Sovereign wealth funds from Muslim countries: Driving the Halal industry and Islamic finance

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If we match demographic projections by religion with the economies showing the highest growth rates and with an emerging middle class, we find that present and future economic growth, and consequently the most attractive business opportunities, are concentrated in the short, medium and long term in countries with Muslim majorities.

In 2010, Muslim population represented 23.4% of the world population, numbering nearly 1.6 billion people. According to the latest estimates, in 2030 this figure will exceed 2.2 billion, and account for 26.4% of the world population, which implies expected growth of 37.5% in the next twenty years.

This population, with an average age of around 25, is concentrated in the world’s most dynamic regions. For the period 2013-2018 the latest estimates indicate that the GDP of the 57 member countries of the Organisation of Islamic Cooperation (OIC) will grow by 6.3% on average, compared with a 5.3% world average. It is also estimated that by 2030, 66% of the world’s middle class will be living in the Asia-Pacific region, of which Muslims represent nearly 25% in 2014, and with a population expected to exceed 1.3 billion inhabitants by 2030 (there were 1 billion in 2010).

Recently, the International Monetary Fund (IMF) has published a list of the ten economies it expects to grow the most in 2015. Among them, we find several countries with Muslim majorities, such as Turkmenistan (9%), Côte d’Ivoire (7.75%) and Chad (7.59%), and countries such as India (7.46%), which while not being a majority Muslim country, remains the country with the third largest Muslim population, 140 million.

In order to manage the wealth generated by this growth, deriving in large part from the exploitation of their abundant natural resources, and to develop a model of intergenerational solidarity that will allow future generations to enjoy the wealth that the finite natural resources are producing for the present generation, many of these countries have decided to establish sovereign wealth funds.

Leading the sovereign wealth funds industry

The establishment of sovereign wealth funds in Muslim countries, while not really taking off until this century, in fact dates from as long ago as 1953, when Kuwait became the first sovereign state to create a fund of this kind. At present there are 92 sovereign wealth funds in the world, with a total value in excess of $7 trillion. The majority of them are in the Middle East, home to a large number of countries with Muslim majorities. In fact, 39% of the world’s sovereign wealth funds (36 out of 92) are in Muslim countries, and 46.4% of the assets managed by such funds worldwide ($3.3 trillion of the more than $7 trillion) are in these countries’ funds. Regionally, 64% of Muslim countries’ vehicles are in the Middle East, with the rest almost equally divided between Africa, Asia-Pacific and Central Asia.
Some of the world’s biggest sovereign wealth funds have been set up in Muslim countries (Table 1), most notably the large funds of the Middle East. Placing second and third after Norway’s fund, the world’s biggest in terms of assets under management are the UAE’s Abu Dhabi Investment Authority and Saudi Arabia’s SAMA Foreign Holdings, managing $773 billion and $744 billion respectively. They are followed, interspersed with other non-Muslim Asian countries, by Qatar, Kuwait and other emirates’ funds, all with more than $100 billion under management. Below the $100 billion mark we start to see funds from Central Asia, Asia-Pacific and Africa, completing the list of regions where Muslim countries’ sovereign wealth funds are located.

We should point out that the United Arab Emirates have as many as nine sovereign wealth funds, managing more than 1 trillion in assets, all deriving from oil and gas export, meaning that a single country controls one third of all the assets of Muslim countries’ sovereign wealth funds and one seventh of the world total.
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As for the source of the resources feeding these funds, it should be borne in mind that those belonging to Muslim countries have mainly been developed from revenues generated by the export of natural resources such as oil and gas, only seven of them having sources of a different nature.

The performance of these funds has been influenced by different macroeconomic, social and geopolitical circumstances which have determined their investment strategies. We should also stress that in these countries, the majority religion of Islam, irrespective of whether or not it constitutes to a greater or lesser degree a source

