Introduction

The Paradox of Foreign State Investments in an Age of Economic Liberalism

In 2007, the state-owned Investment Corporation of Dubai bought the world-famous British landmark Madame Tussauds. Not to be outdone, the Qatar Investment Authority acquired Harrods, historic buildings in London and Paris, and a share of the major football club, Paris St Germain. Meanwhile, in New York, the Abu Dhabi Investment Authority bought the iconic Chrysler Building and the Kuwait Investment Authority a stake in the Hudson's Yard development.

But state-owned foreign investors have gone well beyond landmark buildings and trophy companies. They have also bought shares in strategic firms in sectors that range across finance, food, communications, and transport. The Qatar Investment Authority acquired 20 per cent of the London Stock Exchange Group, in 2008 amassed almost 25 per cent of shares in the popular middle-class British retailer J Sainsbury, and in 2013 procured more than 6 per cent of Barclays bank. Its purchases extended to other countries and firms, such as the German carmaker Volkswagen and the French communications firm Lagardère. Nor was it alone: the Chinese state-owned investor CIC took stakes in Morgan Stanley and the international communications operator Eutelsat, the Kuwait Investment Authority a stake in the German carmaker Daimler, and the Singaporean Temasek shares in Dell and the financial group Standard Chartered. The Saudi Public Investment Fund acquired holdings in BP, Boeing, Facebook, Walt Disney, Cisco Systems, Marriott, Pfizer, and Starbucks.

These are just a few examples of the many major purchases by Sovereign Wealth Funds (SWFs): state-owned investors who buy assets abroad. Not only are SWFs expanding in size and number, but they also offer a prominent case of a wider phenomenon—state-owned organizations using the liberalization of financial markets to acquire overseas economic assets. They also illustrate the rapidly changing nature of the international economic system, since most SWFs are based in the Middle East and Asia.

National responses to SWF purchases might be expected to be hostile, especially as they represent entry into Western stock markets by non-Western overseas states with very different political and economic systems. Yet governments in the UK, France, and Germany have engaged in 'international statism': policies to

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actively encourage and indeed seek overseas state investments as part of economic and political strategies to govern their domestic economies. Only in the US have policy makers introduced significant restrictive legal provisions that discriminate strongly against overseas state investors and been more cautious in seeking out SWFs.

We study policies in the US, the UK, France, and Germany towards non-Western SWFs to examine what happens when overseas states enter markets for domestic assets and in particular, whether internationalized statism is adopted and what forms it takes. In so doing, we engage with central debates in political economy about the nature and effects of the liberalization and internationalization of capital flows and financial markets. Whereas significant academic and popular literatures have argued that these market developments have greatly reduced the power of national policy makers, a 'new statist' literature argues that in fact states both shape such developments and use them to find new opportunities for action.

Academic debates have centred on the internationalization of private capital. Yet SWFs illustrate that states can also internationalize as economic actors, crossing national borders thanks to the very liberalization of financial and capital markets that are supposed to reduce state power. In turn, policy makers in recipient countries may utilize such investment for their domestic purposes. Building on new statist literature, the book therefore develops and applies the concept of 'internationalized statism': policies to use foreign states in domestic markets. Internationalized statism recognizes that thanks to liberalized markets, the state's economic role spans the national–international division and hence internationalization also offers new opportunities for states to govern their domestic markets.

0.1 States as International Investors and the Case of Non-Western Sovereign Wealth Funds

Although the West is said to be living in an age of 'economic (neo-)liberalism', the state has not disappeared as a central economic actor. On the contrary, paradoxically, using liberalization of markets, it has become an international economic actor. Quite apart from its general regulatory and macro-economic functions, it has continued and developed its direct roles in international investment. Today, publicly owned investors increasingly operate across national borders.

Sovereign Wealth Funds (SWFs) represent the most prominent example of these international state investors. They have grown in number and size to reach trillions of dollars today, accounting for significant shares of world equity markets, with the top twenty having assets of $7 trillion and SWFs as a whole being valued at over $9 trillion in 2020. Many of the largest SWFs are based in non-Western countries: China, Abu Dhabi, Saudi Arabia, Kuwait, Qatar, and Singapore, to give just some examples. Their expansion since 2000 has been rapid. They have bought a very wide range of Western assets, including shares in strategic sectors and companies.

