentially not risk-adjusted competitive return, which is effectively, again, why you need to reward what is essentially a mezzanine-type risk with potentially equity-type returns, which arguably is a similar reason why things like the SPIC program exists in the first place where small businesses that otherwise might not be able to deliver the kind of returns to their owners or investors are given a push by guarantees.

So, I think there is a place and there are structures where very specific needs that are sensible, that are reasonable economic propositions are not being met in the current marketplace, and you can put buyer and seller together here with these programs.

MR. ZWIRN: I might just add a few thoughts. First of all, I agree entirely, Martin, with your comments that thinking about how to get the sovereign wealth fund capital into the United States is really dealing with the symptoms and not the root causes of some of our problems here. So, obviously we have to deal with our federal deficit and some of the structural issues we have in our economy that's making us dependent on foreign capital, whether that be equity capital or debt capital, to finance the Treasury.

But I also think we clearly have some key fiscal issues over the next several decades we've got to figure out how to deal with. So, we have to deal with some of those fundamental issues, and then in the near term we have to fund some of these problems. And as we looked at this problem, one gaping hole we think is infrastructure, and frankly infrastructure -- as you think about foreign investors coming in and funding some key infrastructure projects like, for instance, the power grid, it is obviously going to be concerning the issue as a national security matter. But you would argue that these are just the types of assets that a pension-oriented fund would want to invest in, that these are general lower risk projects that ought to be attractive for these types of funds, but you're going to need to have some structure that's going to be acceptable to us here in the United States for the Chinese government to come in and invest in our power grids, for instance. And so that's why the idea here of an infrastructure fund where we're effectively pooling capital from both foreign and maybe also domestic investors can be helpful to, in effect, buffer issues in the interests of any foreign investor and so our national security concerns here. So, that's sort of the nature of thinking about this infrastructure fund to try to put together our needs and manage some of our national security concerns with that issue.

MR. WEST: Okay. Martin, also mentioned the issue of political risk, and we certainly all understand the fears and anxieties that the American public feels on the general subject of foreign investment. And I just want to pose the question to our panel: What should American leaders to reassure Americans about foreign investment, particular investments linked to public sector funds in the various countries. And, the corollary, what should global public investors to reassure Americans -- and we were mentioning Ted Truman and his work on transparency and the Santiago Principles, which we found his work very helpful in our projects. So, what should the GPIs do?

MR. GOLDSTEIN: It's an excellent question, Darrell, and it poses a challenge to each of the constituencies you've identified. Let's begin with -- in the order you asked them.

What should our policymakers and political leaders in Washington do? I think the first thing they should do is get educated, become informed to learn who these investors are, how their investment strategies are defined, how they deploy capital, the asset classes in which they're active, the types of returns that they seek, the governance models that they apply operationally, the third-party asset managers in whom they invest. Many of them are some of our most significant private investment firms -- Rick alluded to them earlier -- you know, big, $100 billion players who invest globally with money from sovereign wealth funds deploying that capital on a global basis and leading a global industry, in this case, private equity. United States, in essence, conceived of the private equity industry and remains the undisputed global leader in part because of their ability to leverage significant capital invested by sovereign wealth funds and pension plans and other global public investors.

So, first step, I think, for Washington is to get up to speed; to de-mystify what these investors do; and to, through their own effort to become familiar and educated with their investment practices and procedures and goals, lower the temperature and the anxiety about what they do and the potential role that they can play.

As for the question of what global public investors in pension funds and others can do, they can participate in a dialogue, I think, with Washington. They can participate in international fora, like the IMF working group, which they did, to create the Santiago Principles for transparency. They can progressively achieve greater levels of transparency and compliance with the Santiago Principles. They can disclose more of their investment practices, more of their holdings, their asset allocations; and they can advance their own self-interest by, again, de-mystifying what they do and lowering the temperature and lowering the anxiety.

I think through these reciprocal approaches over time, it will emerge that what global public investors do is they act like giant global asset managers for the most part, as Rick's introduction and overview indicated, and what Washington will understand is that we are competing for their capital as others do and that we need it and that we can fashion new and creative mechanisms to bring it here to the United States.

