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National policies towards sovereign wealth funds in Europe: A comparison of France, Germany and Italy

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National Policies Towards Sovereign Wealth Funds in Europe: A Comparison of France, Germany and Italy

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National Policies Towards Sovereign Wealth Funds in Europe: A Comparison of France, Germany and Italy

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Abstract

Although France, Germany and Italy are often seen as relatively closed to foreign equity investment, a closer analysis shows that they have often accepted or even welcomed sovereign wealth fund (SWF) investments. In all three countries, there were debates about how to respond to SWFs. But despite initial concerns, there has been considerable support for allowing and attracting SWFs. All three countries have passed legislation regulating foreign equity investment, but the provisions remain limited, as much directed against private equity investors as against SWFs, and have almost never been used. Moreover, SWF investments in individual companies have almost always been welcomed and sometimes actively sought by firm managers and policy makers, including in sensitive and high-profile firms.

1. INTRODUCTION

France, Germany and Italy have a popular reputation of being relatively closed to outside equity investment by factors such as their language, legal restrictions, state 'intervention' and a culture of hostility to outside ownership of national companies. Thus, for instance, the World Bank's ranking of economies for 'ease of doing business' put Germany as 20th, France as 34th and Italy as 73rd, compared with the UK as 7th and the US as 4th, in its 2012 survey (World Bank 2012). Academically too, studies point to several factors that might act as obstacles to sovereign wealth fund (SWF) investment. France is often categorized as a 'statist' economy, in which the state plays a dominant role, notably supporting the firms of French 'national champions', providing finance for firms and leading decisions about mergers and cross-holdings, including of privately owned companies. Germany is often seen as a coordinated or corporatist market economy, where representatives of firms and employees cooperate closely, firms rely on earnings and bank finance for investment, and firms are either privately owned or protected by powerful long-term bank owners of their shares (Schmidt 2003; Hall and Soskice 2001). Italy is often argued to be a mixed market or statist economy, but one with a weak state and heavily reliant on personal and political connections. In all three cases, the economies are seen as relatively closed to outside equity investors. Hence initial

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expectations are that the three countries are likely to be relatively resistant or even hostile to equity investment by SWFs, especially those from non-Western countries.

This policy brief, however, suggests a somewhat different picture. It argues that although political debates were initially hostile to SWF equity investment, this has rapidly changed. Moreover, some of the opposition related more to overseas investors in general rather than SWFs specifically. In line with this, although all three countries placed new legal restrictions on equity investment in the 2000s, these were in fact rather limited and were not specifically targeted against SWFs. Moreover, although numbers of non-Western SWF investments remained limited (compared, for instance, to those in the UK), governments in the three countries increasingly welcomed SWFs and indeed actively sought their investments.

2. France

French policies towards foreign equity investment are complex, as the role of the state and the openness to such investment have changed.[1] Traditionally, French companies were closed to foreign investment. The larger ones were wholly or partially publicly owned directly or indirectly via state-owned banks and financial bodies. Others were majority-owned by families. In any case, firms relied largely on the state for investment capital, rather than on equity capital. Moreover, foreign investment required government approval and the stock market was small. In so far as companies were privately owned, they were often protected by cross-shareholdings. There has been a long tradition of fear of large overseas firms, especially privately owned US ones, which were seen as dangerous competitors to French firms, and policies of creating national or 'international' French champion firms (e.g. Servan-Schreiber 1967; Hayward 1995).

However, from the mid-1980s onwards, this position began to change. Many state-owned companies were privatized. The stock market grew, while state-provided finance declined. European Union law prohibited many restrictions on investment from firms established in other EU member states (including non-EU firms that created subsidiaries), notably 'golden shares' or administrative obligations on investors from other EU member states. Stable cross-holdings of shares began to weaken (Culpepper 2005). After 2002, the establishment of the Euro appeared to aid cross-border investment. Indeed, policies towards foreign direct investment (FDI) changed as France began actively to seek such investment.

[1] For general discussions, see for instance Hall (1986), Hayward (1986), Schmidt (1996, 2003) and Thatcher (2003, 2007).

