65

IPRIS Viewpoints

JULY 2011

Portugal and the craving for sovereign funds

PEDRO SEABRA
Portuguese Institute of International Relations and Security (IPRIS)

In May 2009, amid a brewing international financial crisis, former Portuguese Foreign Minister Luís Amado's words could not have been more explicit: "we need investments by sovereign funds in Portugal".[1] As simple as that, Portugal's needs were clearly stated. Indeed, the early ripple effects on the Portuguese economy were, at that time, already in front display and national authorities scrambled throughout the world in the search of credible heavy-weight investors, willing to take a chance in places where markets were growingly wary. In this context, for Portugal as well as for other troubled economies, the vast financial muscle that sovereign funds so discretely but clearly exert became an understandable target for any active economic diplomacy.

However, despite the clear official and public will to attract this specific kind of foreign investment, much of their actual concept, purpose and structure have often evaded extensive public scrutiny. Still, according to the Sovereign Wealth Fund Institute (SWFI), Sovereign Wealth Funds (SWF) can be defined as state-owned investment funds composed of financial assets such as stocks, bonds, real estate, or other financial instruments funded by foreign exchange assets. These assets can include: balance of payment surpluses, official foreign currency operations, the proceeds of privatizations, fiscal surpluses, and/or receipts resulting from commodity exports. Moreover, since they tend to prefer returns over liquidity, they usually have a higher risk tolerance than traditional foreign exchange reserves, which leads to, among other things, a significant diversification of their investment portfolio. In addition, it is not that unusual to witness these funds occasionally substantiating comprehensive domestic and foreign political agendas of their own countries.

In this context, one should attempt to analyze the results of Portugal's apparent willingness to attract such financial instruments. With an eye on emerging economies and countries with whom Portugal seldom did business before, Minister Luís Amado briefly explained the working rationale for Portuguese diplomacy in another interview in July 2010: "Portugal has to show itself in these markets and in these countries, demonstrate the conditions of its economy, its potential for technological development, the investment projects for the application of capital from sovereign funds who search for opportunities in the middle and long-run".[2]

1 Luís Amado interviewed by Francisco Teixeira, "Precisamos de investimento de fundos soberanos em Portugal" (*Diário Económico*, 22 May 2009), p. 42.

2 Luís Amado interviewed by Luisa Meireles, "Europa deixou se ser o centro do Universo" (*Expresso*, 24 July 2010).

With this reasoning in mind, one particular market quickly began to be targeted by Portuguese authorities. Indeed, the Middle East,[3] and specially Qatar and the United Arab Emirates (UAE), clearly stood out among Portugal's priorities in its search for investments from sovereign funds. In all fairness, this interest did not exactly come as a surprise since these two countries own nothing less than eight SWFs alone with an estimated worth of over US$804 billion, all combined.[4] The possibilities that the investment of their massive oil revenues in business opportunities abroad entail are thus basically limitless. Hence, as far as Portugal was concerned, this was undoubtedly a lucrative niche to explore.

That much explains the consecutive visits made by Portuguese and Qatari officials in the past four years to a level never before seen in bilateral relations, and essentially aimed at laying the institutional ground for new investments in a nearby future.[5] Unsurprisingly, the sale of Portuguese public debt was also consistently brought up.[6] Meanwhile, the UAE, through Abu Dhabi's own IPIC, has since 2008 held a 2% stake in Portuguese energy company Energias de Portugal (EDP), apparently with intentions to eventually expand its assets into other economic sectors.[7]

But while Portugal officially sought to lure Middle Eastern capitals into the country, another sovereign fund had in the meantime already established itself as an inconspicuous investor for many national companies. Indeed, worth nearly US$571 billion, Norway's Government Pension Fund – managed by Norges Bank Investment Management (NBIM) – has long been setting its eyes on Portuguese business opportunities. As of December 2010, Norges Bank held participations in 20 companies, worth in total nearly €920 million – a steep increase from the €615 million in 2009. What's more, it also owned €316 million in Portuguese public debt.[8] And in 2011, besides the qualifying stakes in EDP, papermaker Altri and commercial catering group Ibersol, Norway's fund even reached a 5.09% share in telecommunications company Portugal Telecom (PT),[9] 2.06% in multimedia company ZON[10] and another 4.98% in cement-maker conglomerate Semapa.[11]