MR. ZWIRN: I would just add a couple of additional points.

Getting to know these sovereign wealth funds is not that difficult. The top 10 funds comprise 75 percent of the assets of the sovereign wealth funds, so while there are sovereign wealth funds all around the world, there's a small handful of them that really are the big dollar funds. And so whether it's ADIA, CIC, et cetera, there's an ability to come and get to know these types.

I'd also mention that the China Investment Corporation, CIC, recently opened their first office outside of China, and that was in Toronto. And you might think that they might have done that in Europe or in the United States. They did it in Canada, because they feel welcomed in Canada. They feel certainty that they want to make an investment, that the Canadian government will be receptive to them investing there. Certainly the preponderance of mining and oil assets I think has something to do with it as well. But I think it's a clear statement, frankly, to the United States that they did not want to open their first foreign office here, and I think that should be a concern for us. I think that it's a statement that we have a process that's fairly opaque despite, you know, having this group of CFIUS there to help the approval process. I think it still is viewed as somewhat arbitrary and highly political, and it's going to be very important, as Gordon said, for first the American leaders to understand all these issues, then ultimately to communicate those to the American public. I think that's going to be one of the difficult pieces here, which is going to take time to have the American public understand that we have a set of processes in place to balance our both economic and security interests in this process.

MR. WEST: Okay, Rick mentioned this CIC office in Toronto. Let me just ask one last question -- and then we'll open the floor to questions that you have -- because his comment kind of highlights the issue of other countries and how they are handling this issue of foreign investment. And, you know, places like United Kingdom, Canada, and Australia generally had been more open than in the United States to foreign capital and particularly foreign capital playing a role in helping to rebuild infrastructure and helping to finance other important priorities.

So, the question is: What can we learn from the experiences of other countries as they manage the complex domestic and international issues involved with foreign investment?

MS. RAMACHANDRAN: I think we have a lot to learn, and probably, you know, all of us need to get educated more about what the specifics are of projects in the U.K. and Canada and Australia, and so on, that have attracted foreign capital. I think Australia in particular is pursuing some very interesting ways of attracting financing in mining and other types of sectors as it seeks, like everybody else, the best forms of capital with which to finance its investments. I think at the same time we need to take the long view on this. You know, the report does point this out that these are not problems that are going to go away any time soon. Neither our infrastructure deficiencies nor our public debt problems are going to go away any time soon. So I think in some sense we have the time, and we need to take the time to figure out what these modalities are, even perhaps look at some of the public-private infrastructure financing in Asia, in Latin America, and so on, that has attracted various forms of private capital combined with public capital. The very large dam projects, for example, or road projects that have occurred in the developing world have tended to seek private capital from various sources. And so I think we need to take the time to learn how those things work, how the concessions work around roads and tolls and so on, what the success stories are there, and how we can do this as our own sources of capital are short.

MR. ZWIRN: Darrell, if I can just add one point there on the question of infrastructure investment. As Vij announced, there are best practices out there that have grappled with the issue of risk mitigation about control and operational management of sensitive infrastructure assets, so there are others who have struggled with these challenges and have developed durable solutions that have been emulated in Western countries around the world to a very considerable degree. So, we can just consult best practices as a first step.

But I wanted to add one additional point, which is, I think, quite encouraging. People may not be aware of it. But they're actually already is a discussion, ongoing, here in the United States between senior policymakers in the Obama administration and the Chinese about potential Chinese investment in infrastructure assets. Last November, the Chinese made a proposal that the United States should invest up to $1 trillion in infrastructure renewal, arguing in part that it would enhance U.S. competitiveness, and it could potentially create half a million manufacturing jobs if a program were structured strategically. That dialogue continued in January when the Chinese premiere was here, and Lou Jiwei, who is the head of CIC, was part of that delegation that met with President Obama in Washington and his senior advisors. And part of that discussion was potential infrastructure investment. The Chief of Staff went on some of the Sunday talk shows and alluded to those discussions, so it's somewhat below the radar now, but there is a dialogue that's ongoing. We don't know what it will yield, but I want to identify it as an encouraging sign.

