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The Global Impact of State Capital

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ABSTRACT

This paper examines the nature of state capital, its increasing prevalence and impacts in the global economy, and the implications of current state capital trends for Australia. The paper classifies several key state capital actors and maps their scale, scope and investment strategies in both global and domestic Australian contexts. Finally, the paper focuses on the impact to date of state capital in Australia and the prospect of future impacts in light of diminishing global demand for resources and growing competition for FDI.

I. INTRODUCTION: THE EVOLUTION OF STATE CAPITAL

Vehicles of government-directed capital are taking a more prominent position in the global economy. 'State capital' actors, such as development banks, public pension funds, sovereign wealth funds, and state-controlled corporations, are playing an increasingly important role for both capitalist and emerging economies. For example, sovereign wealth fund (SWF) assets have grown quickly from US$500 billion in 1990 to over US$5 trillion in June 2013.[2] Similarly, state owned enterprises (SOEs), which did not feature at all among the top ten firms in the Fortune Global 100 in 2005, now comprise three out of the top ten firms in the Fortune Global 500, with a combined revenue over US$1trillion as at July 2013.[3] These firms have access to financing through domestic state-controlled as well as foreign banks, often through opaque lending criteria.[4]

State capital is not new; however the impacts of its increasing prevalence in the past decade are significant and warrant specific examination. State Capitalism embodies a form of hybrid capitalism in which a government actively promotes economic growth by picking and/or backing national champions while also using capitalist tools to this end, such as stock market

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[2] Shai Bernstein, Josh Lerner and Antoinette Schoar, *The Investment Strategies of Sovereign Wealth Funds* 27(2) J. ECON. PERSPECTIVES 219, 221 (2013); and Sovereign Wealth Fund Institute, SOVEREIGN WEALTH FUND RANKINGS (2013), at http://www.swfinstitute.org/fund-rankings/

[3] The three firms are all Chinese SOEs: Sinopec (ranked 4), CNPC (ranked 5), and State Grid (ranked 7): Ranking the Brands, FORTUNE GLOBAL 500 (100) (2012), at http://www.rankingthebrands.com/The-Brand-Rankings.aspx?rankingID=50&year=666

[4] It is indicative that the biggest bank on the 2013 Global 500 list is also Chinese, being the Industrial and Commercial Bank of China (ranked 29): *id*.

listing and external financing and subjecting those champions to global competition.[5] This is to be contrasted with Liberal Capitalism, in which regulation of market actors is low interventionist or 'light touch'.[6] The comparison might best be conceptualized as the visible hand of the government massaging economic prosperity versus the invisible hand of the free market system.[7]

Nonetheless, over history and in the present, both developed and developing nations can boast state capital actors. The main groups of state capital actors or 'state pools of capital' comprise SOEs and SWFs, the latter of which can be further sub-categorized into Reserve Investment Corporations (RICs), Commodity Stabilization Funds (CSFs), and Sovereign Pension Funds (SPFs).[8] These pools of capital are acknowledged as increasingly valuable sources of liquidity in capital markets particularly in times of dislocation, such as in the immediate aftermath of the Global Financial Crisis (GFC). However, there is definitional uncertainty around the different forms of state-related capital and how they should be classified. This is partly because numerous types of actor have been collapsed into popular understandings of the term. The following sections in this Part elucidate classifications, motivations and the evolution of two key state capital actors, being SWFs and SOEs.

A. Classification and Structures of State Capital Pools

Although some SWFs have been in existence for 60 years,[9] public recognition of the label SWF is quite recent.[10] SWFs can take a variety of structures, such as legal entities (e.g. Abu Dhabi Investment Authority), corporations (e.g. Singapore's Temasek Holdings) or neither (e.g. Norway's Government Pension Fund - Global). Moreover, the term SWF still lacks definitional certainty. Truman defines SWFs as 'a descriptive term for a separate pool of government-owned or government-controlled financial assets that includes some international assets.'[11] Similarly, the European Commission (EC) defines SWFs as 'state-owned investment vehicles, which manage a

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5 Aldo Musacchio and Sergio G. Lazzarini, *Leviathan in Business: Varieties of State Capitalism and Their Implications for Economic Performance*, HARVARD BUSINESS SCHOOL WORKING PAPER 12-108 (June 4, 2012), 3.

6 For a detailed discussion of state capitalism as a viable alternative to liberal capitalism, see *The Economist Debate* in 2012, at http://www.economist.com/debate/days/view/802 and http://www.financialregulationforum.com/wpmember/state-capitalism-is-a-viable-alternative-to-liberal-capitalism-7505/

7 The visible-invisible dichotomy draws on concepts expressed by Adam Smith over 200 years ago, that markets are more powerful than governments and do their work subtly and without being seen: Adam Smith, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS (1776). *The Economist* implied this distinction in its special report on state capitalism in 2012: Adrian Wooldridge, *The Visible Hand,* THE ECONOMIST (Jan. 21, 2012), at http://www.economist.com/node/21542931

8 Monk offers a similar tripartite classification for SWFs: Reserve Investment Corporations; Commodity Funds; and Pension Reserve Funds: Ashby HB Monk, *Sovereignty in the Era of Global Capitalism: The rise of sovereign wealth funds and the power of finance*, STANFORD UNIVERSITY - GLOBAL PROJECTS CENTER, Version 10 (April 10, 2010), 6-14, available at SSRN: http://ssrn.com/abstract=1587327 *C.f.* Blundell-Wignall and Wehinger who view 'social security reserve pension funds' and 'sovereign pension reserve funds' as separate categories to SWFs, and add another pool of capital being 'official exchange reserves': Adrian Blundell-Wignall and Gert Wehinger, *Open Capital Markets and Sovereign Wealth Funds, Pension Funds, and State-Owned Enterprises, in* SOVEREIGN WEALTH: THE ROLE OF STATE CAPITAL IN THE NEW FINANCIAL ORDER 105, 107 (Renee A. Fry, Warwick J. McKibbon and Justin O'Brien eds. 2011).

9 *E.g.* the Kuwait Investment Office (KIO) was established in London in 1953 as an asset manager for Kuwait's Foreign Ministry.

10 The term Sovereign Wealth Fund appears to have been introduced by Rozanov in 2005: Andrew Rozanov, *Who Holds the Wealth of Nations?* XV(4) CENTRAL BANKING JOURNAL 52 (2005).

11 Edwin M. Truman, *A Blueprint for Sovereign Wealth Fund Best Practices*, *Policy Brief Number PB08-3* PETERSEN INSTITUTE FOR INTERNATIONAL ECONOMICS, 1 (2008), available at http://www.iie.com/publications/interstitial.cfm?ResearchID=902.

diversified portfolio of domestic and international financial assets'.[12] Lowery has defined SWFs as 'a government investment vehicle which is funded by foreign exchange assets, and which manages these assets separately from official reserves,'[13] a definition which only partially covers the range and purpose of these entities. In an attempt to refine the criteria, Jen believes that SWFs have five basic ingredients: (i) sovereign; (ii) high foreign currency exposure; (iii) no explicit liabilities; (iv) high risk tolerance; and (v) long investment horizon.[14] A number of SWFs themselves combined as an interest group in 2008 and offered their own definition as part of their Generally Accepted Principles and Practices (GAPP):

> SWFs are defined as special purpose investment funds or arrangements, owned by the general government. Created by the general government for macroeconomic purposes, SWFs hold, manage or administer assets to achieve financial objectives, and employ a set of investment strategies which include investing in foreign financial assets.[15]

In keeping with the definitional difficulties surrounding SWFs, scholars do not agree on whether certain institutions are sub-groupings of SWFs or additional separate pools of state capital. For example, Blundell-Wignall and Wehinger subdivide government-related pools of capital into behaviorally homogenous groupings such that 'SWFs' are separate to 'official foreign exchange reserves', 'social security reserve pension funds' and 'sovereign pension reserve funds'.[16] In contrast, Grenville argues that the latter two pension fund categories can be combined together as one separate pool;[17] and Monk categorizes pension funds as a sub-grouping of SWF.[18]

This paper adopts a tripartite classification of SWFs similar to that of Monk whereby there are three main types or sub-grouping of SWF namely RICs, CSFs, and SPFs, each with a slightly different purpose. RICs enable countries to self-insure via investment of foreign exchange reserves. Countries with large stockpiles of foreign reserves can invest their assets in higher yielding securities to diversify their portfolios by using a RIC as opposed to their central bank (which is a less fit for this purpose).[19] In contrast, CSFs reflect a burgeoning awareness by policymakers that there is utility in converting physical assets 'in the ground' into financial assets

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[12] Commission of the European Communities, *Communication from the Commission to The European Parliament, The Council, The European Economic and Social Committee and The Committee of the Regions*: *A common European approach to Sovereign Wealth Funds*, Brussels, xxx, COM(2008) 115 provisional, 3 (2008), available at http://ec.europa.eu/internal_market/finances/docs/sovereign_en.pdf

[13] U.S. Department of the Treasury, *Remarks by Acting Undersecretary for International Affairs Clay Lowery on Sovereign Wealth Funds and the International Financial System*, WWW.TREASURY.GOV (21 June 2007).

[14] Stephen Jen, *The Definition of a Sovereign Wealth Fund,* MORGAN STANLEY GLOBAL RESEARCH (2007), http://www.morganstanley.com/views/gef/archive/2007/20071026-Fri.html

[15] International Working Group of Sovereign Wealth Funds, GENERALLY ACCEPTED PRINCIPLES AND PRACTICES (GAPP) – THE SANTIAGO PRINCIPLES, 3 (2008) (hereafter 'GAPP'), available at http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf

[16] Although they note that 'sovereign pension reserve funds' are 'most comparable to sovereign wealth funds': Blundell-Wignall and Wehinger, *supra* note 8, 106-7. Despite the many common characteristics between sovereign pension reserve funds and SWFs, some OECD work has similarly drawn a distinction between them on the basis that SWFs have diffuse investment objectives (and therefore greater capacity to pursue political objectives). *See e.g.* OECD, DRAFT OECD GUIDELINES FOR PENSION FUND GOVERNANCE (2008); Blundell-Wignall and Wehinger, *id.*, 110-11.

[17] Stephen Grenville, *What is a Sovereign Wealth Fund?, in* SOVEREIGN WEALTH: THE ROLE OF STATE CAPITAL IN THE NEW FINANCIAL ORDER 17, 17-18 (Renee A Fry, Warwick J McKibbon and Justin O'Brien eds. 2011).