French policies towards SWFs in the 2000s reflect both the statist inheritance and more recent alterations in the role of the state, resulting in conflicting rhetoric. One strand of political debate has focused on the dangers of overseas takeovers of French firms. The most prominent example was the rumoured attempt by Pepsi to buy the French food firm Danone in 2005, which was met with calls for 'economic patriotism' (Clift and Woll 2012). Parts of the nationalistic right also began to attack overseas equity purchases, including those by SWFs. Moreover, France created its own SWF in 2008, the Fonds Stratégique d'Investissement (FSI), designed to invest in French firms. One explicit reason for its creation, given both by the then president Nicolas Sarkozy and in parliamentary debates, was to prevent SWFs from buying French firms 'too cheaply'.

At the same time, French policy makers have sought to attract SWF investment. There have been repeated visits by senior French officials to selected countries and contacts with SWFs. The best known concerns Qatar, where President Sarkozy went several times during his presidency and indeed afterwards. A report by the Sénat on Gulf SWFs called for France to play a greater role in the recycling of excess petrodollars and to become a 'privileged partner' of Gulf states (Sénat 2007: 44–5). Moreover, in a remarkable volte-face given the rhetoric at its creation, the FSI began to cooperate closely with SWFs in joint investments. Equally, large firms also developed close contacts with SWFs, often in cooperation with state officials. They sought SWF investment as well as joint ventures and orders from the SWF host state. Examples included Areva, which sought orders for nuclear power stations from Qatar and other Gulf Cooperation Council (GCC) states whilst also discussing the QIA (Qatar Investment Authority) and KIA (Kuwait Investment Authority) taking limited stakes, and the European Aeronautic Defence and Space Company (EADS, mostly Franco-German), which has sought defence orders as well as investment from Qatar.

The complex French policy is reflected in the legal structure for SWF equity investment. In 2005 France introduced legislation (in the form of a government decree) designed to ensure state controls over foreign equity investments.[2] Previous legislation in 2003 had been ruled illegal by the European Court of Justice because its definition of foreign investment was too broad, but then Pepsi's rumoured takeover of Danone had raised political controversy. Important parts of the legislation applied to non-EU bodies taking control, defined as control of over one third of shares or voting rights investments, of French firms (based on the headquarters of the firm). It covered certain sectors, notably related to security,

[2] Décret no. 2005-1739 du 30 décembre 2005 réglementant les relations financières avec l'étranger et portant application de l'article L. 151-3 du code monétaire et financier JORF no. 304 du 31 décembre 2005.

information and communication technologies, and defence. Such investments require government authorization. Equally, the decree introduced restrictions on investment by EU firms, which it could block on certain grounds, notably danger of criminal acts or threats to industrial and research and development capacities, security of supply in crucial industries or dangers to defence and national security.[3]

While the decree has attracted much attention, the use of its powers in practice has been very limited. Indeed, the research has found no instances in which they have been applied. On the contrary, the government, public bodies and state-owned firms have actively engaged in cooperation with SWFs. Thus, for instance, in 2009 the FSI signed an agreement of intent with Mubadal, an Abu Dhabi SWF. Equally, the publicly owned Caisse des Dépôts et Consignations, the main state investment bank, created joint funds or partnerships with the Chinese Development Bank and then in 2012 with the QIA. Moreover, a very high-profile (although limited in size) investment by the QIA in French suburbs was announced.

Although the number of SWF equity investments is lower than for the UK (Thatcher 2012), it remains significant and, perhaps of greatest importance, SWFs have made acquisitions in major French firms that have been welcomed and sometimes actively encouraged by the firms themselves as well as the government. These investments include firms in strategic sectors. The most numerous and significant have been by the QIA. Two important examples in defence and high technology were Lagardère and EADS, both very strategic firms. Another was Veolia, whose head, Henri Proglio, then became head of Électricité de France (EDF). Dubai International Capital also bought a stake in EADS in 2007. However, the French welcome to SWF equity investment has also extended to China; for instance, the China Investment Corporation (CIC) has bought shares in GDF Suez, which is majority state-owned, as well as the financial company Dexia.

