Sovereign wealth funds

Sovereign wealth funds move beyond trophy assets

Shift reflects growing 'experience' of investment teams and need for regular income

Luxury items on display at the Louis Vuitton boutique in Moscow © Bloomberg

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Sovereign wealth funds are shifting away from luxury businesses, buying more hotels and increasing their allocations to private deals as they look to offset falling state revenue from lower oil prices, a report on their investment strategies has revealed.

Investment by national funds in trophy assets aimed at wealthy customers, including Tiffany (http://markets.ft.com/data/equities/tearsheet/summary?s=us:TIF), Porsche and LVMH (http://markets.ft.com/data/equities/tearsheet/summary?s=fr:MC), has fallen from $13bn in 2009 to just $1.4bn in 2015, according to the latest figures available for analysis by Madrid-based IE Business School.

By contrast, sovereign wealth funds increased their spending in the hotel sector from $500m in 2012 to $7bn in 2015. The number of direct investments — rather than through a fund — has also increased from 105 in 2012 to 178 in 2015.

Separately, sovereign wealth funds have put $633bn into new investments in private markets, including infrastructure, real estate and tech start-ups, in the three years from 2012 to 12015, according to the analysis, which covered funds from Norway, China and the Middle East among others. That period coincided with rapidly climbing valuations for private companies.

Professor Javier Capape, co-author of the report, said sovereign wealth funds have been struggling recently in light of the drop in oil prices and they are now reassessing their investment strategies.

"The upshot of these shifts and changes in the oil market is that another era of $100 oil is a long way off," the report said. "Those countries that accumulated considerable wealth thanks to high oil prices are going to have to adapt. And the consequences will be far reaching."

Middle Eastern sovereign wealth funds in particular have come under intense pressure as a result of persistently low oil prices, the report added.

"Now that oil prices are lower, the need to diversify the skills base of these economies has arguably assumed greater importance," the report added.

In this environment, Prof Capape said sovereign wealth funds are now looking for assets with steady income streams — such as hotels — to help fund spending at home rather than trophy assets with high brand recognition.

"The report paints a more prudent picture of sovereign wealth funds than people would think," he said.

But the change in tactics is not entirely because of the drop in oil price, which has also taken a toll in Russia and Kazakhstan.

Sovereign wealth funds are also changing their asset allocation as they become more experienced investors.

"With the drop in oil prices sovereign wealth funds have less money to spend so they are more cautious and they want higher returns for the money they invest," said Francesco Rossi Ferrini, vice-chairman of investment banking and head of sovereign wealth funds, at JPMorgan in London.

"They have also been building teams with more and more experience," he added.
