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**KEY NOTE SPEECH AT THE
FIRST LUXEMBOURG FOREIGN TRADE
CONFERENCE**

**“OVERVIEW ON THE KUWAIT INVESTMENT
AUTHORITY AND ISSUES RELATED TO SOVEREIGN
WEALTH FUNDS”**

APRIL 9, 2008

Good Morning

- Your Excellency Jeannot Krecke, Minister of Economy and Foreign Trade of Luxembourg.
- Ladies and Gentlemen.

It is a great pleasure to be here today to talk about a subject which has been getting considerable headlines. I will first give a brief overview on the Kuwait Investment Authority (KIA), followed by a discussion on some of the issues which are currently being raised regarding Sovereign Wealth Funds.

Let me begin by giving you a short background on the history of the KIA.

Although the term of Sovereign Wealth Fund is only two years old, the State of Kuwait realized the need of substituting a depleting asset, oil, with financial investments more than 55 years ago. This was achieved by establishing the Kuwait Investment Board in London in 1953, eight years before Kuwait's Independence.

In 1982, the KIA was established to takeover the responsibility of managing the assets of Kuwait from the Ministry of Finance. Today, the KIA manages two main funds; the General Reserve Fund (GRF) and the Future Generations Fund (FGF). The KIA may also manage any other funds entrusted to it by the Minister of Finance. The KIA does not own any of the assets. It is owned by the State of Kuwait. The KIA is only an asset manager.

Our mission is "to achieve a long term investment return on the financial reserves entrusted by the State of Kuwait to the Kuwait Investment Authority by providing an alternative to oil reserves, which would enable Kuwait's future generations to face the uncertainties ahead with greater confidence".

KIA's objectives are threefold:

- KIA aims to achieve a rate of return on its investment that, on a three-year rolling average, exceeds composite benchmark by designing and maintaining an uncorrelated asset allocation, consistent with the return and risk objectives that are mandated.

- KIA will endeavor to be a world class investment management organization committed to continuous improvement in the way it conducts business.
- KIA is committed to the excellence of the private sector in Kuwait while ensuring that it does not compete with or substitute it in any field.

In 2005, the KIA undertook a comprehensive review of its strategy. The purpose was to ensure that KIA aligns itself to industry best practice in all aspects of asset and investment management. During this review, the consultants undertaking the study stated that KIA had one of the best corporate governance structure within its peer group or within the industry.

We are proud that the KIA is one of the most governed bodies. I can say, with full confidence, that we have one of the strongest governance structures in the industry. Some of the features of KIA's governance are:

- We have an independent and autonomous Board of Directors, majority of whom have to be from the private sector.
- The Managing Director is appointed by the Board of Directors from the private sector representatives.
- An Executive Committee of the Board is responsible for monitoring of KIA's activities.
- KIA has an independent Audit Department, reporting directly to the Chairman of the Board. In addition, the Board of Directors has an Audit Committee, with members from the private sector representative of the Board. The Head of the Audit Committee is the Chairman of the Board.
- KIA has to submit semi-annual statements to the State Audit Bureau. The State Audit Bureau also has on-site personnel to monitor KIA's activities on an ongoing basis.
- KIA's accounts are reviewed, audited and approved by two of the world's leading external audit firms.
- The KIA presents an annual statement of its accounts to the Council of Ministers (Kuwait's Cabinet).

- The KIA presents an annual statement of its accounts to the National Assembly (Kuwait's Parliament).
- The KIA appears before various Committees at Parliament on periodic basis where detailed discussions are held on our performances.

What are the primary strengths and main features of the KIA as a Sovereign Wealth Fund? Some of these are:

- The asset under management are intergenerational savings for future generations. These savings are a result from converting a volatile asset into a diversified portfolio of uncorrelated financial investments. These savings has not resulted from any exchange rate controls.
- History has proven that all KIA's investments are made on a pure commercial basis; with no political bias and with emphasis on maximizing returns. The KIA looks at the bottom line. In some investments, the KIA also looks at synergies through value addition capabilities.
- KIA is a passive and a minority financial investor. The KIA does not seek operational control of any entity. We have been investing globally since 1953. We have stakes which were acquired since late 1960s and early 70s/80s such as in Daimler and in BP.
- Cash inflows are regulated by legislation and is transparent.
- KIA's investments are a force of stability in the financial markets: the KIA does not leverage its own capital; it has a long term investment horizon and has a strong ability to bear risk and accommodate short term volatility.
- KIA is a stable and responsible shareholder and owner of companies. These are based on commonly acceptable international standards of principles for shareholders.
- KIA has a well established investment policy and a defined Strategic Asset Allocation. These are set by KIA's Board of Directors and are reviewed periodically.
- Oil is an asset. The opportunity to invest oil revenues in the global capital markets means that decisions on investing and on oil extraction are separate.
- Sovereign Wealth Funds, such as the KIA, enhance market liquidity by transferring oil revenues into the market.

- KIA has a mutual interest in ensuring value creation and not value destruction of its investments.
- KIA's role is to invest wisely in order to create an alternative source of income. During the 1990 Iraqi invasion, more than 700 oil wells were set on fire, resulting in no source of revenues for the next three years. During that period, the KIA spent more than 80 billion US dollars towards Kuwait's liberation and subsequent reconstruction efforts. These funds were intended, and were used, as savings for a "rainy day".
- The KIA always complies with all regulations and laws domestically and in the host countries where it invests. As an example, in 1988, the KIA was told by the UK authorities to divest a substantial stake which it had acquired in BP. Immediately, it complied with the rule, without recourse to the courts.