On the other hand, interest in the Portuguese economy also surged form another unexpected source, this time Timor Leste. With an estimated US$6.3 billion largely emanating from the Baya-Undan oil field revenues, this Southeast Asian nation's sovereign fund is nevertheless bound, since its creation in 2005, by a strict set of rules that requires 90% of its total to be invested in US Treasury bonds. In that sense, when President José Ramos-Horta announced in November 2010[12] his country's disposition to acquire some of Portugal's public debt, bureaucratic hurdles soon arose around a necessary revision of the sovereign fund's legal provisions. But even though this is still an ongoing process, Timorese authorities have not hesitated to persistently reaffirm their commitment to future investments in Portugal.[13]

With these examples in mind, some considerations are inevitably in order. First and foremost, in the present international economic framework, the appeal that sovereign funds possess over many capitals in the world at large is utterly undeniable. When cyclic crises arise, money frequently runs short and governments immediately scramble to secure new safe sources of investment for their beleaguered economies, which in turn may or may not, after the storm has passed, remain as stable shareholders in the companies and sectors that they had previously selected and invested on.

Indeed, it should be dully noted that "[s]ome funds, such as Norway's, behave as capitalists bent on making as much money as they can. Others may have 'strategic' goals – to nurture national champions, say, or to galvanize regional development" or even to promote greater ties between two countries[14] – Timor Leste's intentions regarding Portugal, for example, can surely fall in the

---

3 For a brief overview of Portugal's relations with countries in this region, see Diogo Noivo, "Portugal and the Arabian peninsula" (*IPRIS Lusophone Countries Bulletin*, No. 7, May 2010), pp. 4-5.

4 These include the Abu Dhabi Investment Authority (ADIA), the Qatar Investment Authority (QIA), the International Petroleum Investment Company (IPIC), the Investment Corporation of Dubai (ICD), the Mubadala Development Company (MDC), the RAK Investment Authority (RAKIA), the Emirates Investment Authority (EIA) and the Abu Dhabi Investment Council (ADIC).

5 Foreign Minister Luís Amado traveled to Doha in April 2008, in July 2009, with former Prime Minister José Sócrates in January 2011 and twice the following May, first to attend a meeting of the International Contact Group over Libya, and soon afterwards for the 11th Doha Forum. In turn, Qatari Emir Sheikh Hamad Bin Khalifa Al-Thani visited Portugal in April 2009 while Prime Minister and Foreign Minister Sheikh Hamad Bin Jassim Bin Jaber Al Thani traveled to Lisbon in May 2010. See for example, Maria de Deus Rodrigues, "Diplomacia: Qatar anuncia intenção de investir fundos soberanos em Portugal" (*Lusa*, 10 April 2008); Luís Reis Ribeiro, "Fundos árabes interessados nas privatizações portuguesas" (*i*, 27 July 2010).

6 Lurdes Ferreira, "Luís Amado diz que Portugal está a tentar vender dívida ao Qatar" (*Público*, 17 January 2011).

7 Stanley Carvalho, "Abu Dhabi's IPIC buy 2 pct stake in EDP" (*Reuters*, 9 April 2008); J. Palma-Ferreira, "Emirados Árabes vão investir em Portugal" (*Expresso*, 17 January 2011).

8 See Norges Bank, "Annual Report 2010"; Rui Barroso e Eudora Ribeiro, "Fundo soberano da Noruega mantêm a aposta em Portugal" (*Diário Económico*, 21 March 2011), pp. 36-37.

9 Cátia Simões, "Norges Bank reforça para mais de 5% na PT" (*Diário Económico*, 24 March 2011).

10 Ana Luísa Marques, "Banco Central da Noruega passou a deter participação qualificada da ZON" (*Jornal de Negócios*, 20 May 2011).

11 "Banco Central da Noruega deixa de ter participação acima de 5% da Semapa" (*Jornal de Negócios*, 15 June 2011).

12 "Timor-Leste disponível para comprar dívida portuguesa" (*Lusa*, 14 November 2010).

13 "Compra de dívida portuguesa é investimento que interessa a Díli - PR Ramos-Horta" (*Lusa*, 1 July 2010); "Presidente de Timor reafirma interesse em comprar dívida" (*Lusa*, 6 July 2011).