MR. WEST: Okay, let's open the floor to questions and comments. There's a question in the very back, and if you could give your name and your organizational affiliation, and we would also ask if you could keep your questions brief just so we can get to as many people as possible.

MR. TALLEY: Ian Talley, Dow Jones, *Wall Street Journal* Bureau.

Gordon, we would be most happy to help mediate this introduction, having covered energy in Norway and here, knowing the difficulty of actually even talking to some of the sovereign wealth funds, except for Norway. Norway is obviously an example. But if you'd like to help those introductions, we would be most happy on that.

Just more broadly, wondering, one, about -- you've already answered -- idea about transparency being reciprocal, the necessary chilling investment but also chilled towards investment. But I wonder if there's a risk of over-exposure to the U.S. dollar, particularly since many of these forex holdings are dollars already, and then reinvesting into the U.S. would be building up your dollar exposure, and obviously exposure in the U.S. during the crisis was a problem.

MR. GOLDSTEIN: Okay, I guess I'll probably start off with a comment.

I think you raise an important issue, which is I think we're already at risk of the central banks around the world and governments around the world wanting to diversify their foreign exchange reserves into other currencies, and given our economic issues that Martin mentioned, I think that that's a real risk to the United States here and something that we need to be concerned about. And so it really gets beyond the scope of this report, which is to get to these more fundamental issues of trying to be more fiscally responsible and manage our fiscal needs in this country. I think that, you know, we could argue that what we need to do is create a more responsible and receptive environment for investment capital in the United States in the long run that's probably going to be better for the dollar. But I think we should all acknowledge that the dollar is vulnerable here given our lack of fiscal responsibility, and so we need to address the root issues here, as Martin mentioned.

MR. ZWIRN: If I could just add one point. The question identifies a very legitimate and important concern over concentration in the dollar, and -- excuse me -- our report would acknowledge that this is an important issue that has to be addressed. I would also point out, however, that for the foreseeable there will be a paucity of options other than to kind of engage in investments that add to the concentration of exposure to the dollar.

If you look at what some of these global public investors have to manage on a weekly and monthly basis in terms of deploying surplus capital, it's a rather remarkable problem that we would be envious to have here in the United States.

I traveled to Asia in November to Japan and to China and to Korea, and I met with some of these global public investors, and one of these asset managers had the authority and responsibility to decide how to deploy their capital on a monthly basis. He had to put $2 billion a month to work. He had to find someplace to put it. Another one of these players had to deploy $4 billion a month -- put it in treasuries, put it in global equities, whatever, he had to figure out where to put it. So, we're part of a very significant paradigm shift where all the surplus capital is really being generated in other parts of the world, and it will need to be deployed, and we think there are constructive ways to channel it here for long-term public policy needs.

MR. WEST: Another thing I'll add to that quickly is when we talk with people in the sovereign wealth funds, they basically made the very valid point that if the U.S. was not hospitable to foreign capital investment, there are plenty of other opportunities around the world, including in emerging markets, which they see as very attractive -- high rates of return, you know, some risk associated with those returns, so that was something that they pointed out that we found interesting.

There's another question right there.

MR. TRUMAN: Hello, I'm Ted Truman from the British Institute for International Economics across the street. I thank Martin for the plug.

I would observe -- one comment is at least as far as the advanced countries are concerned, my impression -- I'm not an expert, but I have looked at some of this -- we have no more problems than any other country. In fact, the regimes in most other countries -- Australia and Canada actually have been also tightened over the last several years on foreign investments. So, they may be better at some particular forums, but they have had a number of high-profile rejections, and so we're -- the advanced countries as a group are a bit in the problem here which partly reflects the changing character of the world, which is not to say that we don't have our own problems, but it certainly is true that many foreign investors are skeptical about the regime. So, I share that.

