Need of Sovereign Wealth Fund for India

For Prelims: **Sovereign Wealth Fund**, **Pension Funds**, **Norway Government Pension Fund Global**, **Global Financial Crisis 2008**, **Planning Commission**, **NIIF**, **Divestment**, **Forex Reserves**, **Non-Debt Financial Resources**, **Current Account Deficit**, **Fiscal Deficit**, **ESG (Environmental, Social, Governance)**, **Hydrogen Energy**, **Semiconductors**, **Biotechnology**, **AI**.

For Mains: Need of sovereign wealth fund for India, Associated concerns and way forward.

Source: FE

Why in News?

India is contemplating creating a **Bharat Sovereign Wealth Fund (BSWF) or The Bharat Fund (TBF)** to tap a **reservoir of national wealth** that lies dormant in India's economy.

What is a Sovereign Wealth Fund (SWF)?

- **About:** SWFs are **government-owned funds** created from **state surpluses**, often from a variety of sources like **natural resources, trade surpluses, or budget excesses**.
  - SWFs help governments generate wealth through **strategic investments,** ensuring **financial stability and economic growth.**
- **Characteristics: Santiago Principles 2008** defines SWFs as having **3 key characteristics:**
  - It is owned by the **general government**, which includes both **central government** and **sub-national** governments.
  - It Includes i**nvestments in foreign financial assets.**
  - They invest for **financial objectives.**
  - These key elements **exclude public pension funds**, owned by policyholders, and **central bank reserve assets,** which are **not invested.**
- **Types:**
  - **Stabilization Funds**: **Absorb shocks** from volatile revenues, ensuring fiscal consistency.
  - **Future Generation Funds**: Invest surpluses for **long-term wealth,** benefiting future generations.
  - **Public Benefit Pension Reserve Funds**: Fund pension systems to meet long-term obligations.
  - **Reserve Investment Funds**: Manage and grow **foreign exchange reserves,** stabilizing currency.
  - **Strategic Development SWFs**: Invest in **key sectors** for national development.
  - **Foreign Currency Reserve Assets**: Maintain **currency stability** and manage global trade power.
- **Examples: Norway Government Pension Fund Global** (USD 1.7 trillion, world's largest SWF), **China Investment Corporation** (USD 1.35 trillion), **Abu Dhabi Investment Authority** (USD 993 billion) etc.
- **SWFs in India:**
  - **2007-08:** The SWF idea in India **gained traction in 2007-08** due to a surge in capital

inflows (exceeding **USD 108 billion in a year**) but lost momentum after the **Global Financial Crisis 2008**.
   - **2010-11**: The **Planning Commission** revived the SWF proposal in **2010-11,** suggesting a **USD 10 billion fund** funded by foreign exchange reserves, PSUs, or budget allocations.
   - **2015: NIIF** was set up that remains **India's main structured investment fund**.

Note: The **Santiago Principles** refer to a set of **24 voluntary guidelines** that promote transparency, good governance, accountability, and prudent investment practices for **Sovereign Wealth Funds (SWFs)**.

- These principles were established in **2008** by the **International Forum of Sovereign Wealth Funds (IFSWF),** a voluntary organisation of **global SWFs.**

Why does India Need a SWF?

- **Unlocking Public Sector Wealth:** A **SWF** could unlock an estimated **Rs 40 lakh crore (USD 450-500 billion)** across **80 listed enterprises** by investing and increasing returns from these state-owned entities.
- **Fiscal Deficit Reduction**: A **2% divestment** from government equity could generate over **USD 10 billion annually**, reducing India's **fiscal deficit from 4.9% to 4.6% of GDP**.
- **Diversifying Investments:** The **2007-09** crisis highlighted the risks of relying on **'secure' securities like US treasuries**.
   - India's SWF could **diversify investments** and seek higher returns.
- **Capitalizing on Excess Reserves**: India's excess **forex reserves**, covering over nine months of imports, could be better utilized to boost **national wealth.**
- **Support for Strategic Sectors**: It can drive **long-term growth and innovation** by investing in sectors like **electric vehicles**, **hydrogen energy**, **semiconductors**, **biotechnology**, **and AI**, positioning India as a global leader.
- **Social Welfare:** SWFs can generate **non-debt financial resources** for social sector commitments, enhancing fiscal flexibility for **welfare programs** and national growth investments.
- **Projecting Soft Power**: SWFs could support **advocacy, incubate ventures, provide disaster relief,** and **invest in SWFs of other nations like Norway** boosting India's international standing and soft power.

What Concerns are Associated with SWFs?

- **Current Account Deficit:** SWFs are typically for countries with **mineral wealth or trade and budget surpluses** but India faces **persistent current account deficits** and a significant **fiscal deficit**.
- **Macroeconomic Risks**: **Global growth slowdown**, rising sovereign debt, and tightening financial conditions could impact SWFs by **lowering investment returns,** straining fiscal health, and increasing financial instability.
- **Geopolitical Tensions**: Geopolitical tensions and the shift away from **globalization** could disrupt SWF **investment strategies**, affecting **cross-border investments**, supply chains, and trade policies.
- **Environmental Risks**: SWFs risk losses from **climate-exposed industries and stranded assets** if environmental policies fail, particularly in **fossil fuels.**
- **Technological Vulnerabilities**: SWFs managing large sums of public money face **growing risks of fraud and data theft**.
   - Rapid advancements in technology could disrupt traditional investment models.

Way Forward

- **Clear Governance Framework:** Establish a clear **legal and regulatory framework** to ensure **transparency, accountability, and compliance** with the **Santiago Principles** for best practices in SWF governance.

- **Strategic Asset Allocation:** Invest in high-growth sectors such as **AI, biotechnology, EVs, and semiconductors** to enhance India's global standing.
  - Consider **co-investment models** with global funds to **leverage expertise.**
- **Fiscal Prudence:** Implement **phased allocation** of resources, ensuring a balance between **fiscal deficit management and investment goals**.
- **Risk Management:** Develop strategies to **mitigate macroeconomic risks**, including market volatility and financial crises.
  - Adopt **ESG (Environmental, Social, Governance) principles** to **avoid stranded assets** in climate-sensitive sectors.

Drishti Mains Question:

What are Sovereign Wealth Funds (SWFs)? Discuss its potential benefits and associated concerns in India?

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims

Q. With reference to 'National Investment and Infrastructure Fund', which of the following statements is/are correct? (2017)

1. It is an organ of NITI Aayog.
2. It has a corpus of `4,00,000 crore at present.

Select the correct answer using the code given below:

(a) 1 only

(b) 2 only

(c) Both 1 and 2

(d) Neither 1 nor 2

Ans: (d)

Mains

Q. "Investment in infrastructure is essential for more rapid and inclusive economic growth." Discuss in the light of India's experience. **(2021).**

Q. Explain the meaning of investment in an economy in terms of capital formation. Discuss The factors to be considered while designing a concession agreement between a public entity and private entity. **(2020)**