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Introduction

Sovereign wealth funds (SWFs) are state-owned investment funds composed of financial assets such as stocks, bonds, property, precious metals or other financial instruments. SWFs invest globally and most of them are funded by foreign exchange assets. They may have their origin in commodities (created through commodity exports, either taxed or owned by the government) or assets transferred from official foreign exchange reserves.

SWFs have been present in the financial world since 1953, when the first of them, the Kuwait Investment Board, was set up. Nevertheless their rapid development and growth of prominence is a rather new phenomena. Their growing position in the world, in terms of asset value as well as number of funds, has been observed in the world since 2005.

Although there has been vivid academic debate as to what extent SWFs are motivated by political reasons (this topic is addressed in Chapter 2), it is rather clear that countries can use state-owned investment funds as a tool of their foreign policy. Such danger was addressed by the IMF and its Santiago Principles (the document that set out the common standards regarding transparency, independence, and governance of SWFs), noticed also by the EU as well as various academics and experts.

Therefore, in our study we made an assumption that SWFs are instruments of state policy, serving to their national interest. This is very much in line with realism, one of the most prominent theories of international relations, that focuses the attention of scholars on the concept of power and the notion that states pursue policies that maximize their power through various means. SWFs in this context are perceived as instruments of economic statecraft (see: Chapter 2).

The complementary theoretical approach focuses on the state and its role as an independent economic agent. As rational economic agents, states seek the best possible ways to maximize their wealth, they try to take advantage of available opportunities and invest their funds where the highest expected return can be found. Looking through this prism then we come to find that investor states employ their SWFs for commercial purposes, with special emphasis on the management of national wealth.

There are also other explanations for the behavior of SWFs (see: Chapter 2), but those two are the most important to conceptualize our theoretical approach. We would like also stress that taking into account the dynamic nature of SWFs and multiplicity of their goals, any single theoretical perspective would be inadequate to explain their behavior.

This book looks at SWF activities in Central and Eastern Europe (CEE). Since entering the European Union (EU) in 2004 the investment attractiveness of Poland and other countries in CEE has grown. Consequently, foreign investors have become increasingly interested in investing in the region than before. As such, it should not be surprising that, SWFs have also begunfinancial activities in CEE.

The main goal of this book is to determine the main motives for SWF presence in CEE. Are the potential financial gains the only reason behind their investments? Are SWF activities in the region dangerous for the stability and security of the CEE countries?

Our hypothesis was that SWF investments in CEE are not only financially driven, with the political motives of their investors, wishing to see reached, also being a factor. This could create potential security threats for Poland and other countries in the region.

Answering the abovementioned questions contributes to the academic discussion about SWF strategies and deeper understanding of the motives behind SWF operation. It is also part of the debate about security risks linked with the growth of global investment activities by states. We hope that this interdisciplinary work will contribute to two fields: political science (notably international relations) and economics (investment management). In particular, the following aspects will be dealt with:

Political science:

1. A better understanding of SWFs as a policy tool used by states in the era of globalization.
2. An insight into the mechanisms of foreign policy used by the global economic powers. The book will help understand the strategies, goals and foreign policy agendas of these countries.

Economics:

1. A review of SWF investment strategies, in particular regarding the balance between investment efficiency and the pursuit of political objectives.
2. Formulation of socioeconomic conclusions in the context of attracting SWFs whose investment strategies are perceived (by the host countries) as desirable and mitigating the outcomes of SWF investment and non-investment engagement, potentially detrimental to the interests of the CEE countries.

Given the qualitative and quantitative character of the research, the methodology will draw on both approaches. In essence, the methodology will enable a thorough and empirical-based testing of the primary research proposition as to the existence and significance of non-investment objectives in the activity of global SWFs operational in the selected CEE economies of: the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland and Slovakia.

In our research we covered seven EU member states. Originally we planned also to analyze two other CEE countries: Ukraine and Belarus. However, it turned out that those countries have not attracted any SWFs investments.