SWFs are part of a wider group of cross-border state investors. State-owned enterprises have established overseas subsidiaries, invested in overseas operations, and taken over foreign companies. To give just a few examples: the majority French state-owned EDF is one of the largest electricity suppliers in Europe, thanks in part to their overseas acquisitions; in 2013 the Chinese state-owned SINOPEC bought a half-stake in oil assets from the American Chesapeake corporation for more than a billion dollars; the Chinese General Nuclear Power Group became part of the consortium for new British nuclear power stations; and Dubai Ports World handles almost 10 per cent of global container traffic and operates ports installations in over forty countries worldwide. Equally, public pension funds have become international investors, buying assets such as shares and bonds. They include entities such as the California Public Employees' Retirement System (CalPERS) with hundreds of billions of dollars of assets or the pension funds of British local authorities. At the end of 2020, public pension funds were valued at over $18 trillion.

State development banks too can become international investors by taking stakes in companies who themselves have overseas assets. They can also form part of international consortia or partnerships and joint ventures with foreign companies. Just one example is provided by the Long-Term Investors Club, started in 2009 by several public investment banks including the French Caisse des Dépôts et Consignations, the Italian Cassa Depositi e Prestiti, the European Investment Bank, and Kreditanstalt für Wiederaufbau (KfW). Equally, states can buy assets overseas or lend funds against them. One prominent example is Chinese state lending on the Belt and Road Initiative to investors in Asia; another is the purchase of overseas land, notably in Africa and Latin America, by countries such as China and Saudi Arabia.

Less visible but of enormous size are state acquisitions of government bonds. Whereas governments traditionally used to finance their deficits by selling their debt to domestic purchasers, today they sell significant amounts overseas, including to public purchasers. The best-known example concerns China, where investors held more than $1 trillion of US government debt in 2020.

The size of public ownership of overseas assets has greatly risen in recent years, especially after the 2008 financial crisis and the Covid pandemic of 2020. Governments and public bodies such as central banks have rescued companies. Equally, state development banks have expanded their investments, both through their own spending and via guarantees. The largest and most visible forms have been central bank purchases of company debt and then government rescues of failing companies. Many of these companies have assets overseas, and hence public bodies find themselves as direct and indirect owners of foreign assets.

Not only have states become important owners of overseas assets, but the distribution of assets has altered dramatically. Whereas Western bodies dominated financial markets after 1945, in recent decades non-Western states have become large international investors. The most prominent example after the 1973 oil price shock was Middle Eastern states, notably in the Gulf, who had enormous surpluses to recycle and invest. Then since the early 2000s, as China became a large economy and enjoyed very substantial trade surpluses, the Chinese state emerged as one of the largest overseas state investors, be it in terms of shares, bonds, or foreign currencies.

Overseas state acquisition of domestic assets raises many political issues and potential fears. One concerns 'national security', which may extend beyond defence equipment to cyber security, energy security, or economic security. There may be concerns that the overseas state will use its ownership for political aims. More subtly, it may be able to alter incentive structures for domestic actors, threatening retaliation if its wishes are not met while increasing gains if they are. It may also engage in unfair competition to aid its own firms, through forms that range from currency manipulation to restricting entry and price competition. These fears are likely to be strongest for states which differ greatly politically and culturally from the recipient country.

Political, security, and economic concerns in the West (whether justified or not) would be expected to be especially strong for non-Western SWF purchases of company shares. Many SWFs are from non-democratic states, frequently in unstable regions of the world. Some may be seen as rivals to Western countries, notably China. Others are regimes subject to political and religious ideologies that are far from those of the West, notably in the Middle East and Asia. Equity stakes can raise particular concerns since they offer corporate influence or control. Policy makers may fear that SWFs and their state owners will use their shareholdings for non-commercial political purposes—through exercising their voting rights, obtaining sensitive information, acquiring new technologies, or disrupting markets. In addition, their purchases represent the reversal of decades of privatization in Western countries, and moreover by an overseas state. Given these concerns, we could expect vigorous Western state responses to SWF investments. Regardless of whether SWFs are in fact threatening, they offer many opportunities for being criticized and labelled as such, especially in times of nationalism and backlash against 'globalization'.

Thus, non-Western SWFs represent an important and expanding example of state economic internationalization. Given potential resistance to their investments on security, symbolic, and financial grounds, they offer a politically unlikely case for Western policies of internationalized statism. This concept relates to central debates in political economy about the capacities of national policy makers in an age of internationalized and liberalized financial markets.