### Table 1: Sovereign wealth funds of Muslim countries

<table>
<thead>
<tr>
<th>Ranking</th>
<th>Sovereign Wealth Fund</th>
<th>Assets under management ($ millions)</th>
<th>Source</th>
<th>Country</th>
<th>Established</th>
</tr>
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<tbody>
<tr>
<td>1</td>
<td>Abu Dhabi Investment Authority</td>
<td>773.00</td>
<td>Oil</td>
<td>UAE</td>
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<tr>
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<td>SAMA Foreign Holdings</td>
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<td>Saudi Arabia</td>
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<td>Kuwait Investment Authority</td>
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<tr>
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<td>Qatar Investment Authority</td>
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<td>Oil &amp; Gas</td>
<td>Qatar</td>
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<td>5</td>
<td>Investment Corporation of Dubai</td>
<td>160.00</td>
<td>Oil</td>
<td>UAE</td>
<td>2006</td>
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<td>6</td>
<td>Abu Dhabi Investment Authority</td>
<td>90.00</td>
<td>Oil</td>
<td>UAE</td>
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<td>7</td>
<td>Samruk-Kazyna</td>
<td>88.30</td>
<td>Fiscal Surplus</td>
<td>Kazakhstan</td>
<td>2008</td>
</tr>
<tr>
<td>8</td>
<td>National Oil Fund of the Republic of Kazakhstan</td>
<td>71.80</td>
<td>Oil</td>
<td>Kazakhstan</td>
<td>2000</td>
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<td>Oil</td>
<td>UAE</td>
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<tr>
<td>11</td>
<td>National Development Fund of Iran</td>
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<td>Oil &amp; Gas</td>
<td>Iran</td>
<td>2011</td>
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<td>Libya Investment Authority</td>
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<td>Oil</td>
<td>Libya</td>
<td>2006</td>
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<td>13</td>
<td>Revenue Regulation Fund</td>
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<td>Oil &amp; Gas</td>
<td>Algeria</td>
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<td>Khazanah Nasional</td>
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<td>Fiscal Surplus</td>
<td>Malaysia</td>
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<td>Brunei</td>
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<td>State Oil Fund of Azerbaijan</td>
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<td>Azerbaijan</td>
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<td>T&amp;T Malaysia Development Fund</td>
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<td>Fiscal Surplus</td>
<td>Malaysia</td>
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<td>Oman</td>
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<td>23</td>
<td>Arab Petroleum Investment Corporation</td>
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<td>Oil</td>
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<td>Sandib Investments</td>
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<td>Oil</td>
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<td>25</td>
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<td>Oil</td>
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<td>26</td>
<td>Government Investment Unit</td>
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<td>Fiscal Surplus</td>
<td>Indonesia</td>
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<td>27</td>
<td>Nigerian Sovereign Investment Authority</td>
<td>1.80</td>
<td>Oil</td>
<td>Nigeria</td>
<td>2011</td>
</tr>
<tr>
<td>28</td>
<td>Fonds Souverains d’Investissements Strategiques</td>
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<td>Fiscal Surplus</td>
<td>Senegal</td>
<td>2012</td>
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<td>30</td>
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<td>Mauritania</td>
<td>2006</td>
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<td>31</td>
<td>Future Generations Fund</td>
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<td>Bahrain</td>
<td>2006</td>
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<td>32</td>
<td>National Investment Corporation</td>
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<td>Oil</td>
<td>Kazakhstan</td>
<td>2012</td>
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<td>33</td>
<td>RAK Investment Authority</td>
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<td>Oil</td>
<td>UAE</td>
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<td>Oman Investment Corporation</td>
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</tr>
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<td>Dubai World</td>
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<td>Oil</td>
<td>UAE</td>
<td>2006</td>
</tr>
<tr>
<td>36</td>
<td>National Investment Fund</td>
<td>0/0</td>
<td>Oil</td>
<td>Syria</td>
<td>2012</td>
</tr>
</tbody>
</table>

Total 3,300

Source: ESADEgeo, 2015
of law in the country’s legal system, is in any case a source of rules, solutions and restrictions for business and finance which are different from conventional non-Muslim ones, thus creating additional possibilities of action in the market that other countries do not consider.

Governance, transparency and supervision

More than half of all Muslim countries’ sovereign wealth funds were created in the first ten years of this century, coinciding with the rise in oil prices. Thus at the end of the twentieth century there were only eight funds: within the first ten years of the twenty-first, 22 new funds were established, tripling the number of Muslim countries with sovereign funds.

The last international crisis led to sharp corrections, due to excessive risks incurred, coinciding with the rise in oil prices. This translated into sharp internal criticism and adjustments to governance and the management of risks, which now, with the fall in oil prices, are once again starting to increase. Muslim countries’ sovereign wealth funds, especially those of the Middle East, are transforming the image of their countries, basing themselves more on financial asset economies and leaving behind that of oil and gas producers.