3. Germany

German companies were traditionally closed to foreign equity investment. The major reason is that very few firms were public companies with shares quoted on stock markets; indeed, there were only 450 listed on the exchanges in 1982, a lower number than in the 1950s (Story 1997). German companies obtained finance from banks and/or their retained profits. Moreover, a system of cross-shareholdings and especially ownership of shares by banks kept stock markets very small. Suppliers in the utility sectors were usually publicly owned.

[3] The 2005 decree was subsequently subject to minor alterations following queries by the European Commission concerning its compatibility with EU law on free movement.

However, this situation began to change in the 1990s and especially the 2000s. A determined policy of developing financial markets, including the stock markets, was undertaken. Bank and cross-shareholdings diminished. Major utility companies, especially in telecommunications and energy, were privatized. Hence the German equity market became considerably more open to foreign purchases.

In this context, the rise of SWFs as well as other large foreign investors in the 2000s was met with concern in Germany. There were worries about the entry of short-term 'speculative' investors, who stood in contrast to long-term relationships built up between German banks and firms through cross-shareholdings, long-term loans and seats on company boards. In 2005, Franz Müntefering, chairman of the Social Democratic Party (SPD), attacked foreign private equity firms as 'swarms of locusts that fall on companies, stripping them bare before moving on'. A second fear was 'state capitalism', in which SWFs from countries that were not open themselves to foreign investment would take over German companies and then use their holdings for political purposes.

Senior politicians and policy makers called for protection against FDI, especially from outside the EU. Several suggestions were debated in 2005–8, notably by Peer Steinbrück (SPD), then the federal finance minister. One was registration and authorization of non-EU investments in German firms. Another was a list of sectors to be protected, notably strategic sectors such as energy and telecommunications. A further proposal was that a German SWF should be set up, to take stakes in major German firms.

Yet despite the concerns about SWFs, there was also strong support for keeping Germany equity markets open and indeed sometimes for welcoming SWFs. For a start, many of the fears were focused on certain countries, notably Russia and to a lesser extent China, rather than others. It is noteworthy that German politicians and certain large firms welcomed and indeed sought investment from SWFs in the Gulf, notably Kuwait and Dubai. A second factor is that calls for protectionism were countered by arguments that openness to foreign investment benefited Germany. Key policy makers, such as the 'liberal' Free Democratic Party (FDP) or major business associations (e.g. the German Association of Chambers of Commerce and Industry) and banks, actively supported 'liberal' economic policies of openness. A further point is that attacks (for instance, Müntefering's comments about 'locusts') concerned private equity investors, including from the US, as much as or more than SWFs, on grounds of their short-termism rather than foreign ownership.

Legislative changes, policies and individual investments reflected these contrasting positions. After much debate, in 2009, an amendment was passed to the Foreign Investment

Act, the Dreizehntes Gesetz zur Änderung des Außenwirtschaftsgesetzes und der Außenwirtschaftsverordnung.[4] It gave powers to the Federal Economics Ministry (formally the Ministry of Economics and Technology) to verify whether a stake of 25 per cent or above taken by a non-EU investor in a German company posed a threat to public order or security. If the Ministry finds that it does, it can impose conditions on the purchase or prohibit it. However, its scope for controlling SWFs is in fact rather limited. For a start, few SWFs take 25 per cent stakes: almost all have been lower. Second, the Ministry is not obliged to undertake an investigation. Third, firms can apply for a 'certificate of non-harm' which protects them against any action under the law. Fourth, the Economics Ministry needs the consent of other ministries to act: decisions are made by the federal government. Finally, there are strict time limits: the Ministry must start its investigation within three months of the share purchase and then complete it within a further two months. After this period, the SWF investment is deemed accepted by default.

While German legislative restrictions on non-EU share purchases were slightly tightened, German policies towards SWFs became increasingly positive. This began before the 2007/8 financial crisis, but accelerated thereafter. Thus even supporters of restrictions on foreign investors, such as Steinbrück, argued that SWFs were welcome (*Handelsblatt*, 21 May 2008). Other ministers argued that interventions under the 2009 law would be very rare and that SWFs, even from China, were very welcome.[5] Several ministers travelled abroad, notably to the Gulf as well as China, underlining that their SWFs were welcome.[6] The research has not found any cases in which the 2009 law has been used against SWF equity purchases.