0.2 Internationalized Statism, SWFs, and Domestic Politics

The effect of international capital liberalization on national policies to promote selected domestic firms is a core question in political economy. An important literature argues that vast transnational capital flows have eroded the capacity of states to take autonomous decisions about how to govern their domestic economies. States can no longer close markets to protect selected domestic firms and instead must attract highly mobile international capital.

In contrast, a 'new statist' scholarship has argued that policy makers in advanced capitalist nations continue to enjoy autonomy to govern their domestic economies. They can lead and mould the internationalization and liberalization of markets. They can combine opening markets and continuing to promote domestic firms, but through new forms of action, notably selective liberalization and regulation. The state, far from being weakened, uses the international opening of markets to enhance its capacities within the domestic economy.

However, new statist works focus on the internationalization of private capital, ignoring the capacity of the state itself to become a cross-border economic actor. To extend statist studies, we develop the concept of internationalized statism: public policies in recipient countries to seek and use foreign states as part of strategies to govern domestic markets. In the case of cross-border state investments, we distinguish two dimensions of internationalized statism. The first is its extent: the degree to which policy makers actively seek to attract overseas state investment as part of strategies to govern their domestic economies. The second concerns its form: the degree to which the recipient state looks to select specific overseas state investors and channel their purchases towards particular firms and sectors (i.e. its directedness).

Internationalized statism is not just accepting or encouraging overseas investment in general—it refers to *policies* that specifically aim to attract overseas *state* investors as part of political and economic strategies concerning the domestic economy. Internationalized statism matters for political economy because it reveals how policy makers use capital market internationalization and liberalization to find new sources of capital from overseas states, who may operate according to different logics than private (domestic or foreign) investors. More broadly, it offers a new conceptual framework to analyse changes in financial markets that may not just constrain national policy makers but also give them new instruments and opportunities to govern their domestic economies. The framework allows us to analyse the growing and important phenomenon of cross-border state investment. It thereby adds to new statist literatures by bringing in the economic internationalization of the state and counters arguments that national policy makers are necessarily facing reduced abilities to govern their economies.

We develop arguments about the prevalence and limits of internationalized statism—whether, how, and why it occurs and the forms it takes. We do so by comparing policies towards equity investments by non-Western SWFs in four Western polities that are often contrasted in the comparative political economy literature—the UK, France, Germany, and the US—between 2000 and 2020. We analyse public debates, legislation, and the use of formal and informal policy instruments to understand not just rules but also the politics of their development and use. Using structured comparisons and process tracing, we look within the state to identify specific policy makers and to find explanatory factors and processes for the patterns identified.

We find that several Western governments have engaged in internationalized statism. They have welcomed and sometimes actively sought equity purchases by SWFs from non-democratic foreign states. We show that this surprising openness is not the result of passivity or a lack of state autonomy. Rather, public policy makers actively attract overseas state capital as another means of influence over domestic firm ownership, forming part of their economic strategies. They welcome foreign state investors to aid the governance of their domestic markets.

Moreover, the patterns of policy differ sharply from those that might be expected given the countries of origin of SWFs and their choice of investments. Far from closing their equity markets, policy makers in the UK, France, and Germany have accepted, welcomed, or sought SWFs from states ranging from China to Kuwait, Qatar, Libya, and Singapore. Their openness has extended to welcoming SWF purchases in firms that have strong symbolic value and to 'national champions' in strategic industries, including those that have obvious national security implications such as energy, aerospace, and banking, as well as many other major sectors. To underline the extent of the paradox, several European governments have preferred SWF ownership over domestic state ownership or investment by American private equity funds. They have sought to use SWF investments to support domestic firms and markets. Even very recent (2019–20) provisions for greater screening of foreign investment have been limited, not directed at SWFs, and driven by specific concerns about China. Moreover, previous legal powers have almost never been used, and instead governments continued to welcome SWFs.

But we also find significant variations in internationalized statism, many of which run counter to popular and academic expectations about the role of the state and general economic openness. The UK emerges as the most open of the four, but contrary to its rejection of public ownership and planning, thanks to a state that actively pursued SWF investments. Public policy makers have given strong public support to SWF equity purchases, with very few restrictions. They have not just accepted but also vigorously welcomed and sought SWF investments, including in core strategic industries such as finance, nuclear energy, and utilities. They have sought SWF investment across the board, without seeking particular SWFs or directing them to specific firms, with the exceptions of the sale of state assets and public contracts. SWF investments have occurred across several sectors, with many being in finance and real estate in London.