This research study is based on empirical data gleaned from the Sovereign Wealth Fund Institute Transaction Database – arguably the most comprehensive and authoritative resource tracking SWF investment behavior globally. In the database (till mid 2014) 11,633 SWF transactions were catalogued, including 1,118 domestic investments with a value USD 174.1 billion and 10,515 foreign investments with a value of USD 675.8 billion. Therefore, about 90% of the number of SWF investments and about 80% of the total value of SWF deals are cross-border transactions. Combining this database with additional media sources we selected 47 transaction in CEE, valued at USD 8.274 billion. The full list of transactions is presented in Annex 9.

Certainly, the outcome does not pretend to be fully comprehensive of all SWF activities in the region. SWFs are widely perceived as relatively opaque even among alternative investment managers. Due to this fact their investment activity is commensurately obscure. SWFs often operate through special purpose vehicles (SPVs), which complicates identification of their beneficial ownership or accurate and timely portfolio compositions. Moreover, the majority of sovereign wealth funds are notorious for inferior standards of transparency measured via the Linaburg-Maduell Transparency Index. Suffice it to say that only 4 out of the 12 biggest SWFs, managing 80% of total SWF assets, scored more than 6 out of a maximum of 10 points and can be perceived as relatively transparent. However, considering the aforementioned constraints and inevitable simplifications, it can be claimed that we managed to collect a sufficient probe to enable the postulation of academic conclusions.

Our research activities presented in the book were limited by a number of practical factors, such as:

- relative opacity: SWFs, as (largely) unregulated institutional investors do not offer lofty standards of institutional transparency, which is likely to complicate an in-depth and comprehensive analysis;
- limited history: SWFs are a relatively novel form of alternative investment management: this by definition limits the time horizon of empirical research and the scope for far-reaching systemic conclusions and policy recommendations;
- uniqueness: every SWF pursues its own strategy (a function of the political agenda set by its creators/contributors); due to the variations in SWF activity any aggregate conclusion could be precarious.

The book is a result of the research project "The Political Impact of Investments of Sovereign Wealth Funds in Central and Eastern Europe Political" financed by the (Polish) National Science Centre (Decision no. DEC-2012/07/B/HS5/03797). The project was implemented in the years 2013–2015 by a team of researchers engaged by the Faculty of International and Political Studies at the University of Łódź.

The team of authors involved on the creation of this book is composed of three political scientists and two economists of diverse ages and academic backgrounds. This makes a persuasive case for a well-rounded and balanced piece of research (between political science and economics) and will enable a comprehensive approach to the study.

The book is divided into seven chapters. Chapter 1 presents the SWFs from the economic point of view. It encapsulates the most recent findings on SWF investment activity globally. The author discusses the position of global SWFs among conventional and alternative asset managers, SWF allocation strategies, their recent investment behavior and its likely evolution in the foreseeable future. Chapter 2 conceptualizes the political significance of SWFs. The analysis starts from the concept of economic statecraft, its instruments and position of SWFs in this context. Then a review of the academic discussion concerning motives behind SWF activities is presented, with a central question about the importance of political ones being addressed. Finally, the list of risks that should be taken into account as long as SWF investments in the CEE are concerned are outlined. Chapter 3 looks at the problem of the global competitiveness of CEE financial markets. The assessment is made using quantitative and hybrid metrics of financial center development while placing particular emphasis on competitiveness drivers relevant to the activity of global SWFs in the CEE region. Chapter 4 offers an overview of SWF investments in CEE. This chapter also aims to inquire into the possible reasons for the relatively low investments by presenting them and analyzing their specificity.

The case study section starts from Chapter 5 that looks at the role of SWFs in China's policy toward CEE. Despite a visible growth of economic ties, Beijing presented a very limited will to use investments as a political instrument in the region. Chapter 6 presents the picture of portfolio and political implications of Norway's SWF investments in CEE. However, seeing as the Norwegian fund is the most transparent one, it is also probably the most politically biased. The final chapter gives insight into Gulf Cooperation Council (GCC) countries, which invest in CEE through their SWFs. It analyzes the main directions of these investments, political and economic interests behind them and finally concludes with the political risks analyses. A summary of all these findings and comparative analyses of all three cases studies are presented in the concluding section, at the end.