[18] Monk, *supra* note 8, 6-8.

[19] *Id. See also* Blundell-Wignall and Wehinger who note that '[e]xtremely large concentrations of high saving-country investments in Treasuries have long been a concern in respect to asset price (including exchange rate) stability': Blundell-Wignall and Wehinger, *supra* note 8, 105.

for the long-term. Monk describes how CSFs 'help countries to manage rents, restoring a certain amount of stability and, indeed, autonomy to resource-rich countries that have seen their position in the global economy change due to factors beyond their control'.[20] In so doing, CSFs are also a means of securing inter-generational equity by managing finite resources for future generations in an uncertain world.[21] Finally, SPFs are a policy response to looming social welfare costs of a nation's aging population. They assist a government to fill an unfunded pension liability via investments in riskier assets.[22] As such, they embody a politically palatable alternative to increasing industry superannuation fund contributions or cutting benefits.[23] Unlike private pensions[24] or very large pension funds run by governments but where the assets are actually owned by the beneficiaries (e.g. CalPERS),[25] SPFs have no designated claimants on the available assets.[26] In this way SPFs, like RICs, are 'commitment mechanisms for politicians that might prefer to spend the countries' wealth today instead of saving it for future generations',[27] and can thus facilitate inter-generational as well as intra-generational benefit.

In contrast, SOEs are widely deemed to be state-owned operating companies rather than investment mechanisms like SWFs. SOEs can be defined as a commercial enterprise in which the state has control through total, majority or significant minority ownership.[28] Instead of making portfolio or indirect investments like SWFs, SOEs tend to make commercially strategic direct investments, such as mergers and acquisitions (M&A). However, unlike private corporations, SOEs are administratively and financially controlled by a state entity. So, in a state capital jurisdiction such as China, central or local government will be a controlling shareholder of an SOE, whereas in a liberal capital jurisdiction such as the US or Australia, that controlling entity would more likely be private institutional investment.

Indeed, China provides a useful illustration of SOE evolution and the centrality of government to their corporate purpose. The traditional Chinese SOE was an organizational form, not a legal form. The economic reforms from the 1970s first took place in rural China whereby agricultural industry was decentralized to local governments, and commercial 'township and village enterprises' (TVEs) emerged as an early form of SOE. Thus, historically, state players in SOE control were local or provincial, not central, governments.[29] Moreover, an SOE did not have separate legal personality nor issue ownership in itself; instead it was administratively controlled by the state, which had the right to appoint management and appropriate profits. Since commencement of the Chinese corporatization program, as expressed in the 1994 Company Law and 2006 PRC Company law, Chinese companies can take one of three legal forms: (i) a company limited by shares (CLS); a company limited by liability (LLC); or (iii) a company wholly owned by a state agency (WSOC). However, Howson is clear that this legal process has not

[20] Monk, *supra* note 8, 12.
[21] *Id.*, 11.
[22] *Id.*, 21.
[23] Robert J. Palacios, *Managing Public Pension Reserves Part II; Lessons from Five Recent OECD Initiatives*, WORLD BANK - SOCIAL PROTECTION DISCUSSION PAPER 219 (2002).
[24] *See* Juan Yermo, *Revised Taxonomy for Pension Plans, Pension Funds and Pension Entities*, OECD (October 2002), which provides a classification of pension systems as pension plans, pension funds and pension entities for the OECD Working Party on Private Pensions.
[25] Blundell-Wignall and Wehinger, *supra* note 8, 107.
[26] Monk, *supra* note 8, 14.
[27] *Id.*
[28] OECD, GUIDELINES ON THE CORPORATE GOVERNANCE OF STATE OWNED ENTERPRISES, Preamble (2005), available at http://www.oecd.org/corporate/ca/corporategovernanceofstate-ownedenterprises/oecdguidelinesoncorporategovernanceofstate-ownedenterprises.htm
[29] Teemu Ruskola, LEGAL ORIENTALISM: CHINA, THE US AND MODERN LAW 60-107 (2013).

resulted in wide-spread private corporate ownership; rather Chinese companies are now corporatized, not privatized.[30]

The above classifications of SWFs and SOEs illustrate the clear potential for influence over their objectives and activities by a sovereign state. This has created some concern by recipient countries about the political (rather than commercial) motives of SWF- and SOE-directed foreign direct investment (FDI).[31] Specifically, there is concern that, through the investments of SWFs and SOEs, foreign governments may obtain access to sensitive information or technology that may jeopardize the recipient country's national interests or security.[32] Nonetheless, while state capital actors certainly have close ties to their government sponsor, they are established for a variety of macro-economic purposes and espouse a range of different motivations, as demonstrated in the next section. This is not to say that the state has no influence; rather the interest of the state is subject to a range of competing and at times conflicting influences.

B. Motivations and Objectives of State Capital Actors

The motivations of state capital actors tend to vary with the objectives and interests of their enabling government.[33] The traditional view of state capital actors, particularly SWFs, is as long-term investors that can provide liquidity in times of crisis. Specifically, Monk demonstrates that governments, independent of their variety of capitalism, use SWFs as a form of special purpose vehicle to invest assets in private financial markets.[34] And while different state capital actors might have various macro-economic purposes, they exist primarily 'to preserve local autonomy and state sovereignty by harnessing the power of finance'.[35]

It is only in recent years that scholars have been able to explain the rise and motivations of SWFs. In 2009 Das et al. stated that no accepted explanation existed regarding why and when nations establish SWFs.[36] In 2010 Monk proffered the explanation that SWFs are an assertion of sovereignty and authority in response to increasing globalization and financialization.[37] And in 2011 Grenville noted 'the diversity of origin and motivation behind institutions that are commonly described as sovereign wealth funds' with the effect that SWFs have a 'mish-mash of motivations'.[38] Indeed, the International Monetary Fund (IMF) recognizes that SWFs are a heterogeneous group with five main objectives: (i) stabilization funds whose primary objective is to help insulate the economy from the effects of commodity (usually oil) price swings; (ii) savings

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[30] Donald C. Clarke and Nicholas C. Howson, *Pathway to Minority Shareholder Protection: Derivative actions in the People's Republic of China, in* THE DERIVATIVE ACTION IN ASIA: A COMPARATIVE AND FUNCTIONAL APPROACH 243, 245-249 (Dan W. Puchniak, Harald Baum & Michael Ewing-Chow eds. 2012).

[31] Bernstein et al., *supra* note 8. *See also* Justin O'Brien, *Mapping the Trajectory of the Regulatory Debate: Securing the National Interest or Justifying Protectionism, in* SOVEREIGN WEALTH: THE ROLE OF STATE CAPITAL IN THE NEW FINANCIAL ORDER 155 (Renee A Fry, Warwick J McKibbon and Justin O'Brien, eds. 2011).

[32] Greg Golding, *Australia's Experience with Foreign Direct Investment by State Owned Enterprises: A Move Towards Xenophobia or Openness*, SEATTLE UNIVERSITY LAW REVIEW (2013) (forthcoming); Blundell-Wignall and Wehinger *supra* note 8, 115-116. Nonetheless, there are very few examples of where SWFs in particular have 'demonstrably compromised the national interests of the host country (however these are defined)': Blundell-Wignall and Wehinger, *id.*, 105-106.

[33] Ashby HB Monk, *Recasting the Sovereign Wealth Fund Debate: Trust, Legitimacy, and Governance,* 14 NEW POLITICAL ECONOMY 14 (2009).

[34] Monk, *supra* note 8, 3. Unlike SWF-directed investment, which is primarily undertaken by non-OECD nations, both OECD and non-OECD countries are actively involved in SOE-directed FDI: *see* Blundell-Wignall and Wehinger, *supra* note 8, 128-38.

[35] Monk, *id.*, 2.

[36] Udaibir S. Das*,* Yinqiu Lu*,* Christian Mulder and Amadou Sy, *Setting Up a Sovereign Wealth Fund: Some policy and operational considerations*, IMF WORKING PAPER 09/179 (2009).

[37] Monk, *supra* note 8.

[38] Grenville, *supra* note 17, 17-18.

funds for future generations that mitigate the effects of Dutch disease;[39] (iii) reserve investment corporations; (iv) development funds; and (v) contingent pension reserve funds which provide for unspecified pension liabilities on the government's balance sheet.[40]

Using the IMF categorizations, we can analyze where and why several large SWFs fit into which categories, belying their motivations. For example, Norway is primarily a resource dependent economy (petroleum) and therefore vulnerable to changes in the global market for commodities. Its SWF[41] fits within category (ii) as it was established to mitigate Dutch disease and the 'curse' of resource wealth that leads to currency appreciation, declining manufacturing, substantial restructuring costs and accompanying unemployment.[42] It also fits within category (v) given its second purpose is to 'facilitate government savings to finance rising public pension expenditures'.[43] Similarly, the Australian Future Fund, established through the privatization of Telstra, straddles categories (ii) and (v) as a tool for managing commitments to future generations via a state-run pension fund structure designed to meet pension liabilities for public sector employees.[44] The establishment of a SWF may, therefore, be a policy response to not only concerns about the costs of providing social welfare to an increasingly aging population but also to Solow's question: 'How much of the world's – or a country's – endowment of non-renewable resources is it fair for the current generation to use up, and how much should be left for generations to come who have no active voice in contemporary decisions?'[45] Similar motivations prompted the creation of SWFs (in the form of SPFs) in Ireland and New Zealand that invest assets in equities for long-term social welfare benefit.[46] In contrast, category (iii) SWFs have become prevalent in Asia over the past decade. This can be traced to lessons derived from the liquidity dislocation found in the 1997 Asian financial crisis, with China and South Korea establishing SWFs similar to that of Singapore and Hong Kong in the form of Reserve Investment Corporations. The main objectives of these RICs are threefold: self-insurance in the event of another crisis; stabilizing foreign exchange rates to mitigate another crisis; and wealth augmentation via the investment of accumulated ('hoarded') assets in less liquid securities for

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39 Dutch disease is defined by Investorwords.com as: 'The deindustrialization of a nation's economy that occurs when the discovery of a natural resource raises the value of that nation's currency, making manufactured goods less competitive with other nations, increasing imports and decreasing exports': http://www.investorwords.com/1604/dutch_disease.html The phenomenon of Dutch disease was first identified by Max Corden, *see* W. Max Corden, *Booming Sector and Dutch Disease Economics: A survey and consolidation*, 36 OXFORD ECONOMICS PAPERS 359 (1984); W. Max Corden and J. Peter Neary, *Booming Sector and De-industrialization in a Small Open Economy* 92 ECONOMIC JOURNAL 825 (1982). The term originated in the Netherlands after the discovery of North Sea gas in the 1970s and is an ongoing concern for resource-rich jurisdictions, prompting several to establish SWFs. *See* Paul Krugman, *The Narrow Moving Band, the Dutch Disease, and the Competitive Consequences of Mrs. Thatcher,* 27(1-2) J. DEV. ECONS. 50 (1987).