Despite suspicion towards private overseas share investors, France and Germany have also welcomed SWFs, although after greater debate than the UK. But both have had much higher levels of state direction—policies by domestic policy makers to build close relations with specific SWFs and/or encourage investments in certain firms and sectors. French policy makers have pursued a policy of state-influenced openness in which state officials have enjoyed close relationships with selected funds. Equally, they have acted in close cooperation with SWFs, whose investments have been sought for particular sectors and firms, especially 'national champions' and high-technology sectors. German policies have been led by an alliance between large firms and business associations with the government. They have sought SWFs as sources of capital that is both passive and patient, especially for both large- and small- to medium-sized industrial firms.

The major exception to welcoming SWFs has been the US—the land of 'free markets' and a 'liberal market economy'. It has seen strong debates about whether to allow overseas state investments, with conflicts between a favourable Executive and more hostile Congress. Then, in recent years, there have been particular concerns about investment from China by both bodies. The result has been legislation that has established considerable restrictions on foreign investment and discriminated against state-owned foreign investors. SWF investments have remained low relative to the size of the US stock exchanges.

Thus, policy makers in the UK, France, and Germany have pursued internationalized statism. They have actively sought non-Western SWFs as a source of capital, despite those SWFs being state owned, and accepted them in strategic firms and sectors. But they have followed different forms in terms of the extent of directedness. The US provides the counter-example, indicating the limits of internationalized statism.

To analyse the prevalence of internationalized statism, the book offers an explanation grounded in domestic politics, rather than one based solely on economic needs or security risks, which often fail to account for the patterns found. Instead, it examines the strategies of policy makers in their institutional context. It uses cross-national and cross-case comparisons to identify the role of certain factors and to exclude others.

Key factors in all four countries have been the power and aims of the political executive and its relationship with the legislature. In the UK, France, and Germany, the heads of the executive and ministries responsible for economic matters have strongly favoured openness to SWFs for both political and policy benefits. They have dominated policy making and defined SWFs as an economic issue, while defence and security services have played less of a role. Equally, they have formed pro-SWF alliances with major firms who have benefited from SWFs. In contrast, legislatures have been more sceptical, raising security concerns. But the executive has been able to overcome such resistance, leading to policies of welcoming SWFs.

A major attraction for the pro-SWF coalitions in the UK, France, and Germany has been that SWF investments can be used to pursue long-standing national types of industrial policy, albeit in modernized forms. The highly open but largely undirected British policy was part of a strategy of general openness to foreign investment—the 'Wimbledon strategy' of hosting markets even if 'British players' were taken over by overseas owners. It strengthened politically important sectors of the UK economy, notably finance and real estate. France's 'state-influenced' form of internationalized statism fits with its state support for specific sectors and 'national champion' firms, with both financial and political aims. German policy makers have seen SWFs as a new source of patient capital and exports, especially for industrial and manufacturing firms, the traditional bedrock of the country's capitalism.

In contrast, while initially supportive of openness, the American political executive has been ambiguous and less enthusiastic about overseas state investment in recent years under Presidents Obama and especially Trump. Moreover, Congress has strongly resisted openness to foreign investment and, thanks to its considerable power and autonomy, has been able to pass legislation that not only creates new controls but also discriminates against state investors.

Thus, the apparently surprising acceptance of non-Western overseas state investors is rooted in the advantages they offer to certain national actors, especially the economic parts of the political executive. The policies adopted depend on whether those parts have the capacity to maintain the welcome for overseas state investors or whether other actors, notably legislatures, insist on restrictions.

The findings have wider implications for our understanding of the role of the state as financial markets grow, internationalize, and attract more non-Western capital. The state itself has internationalized, as an economic actor, investor, and policy maker. Western states today pursue new forms of internationalized industrial policies that involve attracting overseas state investment as part of updated strategies to support domestic firms and industries. Paradoxically, cross-border state investment is aided by the liberalization of capital flows and financial markets, which have been claimed to reduce state power but in fact also offer states new opportunities. Internationalized statism offers a conceptual framework to analyse how national policy makers can use overseas states to govern their domestic economies.

0.3 Outline of the Remainder of the Book

Chapter 1 develops a statist political economy framework for analysing Western policies towards overseas state investors. We identify the limitations of important approaches in international and comparative political economy that focus on domestic private interests and downplay the role of the state. We discuss traditional and 'new' statist analyses, underlining both their value and their current limitations in terms of hypotheses and explanatory processes. Then we turn to our central concept of 'internationalized statism', outlining how it can be assessed and its two dimensions of extent and directness. We set out how it is applied in the present study and the aims of identifying specific state officials and explanatory factors for policies of internationalized statism.