Indeed, SWFs, especially from the Gulf, have made significant investments in major German firms, and other further attempts to attract SWFs have been seriously discussed. On almost all occasions, the investment was welcomed and sometimes was actively sought by the firm's management and/or senior policy makers. Thus, for instance, the KIA had held a stake in Daimler since the 1970s, and in 2001 was reported to be its largest shareholder, with 7 per cent of shares; it is noteworthy that it did not have a member on the supervisory board. Daimler also welcomed purchases by Dubai Holdings in 2005 (reportedly 2 per cent, sold in 2009), as well as by the Abu Dhabi Investment Authority (ADIA; initially a 9 per cent holding in 2009 but then reduced to 3 per cent). The QIA was also welcomed into Porsch and Volkwsagen. Other companies such as Siemens or the publicly owned railway Deutsche Bahn

[4] For a legal analysis see Theiselmann (2009).
[5] For example, Michael Glos, Economics Minister (*Handelsblatt*, 17 August 2008, 30 January 2009).
[6] For instance, Glos, von Guttenberg and even Steinbrück.

began to look for SWF investors, notably from the Middle East. Sometimes SWFs were welcomed as a protection against hostile takeovers (e.g. Siemens or Hochtief). At other times they were also seen as a valuable source of capital and long-term investors. Finally, share purchases by SWFs were sometimes seen as a means of entering the SWF's home market.

Several of the firms cited are large and politically and nationally prominent. However, in aggregate, the number of significant investments remains small. Equally, SWFs have almost always taken limited stakes rather than majority ones. This however, does not mean that they were insignificant: at times, stakes of 6–7 per cent are the largest ones in the company.

4. ITALY

Traditionally, Italian stock exchanges were tiny compared with those of London or New York, or indeed relative to the size of the economy. Italy had few large firms, with much of the economy in the hands of small to medium-sized companies. Family ownership was high. Even large firms were owned by families or by the state, which directly or indirectly owned a very large proportion of the commercial sector, notably through holding companies such as the Istituto per la Ricostruzione Industriale (IRI). Thus there was little scope for foreign equity investment.

However, from the 1990s onwards, the position gradually began to change. The government pursued active policies to develop the Italian stock exchange. There were international and competitive pressures to develop larger Italian companies. Capital was sometimes in short supply. Economic growth had also been very low, increasing pressure to attract overseas investment.

In the 2000s there was significant debate about whether Italy should welcome SWFs or be wary of them. Leading politicians, including the then prime minister Silvio Berlusconi and finance minister Giulio Tremonti, in 2008 expressed their concerns about SWF entry, as did on a few specific occasions their allies, the Lega Nord (notably in relation to a bank based in Northern Italy, Unicredit). They sought to strengthen defences against SWF equity purchases greatly. However, other politicians, such as the then foreign minister Franco Frattini, opposed altering the regulatory framework against SWFs, while many business leaders welcomed SWFs, notably from Libya. Moreover, the acceptance of SWFs grew after the financial crisis of 2007/8, as the positions of opponents changed sharply, including that of Berlusconi and Tremonti (see below). Under Mario Monti, the government actively sought SWF investment, including that from Gulf countries and China.

The regulatory framework reflects the changing pressures on Italy, both from the EU and internally. General Italian law, notably legislation passed in 1994 (Legge no. 474/1994), provided for the possibility of limits on shareholdings or at least voting rights in companies and sometimes for state special powers, especially in strategic industries, for shareholdings above 5 per cent. These restrictions were challenged by the European Commission and modified. Moreover, stakes of 3 per cent had to be notified to the stock exchange regulator, the Commissione Nazionale per le Società e la Borsa (CONSOB). However, in 2008, there were discussions on restrictions specifically aimed at SWFs. One small political party, Italia dei Valori, which focuses on corruption and was then allied with the left, put forward a proposed law in the Senate suggesting an absolute limit of 20 per cent on the share that SWFs could own in Italian strategic companies. The main argument was that transparency was insufficient and hence limits to investments in strategic companies were necessary. But the proposal was not debated in parliament. In 2008, Berlusconi and Tremonti talked of a 5 per cent cap on SWF share ownership in strategic companies, but their views were opposed by Frattini, who argued that it was unnecessary; and indeed no law was passed. On the contrary, Berlusconi and Tremonti changed tack and began to welcome SWFs publicly.