My question really has to do with sort of the numbers that you're thinking about, and I don't really know what's giving your report -- what you're thinking about in terms of infrastructure per year, if you want to think about that, but one can exaggerate, I think, notwithstanding the previous comments, about how large you -- the funds you're dealing with. So, we've got $4 trillion in sovereign wealth funds, which is a reasonable estimate. If it increases the -- by 15 percent a year from returns and new flows, which is a reasonable estimate -- could be higher -- that's $600 million a year. Some fraction of that goes to the United States anyhow. Maybe we get a quarter, which is $150 billion a year. Now, one question is are we diverting that $150 billion from buying what they now buy into something else, which is a good question, right? And then, therefore, there might be three things to do on that. Or are we getting a larger share of that pie and the question is whether that -- how much really you're talking about in terms of the larger share of that pie relative to what you're talking about in terms of financing -- of annual financing of infrastructure needs. So, I'd be interested if people preparing the report have some sort of dibs on thinking about matching up those numbers.

Thank you.

MR. GOLDSTEIN: Yeah, I think that -- I think it's hard to match up those numbers. I don't know that those numbers necessarily exist. I also don't know how easy it is to ascertain just how much infrastructure investment is out there that is not funded that could be. I would also point out that looking at it as if the funds collectively have to put out -- you know, only that 600 billion may underestimate the amount of funds that need to be deployed when you think about the whatever duration and liquidity of the investments they have in that core 4 trillion. So, just to take it piece by piece, I do think that it would be a valuable exercise to try to match those two up to the extent that the numbers are out there. I don't know that it's possible, but I think getting too far into the weeds of that takes you away a little bit from what we were saying before about the ultimate message being how do we make ourselves more competitive as a domicile for investment for these funds, whether that's through keeping our fiscal house in order, providing more transparency, more predictability, et cetera. I think that's the greater message.

MR. BAILY: I had a quick comment on that. I may not be getting my numbers exactly right but they're close. Between about 2000 and 2007, about 85 percent of the available capital flows from around the world came to the United States. In other words, we got almost -- not almost all of it, about 85 percent of it. So, I'm not going to put words into the panel's mouth, but I'm assuming that that may be actually a little bit more than one would like to see. One would like to see more domestic investment and less reliance on foreign capital. But in general, I'm thinking that it's really diverting some of the flow coming in, which is now going into financial assets and obviously went into CDOs and all kinds of things, and using it for more what we hope would be more productive investments in infrastructure. But there's certainly plenty of money that has come in and actually continues to come in to the United States. So, I would have thought you could get -- the goal would be to make investing in infrastructure more attractive as part of that flow.

MR. WEST: Question over here.

MR. DILLON: Ken Dillon, Scientia Press.

What about the idea of an independent organization that would study the various GPIs and sovereign wealth funds and give them a kind of Good Housekeeping Seal of Approval?

MR. ZWIRN: I think Ted Truman does that across the street right now, doesn't he? (Laughter)

MS. RAMACHANDRAN: That's what I was thinking.

MR. ZWIRN: To some degree. It's a very interesting question. I mean, first to acknowledge for the group, Ted has been one of the thought leaders on this question of transparency and actually measuring compliance with the so-called Santiago Principles, which in turn were generated out of a sense of concern a couple of years ago about the potential backlash to sovereign wealth funds as actors on the world economic stage. But there potentially could be third parties who provide additional assessments of compliance with expectations relating to transparency and provide authoritative information about the investment practices of sovereign wealth funds.

I would point out for those who are in the financial community; there is a very significant and robust amount of information out there right now about how these players deploy their capital and what their practices are for the very simple reason that there are so many American investment interests that are knocking on their door seeking their dollars. So, there's already a very significant dialogue that occurs between, say, a CIC and, you know, global investment banks, which are trying to source opportunities for them, and global private equity firms that are trying to raise significant funds from them. So, there is a very significant degree of information sharing that already occurs. But as your question notes, perhaps there are ways to even elevate it further.