40 International Monetary Fund, SOVEREIGN WEALTH FUNDS – A WORK AGENDA, 5 (2008), available at http://www.imf.org/external/np/pp/eng/2008/022908.pdf Note that all SWF countries are members of the IMF.

41 The Government Pension Fund of Norway comprises two separate SWFs, being the Government Pension Fund - Global (known as the 'Government Petroleum Fund' until 2006) and the Government Pension Fund – Norway (known as the 'National Insurance Scheme ' until 2006): http://www.swfinstitute.org/swfs/norway-government-pension-fund-global/ In 2012 the Government Pension Fund - Global was the second largest pension fund in the world behind the Abu Dhabi Investment Authority: Bernstein et al. , 221 (Table 1). *See* also Norges Bank Investment Management, GOVERNMENT PENSION FUND GLOBAL: ANNUAL REPORT 2012 (2012).

42 Thorvaldur Gylfason, *A Nordic Perspective on Natural Resource Abundance, in* RESOURCE ABUNDANCE AND ECONOMIC DEV'T 296 (R.M. Auty ed. 2001); Martin Skancke, *Fiscal Policy and Petroleum Fund Management in Norway, in* FISCAL POLICY FORMULATION AND IMPLEMENTATION IN OIL-PRODUCING COUNTRIES 316 (J. Davis, R. Ossowski and A. Fedelino eds. 2003.

43 Ministry of Finance, THE GOVERNMENT PENSION FUND (undated), at http://www.regjeringen.no/en/dep/fin/selected-topics/the-government-pension-fund.html?id=1441

44 *See* http://www.futurefund.gov.au/

45 Robert Solow, *On the Intergenerational Allocation of Natural Resources*, 88(1) SCAND. J. of ECONOMICS 141 (1986).

46 Being the National Pensions Reserve Fund (Ireland) and the New Zealand Superannuation Fund respectively: *see* Blundell-Wignall and Wehinger, *supra* note 8, 111; and Monk, *supra* note 8, 14.

higher returns because hoarding reserves can be extremely costly for emerging economies (around 1% of GDP in the first years of the 21st Century).[47]

In the case of SOEs, the traditional view is that they are national corporate champions purpose-built to fulfill government investment mandate abroad. Accordingly, SOEs have tended to invest in areas of nation-wide priority, being natural resources, utilities, telecommunication services, and defense.[48] However, there is growing debate about the extent to which SOE investment decisions are being exercised independently of their sovereign sponsor. Multiple external parties are involved in SOE investment decision-making abroad, including domestic consultants, corporate partners and financiers,[49] such that decisions cannot be made solely by a government entity. On this point, the Peterson Institute for International Economies asserts that SOEs operate and make investment decisions not as agents of the state but similar to any other corporation.[50] With regard to China in particular, Howson claims that the 'going global' strategy is being directed by the corporations themselves, citing the action of CNOOC in bidding for Unocal in 2005 despite central government opposition.[51] Similarly, KPMG argues that 'Chinese SOEs abroad have shown strong commercial motivations, similar to those of multinational corporations from developed countries'.[52] SOE commercial motivations are evinced by capital investments to secure stable and high-quality supplies of natural resources, mergers and acquisitions to acquire new brands and technology, accessing new markets, and exporting home brands.

The increasing diversification and changing investment strategies of state capital actors is detailed further in Part II.

C. Evolution of State Capital Actors

Recent developments regarding the investment activity by state actors have a sense of back to the future about them. For example charter companies such as the East India Company (EIC) bear similarities to many contemporary state capital actors with their close linkages to state power and, in many cases, an emphasis on trading in commodities.[53] The first manifestation of the EIC was established in 1600 during the reign of Queen Elizabeth I as the *Governor and Merchants of London trading with the East Indies*. The EIC evolved through several forms, received monopoly trading advantages and other support from the Crown, including five Acts in 1670 during the reign of Charles II which accorded regal legitimacy to the EIC to command troops, make war and peace, mint money, annex territory and administer criminal and civil justice over

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47. Monk, *id.*, 6-8; Dani Rodrick, *The Social Cost of Foreign Exchange Reserves* 20(3) INTERNATIONAL ECON. J. 253 (2006).

48 John Lee, *The Re-emergence of China: Economic and Strategic Implications for Australia* 45(4) THE AUSTRALIAN ECONOMIC REVIEW 484, 484 (2012). The OECD also notes that SOEs are often prevalent in utilities and infrastructure industries whose performance is of great importance to broad segments of the population: OECD, *supra* note 28, Preamble.

49 Clayton Utz, DIGGING DEEP: CHINESE INVESTMENT IN AUSTRALIAN ENERGY AND RESOURCES 25 (2013).

50 Petersen Institute for International Economics, CHINESE INVESTMENT IN LATIN AMERICAN RESOURCES: THE GOOD, THE BAD, AND THE UGLY (2012), available at http://www.piie.com/publications/interstitial.cfm?ResearchID=2046

51 Howson makes this point in relation to the CNOOC bid for Unocal, which was opposed by Chinese central government actors: Nicholas C. Howson, *China's Acquisitions Abroad – Global Ambitions, Domestic Effects* (Winter/Spring) LQN 73, 73 (2006).

52 KPMG and the University of Sydney, DEMYSTIFYING CHINESE INVESTMENT 13 (2012) (hereafter 'KPMG 2012').

53 For a discussion of how various interest groups interacted in shaping the policy priorities of the East India Company *see* Huw V. Bowen, THE BUSINESS OF EMPIRE: THE EAST INDIA COMPANY AND IMPERIAL BRITAIN, 1756-1833 (2006).

the territory they controlled.[54] Similarly the Dutch East India United Company, the *Verenigde Oostindische Compagnie* (VOC), was founded in 1602 when the States General of the Netherlands granted the charter company a 21 year monopoly to trade and develop Dutch influence in Asia. Like the EIC it was enormously successful in these ventures and they were dominant actors in Asia for 200 years.[55] The EIC equivalent in North America was the Hudson Bay Company (HBC), which was incorporated by English royal charter in 1670 to administer trade in the Hudson Bay region and beyond, effecting a monopoly on the fur trade; for many years the HBC acted as a *de facto* government across large swathes of territory.[56]

Fast forward to a post-GFC environment, and it seems inevitable that state capital actors will become increasingly important vehicles for the recycling of global finance, namely, channelling capital from surplus (balance of payments) generating countries to deficit countries. Indeed, the growing influence of these actors was evident before the onset of the crisis, with significant (loss-making) investments made in major banks on both Wall Street and the City of London. However their size, number, growth and scale of activity will still be influenced by the corresponding size and trends in global macroeconomic imbalances themselves. Exchange rate regimes, namely the prevalence or otherwise of dollar-type pegs and domestic inflation issues will also have an influence on their size, growth and number. Real and nominal rates of return on benchmark sovereign assets in the major advanced economies will also have an influence in as far as sovereign wealth portfolio shifts are affected. The public accumulation of assets by energy exporting countries is expected to continue if constraints on energy supply relative to demand remain, which does seem likely over the medium to longer term. It is highly likely that state capital actors increasingly will be seen as favoured pools of available liquid capital. Continuing relatively low growth rates and subsequently low returns on investment capital can be expected in major advanced economies, so investment will be channelled increasingly into emerging markets and state capital actors will be an important conduit in such processes.

Yet despite the growing prevalence of state capital, there remains substantial reliance on *best guesswork* regarding its impacts. State capital actors are difficult to define in a prescriptive sense and often powerful actors are involved who do not welcome scrutiny. This creates difficulties in measuring the scale of activity and its effects, and evaluating regulatory responses. Compounding this empirical uncertainty is the diffused impact especially in geo-political contexts. Indeed, while contemporary state capital actors obviously do not play the same militaristic and governmental roles as the EIC, VOC or HBC, they do have close linkages to their national governments and play important roles in facilitating their sovereign's economic and political influence in foreign territories. It is perhaps unsurprising that levels and locations of investment activity cannot be easily evaluated given that a significant number of state capital jurisdictions also have authoritarian political regimes, as evidenced in the next Part.

II. STATE CAPITAL IN THE GLOBAL ECONOMY

A. Changing Character of the Global Economy

The activities of state-related pools of capital need to be understood within the context of an era of globalization. Economic and political ties between many jurisdictions are deepening, and jurisdictions increasingly are playing a mediating role regarding the interests of business that may

[54] 8 *East India Company*, ENCYCLOPÆDIA BRITANNICA ELEVENTH EDITION 835 (11 ed. 1911).
[55] For a more detailed analysis of the VOC *see* Charles R. Boxer, THE DUTCH SEABORNE EMPIRE: 1600–1800 (1977).
[56] *See* Bryce George, THE REMARKABLE HISTORY OF THE HUDSON'S BAY COMPANY (1968).

be conducted within their spheres of influence.[57] One significant effect of globalization has been to further elevate deficits and surpluses run by countries and the subsequent macro-economic trade imbalances that they bring. As ever with regard to international trade the political context remains crucial and almost inevitably it is intertwined with expectations regarding vested interests. These developments are affecting the sovereignty of jurisdictions as local political priorities become more intertwined with international politics and the requirements of international business. The regulatory world reflects the realities of the domains it purports to influence and so a major consequence of these developments is that regulatory structures and processes have become more internationalized. A variety of modes of governance are emerging that have a capacity for impacts of broad international scope. This political reality interacts with how state-related pools of capital have been increasing in recent years, not only in their number, but also in the scale of their effect. The rising influence of more proactive state-led investment capitalism is one of the shaping variables in how the global economy has been changing swiftly in recent decades; arguably these structural shifts have been accelerated by GFC impacts.[58] Of critical significance in this regard is the fact that the relationship is in turn impacted by the policies adopted by recipient countries.

The increasing investment role of SWFs and SOEs reflect changing relationships in the global economy, especially the economic rise of the BRIC countries (Brazil, Russia, India and China). As the strategic economic and political importance of these countries increases, so does the need to understand how international regulatory infrastructures might evolve in order to accommodate such changes.