There has also been internal pressure to increase the weight of sovereign funds, especially those of the Middle East, in view of how this sector held up better than most during the crisis. Accordingly funds are considering increasing their investment in Islamic banking, takaful insurance, etc., and the use of Shariah-compliant financial vehicles.

The geopolitical position of these funds is an important factor, above all for those that are in areas with open conflicts or geostrategic struggles, since certain investment decisions may be taken as political and not strictly financial decisions, which in some cases has led to sharp criticism.

From a legal point of view, the majority of sovereign wealth funds from Muslim countries have been established through entities with their own legal personality (Kazakhstan, Azerbaijan, Algeria, Iran, Oman, Indonesia, Qatar, Bahrain and the majority of the Emirates’ funds). Some, however, such as that of Brunei, are merely agencies of one or another public administration branch. Those of Malaysia and Palestine are public limited companies.

The majority of sovereign wealth funds from Muslim countries report to their respective governments or rulers, whereas those of other countries generally report to the central bank or an independent board of directors.

In terms of governance structure and transparency, these are the funds that give rise to the greatest concerns in this respect, and this has led them to making greater efforts to improve and bring themselves into line with international practices. Thus, only one third of sovereign wealth funds from Muslim countries belong to the International Forum of Sovereign Wealth Funds (IFSWF).

Muslim countries’ sovereign wealth funds and Islamic finance

In analysing the strategies and transactions of Muslim countries’ sovereign wealth funds under the precepts of Islamic finance, the terms of these investments must be differentiated by reference to the greater or lesser extent to which they comply with these rules or promote this way of operating in the market.

Apart from this, and in highly practical terms, those that promote the use of Islamic finance in sovereign wealth funds’ transactions base their arguments on the fact that its precepts promote transparency in transactions in order to achieve social justice, equity and equanimity (Quran, 2:282). Furthermore they explicitly stress compliance with contracts and commitments based on honesty (Quran, 4:135; 5:89; 5:108). They therefore press for sovereign wealth funds’ transactions to be conducted within the framework of Islamic law, whilst simultaneously implementing reforms and enhancing commitments to best practices, such as the Santiago Principles’, attention be paid to the precepts that stem from their culture and share the same philosophy.

There are several circumstances that are bringing about changes in the strategy of using or not using Islamic finance in the transactions of Muslim countries’ sovereign wealth funds. The recent international crisis has shown how the sectors under the umbrella of these precepts have suffered much less, gradually becoming a refuge for capital from Muslim and non-Muslim countries alike.

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4 Soft regulation, proposed by the International Working Group (IWG) of SWFs in 2008, under the supervision of the IMF, seeking to alleviate fears among recipient countries and to improve the governance of its members.

5 The data will be presented in aggregate form, since the information is highly sensitive for these funds, given the implications as experts comanage or otherwise with risks promoted by or forming part of the legal system of the states on which they depend. Apart from this, it is obviously impossible to confirm whether in their investment transactions the various sovereign wealth funds are using Shariah-compliant contractual forms, or to what extent the rules of Islamic finance are incorporated into them. Therefore the data presented are estimates based on information gathered on investment transactions and statements of senior management of the majority of the sovereign wealth funds dealt with here. Obtaining these data in the course of this research required us to undertake not to disclose their source and not to report them in such a way as to make it possible for calculation to reveal to which sovereign wealth fund they correspond. The opinions expressed by those consulted, while they correspond to the highest levels of governance, may not necessarily correspond to the reality of the whole institution, although we have shown that they are at least highly representative. In any case we express our thanks for the trust placed in us in sharing this information.
Different social movements have asked the managers and rulers of these countries, who like them are under Islamic law (in some cases applied very strictly), to bring the strategies and transactions of their sovereign wealth funds into line with such precepts.

The rapid growth of Islamic finance, with two main centres in the Middle East and Southeast Asia, has led to the development of markets specialising in Shariah-compliant products, making more opportunities available to sovereign wealth funds.

At the same time, the arrival of Islamic finance in the financial markets of non-Muslim countries (remembering the legal reforms carried out in several European countries to be able to operate under Islamic finance) has led to opportunities being generated beyond Muslim countries, primarily Western countries’ needing to attract capital, resulting in their offering these transactions as a way of capturing funds.

On the other hand, Muslim countries’ sovereign wealth funds’ use of Shariah-compliant financial instruments or promotion of Islamic businesses with its foreign investments is seen by some sectors as Islamisation of the economy and imposing a cultural and religious heritage that do not belong to the countries in which these investments are made.