MR. KIMBALL: I was just out. I have in front of me a list here of the sovereign wealth funds, and I have their Linaburg-Maduell transparency index score. So, somebody has, you know, come up with this score, and I'm sure Ted knows more about this than I do, and scored them. But the problem I see here is they all range from -- you know, some are 1 and some are 10 and they're all over the place. So, we don't have a consistency here yet. We have not gotten uniform transparency across these, and I think, rightly so, it's one of the issues that's plaited in the minds of the American political leaders and the American public, because they know that Norway has been quite transparent but some others have not been. And so I think part of what we want to try to accomplish with this roundtable that we're proposing is to encourage more transparency to help these GPIs understand the value of being transparent, and then on the other side of course to work to try to make the whole process of foreign investment in the U.S. also more transparent and more predictable.

MR. WEST: There on the aisle.

MR. DIAZ: Hi, there. I'm Mark Diaz, Washington, D.C.'s Office of Planning and Economic Development.

To change the direction of the conversation a little bit, on the investment-seeking side, municipalities, local and state governments in the U.S., like the office that I represent, are beginning to seek for our mega projects, such as the Bay Bridge you highlight on the cover of your report, large-scale participation from these global public investors. The District recently secured $900 in equity investment from ADIA for the redevelopment of our old convention center site, and that's a project we're excited about moving forward with. We expect to do more of this in the future, and as we think about being competitive against other states and localities both in the U.S. and even the rest of the developed world, we'd value your reflections from conversations. You know, what do the global public investors look for in local and state partners? What are the types of investment environments this profiles and, frankly, operating activities that we at the local and state level can do, particularly at the mega project level while we're waiting for all these great federal guarantees and infrastructure banks to get built?

MS. RAMACHANDRAN: I think it would be really interesting, actually, to hear more from you about the interaction between the D.C. Government and ADIA over the capital you secured. That's a very interesting thing that we did not highlight in our report. But I think that, you know, what GPIs are looking for also are reassurances that we're not going to exit in an ad hoc manner. I think everybody still remembers the example of DP World and how that was handled, and I think for DP World itself -- I was there last year talking to some people about their foreign investments. DP World now has -- I think manages 40 or so ports across a dozen or more countries, and they still remember the experience here, and I think it's left, you know, a really bad mark, and so I think from their side they're looking for assurances from us as well that we will proceed with these transactions in an open manner and that our politics will not crowd out the economics of the rationale of these types of investments. I mean, clearly there needs to be education on both sides, and both sets of players in this have to be transparent. But there's no doubt that from their side I think they're looking for assurances, but we will stick with the investment and with the parties once they attract the capital. But it would be interesting to know more about your experience with ADIA.

MR. WEST: Here.

MR. SILBY: Thank you. My name is Wayne Silby. I'm with the Calbert Funds, Calbert Foundation, and we look at some of this double bottom line kind of impacts. In fact, we've been working with Treasury on this enterprise impact fund that is also the SPIC people and some changes there.

But I was, like, with the Treasurer of the World Bank a few months ago, who was talking about investments in agriculture, like, those large-scale investments --

Somalia and other places -- and speculating about how to encourage investors to come in, where the impact, while there's some rate of return -- maybe a 3 percent real rate of return, which is actually pretty decent -- but also with the food security issue, which goes into national security issues, world security. To what extent do you see, or have any of you seen, where the sovereign wealth funds are trying to think strategically about their investments to make sort of more of a win-win world, to create more of a -- not an infrastructure, but a context in which others can do their kind of money-making-type maximizing return investments?

Again, in fact, I'll be with the Secretary of the Treasury in a couple of weeks, further discussing this enterprise impact portfolio, which has not just the returns, which we don't look to maximize -- we look to optimize with regard to the social impact, but the overall impact, especially if you're a national sovereign interest in a kind of win-win, more stable world would seem to make sense. So, we're beginning those conversations, and I wonder if -- does that resonate yet or, as Mr. Kimball said, is it just about maximizing returns?