B. Scale and Scope of State Capital in the Global Economy

Importantly, emerging economies have significant state capital investment actors. Coleman demonstrates that China, the UAE, Saudi Arabia, Kuwait, Hong Kong, Russia and Qatar are amongst the countries that possess the ten largest SWFs by assets under management at March 2013.[59] Indeed the SWF Institute (SWFI) has specified the geographical origins of SWFs as follows: 40% in Asia; 35% in the Middle East; 17% in Europe; 3% in Africa; 3% in the Americas; and 2% in other areas of the world.[60] Similarly, SOE capitalization constitutes a significant element in three of the BRIC countries: SOEs comprised 80% of the value of the stock market in China, 62% in Russia and 38% in Brazil in 2012; and SOEs accounted for one-

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[57] *See*, *e.g.*: Jeffry A. Frieden, GLOBAL CAPITALISM: ITS FALL AND RISE IN THE TWENTIETH CENTURY (2006); Jan A. Scholte, GLOBALIZATION: A CRITICAL INTRODUCTION (2005); and Joseph E. Stiglitz, GLOBALIZATION AND ITS DISCONTENTS (2003).

[58] This paper is not focused on the GFC, but there is a substantial literature on its causes and effects, including: Christopher J. Arup, *The Global Financial Crisis: Learning from Regulatory and Governance Studies*, 32(2) LAW & POL'Y, 363 (2010); Emilios Avgouleas, *The Global Financial Crisis: Behavioural Finance and Financial Regulation: In Search of a New Orthodoxy*, 9 J. CORP. L. STUDIES 23 (2009); Philip Booth (ed.), *Verdict on the Crash: Causes and Policy Implications*, INSTITUTE OF ECONOMIC AFFAIRS (2009); Essential Information and Consumer Education Foundation, SOLD OUT: HOW WALL STREET AND WASHINGTON BETRAYED AMERICA (2009); Gary B. Gorton, *Questions and Answers About the Financial Crisis*, NBER WORKING PAPER NO.W15787 2010, available at http://www.nber.org/papers/w15787; International Monetary Fund, GLOBAL FINANCIAL STABILITY REPORT: MEETING NEW CHALLENGES TO STABILITY AND BUILDING A SAFER SYSTEM (2010); International Monetary Fund, FISCAL IMPLICATIONS OF THE GLOBAL ECONOMIC AND FINANCIAL CRISIS, SPN/09/13 (2009); Carmen M. Reinhart & Kenneth S. Rogoff, THIS TIME IS DIFFERENT: EIGHT CENTURIES OF FINANCIAL FOLLY (2009).

[59] Isobel Coleman, *Graph: Sovereign Wealth Funds, Council on Foreign Relations*, COUNCIL ON FOREIGN RELATIONS (April 24, 2013), http://blogs.cfr.org/coleman/2013/04/24/graph-sovereign-wealth-funds/ The other top ten countries are: Norway, Singapore, and Australia. *See also* Sovereign Wealth Fund Institute, *supra* note 2. SWFI notes that one of the Russian funds 'includes the oil stabilization fund of Russia' and that the figure for China's largest fund 'is a best guess estimation': Sovereign Wealth Fund Institute, *id.*

[60] Sovereign Wealth Fund Institute, *id.*

third of the emerging world's FDI from 2003-2010.[61] Moreover, Chinese government records attest that Chinese FDI is set to increase by 15% in 2013.[62]

This rapidly rising pool of state investment capital is part of the story of the decoupling effects of contemporary fundamental changes in East:West capital flows with attendant global imbalances regarding the management of exchange rates and reserves. The most obvious example of this is the rapidly increasing global economic influence of China. For example, China has increased its foreign reserves from $21 billion in 1992 (5% of its annual GDP)[63] to $31,202 billion in 2012 (45% of its annual GDP).[64] These decoupling effects are fuelled by the fact that emerging markets have been growing at an average of 5.5% (in contrast to 1.6% for developed nations) in recent years and the activity of these emerging markets is projected to make up half of the world's GDP by 2020 (Table 1 below).

Table 1 GDP Growth: Advanced vs. Emerging Economies[65]

	Actual average annual percent change							*Projected*	
	2006	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2018**
Total Advanced Economies	**3.0**	**2.8**	**0.1**	**-3.5**	**3.0**	**1.6**	**1.2**	**1.2**	**2.5**
E.g. *United States*	2.7	1.9	-0.3	-3.1	2.4	1.8	2.2	1.9	2.9
Euro Area	3.2	3.0	0.4	-4.4	2.0	1.4	-0.6	-0.3	1.6
Japan	1.7	2.2	-1.0	-5.5	4.7	-0.6	2.0	1.6	1.1
Australia	2.7	4.6	2.7	1.4	2.6	2.4	3.6	3.0	3.2
Total Emerging Economies	**8.3**	**8.8**	**6.1**	**2.7**	**7.6**	**6.4**	**5.1**	**5.3**	**6.2**
E.g. *Brazil*	4.0	6.1	5.2	-0.3	7.5	2.7	0.9	3.0	4.2
Russia	8.2	8.5	5.2	-7.8	4.5	4.3	3.4	3.4	3.6
India	9.4	10.1	6.2	5.0	11.2	7.7	4.0	5.7	7.0
China	12.7	14.2	9.6	9.2	10.4	9.3	7.8	8.0	8.5
Qatar	26.2	18.0	17.7	12.0	16.7	13.0	6.6	5.2	6.5
Saudi Arabia	5.6	6.0	8.4	1.8	7.4	8.5	6.8	4.4	4.3

Indeed, China has emerged to rival the US as the most important economy in the world. Table 2 below shows how the top seven global economies based on Purchasing Power Parity (PPP) were ranked in 2011 and how they might look in 2030 and 2050.[66] By 2020 China will have replaced

[61] Wooldridge, *supra* note 7.
[62] National Development and Reform Commission (NDRC), REPORT ON THE 2013 DRAFT PLAN FOR NATIONAL AND SOCIAL DEVELOPMENT (2013), submitted to the National People's Congress on 5 March 2013.
[63] Zheng M. Song, Kjetil Storesletten & Fabrizio Zilibotti, *Growing Like China*, CEPR DISCUSSION PAPER NO. DP7149 (2010), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1345675.
[64] Kenneth Rapoza, *China's Cash Hoard Nearly Half its GDP*, FORBES INVESTING (May 25, 2012), http://www.forbes.com/sites/kenrapoza/2012/05/25/chinas-cash-hoard-nearly-half-its-gdp/
[65] International Monetary Fund, WORLD ECONOMIC OUTLOOK: HOPES, REALITIES, RISKS, Statistical Appendices Tables A1, A4 (2013).
[66] PwC Economics, WORLD IN 2050, THE BRICS AND BEYOND: PROSPECTS, CHALLENGES AND OPPORTUNITIES, 2 (2013), available at http://www.pwc.co.uk/economic-services/global-economy-watch/index.jhtml *See also* Dale W. Jorgensen & Khuong M. Vu, *The Rise of Developing Asia and the New Economic Order*, LEE KUAN YEW SCHOOL OF PUBLIC POLICY RESEARCH PAPER NO. PP11-21, 25 (July 7, 2011), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1904716, who used a sample of 122 countries

the US as the world's largest economy with 20.08% of global GDP (up from 13.92% in 2010). In the same period the US share of global GDP is expected to fall from 20.14% to 17.44%. This *changing of the economic guard* as it were in terms of the global economy is not confined merely to China and the US because there are regional forces at work as well, especially in Asia. For example, the G7 (Canada, France, Germany, Italy, Japan, UK and US) share of global GDP is expected to fall from 40.62% in 2010 to 33.30% in 2020 and the Asia 7 (China, Hong Kong, India, Indonesia, Singapore, South Korea and Taiwan) share to rise from 25.16% in 2010 to 33.18% in 2020. The US and China dominate their respective groupings. The US share of G7 GDP is estimated to be 49.59% in 2010 and 52.385 in 2020. China's share of Asia 7 GDP is estimated to be 55.35% in 2010 and 60.52% in 2020.

Table 2 Actual and Projected Top Economies Based on GDP (in PPP)[67]

	2011		**2030**		**2050**	
PPP rank	**Country**	**GDP at PPP (2011 US$bn)**	**Country**	**Projected GDP at PPP (2011 US$bn)**	**Country**	**Projected GDP at PPP (2011 US$bn)**
1	US	15,094	China	30,634	China	53,856
2	China	11,347	US	23,376	US	37,998
3	India	4,531	India	13,716	India	34,704
4	Japan	4,381	Japan	5,842	Brazil	8,825
5	Germany	3,221	Russia	5,308	Japan	8,065
6	Russia	3,031	Brazil	4,685	Russia	8,013
7	Brazil	2,305	Germany	4,118	Mexico	7,409

If these estimates are correct then a direct 7%+ transference of total global GDP from the G7 to the Asia 7 will occur in only ten years. On these projections, China is likely to be the dominant global economic power before the middle of the century. This constitutes a dramatic shift in economic power; and history demonstrates that these economic shifts influence change in other arenas such as foreign policy, strategic alliances and regulation in multi-lateral contexts.

Indeed, the last five years have seen a dramatic movement away from the pre-dominant philosophy that has driven financial markets development and their regulation in the last three decades. That is, a commitment to free market ideology underpinned by light-touch regulation under the canvas of regulatory competition in order to attract increasing amounts of inward investment. Since 2008 liquidity in global markets has reduced and concerns about sovereign debt have grown as appetite for risk has diminished globally. Interwoven with this is a new era of more proactive state-led investment capitalism that is emerging with state-related pools of capital key to this process. In terms of state-related pools of investment activity there remains

accounting for more than 95% of global GDP, to predict how shares of global trade between major trading blocs may change if current growth trends are maintained.

[67] *Id.*

considerable uncertainty and ambiguity about their levels of investment, but in general they tend to be less leveraged than many of their private sector counterparts and therefore perceived by some as less of a threat to market stability. This is the new international financial environment and geo-political reality in which existing and future state-related pools of capital are likely to become increasingly proactive and influential, contributing to financial markets and the broader economy globally and domestically in Australia.

Yet, in this new landscape, the entwined regulatory/investment role of the state becomes more opaque. Jurisdictions that might previously have slotted comfortably into the category of recipients of state capital have become more active state capital investment actors themselves. This raises questions about how the state can manage simultaneously the potential conflicts of being an active investment actor, a detached and independent regulator, a recipient of inward investment from both state and non-state sources, and the promoter of the national interest.

