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High-rise residential towers under construction are pictured behind an old residential building in central Mumbai September 9, 2011. Vivek Prakash / Reuters

India's allure for sovereign wealth funds

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Sovereign wealth funds have been quietly making moves to India as the value of assets in more established markets elsewhere in he world have fallen.

Why is India of interest to sovereign wealth funds (SWFs)?

The country has for long been on the radar of many SWFs, but it has only recently opened up more to institutional investors who picked up on India's growth story.

"Traditionally SWFs have not invested huge amounts of money in India because of its volatility and rela ively low ability to absorb dollars but have had their focus in Europe instead," says Raj Bhatt, the chairman of Elara Capital, based in Mumbai.

"But because of changes in the global economy and growth opportunities presented in India, the funds have started to look this way."

India's story has become so important that GIC, a Singapore-run sovereign wealth fund, recently opened an office in India.

"Strategically, India is an important developing country in the Asian region and globally, and he next level of healthy grow h is expected to happen in India, thanks to its robust consumption story," says Amar Ranu, a senior manager of third party products research at Motilal Oswal Weal h Management.

"India also seems important from geographical diversification and is poised to share a big pie in the ring-fenced club of elite countries in the near future."

The stability of sovereign weal h funds enables them to engage in longer-term strategic opportunities, making them an ideal match for countries like India.

The Indian government has realised the importance of tapping into such capital pools.

"This matches well with India's needs for capital for building up its infrastructure, energy and healthcare sectors that require patient capital," says Richie Sancheti, a senior associate at he legal and tax specialist Nishith Desai Associates.

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SWFs make their mark with Indian investments

Australia's Future Fund Board of Guardians The fund's money comes mainly from budget surpluses. It was created in 2006 as part of the Future Fund Act and invests in domestic and international shares, private equity funds, property, infrastructure, debt and alternative assets. The fund has about US$60 billion (Dh220.39bn) of assets, says the Sovereign Wealth Fund Institute (SWFI)

Brunei Investment Agency The Brunei Investment Agency is owned by the government of Brunei. The money for the fund comes mainly from the country's oil and gas revenue. This is another highly secretive investment agency and very little is known about its investments or methodology. In 2009, the fund reportedly had assets worth $30bn under management.

"These spaces should attract the SWF [sovereign weal h fund] attention as they have capacity for larger capital deployment opportunity matched with ability to generate higher returns."

Globally, there have been sensitivities around SWF participation in local markets because of political and strategic tensions.

"While certain jurisdic ions are sensitive to which players to permit and how much leeway should be offered to SWFs, India seems to have taken a more liberal approach to SWFs at this point, as they could provide the necessary scale and quality of investments that the country needs for infrastructure and o her sectors," says Mr Sancheti.

Investors across Indian asset classes have learnt their lessons over the years, the experts say.

"India became the growth story and investors woke up to it in 2006; the investment and poli ical climate was very good," says Shobhit Agarwal, a joint managing director of capital markets at Jones Lang LaSalle India.

"Today, the attractiveness is still here because the fundamentals have not changed.

China's National Social Security Fund (CNSSF) The CNSSF works independently from the Chinese government, but it is managed on a ministerial level. The fund was established as a reserve for the country's social security system to support its citizens through economic hardship, and the government makes regular payments to the fund. According to the SWFI, the assets managed by CNSSF are worth about $146bn.

GIC GIC is fully owned by the Singaporean government, although it acts as an independent company. It needs government approval for certain functions such as the appointment of directors. The GIC manages funds on behalf of two clients, the government of Singapore and the Monetary Authority of Singapore. It was established in 1981 with a view to boost the country's wealth fund and invest in higher-yielding assets with long-term holdings. GIC has assets worth $247.5bn, said the SWFI.

Temasek Similar to GIC, Temasek is a company owned by the government of Singapore. It manages funds on behalf of the government with a major focus on local investments as well as elsewhere in Asia. Temasek operates like a company, although it has certain concessions such as the fact that the country's president approves senior-level appointments and the company is audited by the government. Temasek Holdings has assets worth $122bn, according to the SWFI.

"But funds are more value-driven than they were hen, and the second wave of money is much more value-conscious and has learnt from he first wave of investment."

So what kind of targets are the SWFs after in India?

Stakes in publicly listed companies are always a good long-term bet for those careful fund managers.

"There is no doubt that equity remains the top priority for any sovereign wealth funds investing in India as India stands cheaper in terms of valuation in comparison to other emerging countries," says Mr Bhatt.

Bricks and mortar is always a good bet, the experts note.

"In India, infrastructure needs a huge boost; so, in lieu of returns and future growth, SWFs have been inves ing in real estate directly or through real estate private equity funds.

"In a nutshell, they aim to diversify their portfolio geographically and also multiply their returns at a faster pace," says Mr Bhatt.

"Some of the SWFs have a mandate to diversify their portfolio geographically in emerging nations, and India better fits their portfolio, as India offers a strong growing opportunity among other emerging na ions," says Mr Ranu.

On the debt instrument side, there are limitations, however. "The high interest rate scenario in India which leads to high interest rate arbitrage relative to developed countries also make one of the other options to invest into," Mr Bhatt notes.

"However, the government has set limited allocations to SWFs for investing into corporate bonds and the window opens as and when the government thinks it prudent."

The Indian government regards SWFs as important and made hings a little easier last year when a takeover code was introduced by the Securities and Exchange Board of India (Sebi), the country's financial regulator.

It allows SWFs to acquire a much larger stake in a local public listed firm without having to launch an open offer for the rest of the company, giving a larger investment window to funds but at the same time allowing companies to retain their independence.

"These SWFs do not participate actively in day-to-day management activities and mainly act as passive investors, hence they refrain from taking higher exposure so as to invite Sebi's rule," says Mr Ranu.

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