MR. KIMBALL: I think it does resonate. The concern I think that some of the sovereign wealth funds have had is whether they get perceived too political and too nationalistic in what they're trying to accomplish by virtue of these investments. But I think the truth of the matter is they do have these interests. So, you know, for instance, when General Motors went public, a number of the sovereign wealth funds invested in the General Motors IPO, and they were doing so both because they thought it was an attractive investment but they had an interest to get involved with General Motors, particularly in China. Of course, GM has a big joint venture in Shanghai, and so there was an interest to solidify that relationship. And I think there's been interest in the financial institutions area where both in the financial crisis and separate from that you've had banks around the world together with their sovereign wealth funds wanting to secure relationships there that could be valuable.

You've seen -- in Qatar, you've seen an interest there to develop their health care system, and so they've got into a relationship with the Cleveland Clinic and they're trying to help develop hospitals in Qatar using the capability from Cleveland Clinic. And of course, there's capital that Qatar can give to the Cleveland Clinic as part of that process. And, in fact, as HCA just went public this week, there were some conversations between HCA and various sovereign wealth funds and at least trying to explore the opportunity for HCA to help develop health care in some of these countries, and amongst the top 10 investors in that IPO was one of the large sovereign wealth funds.

So, I think that it is going on. It is on their minds. I think they are wanting to try to keep it at a fairly confidential level to not raise the political implications of what they're doing. So, I do genuinely think that their primary mission is preserving capital and maximizing returns. But they also know there's benefit both to their countries and, frankly, to their investment returns if they can draw connections between the investments they make and what's happening economically in their country and where they're making the investment.

MR. WEST: Question over there on the side?

MR. CHEN: Chao Chen, (inaudible) correspondent, Bethesda, Maryland.

If I may, I would like to get to very fundamental issue. GAO in 2009 have a report and it said that American political and policy elite are not interest in the issue we talk about. If they're not coming up to lead, I think no matter how good design you have or what good thinking you talk about, then you get nowhere.

Thank you.

MR. KIMBALL: Part of our goal is to help educate and inform American policymakers about the issues in this area. And I think now there are so many fiscal pressures on government at all levels in the United States -- local, state, and federal -- that there's an opportunity, although there's also a risk as well, because sometimes in past periods of fiscal distress, you know, America turns protectionist. We get xenophobic. We bash foreign investments. So, our hope is that we can help people understand the upside as well as ways to mitigate risk in a way that then helps all sides involved in this issue.

MR. ZWIRN: If I could just add, you fairly quote from that GAO report that we cite in our paper, but since that report came out, there have been some developments that, to my mind at least, suggest that the environment is changing somewhat. And it's really coming from this administration, which I think increasingly appreciates the role some of these foreign investors have played in alleviating the severity of the financial crisis. We should all know that sovereign wealth funds took substantial positions in American financial institutions and absorbed substantial losses in the crash of 2008, which they have since recovered from, to a large degree, as those institutions have become healthier and their share prices have returned to stronger levels. But they were a very stabilizing force during that period.

Just a few weeks ago, when the Obama administration was looking to try to exit some of its capital invested in AIG, it approached sovereign wealth funds, including the Singaporean sovereign wealth fund, GIC, seeking potentially up to

$20 billion investment in AIG, again, you know, in an effort to try to try to recoup some of that money that was put into those institutions at the crash. So, I wonder if there is a growing appreciation among some in this administration in Washington generally about the constructive role that some of these investors have played in the past two years.

MR. WEST: Question right there, this gentleman.

MR. RAJKOMAR: Hi. Sotea Rajkomar from the World Bank Treasury speaking in my personal capacity.

One way of addressing this issue of transparency, which keeps on coming up, would be to try to create a level playing field and link it with the transparency standards for -- for instance, the hedge fund industry or for large privately held companies which invest globally, around the world, and have very limited public disclosure requirements, because they're not traded on the exchange. That might help to sort of bring the two sides together, make it much more comfortable for both, and also avoid this issue where there's this perception that there will be a financial loss as a result of this insistence on transparency.

Thanks.