C. Impacts of Investment Strategies of State Capital Actors

As detailed in Part I, the activities of both SOEs and SWFs evidence a trend towards investment diversification and a growing desire and capacity for risk. Furthermore, this Part has documented the occurrence of a global economic 'changing of the guard' as the investment symbiosis between recipient-acquirer nations evolves. Indeed, this is best evidenced by patterns of investment strategies of state capital actors over time. Blundell-Wignall and Wehinger show that, prior to 2006, the largest SOE foreign investment deals involved OECD nations as both recipient and owner countries. However, since 2006, that picture has changed dramatically with the majority of deals involving non-OECD nations as the acquiring entity and OECD nations as the target or recipient.[68] Furthermore, from 1990 – 2009, nearly two-thirds of the largest 50 SOE foreign investment deals took place in four key sectors: energy and power; telecommunications; materials (including non-renewable resources); and high technology (with potential military use).[69] Importantly, these sectors are considered 'areas of strategic concern' to recipient nations, being germane to their national security and national interest.

In contrast however, Blundell-Wignall and Wehinger show that only five of the 50 top deals for that same time period were made by SWFs in sensitive sectors.[70] Indeed, papers by Gompers and Metrick,[71] Lerner, Schoar and Wongsunwai,[72] and Hochberg and Rauh[73] highlight the heterogeneity of institutional investment strategies and ultimately returns. Specifically, Bernstein et al. note that a growing number of nations that hoard foreign currency, such as China, are seeking broader portfolios in which to invest it, rather than putting these reserves 'under the mattress' in low-risk/low-return US Treasury bonds.[74]

Accordingly, the majority of government-related investment deals in 'sectors of strategic concern' tend to be undertaken by SOEs and not SWFs. Analyzing the data above, we suggest that SWFs are a state capital actor of less concern than SOEs. However, little differentiation at

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[68] Blundell-Wignall and Wehinger, *supra* note 8, 128-139.
[69] *Id.*, 128.
[70] *Id.*, 139, 145.
[71] Paul A. Gompers and Andrew Metrick, *Institutional Investors and Equity Prices* 116(1) QUARTERLY J. ECONS 229 (2001).
[72] Josh Lerner, Antoinette Schoar and Wan Wongsunwai, *Smart Institutions, Foolish Choices? The Limited Partner Performance Puzzle* 62(3) J. FINANCE 731 (2007).
[73] Yael Hochberg and Joshua Rauh, *Local Overweighting and Underperformance: Evidence from Limited Partner Equity Investments* NBER WORKING PAPER 17122 (2011), available at http://www.nber.org/papers/w17122
[74] Bernstein et al., *supra* note 2, 221.

this granular level is evidenced by policymakers.[75] Australia is a partial exception. It calibrated the policy governing state-capital investment in the aftermath of a contested raid of the Rio Tinto share register in London.[76] Generally, however, the impacts of state capital investment activity tend to be viewed in the aggregate whereby the combined impact of (a) a trend towards investment diversification and risk, and (b) investment in 'areas of strategic concern' carries overall implications for cross-border foreign exchange liquidity. And the more varied and aggressive investment strategies of state capital actors in recent years, the more likely recipient states are to find forms of financial protectionism to defend against such activity.[77] These challenges have been heightened by GFC ramifications such as governments part-nationalizing/saving failing banks (e.g. Royal Bank of Scotland and Lloyds in the United Kingdom (UK)), or nationalizing them (e.g. Anglo Irish Bank in the Republic of Ireland and Northern Rock in the UK), which continue to impact heavily on political, economic and legal agendas.[78]

Overall, the activities of state capital actors raise implications for cross-nationalization of assets and industries in jurisdictions all over the world. If further regulatory initiatives for state capital actors are to emerge at the international level it is likely to be through codes of best practice such as the GAPP[79] and then multi-lateral agreements brokered by international organizations such as the Financial Stability Board (FSB)[80] under its G20[81] imprimatur or the OECD.[82] Thus, political economy factors will continue to be crucial in shaping international regulatory processes. An emphasis on intermediation rather than new regulatory institutions in the form of an evolutionary approach is congruent with market realities and legitimate exercising of regulatory power.

Yet despite international regulatory developments, many recipient countries seek to use domestic FDI regimes to protect their national interests. In Australia for example, the Economics References Committee of the Commonwealth Senate has stated that: 'the committee believes

[75] Noting the suggestion by Blundell-Wignall and Wehinger that international debate needs to move into the SOE area and away from SWFs for both OECD and non-OECD nations: Blundell-Wignall and Wehinger, *supra* note 8, 145.

[76] Greg Golding and Rachael Bassil, *Australian Regulation of Investments by Sovereign Wealth Funds and State-Owned Enterprises*, *in* SOVEREIGN WEALTH: THE ROLE OF STATE CAPITAL IN THE NEW FINANCIAL ORDER 171 (Renee A. Fry, Warwick J. McKibbon and Justin O'Brien eds. 2011).

[77] Steven J. Weisman, *Concern about Sovereign Wealth Funds Spreads to Washington*, INTERNATIONAL HERALD TRIBUNE (August 20, 2007).

[78] There has been significant academic and media coverage of these events and their implications. *E.g.*: Philip Aldrick, *RBS and Northern Rock to Unveil Radical Strategies*, TELEGRAPH.CO.UK (February 22, 2009), at http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/4782762/RBS-and-Northern-Rock-to-unveil-radical-strategies.html; Roman A. Tomasic, *The Rescue of Northern Rock: Nationalization in the Shadow of Insolvency*, 1(4) CORPORATE RESCUE AND INSOLVENCY 109 (2008); Robert J. Rhee, *Nationalization of Corporate Governance and Purpose During Crisis*, 17 GEO. MASON L. REV. 661 (2010).

[79] For details and sources regarding the GAPP negotiation and implementation process, *see* George Gilligan and Megan Bowman, *State Capital: Global and Australian Perspectives*, SEATTLE UNIV. L. REV. (forthcoming 2013).

[80] *See* www.financialstabilityboard.org

[81] The Group of Twenty (G-20) Finance Ministers and Central Bank Governors was established in 1999 to bring together systemically important industrialized and developing economies to discuss key issues in the global economy. The inaugural meeting of the G-20 took place in Berlin on December 15-16, 1999, hosted by the German and Canadian finance ministers. The G-20 is made up of the finance ministers and central bank governors of 19 countries: Argentina; Australia; Brazil; Canada; China; France; Germany; India; Indonesia; Italy; Japan; Mexico; Republic of Korea; Russia; Saudi Arabia; South Africa; Turkey; United Kingdom; United States of America. The European Union, who is represented by the rotating Council presidency and the European Central Bank, is the 20th member of the G-20. *See* http://www.g20.org/about_what_is_g20.aspx

[82] As long ago as 2005 the OECD issued its guidelines on corporate governance of state-owned enterprises but political economy and commercial realities have limited the scale of influence of the OECD. *See* OECD, *supra* note 28.

that the best way for Australia to regulate the conduct of foreign investors (be they SWF, SOE or private commercial operator) is through developing robust domestic legislation.'[83] Accordingly, Part III focuses on the Australian FDI regime and the implications and impacts in Australia of global state capital trends.

III. IMPLICATIONS FOR AUSTRALIA

Parts I and II classified key pools of state capital and mapped their global evolution and momentum, particularly from emerging economies such as China. This has important implications for FDI into Australia given that Australia's 'post-boom' economic well-being is increasingly intertwined with neighboring jurisdictions in the Asian region. So Part III focuses on the impact to date of state capital in Australia and the prospect of future impacts in light of diminishing resources demand and rising global competition within the Asian Century.

A. Investment Impact of State Capital in Australia

For the fiscal year 2011/12, there were 10,703 FIRB-approved proposed foreign investment contracts (Table 3).[84] Chinese investment contracts comprised nearly half of this number, making China the largest proposed investor by contract *volume* followed by the UK, Japan, the US and Canada. However, in dollar *value*, the US is Australia's largest proposed investor, followed by the UK and then China, Japan and Canada. Moreover, Australia is currently the top destination for actual Chinese investment, narrowly ahead of the US (Table 4 below). However, while Australia is the largest recipient of Chinese FDI, China is not Australia's largest investor (Table 5 below). ABS data for the calendar year period 2006 to 2012 show that accumulated actual direct investment in Australia from the US equated to AU$747 billion, being a 24% share of Australia's total foreign direct investment stock.[85] This compares strikingly to China's direct investment for that same period which equated to only AU$57.3 billion or 2% share of the total. Accordingly, by the end of 2012, China was Australia's ninth largest direct investor, which may be lower than that assumed by many in the community given the high media coverage of China as Australia's most important trading partner.[86]

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[83] Parliament of Australia, The Senate Economics References Committee, FOREIGN INVESTMENT BY STATE-OWNED ENTITIES 47 (2009).
[84] Commonwealth of Australia, FOREIGN INVESTMENT REVIEW BOARD: ANNUAL REPORT 2011/12 (2012).
[85] Australian Bureau of Statistics, 5352.0 - INTERNATIONAL INVESTMENT POSITION, AUSTRALIA: SUPPLEMENTARY STATISTICS 2012, Table 2 (2012), available at http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/5352.02012?OpenDocument
[86] Indeed, Clayton Utz asserts that the value of completed Chinese investment in mining and energy sectors would 'likely amount to considerably less than 10%' of the total value of resources and energy projects in Australia: Clayton Utz, *supra* note 49, 9.