Recently, there has been increasing calls for regulating Sovereign Wealth Funds. Let me share some of my opinions on this issue with you.

According to various press reports, on March 28th, European Trade Commissioner, Mr. Peter Mandelson, called for Sovereign Wealth Funds to agree to a code of conduct to avoid being cast as "villains" by governments fearful of their power and influence.

It is time to call a spade a spade by its name. Recipient countries are placing handcuffs on Sovereign Wealth Funds in the form of regulations, termed in the best tradition of George Orwell's Newspeak, by calling them code of conduct or principles of operations or best practices. These regulations will not solve or prevent any future financial crises.

The American economy today faces the "mother of all crises". This crises will drag Europe down and, subsequently, the rest of the world. Let me go to the main point: how was this crisis created? It is important to identify the root for the creation of funds which permitted entities to borrow 30 to 40 times their capital, without any discussions or calls for any regulation of these entities. Based on public information, these funds apparently grew geometrically without any governance or oversight.

Sovereign Wealth Funds have acted responsibly and swiftly during these highly volatile times. They have taken on the responsibility of pumping more than

65 billion US dollars in some of the impacted financial institutions. At the end, these Sovereign Wealth Funds will be held responsible by their stakeholders and their citizens, the ultimate owners of these funds.

If a set of principles or codes of conduct are established for Sovereign Wealth Funds, then recipient countries should also have the same set of principles for all pools of capital, including Hedge Funds, Private Equity Funds, Pension Funds, Savings Funds, and other non listed funds, in OECD and non OECD countries. There should be a common and level playing field for all.

“If it is not broken, don’t fix it.” There is no evidence, over the past many decades, of any wrong doing by any Sovereign Wealth Fund. The consequences of imposing regulations on Sovereign Wealth Funds will result in an adverse impact on global capital flows, which is not in our common interest. Regulating Sovereign Wealth Funds will not stimulate the global economy. Let us address the issue at hand by regulating those entities who are responsible for the current crises.

The European Union has recently issued a paper called “A common European approach to Sovereign Wealth Funds”. If I look to the main conditions of this report, there are two main requirements: one under governance and one under transparency.

Governance can be summarized as:

- Clear allocation and separation of responsibilities.
- Issuing of an investment policy that defines the overall objectives of Sovereign Wealth Funds investment.
- Operational autonomy for the entity to achieve those objectives.
- Public disclosure of the general principles of a Sovereign Wealth Fund’s relationship with government authorities.
- Disclosure of general principles of internal governance that provide assurances of integrity.
- Issuing of risk management policies.

Transparency can be summarized as:

- Annual disclosure of investment positions and asset allocation.
- Exercise of ownership rights.
- Disclosure of the use of leverage and of the currency composition.
- Size and source of an entity’s resources.
- Disclosure of the home country regulation and oversight governing the Sovereign Wealth Funds.

As I mentioned earlier, you will notice that the KIA has already met with all of the proposed EU requirements under governance and some related to transparency, as I will explain further.

Recipient countries have asked Sovereign Wealth Funds to be “transparent”. The KIA is completely transparent with its stakeholders through periodic and regular reporting to the Cabinet as well as to the Parliament.

None of the recipient countries are able to explain how transparency; through declaration of size of assets under management and performances; would enhance global financial markets stability as well as ensure security of their domestic markets.

The KIA has one of the most transparent processes, where Kuwait’s State Audit Bureau sends a detailed report on all aspects of KIA’s activities to Kuwait’s Parliament every six months.

I believe that there should be limits to be placed on transparency. Complete transparency would raise more questions than answers. I can just imagine KIA being bombarded with questions, on our tactical investment decisions, such as why we increased our holdings in a specific asset class or decreased our level of investments in a specific country. The KIA needs to be transparent with its stakeholders, which it is.

If you look at the top 20 pools of long term capital, 12 are from the OECD representing nearly 62% of the total assets under management from this group. When you read about Sovereign Wealth Funds, you assume that it is about a non-OECD government owned entity. Actually, such sources of capital would also include entities from OECD countries. Not all of these entities are in non-OECD countries.

What does the KIA recommend regarding Sovereign Wealth Funds and investing in recipient countries? Actually, it is quite simple:

- An open investment environment is in the best interest of all concerned parties.
- To increase dialogue between recipient countries and main Sovereign Wealth Funds through outreach programs.
- Governments of recipient countries should treat Sovereign Wealth Funds as any large institutional investor.

An important point to note is the size of Sovereign Wealth Funds. Various amounts have been stated ranging from 1.5 to 3.5 trillion US dollars. Even assuming the highest level, this would not exceed 5% of the more than 75 trillion US dollars of global assets under management.

Another distinction, which many may not be aware of, is that not all of the assets of Sovereign Wealth Funds are invested in global markets. A high percentage of their assets are domestic investments, which are required for the effective operation of a country, such as in various infrastructure; holdings in financial institutions; and others.

The main message which I am trying to convey today is very basic: Sovereign Wealth Funds, such as the KIA, have been around for nearly 55 years. We have an excellent track record of being a responsible and disciplined investors. What has changed that recipient countries suddenly want to regulate us? The KIA has a vested interest in maintaining mutually beneficial cooperation with recipient countries. The more the KIA invests in Europe, the greater our vested interest to ensure Europe's continued economic growth and stability. Otherwise, our investments would be adversely impacted.

Finally, any fear of Sovereign Wealth Funds are unfounded and unjustified. I propose that there should be greater deregulation in order to facilitate capital flows. This will help global growth. Let capital flow to where there are investment opportunities.

Thank you.