MR. GOLDSTEIN: Well, I think -- I mean, as Rick was mentioning and Gordon, sovereign wealth funds fundamentally act like very large pensions, and there are a lot of -- there's a lot of precedence in the state pension fund community for very detailed disclosure regarding holdings that has certainly not limited their ability to be competitive in the marketplace.

In terms of prescribed action, I think there's -- we allude to the fact that in the paper that in certain instances there's not necessarily a tremendous amount of incentive for compliance around transparency, and there are arguments out there that would suggest that say that to the extent that you had a level playing field, as you call it, created by a regime of transparency. In order to incentivize that, you might create differentiated levels of activity that could be engaged in by actors that had different levels of transparency. In terms of whether you had -- similarly like you have in public markets or in the regulation of financial institution ownership, there might be certain aspects of a GPI that might allow it to own up to 9.9 percent versus 14.9 versus 24.9 in a U.S. entity, et cetera.

I think at the same time there is some resistance to making -- you know, creating kind of very black-and-white criteria and risking -- signaling to the GPIs that there's -- that all of the responsibility is incumbent upon them as opposed to more the two-way street that we discussed here.

MR. WEST: Other questions? Yes, in the very back, there's a question.

MS. ALEXANDER: Hi. I'm Nancy Alexander with the Heinrich Boell Foundation.

And it would seem as though kind of broader consideration of this topic could be informed by an assessment of, you know, the bilateral and regional and multilateral investment treaties that the U.S. is part of, because some of these treaties give foreign investors greater rights than domestic investors. And so if you have a large foreign investment presence in infrastructure services or another sector covered by, for instance, a bilateral investment treaty, then in many cases that foreign investor can bring a claim against a municipality, against the country that would be heard in an international arbitration court. And sometimes we think about these treaties as just -- or these trade agreements as just covering exports and imports of goods but pertains to all services and procurement, land ownership, any number of areas. So, I'm really wondering what kind of scholarship is going on to better inform policymakers about the pros and cons of these agreements for the presence of GPIs.

Thank you.

MR. GOLDSTEIN: We looked through the academic literature on this area, and there are -- there is research on various aspects of it, like transparency, which we talked about, has attracted a lot of attention. But in terms of the specific topic that you've mentioned -- the bilateral investment treaties -- I have not personally seen research on that, and so I think it kind of tells me there are many important aspects of this topic where we do need further research. And certainly one of the things we hope to stimulate out of this discussion is more interest in the topic, more research, and more understanding. So, I think the point you raise obviously is very important, and there are other aspects of sovereign wealth fund and GPI investment practices that we need to understand.

MR. WEST: Other questions? I think we have time for one last question, so we'll give you that question.

MS. ROCHELLE: I'm Helen Rochelle, Resources for the Future.

I'm wondering which foreign countries would invest in a green bank for United States development of replacement of the oil that the oil exporting countries depend principally on for their own wealth and why China wouldn't prefer to invest in sustainable energy in its own country rather than in its competitor, United States.

MR. KIMBALL: I think you raise a very logical question, and so what that -- in my mind, we need to be able to be attractive enough, to China for instance, to be a place to do that. And so while China's done -- China is investing a lot in alternative energy and green technologies, and they've got a, you know, huge body of engineers and scientists that they're producing. I think we pretty consistently in the United States have shown ourselves to be pretty good innovators. So, presumably we have to show that we've got some innovations here that are valuable to them, that they're going to get an attractive financial return to invest in those technologies and help accelerate the development of these, and presumably a selfish interest for them would be to ultimately manufacture some of that equipment that maybe is developed by our green technology companies here in the U.S.

MR. ZWIRN: I thought some of the oil countries were investing in green technology. They are?

MS. RAMACHANDRAN: Yeah. That's right, they are.

MR. ZWIRN: I think they're sort of hedging their bets, if you like, on the energy front.

MR. KIMBALL: That's right.

MR. WEST: Okay, we're out of time, but I want to thank Rick, Vij, Dan, Gordon, and Martin for their comments on this subject, and also thank you for coming out. So, thank you very much. (Applause)

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