14 "Sovereign-wealth funds: Assets-backed insecurity" (*The Economist*, 17 January 2008).

latter category.[15] A few can even hold less transparent agendas, with inherent unsettling consequences whenever developments go sour, as it recently happened with Libya's Investment Authority.[16]
However, amid growing international demand for greater financial muscle and visibility by such instruments, it is not difficult to understand why Portugal is not an exception among all the other 'recipient' countries. The need for considerable financing, whether in the purchase of public debt or of qualifying positions in national flag companies, are of paramount importance to the survival of the current economic model, and as such, suspicions surrounding the frequent lack of transparency of some of these funds or even fears of over dependence on foreign powers will certainly not be any kind of a deal-breaker in the immediate future.
One needs only to look at the Linaburg-Maduell Transparency Index classifications to prove this argument right. For example, Norway's sovereign fund is currently graded 8 – with 1 being the lowest and 10 the highest – but the Timorese fund is only ranked at 6th place. On the other hand, Arab funds are not exactly the epitome of transparency, with the disclosure of public data varying considerably from one to the other.[17] Nevertheless, as demonstrated above by the expansion of investments and exploratory contacts, these disparities in public accountability have in no way affected Portugal's willingness to seek out such funds capital.
It is therefore safe to say that the only presently relevant question regards the level of emphasis that the new government in Lisbon will actually confer to this particular foreign overture. Evidently, Prime Minister Pedro Passos Coelho and Foreign Minister Paulo Portas are fully aware of the daunting economic and financial situation that the country still faces, and will most likely continue to face in the next couple of years. Hence, it is not overly farfetched to assume that the country's new leadership will carry on courting major sovereign funds in an attempt to counterbalance the distrust of international markets. Even more, it is only expected that such efforts be stepped up a notch, specially when the upcoming major privatizations that have already been announced are taken into consideration.[18] The fact that news has begun to circulate pointing to an interest by, among others, Arab sovereign funds in such future bids, should then come as no surprise.[19]
But probably the most valuable lesson that the new government ought to learn from its predecessor is that such new intended flows of foreign capital will only be available after much backstage diplomatic work, as the case of Qatar and UAE's funds precisely reflects. In that sense, officially claiming that Portugal is "on the hunt" for any sovereign fund who might be interested in investing should not be an imperative for Portuguese authorities – not the least because that fact has already been made abundantly clear. Instead, Portugal has to recognize that only steady high-level political contacts can, at this point, generate the kind of trust and appeal that in the end attracts such foreign investments. In truth, it amounts to nothing short of a laborious undertaking with dividends only sure to arrive on a mid-term basis. Still, as opportunities abroad begin to dwindle and as traditional financial investors remain persistently skeptical, sovereign funds will most certainly continue to be a mandatory target for Portuguese economic diplomacy.

15 In fact, José Ramos-Horta's idea is to coordinate efforts with Brazil and Angola in order to demonstrate these countries' full confidence in Portugal's recuperation and stability. See "Brasil, Angola e Timor devem comprar dívida para moralizar mercados - Ramos-Horta" (*Lusa*, 18 April 2011).

16 See for example, "Sovereign-wealth funds: From Tripoli to Mayfair" (*The Economist*, 10 2011); Natsuko Waki, "Secretive Libya wealth fund vital for reconstruction" (*Reuters*, 22 February 2011).

17 The IPIC – at the moment the only Arab sovereign fund publicly investing in Portugal, through its share in EDP – is presently not evaluated by this specific ranking due to the lack of public data.

18 Elisabete Felismino e Ana Maria Gonçalves, "Governo antecipa privatização da EDP e REN" (*Diário Económico*, 1 July 2011).

19 Hermínia Saraiva, "Brasileiros, árabes e chineses interessados na EDP" (*Diário Económico*, 4 July 2011).

EDITOR | Paulo Gorjão
ASSISTANT EDITORS | Laura Tereno • Vasco Martins

DESIGN | Atelier Teresa Cardoso Bastos

Portuguese Institute of International Relations and Security (IPRIS)
Rua Vitorino Nemésio, 5 - 1750-306 Lisboa
PORTUGAL

http://www.ipris.org
email: ipris@ipris.org


www.edp.pt
Dow Jones Sustainability Indexes
Member 2010/11
1st
EDP ranks top 1 worldwide in the Dow Jones Sustainability Indexes, in the electricity sector. It reflects our role in the economical, environmental and social dimensions.
For the third consecutive year, EDP is listed on the Dow Jones Sustainability Indexes, the most widely quoted stock market indicators to track the financial and sustainability performance of companies. This year we are the worldwide leader in our business sector, a recognition that rewards EDP's commitment to sustainable development. A company capable of creating wealth without ever losing sight of the social and environmental aspects. This is the way EDP performs, which reflects all our employees and stakeholders engagement for a better future.
UKAS
edp
feel our energy