In 2012, legislation was introduced that modified state powers concerning equity investments in selected sectors.[7] It did not refer specifically to SWFs. It covered the defence sector, where, if the government identified a 'serious threat' to defence and security, it could block the acquisitions of shares, as well as company decisions, or impose conditions on matters such as security of supply or exports of information and transfer of technology. Then in certain other strategic industries – energy, transport and telecommunications – it could block or impose conditions on non-EU buyers of shares in 'exceptional cases of risk' to the security and functioning of networks and continuity of supply, as well as blocking certain company decisions.

Yet while debates grew about foreign investment in strategic Italian firms, at the level of individual companies some SWFs have been welcomed or at least accepted for decades. In particular, Italy has had long links with Libya. As early as 1976, the Libyan Arab Foreign Investment Company (Lafico, which later became part of the Libyan Investment Authority, LIA) bought a stake in Fiat, as the company needed liquidity; the stake was substantial, reaching 15 per cent by the 1980s. This was done and accepted by the government despite Libya's being ruled by Colonel Gaddafi and also despite rumoured US displeasure. The LIA

[7] Decreto legge 15 marzo 2012 no. 21, convertito, con modificazioni, nella legge 11 maggio 2012 no. 56.

sold the stake at a considerable profit in 1986. However, the 2000s saw the return of the LIA, not just to Fiat but across several firms. It and/or the Libyan central bank bought a share in Fiat of 2 per cent, in banks (Banca di Roma, Unicredit and Capitalia), in energy companies (the largest gas supplier, ENI, which had been partially privatized) and in Finmeccanica, the large defence and aerospace conglomerate, with which the LIA signed a memorandum of understanding for a joint venture in 2009. ADIA too made purchases in banks (Banca di Roma, Banca Populare Commercio e Industria). It is also reported as having bought a stake in Mediaset, the media group owned by Berlusconi, who has been Italian prime minister on several occasions. Other SWFs were less active but purchases were made by the Government of Singapore Investment Corporation, while there were discussions of possible purchases by the CIC.

SWF investment in individual companies has almost always been welcomed. Indeed, often it has been sought by the management of companies: prominent examples include the Agnelli family for Fiat in 1976 or Geronzi for Unicredit. One reason for the welcome has been that SWFs have provided valuable capital to owners or to the companies at times of recapitalization. Another is that SWF interest has often been followed by rises in share prices. A further factor is that usually SWFs have been allies of existing managers, both in terms of vote and on the rare occasions when they have had representatives on the board. Indeed, they have occasionally been seen as barriers to hostile takeovers – for instance, in the case of Libyan stakes in Unicredit.

The number of SWF shareholdings in Italy is much smaller than in the UK. However, they include strategic firms, notably banks and Fiat, as well as small but well-known companies such as Juventus. Moreover, while the stakes are limited, they are often significant given that shareholdings can be fragmented. Thus, for instance, the joint stakes of the LIA and the Libyan central bank in Unicredit, one of Italy’s largest banks and a large international Italian company, in 2010 made them the largest shareholders.

5. Conclusion

In France, Germany and Italy, SWF equity investments led to political debate about how policy makers should respond. Concerns and sometimes opposition to SWFs taking shares in major national companies were expressed. Yet the striking feature is that there was strong support for allowing SWFs to buy shares freely. Indeed, policy makers usually actively sought SWFs. Legislation remained very limited, with almost no specific provisions for SWFs or restrictions on their investments. Rather, on occasion, greater opposition to private equity firms, especially from the US, was expressed than to SWFs.

The number of non-Western SWF equity investments remains small compared, for instance, with that in the UK. Equally, most SWF stakes were limited and they have almost never been a majority or even a controlling minority, say 25–30 per cent. Nevertheless, they have been significant at times, especially when share ownership is very dispersed, which makes even stakes of 5–10 per cent important for control. Above all, they have involved major national companies, sometimes in very sensitive sectors such as high technology, nuclear energy and even defence. This indicates the extent to which European countries have remained open to SWF equity investment, contrary to popular views and academic expectations based on traditional views of these economies.

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