Table 3 FIRB Approved Proposed Investment: 2011/12[87]

Approved proposed investment	Deal Value (AU$ billions)	Number of Contracts
TOTAL	170.71	10,703
Top 5 countries by proposed investment value		
United States	36.613	268
UK	20.343	1,018
China	16.190	4,752
Japan	13.920	324
Canada	8.871	131

Table 4 Accumulated Chinese Investment by Country for Deals Above US$100 million: 1 January 2005 - 31 December 2012 (US$ millions)[88]

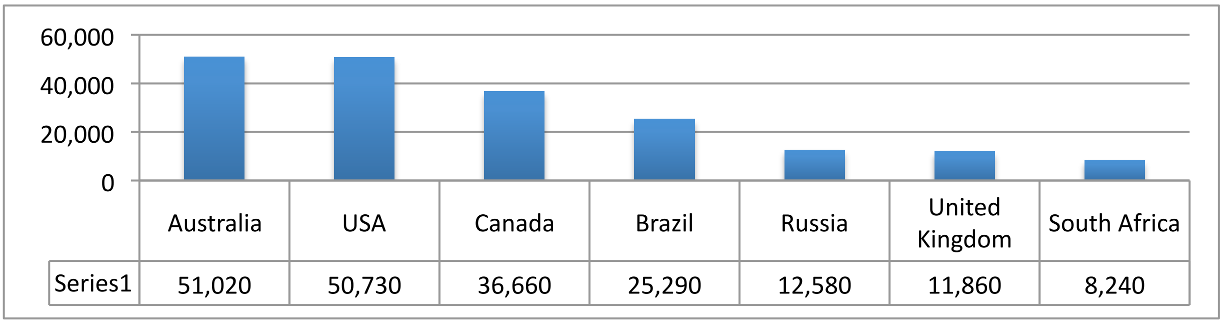

Table 5 Accumulated Direct Investment in Australia: 1 January 2006 – 31 December 2012 (AU$ millions)[89]

	Value	Percentage of Total	Investor Ranking
TOTAL - all countries	**3,099,195**		
Top 10 Countries			
United States	746,792	24.1%	1
UK	443,804	14.3%	2
Japan	303,638	9.8%	3
Netherlands	196,334	6.3%	4
Switzerland	136,602	4.4%	5
Singapore	109,532	3.5%	6
Germany	108,479	3.5%	7
France	78,034	2.5%	8
China (excluding SARs & Taiwan)	57,340	1.9%	9
Hong Kong (China SAR)	47,992	1.5%	10

87 Commonwealth of Australia, *supra* note 84.
88 The Heritage Foundation, *Chinese Outward Investment*, CHINA GLOBAL INVESTMENT TRACKER, Dataset 1 Investments (2013), available at http://www.heritage.org/research/projects/china-global-investment-tracker-interactive-map. *See* also KPMG and the University of Sydney, DEMYSTIFYING CHINESE INVESTMENT IN AUSTRALIA: UPDATE MARCH 2013, 2 (2013) (hereafter 'KPMG 2013').
89 Australian Bureau of Statistics, *supra* note 85.

However, if we view FDI through the lens of state capital investment, we see a very different picture. The majority of the 50 largest acquisitions of Australian assets since 1990 have been made by non-OECD state-related capital actors.[90] Indeed, the four most frequent state capital investors in Australia in descending order have been Singapore, China, UAE and New Zealand; and over 60% of investment number occurred in 'strategic' sectors of national interest (i.e. energy and power, telecommunications, materials and high technology) with the largest investments by value occurring in energy and power (Table 6).[91]

Table 6 State-related Capital Investment into Australian Companies: Ten Largest Deals from 1990-2009[92]

Deal Value ($US mn)	Target Sector	Acquirer Name (Nation)	Target Name	Date Effective
8,491.1	Telecommunications	SingTel (Singapore)	Optus Ltd	17 Sept. 2001
3,720.0	Energy & Power	Singapore Power Ltd (Singapore)	TXU Australia Ltd	30 July 2004
2,489.2	Energy & Power	PETRONAS (Malaysia)	Santos Ltd-Gladstone Liquefied	23 July 2008
1,376.9	Materials	Sinosteel Corp (China)	Midwest Corp Ltd	15 Sept. 2008
1,264.2	Energy & Power	Singapore Power Ltd (Singapore)	GPU Power Net Pty Ltd	30 June 2000
1,098.0	Energy & Power	IPIC (UAE)	Oil Search Ltd	5 Mar. 2009
595.6	Real Estate	GIC Real Estate Pte Ltd (Singapore)	Westfield Parramatta	30 Apr. 2007
556.0	Energy & Power	Sinopec Intl Petro Expl, Prodn (China)	AED Oil-Expl Permits	18 June 2008
537.3	Energy & Power	CNOOC Ltd (China)	North West Shelf Gas Pty Ltd	18 Dec. 2004
465.0	Energy & Power	SINOCHEM (China)	SOCO Yemen Pty Ltd	21 Apr. 2008

Specifically, SOE-led investments dominate the Sino-Australian investment landscape. FIRB Annual Reports do not differentiate between SOE and non-SOE foreign investments in Australia; however private sector research goes someway to filling these gaps. Clayton Utz, an Australian law firm, reports that for the period January 2005 to December 2012 in the Australian mining and energy sectors, Chinese SOEs accounted for 76% of deal volume and 100% of *all* deals greater than AU$250 million; and 97% of the accumulated *value* of those actual investments.[93] Regarding *total* Chinese SOE-led FDI in Australia, KMPG reports that investments valued US$5million and above for the period September 2006 to June 2012 comprised 116 deals by *volume* of which nearly 80% were made by 45 SOEs; and over 95% of deal *value* involved SOEs during this same timeframe (Table 7 below).[94] Those percentages are notably higher than average Chinese SOE-led investment deal value figures for the US (65%) and Europe (72%).[95] Indeed, the ten largest Chinese corporate investors in Australia all happen

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[90] Blundell-Wignall and Wehinger, *supra* note 8, 139, Table 6.5.
[91] *Id.*
[92] Statistics excerpted from Blundell-Wignall and Wehinger, *id.*, Table 6.5.
[93] Clayton Utz, *supra* note 49, 4.
[94] KPMG 2012, *supra* note 52, 9. In 2012 alone, SOEs completed 74% of all deals (valued US$5mn and above) by volume and 87% by deal value of the total Chinese inward investment into Australia: KPMG 2013, *supra* note 88, 1. Note, however, that the KPMG reports do not reveal original sources of their SOE figures.
[95] *See*: Daniel H. Rosen and Thilo Hanemann, *An American Open Door? Maximizing the Benefits of Chinese Foreign Direct Investment*, RHODIUM GROUP 33 (2011), noting that SOE investment in the US by deal *volume* is much less at

to be SOEs. These ten SOEs accounted for US$39,000 million out of a total accumulated direct investment of US$51,020 million for 1 January 2005 to December 2012, which equates to 76% of accumulated Chinese direct investment into Australia over the past seven years.[96]

Table 7 Chinese Investment into Australia: September 2006-December 2012 vs. 2012[97]

	2006-2012		**2012**	
	By volume	**By deal value**	**By volume**	**By deal value**
SOE share of capital invested	80%	94%	74%	87%
Private (non-state) investment	20%	6%	26%	13%

The preceding data provide three key findings. First, they demonstrate that the largest (by value) acquiring nations in Australian assets over time have been Singapore, China and the UAE. Secondly, they confirm sectoral targets of investment by state capital actors (specifically SOE-led investment) in the 'strategic' areas telecommunications, energy & power, and materials. Finally, energy and power state-led capital investments dominate the Australian FDI landscape, which reflects its relative abundance of natural resources. This has given Australia a comparative advantage as an investment destination in this sector to date.

However, there are important implications for state-led FDI into Australia given the 'post-boom' economy and increasing global competition for FDI. Accordingly, the next section examines Australia's policy response to state capital investments in a changing global context.

B. National and International Regulatory Issues

OECD 'soft law' documents, such as the *OECD Code of Liberalisation of Capital Movements of 1961*[98] and *OECD Declaration on International Investment and Multinational Enterprises of 1976*,[99] advance a general principle of non-discrimination whereby foreign investment should be treated in the

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26%; and Thilo Hanemann & Daniel H. Rosen, China Invests in Europe: Patterns, Impacts and Policy Implications, RHODIUM GROUP 4, 45 (2012), noting that SOE investment in Europe by deal *volume* is only 33%. Chinese statistics of SOE-led outward foreign investment is approximately 70%: Ministry of Commerce China, 2010 STATISTICAL BULLETIN OF CHINA'S OUTWARD FOREIGN DIRECT INVESTMENT (2011).

[96] The Heritage Foundation, *supra* note 88. Note that these figures comprise deals valued at US$100 million and above.

[97] KPMG 2013, *supra* note 88, 1, 15.

[98] OECD, OECD CODE OF LIBERALISATION OF CAPITAL MOVEMENTS (2013), available at http://www.oecd.org/D3B892FA-AAE2-4962-B534-04D01D8EF955/FinalDownload/DownloadId-204837D2BD7E4DA397063176D16CE1C9/D3B892FA-AAE2-4962-B534-04D01D8EF955/daf/inv/investment-policy/capital%20movements_web%20english.pdf Article 1 states that member States shall progressively abolish restrictions on movements of capital to the extent necessary for effective economic co-operation between each other, including treating all non-resident owned assets in the same way irrespective of the date of formation.

[99] OECD, OECD DECLARATION ON INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISE (1976) as reviewed 1979, 1984, 1991 and 2000, available at http://www.oecd.org/daf/investment/declaration. Item II of the declaration requires that governments should, 'consistent with the need … to protect their interests', accord to enterprises operating in their territories and owned by foreign nationals treatment under their laws treatment that is no less favorable than that accorded in like situations to domestic enterprises.

same way as domestic investment.[100] Nonetheless, the OECD also recognizes that governments are entitled to protect their national security under international law.[101] Foreign investment may threaten national interests or security if it is for non-commercial (i.e. political) purposes in sensitive areas, such as defence or information technology. Thus, it is accepted that domestic foreign regulation may be appropriate where national security is at stake.

The Australian regime under which foreign companies can invest in businesses and purchase Australian property comprises three main documents: the *Foreign Acquisitions and Takeover Act* 1975 (Cth) (FATA); the *Foreign Acquisitions and Takeovers Regulations 1989*; and Australia's Foreign Investment Policy (AFIP).[102] The Australian Federal Treasurer has ultimate responsibility for decision-making under Australia's foreign investment regime and has a broad discretion to decline any foreign investment applications that he or she considers to be against the national interest. The Treasurer receives recommendations on specific foreign investment proposals from the Foreign Investment Review Board (FIRB) which is an advisory not policymaking body that administers FATA and AFIP.[103] Once a review is triggered, chief consideration is given by FIRB to whether the proposed investment will be contrary to the national interest.