Chapter 2 discusses SWFs and international debates about whether they pose dangers and how they should be regulated. It sets out the rapid growth in the number and size of SWFs from the 1990s until 2020 and shows that the effects of SWF investments in companies are a matter of lively debate. It then lays out the international legal and normative context within which SWFs and Western policy makers operate. It also studies key relevant elements of the EU's policies and legal regulation and the scope for policies in its member states.

The next four chapters (Chapters 3–6) constitute the core of our empirical analyses. They analyse whether countries have adopted internationalized statism and its extent and forms by looking at policies towards economic openness and SWFs and other overseas state equity investors. They look at the key elements of policy—public debates, legislative frameworks, and then policy making in practice through the use of formal and informal instruments.

The US is often classified as a 'liberal market economy', but Chapter 3 argues that policies of economic openness have been highly contested and it has increasingly moved towards low and directed internationalized statism. The executive branch initially favoured openness to SWFs as it has usually treated inward investments by foreign states as a matter of economic governance, and hence been favourable on grounds of free trade. This policy has weakened in recent years, especially because of concerns about investments from particular countries, notably China. In contrast, Congress has often been suspicious of and sometimes hostile towards overseas state investment, treating it as a national security matter. As a result, legislation has been passed that establishes additional controls over inward equity investment and discriminates against state-owned investors. Non-Western SWF purchases of significant stakes in American companies have been relatively low, especially from Middle Eastern and Chinese SWFs, and mostly welcomed for companies in distress, especially in times of financial crisis.

In stark contrast to the US, the UK has pursued a strong policy of undirected internationalized statism. Despite also being labelled a 'liberal market economy', public officials have actively welcomed and sought SWF equity investments from all over the world. Chapter 4 shows how policy makers have treated SWF purchases as a question of economic governance. They have followed a 'Wimbledon strategy' of seeking to attract SWFs from all over the world to invest wherever they wish, even if these overseas state funds take shares in prominent British firms. Both formal and informal instruments have been actively used to attract SWFs, who have taken significant stakes in leading British firms in strategic sectors as well as companies and buildings that are national symbols.

France has a popular and academic reputation as a polity that is suspicious of foreign investors, especially in strategic sectors. Yet Chapter 5 argues that it has followed a strategy of highly directed internationalized statism. The political executive has welcomed SWFs, in contrast to a rhetoric of 'economic patriotism' that arose when private American firms sought to take over French ones. Although legislative powers for non-European equity purchases were established, they were never used against SWFs. On the contrary, state officials have worked closely with selected SWFs to attract investment into selected large 'national champion' firms and sectors. France has therefore followed a policy of openness towards SWFs as part of adapting its traditional statism to an internationalized economy.

Germany too has been seen as relatively closed to overseas equity purchases because of its corporate governance system. Yet, as Chapter 6 argues, after an initial period of debate, its policy makers have pursued a policy of directed internationalized statism coordinated by the state and business. In public debates policy makers have welcomed SWFs as patient and passive investors, in contrast to hostility towards short-term Western private investors. Although a new legislative framework for non-European share purchases has been established, its application to SWFs has been very limited. Instead, firms and business associations in cooperation with government officials have welcomed and sought SWF investment in industrial firms, large and small.

The main findings of the four countries are compared in Chapter 7. It argues that the UK, France, and Germany have all adopted forms of internationalized statism, with the UK being the most open in terms of policies to attract SWFs, followed by France and Germany. In contrast, the US offers an example of the limits of internationalized statism. But it also underlines differences in the form of such internationalized statism, being undirected in the UK but much more directed in France and Germany. It underlines the diverse processes and political strategies of the four countries. Using cross-national comparison as well as drawing on the within-country variations and process tracing, it puts forward key explanatory factors for the patterns found. It then returns to the general discussion of the state and internationalized and liberalized financial markets. It further develops the concept of internationalized statism by using the factors identified as influencing policy towards openness to put forward hypotheses about why, how, and through which processes internationalized statism occurs. It underlines the role of the state in economic openness—both as an investor and as an active actor that influences the extent and form of openness. It then discusses the implications of internationalized statism for wider 'new statist' theoretical frameworks and debates in political economy about the effects of the liberalization and internationalization of markets, and argues that political economy analyses need to take more account of the role of the state as an internationalized investor.