Under the current AFIP any 'direct investment' in land or business by a 'foreign government investor' (such as a SOE or SWF) is subject to review by FIRB. An entity is considered to be a 'foreign government investor' if a foreign government has a 15% or more interest in it. 'Direct investment' comprises an investment of an interest of 10% or more; however, AFIP was amended on 4 March 2013 such that a 'direct' investment may now be less than 10% where the 'acquiring foreign government investor is building a strategic stake in the target, or can use that investment to influence or control the target'.[104] Moreover, additional *Guidelines for Foreign Government Investment Proposals*[105] (the Guidelines) were released in 2008 that set out six factors to which the government will have regard when assessing an investment proposal by a SWF or SOE specifically. These factors are: the degree to which a state actor is independent from their government sponsor and is observing common standards of business behaviour; and the degree to which an investment may impede competition in the relevant industry/sector, impact on revenue or other policies, impact on the Australian economy, broader community, and/or national security. The Guidelines purported to 'enhance the transparency of Australia's foreign investment screening regime'.[106] However, no guidance was given by the government regarding how these six factors might impact upon consideration of the national interest, or the extent to

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100 This commitment was recently confirmed in this statement: 'G-20 Leaders, at their last Summit meeting in Los Cabos in June 2012, expressed their firm commitment to open trade and investment, expanding markets and resisting protectionism in all its forms, which were considered as necessary conditions for sustained global economic recovery, jobs and development': OECD, WTO OMC and UNCTAD, REPORTS ON G20 TRADE AND INVESTMENT MEASURES (MID-OCTOBER 2012 TO MID-MAY 2013) 5 (June 17, 2013), at http://www.oecd.org/daf/inv/investment-policy/foi.htm

101 *See* OECD, ROUNDTABLE ON FREEDOM OF INVESTMENT 18, 4 (March 20, 2013), at http://www.oecd.org/daf/inv/investment-policy/foi.htm The Freedom of Investment Roundtable forms part of the Freedom of Investment Process, which is an intergovernmental forum hosted by the OECD Investment Committee since 2006.

102 Australian Government, The Treasury, AUSTRALIA'S FOREIGN INVESTMENT POLICY (2013), available at www.firb.gov.au/content/_downloads/AFIP_2013.pdf (hereafter 'AFIP').

103 *See* www.firb.gov.au/content/default.asp

104 AFIP, *supra* note 102, 14

105 Treasurer of the Commonwealth of Australia, *Government Improves Transparency of Foreign Investment Screening Process*, MEDIA RELEASE 009 (February 17, 2008), at http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2008/009.htm&pageID=003&min=wms&Year=&DocType

106 *Id.*

which government needs to be satisfied about each of them in order to approve an investment proposal.

Furthermore, the phrase 'national interest' is not legislatively defined despite the clear importance of knowing what it is in order to protect it. Indeed, cases are decided on an individual basis in the context of the following issues: national security; competition; impact on the economy and community; Australian government policies such as tax; and the character of the investor.[107] Arguably, therefore, the above policy developments indicate shifting ground with a more restrictive and less consistent approach toward state capital FDI *vis à vis* other forms of FDI capital, as discussed in detail below.

There are many factors that can help to shape the 'national interest' including the government of the day, scale and types of FDI, the prevailing economic climate especially the national fiscal budgetary position, broader political influences, and on occasion unfortunately, populism. While rejection of foreign investment applications is not statistically a common event in Australia,[108] the increased desire of state capital actors to invest in Australia, especially regarding the acquisition of Australian natural resources assets has seen politics and populism assume a higher profile in the discourse on Australian foreign investment.

In this respect, the intrinsic nature of an SOE seems to capture media sensationalism and influence political discourse and policy. For example, recent media headlines in Australia include 'China's state-owned enterprises obtain FIRB approval by stealth',[109] and 'Don't mix politics and deals: FIRB in warning to state-owned investors'.[110] Moreover, there have been specific Australian regulatory responses to the spectre of Chinese state capital inflows. For example, during 2008 a Chinese SOE Chinalco first sought to take a significant stake in major Australian miner Rio Tinto and there was heated public debate about potential threats posed by state capital interests owning strategically important Australian entities. Two weeks later on 17 February 2008, the then Treasurer Mr. Wayne Swan released six principles to improve the transparency of foreign investment screening processes that more clearly distinguish between investments by private entities and by foreign governments.[111] Eventually on 24 August 2008 the Treasurer did grant approval to Chinalco to acquire up to 14.99% of Rio Tinto because Chinalco had undertaken to the Treasurer not to raise its holdings without seeking fresh approval from the Australian Government and would not seek to appoint a director to Rio Tinto plc. or Rio Tinto Limited.[112] Similarly, on 27 March 2009, the Treasurer announced that China Minmetals Non-Ferrous Metals Co Ltd could not make a 100% acquisition of Oz Minerals if it included the Prominent Hill mining operations located within the Woomera Prohibited Area in South

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107 AFIP, *supra* note 102, 7-8

108 *E.g.*, in 2011-2012, 10,703 applications for foreign investment proposals were approved with 5,803 subject to conditions and 4,900 without conditions being imposed, 13 were rejected, 534 proposals were withdrawn and 170 were deemed exempt. It is noticeable that real estate comprised the vast bulk of activity with 10,118 (94.5%) of the approvals and all of the 13 rejections: Commonwealth of Australia, FOREIGN INVESTMENT REVIEW BOARD: ANNUAL REPORT 2011-12, 19, 20 (2012).

109 Bryan Frith, *China's State-Owned Enterprises Obtain FIRB Approval by Stealth*, THE AUSTRALIAN (March 13, 2013), at http://www.theaustralian.com.au/business/opinion/chinas-state-owned-enterprises-obtain-firb-approval-by-stealth/story-e6frg9kx-1226595937750

110 Enda Curran and Michael Sainsbury, *Don't Mix Politics and Deals: FIRB in Warning to State-Owned Investors,* THE AUSTRALIAN (August 7, 2012), at http://www.theaustralian.com.au/national-affairs/foreign-affairs/dont-mix-politics-and-deals-firb-in-warning-to-state-owned-investors/story-fn59nm2j-1226444324395

111 Treasurer of the Commonwealth of Australia, *supra* note 105.

112 Treasurer of the Commonwealth of Australia, *Chinalco's Acquisition of Shares in Rio Tinto*, MEDIA RELEASE NO.094 (August 24, 2008), at www.treasurer.gov.au/DisplayDocs.aspx?doc=pressrelease/2008/094.htm&pageID=003&min=wms&Year=&DocType

Australia.[113] On 23 April 2009, the Treasurer did give approval, but with the Prominent Hill mine not included and numerous other undertakings from China Minmetals Non-Ferrous Metals Co. Ltd.[114] These are just a couple of the decisions made in recent years under Australia's foreign investment regime that Chinese interests have felt have been discriminatory towards them. This disquiet has received media coverage recently following the high-profile Australian Government delegation to China in April 2013 led by then Prime Minister Julia Gillard that undertook trade and other inter-governmental negotiations. At that time, then-Trade Minister Craig Emerson 'admitted that talks on a free-trade deal with China have stalled because of a dispute over restrictions on investment in Australia by Chinese state-owned enterprises.'[115]

The OECD Council on Recipient Country Investment Policies relating to National Security has recommended that, while nations may impose restrictions on foreign investment for national security reasons, those measures ought to be applied in a way that ensures the regime is predictable, transparent, proportionate and accountable.[116] This commitment was recently affirmed by G20 Leaders in June 2013:

> We recall that G-20 Leaders, at their last Summit meeting in Los Cabos in June 2012, expressed their firm commitment to open trade and investment, expanding markets and resisting protectionism in all its forms, which were considered as necessary conditions for sustained global economic recovery, jobs and development. They underlined the importance of an open, predictable, rules based, transparent multilateral trading system, and their commitment to ensure the centrality of the WTO. Recognizing the importance of investment for boosting economic growth, they made the commitment to maintaining a supportive business environment for investors.[117]

This commitment to predictability and transparency ensures that the national security clause of the OECD investment instruments does not become an 'escape clause' for nationalism or protectionism in the sectors concerned.[118] However, industry commentators, such as Golding, have opined that Australia's shifting formulation and application of the 'national interest' test and its differential policy development for state capital FDI *vis à vis* other forms of FDI capital have undermined this commitment.[119]

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113 Treasurer of the Commonwealth of Australia, FOREIGN INVESTMENT (March 27, 2009), at www.treasurer.gov.au/DisplayDocs.aspx?doc=pressrelease/2009/029.htm&pageID=003&min=wms&Year=&DocType

114 Treasurer of the Commonwealth of Australia, FOREIGN INVESTMENT DECISION (April 23, 2009), at www.treasurer.gov.au/DisplayDocs.aspx?doc=pressrelease/2009/043.htm&pageID=003&min=wms&Year=&DocType

115 John Kerin and Natalie Gerritsen, *Curbs on State Business Stall China Deal*, THE AUSTRALIAN FINANCIAL REVIEW 9 (April 19, 2013).

116 OECD, OECD GUIDELINES FOR RECIPIENT COUNTRY INVESTMENT POLICIES RELATING TO NATIONAL SECURITY (2009) (adopted by the OECD Council on 25 May 2009), available at http://www.oecd.org/daf/inv/investment-policy/41807723.pdf

117 OECD WTO OMC and UNCTAD, *supra* note 100.

118 Blundell-Wignall and Wehinger, *supra* note 8, 116.

119 *See e.g.* Golding, *supra* note 32.

C. Prospective Impacts of State Capital in Australia?

The preceding section demonstrated how Australian politics and populism can interact and inform responses to FDI. While the use of *law* via FATA to deny resource investment has been relatively infrequent, the question is whether Australia can afford to restrict state capital due to shifting *policy* on 'national interest' particularly in the context of diminishing demand for resources and growing competition for FDI.

The release in May 2013 of the report *Energy in Australia* by the Commonwealth Government's Bureau of Resources and Energy Economics (BREE) fuelled the debate about whether Australia's so-called 'resources boom' has peaked.[120] BREE is the key forecaster on commodities for the federal government and it delivered a number of chilly messages on the near-term projections for Australia's resources and energy sector, despite the current rosy picture. For example, on the plus side, Australia's energy sector accounts for 6% of Australia's total industry value, and has provided $77 billion of energy exports in 2011-2012; currently it has committed and potential projects totaling $350 billion (approximately 18% of GDP). However, on the negative side, the value of committed and potential projects is expected to fall to $25 billion in 2018. This dramatic downturn has already been signaled during the last year by the setting aside of $150 billion in energy and mining projects including Aquila's West Pilbara iron ore mine in Western Australia, BHP's Olympic Dam expansion in South Australia and Woodside Petroleum's Browse LNG project in Western Australia. The bad news concerning shelved projects such as these is amplified by revelations of cost blowouts of more than $29 billion regarding existing projects. A 96% fall in large-scale investment in energy and resources in only five years is a massive slide and prompted a flurry of headlines proclaiming that Australia's resources boom has indeed ended.[121]

To this end, there is some disparity between domestic jurisdictions *within* Australia regarding their approach to and the impacts of state capital. In particular, the West Australian (WA) government welcomes foreign investment in mining and minerals resources, particularly from China. According to qualitative evidence from O'Brien, WA officials differentiate between 'stock market miners' and 'real miners' when facilitating inward investment.[122] Given the decrease in commodities' value, many stock market miners are not activating their exploration rights to actualize extraction and hence royalty accumulation.[123] However, Chinese investors are activating their rights and therefore making real mining investments that manifest real dollars to help perpetuate the state's long-term agenda.[124] Indeed, the 2011 WA-China Memorandum of

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[120] Australian Government, Department of Resources, Energy and Tourism, Bureau of Resources and Energy Economics, ENERGY IN AUSTRALIA, May 2013 (2013), available at http://www.bree.gov.au/publications/energy-in-aust.html

[121] Paul Garvey, *Resources Boom is Truly over Says Focus Minerals Chair Don Taig*, THE AUSTRALIAN (May 15, 2013), http://www.theaustralian.com.au/national-affairs/treasury/resources-boom-is-truly-over-says-focus-minerals-chair-don-taig/story-fnhi8df6-1226642524237; Gemma Daley, *The Party's Over: Resources boom has peaked says chief commodities forecaster*, BUSINESS REVIEW WEEKLY (May 23, 2013), http://www.brw.com.au/p/business/forecaster_party_over_resources_xmIAuQKUh2Iq3Yx4cbYtlN;

[122] O'Brien, *supra* note 31, 165.

[123] Richard Schodde, and Pietro Guj, *Where are Australia's Mines of Tomorrow?* CENTRE FOR EXPLORATION TARGETING (CET) UNIVERSITY OF WESTERN AUSTRALIA (UWA) (September 2012), at http://www.cet.edu.au/research-outcomes/publications/revised-cet-paper---australian-mineral-exploration-3-sept-2012927088B5F038 They state that 'Australian exploration expenditure fell during the March 2012 quarter in all states and for all commodities, particularly for iron ore and coal': *id.* at 1.

[124] *E.g.* Between 2006-2012 China invested US$16, 030.82 million total into WA of which 89% ($14, 307.66 million) was in the mining sector alone: KPMG 2013, *supra* note 88, 13.

Understanding on the promotion of investment cooperation[125] and the opening of a WA Trade and Investment Promotion office in Shanghai in 2012[126] send very clear messages that this Australian state is open for Chinese investment.

The disparity between regulatory approaches at federal and state levels in Australia has led commentators to speculate whether the nation is operating a 3-speed economy. That is, Tasmania and South Australia may well be moving in reverse (to a recession); WA and Queensland appear to be moving ahead due to intrinsic abundance; and New South Wales and Victoria are sitting somewhere in the middle.[127] However, this outlook can be questioned based on recent Australian Bureau of Statistics (ABS) figures.

Quarterly ABS figures released on 5 June 2013, show that Australia's GDP grew 0.6% in the quarter from December 2012.[128] However, disaggregating figures for each state via 'state final demand' - the partial measure of state economic growth contained in the national accounts - is revealing. State final demand in Queensland grew 0.6%, as did Victoria (0.8%) and NSW (0.4%). Moreover, South Australian state final demand fell 0.3% (the third quarterly fall in a row) and Tasmania fell 1.1%. However, WA's state final demand fell by 3.9%, seasonally adjusted, which is the biggest fall in the country and came on top of a 0.9% decline in the previous quarter. While WA has averaged annual growth rates of almost 8% over the past decade, these state final demand statistics have wiped 0.6 percentage points off the Australian economy in the past year.[129] While we need to be cautious with causality, arguably the decline in state final demand for WA can be correlated to the declining demand for natural resources. In June 2013, then-Treasurer Mr. Wayne Swan stated that 'WA is a demonstration of the transition that we are making which is amplified in WA because mining is such a greater proportion of the economy'.[130]

IV. CONCLUSION

The increasing prevalence and impact of state capital actors in the global economy is undeniable, which carries significant implications for Australia as an investment destination. While definitional difficulty surrounds pools of state capital, this paper has classified SWFs and SOEs as key state capital actors, and mapped their scale, scope and investment strategies in both global and Australian contexts. The prospect of future impacts of state capital in Australia remains uncertain in light of diminishing global demand for resources and shifting domestic policy

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125 Western Australia and National Development and Reform Commission of the People's Republic of China, MEMORANDUM OF UNDERSTANDING BETWEEN THE GOVERNMENT OF THE STATE OF WESTERN AUSTRALIA OF THE COMMONWEALTH OF AUSTRALIA AND THE NATIONAL DEVELOPMENT AND REFORM COMMISSION OF THE PEOPLE'S REPUBLIC OF CHINA ON PROMOTION OF INVESTMENT COOPERATION (2011), at http://www.dsd.wa.gov.au/4868_8430.aspx

126 *See* http://www.westernaustralia.cn/index.asp

127 Alicia Barry, *Australia Running on 3-speed Economy*, WWW.ABC.NET.AU (Jan. 23, 2012), at http://www.abc.net.au/news/2012-01-23/australia-running-on-3-speed-economy/3787232

128 Australian Bureau of Statistics, 5206.0 - AUSTRALIAN NATIONAL ACCOUNTS: NATIONAL INCOME, EXPENDITURE AND PRODUCT, MAR 2012 (2012), at http://www.abs.gov.au/AUSSTATS/abs@.nsf/Previousproducts/5206.0Main%20Features6Mar%202012?opendocument&tabname=Summary&prodno=5206.0&issue=Mar%202012&num=&view=

129 David Uren, *Growing Pains as Western Australia Hits Slow Lane*, THE AUSTRALIAN (June 6, 2013), at http://www.theaustralian.com.au/national-affairs/state-politics/growing-pains-as-western-australia-hits-slow-lane/story-e6frgczx-1226658170307 *see* also Bernard Keane, *National Accounts: How long will exports keep us growing?* CRIKEY.COM (June 5, 2913), at http://www.crikey.com.au/2013/06/05/national-accounts-how-long-will-exports-keep-us-growing/

130 *Id*. Uren describes Queensland's mild growth as 'reflecting sharp cuts in government investment in infrastructure and lower growth in private sector investment': Uren, *id*.

regarding government-directed foreign actors. What is certain, however, is that Australia will remain a net importer of capital in a world in which competition for that investment dollar is increasing from many countries. Yet it remains to be seen how much the twin pressures of increased FDI competition and declining demand for Australian resources impact upon the *realpolitik* of Australia's foreign investment regulatory regime at national and state levels.

Certainly, federal political influence was palpable in the June 2013 Final Report of The Senate Rural and Regional and Transport Committee (the Committee), which focused on foreign investment into Australian agriculture.[131] Of most relevance to FDI generally in Australia,[132] was the Committee's recommendation that the federal government instigate 'an independent and wide-ranging review of Australia's foreign investment regulatory framework' (Recommendation 4). To this end, the Committee specified that regulatory review must ensure that foreign investments in Australian agriculture are genuinely commercial, do not distort the capital market or trade in agricultural products, and compete fairly with Australian farmers and agribusinesses. In particular, the Committee noted evidence of rising concerns about foreign investment in Australian agribusiness, stemming from: increasing global food security issues ('the growing global food task'); a lack of transparency about the FIRB national interest test; and empirical information gaps regarding levels and types of foreign investment in Australia.[133] Specifically, the Committee recommended forensic examination of company structures (including management relationships in joint Australian/foreign ventures); the relationship between a foreign government's acquisitions strategy (such as food security) and the commercial operation of their subsidiary businesses in Australia; and ways of setting clear and auditable ongoing undertakings that are in the 'national interest'.

Such a review, if undertaken, may well encourage state capital investment by increasing predictability and transparency as agreed by the OECD and G20 Leaders. Yet it may not be sufficient to remedy disparity between federal and state approaches to state capital FDI. Perhaps one way forward is regulatory harmonization across domestic jurisdictions, as recommended by the 2013 *Advantage Australia* report.[134] Similarly, the federal government's 2012 *Australia in the Asian Century White Paper*[135] (White Paper) stipulates that: 'The Australian economy will be more open and integrated with Asia, through efforts to improve our domestic arrangements'.[136] This includes 'improving regulatory frameworks in support of greater financial integration', maintaining consistent and transparent foreign investment decision-making, and 'welcoming foreign investment' as a way of supporting Australian businesses.[137] However, as the 2013 federal election looms ever closer, it is less certain whether Australia will remain on course for regulatory integration and transparency as per the White Paper roadmap. And, if Australia is to develop a new roadmap under a government led by the current Opposition, it remains to be seen whether it would lead the nation and its constituent jurisdictions toward or away from a more coherent regulatory approach to state capital investment.

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131 Commonwealth of Australia, Senate Standing Committees on Rural and Regional Affairs and Transport, FOREIGN INVESTMENT AND THE NATIONAL INTEREST (2013).

132 The Committee made 29 recommendations in all, ranging from topics of tax revenue leakage (Recommendations 1-2), establishing an Independent Commission of Audit into Agribusiness (Recommendation 3) and a national agricultural land register (Recommendations 6-9, 11-15), and improving access to domestic finance for Australian agricultural businesses from Australian banks (Recommendation 27): *id.*

133 *Id.*, par 1.3.

134 Leah Mason, Nic Mikhailovich, Gavin Mudd, Samantha Sharpe and Damien Giurco, ADVANTAGE AUSTRALIA: RESOURCE GOVERNANCE AND INNOVATION FOR THE ASIAN CENTURY (prepared for CSIRO Minerals Down Under Flagship by the Institute for Sustainable Futures (UTS, Sydney and Monash University, Melbourne, 2013).

135 Australian Government, *Australia in the Asian Century* WHITE PAPER: OCTOBER 2012 (2012).

136 *Id.*, 195 'National Objective 18a'.

137 *Id.*, 195, 187.

Regardless, it is clear that the global economic center of gravity is moving progressively eastward as China develops ever-deepening international linkages. Indeed, the chief economist of HSBC, Stephen King, has described the strategic integration by China of global trading nodes (largely financed through pools of state capital) as the re-emergence of the Southern Silk Road.[138] Arguably, concerns about the increasing prevalence and potentially political nature of SWFs and SOEs obscures the real issue of contention which is 'how do we deal with China?' Masking the nature of that real debate will not help to resolve it.

[138] Stephen King, *The Southern Silk Road: Turbocharging South-South Economic Growth*, HSBC GLOBAL RESEARCH (2011).