The use of Islamic finance in the investments of Muslim countries’ sovereign wealth funds cannot be considered as a homogeneous block of transactions, since depending on how and where the investment is carried out, large differences arise. Thus we could group these funds’ transactions into: a) certified transactions or investments in Shariah-compliant financial products, b) investments that comply with the rules of Islamic finance but are not certified as such, c) investments in Islamic institutions or projects and d) the rest.

There is also a great difference between the investments they make in their own countries and those they carry out internationally: both the transactions and the investees might already be subject to Islamic laws if the legal system so decrees.

There are 1,181 Islamic funds in the world, none of which is a sovereign wealth fund. At present there are no Islamic Sovereign Wealth Funds (ISWF), although there is some work dealing with the pros and cons of creating them.

With regard to how Islamic finance forms part of these funds’ investment strategy, we would point out that:

- Of the funds from Muslim countries where we have had access to the necessary documentation, not one includes in its legal documents of establishment, statutes or basic principles, a mandate to operate or a preference for operating under Islamic precepts or investing in Islamic products. A few refer to Islamic law, but only as the legal framework of the country in which the institution operates.

- The governance bodies of 77% of Muslim countries’ sovereign wealth funds have expressed the wish to increase significantly the number of transactions carried out under Islamic finance.

- 28% of them have support for Islamic businesses as a strategy, but only for their domestic investments. 3% list the promotion of Islamic businesses in international investments as a strategy, although always taking up action policies from other branches of the government or public bodies that promote Islam abroad.

- 71% of those consulted say that the precepts of Islam are not, in principle, a parameter taken into consideration when taking investment decisions.

We were not able to determine, for lack of data, the possible differences from one sector to another. However, in general terms:

- 26% of those consulted say that they use both Shariah-compliant and conventional instruments.

- Of the respondents stating that they operate with projects under Islamic finance, 72% say that this usually depends on the partner with whom they are working on each investment.

- 61% acknowledge that the possibilities for transactions under Islamic finance in financial markets of non-Muslim countries have increased.

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6 Countries such as the UK, France and Ireland have recently carried out the necessary legal changes for Islamic finance to be able to operate easily in their respective economies. Spain, in contrast, has still not decided on the possibility of this regulatory change, although there has been an initiative on the part of the country’s experts in Islamic finance, in collaboration with international institutions, to promote it and make information on it available to the government.

7 Thomson Reuters, 2015.

Using the classification set out above, we estimate that 21% of investments can be considered Islamic, taking the first three categories as being such (a, b, and c). This figure is surprisingly high in view of the above remarks, bearing in mind that, as we have explained, Islamic finance does not constitute a specific mandate for the sovereign wealth funds. However, it is explained by the number of investment transactions carried out in the internal market or in other Muslim countries, and also in industries that fall within the Islamic category (banking, issuance of sukuk bonds, halal agrifood industry, takaful insurance, etc.) Of these, approximately 87% correspond to domestic investment transactions.

The most typical investment in this regard is that made in a national Islamic bank, as we shall see presently. We should also highlight the increase in transactions with sukuk bonds. The importance and the volume of sukuk in international markets in the past few years have grown increasingly, going far beyond the borders of the Islamic world, becoming attractive investments for sovereign wealth funds in their own right. In fact, the sovereign wealth funds are not only buying them, but have also started issuing them (Table 2). Recently, one of Bahrain’s sovereign wealth fund, Mumtalakat Holding Company, raised $600 million by selling Islamic bonds, and Malaysia’s two sovereign wealth funds, Khazanah Nasional and 1MDB, announced new issues of $278 million and $2.4 billion respectively. Khazanah Nasional is planning to launch this year the first $27 million tranche of the $278 million and $2.4 billion respectively. Khazanah Nasional is one of Bahrain’s sovereign wealth fund, Mumtalakat Holding Company, raised $600 million by selling Islamic bonds, and Malaysia’s two sovereign wealth funds, Khazanah Nasional and 1MDB, announced new issues of $278 million and $2.4 billion respectively. Khazanah Nasional is planning to launch this year the first $27 million tranche of the $278 million and $2.4 billion respectively. Khazanah Nasional is planning to launch this year the first $27 million tranche of the $278 million and $2.4 billion respectively. Khazanah Nasional is planning to launch this year the first $27 million tranche of the $278 million and $2.4 billion respectively.

In summary, it can be said that with the drying up of the great opportunities that the crisis brought with it in developed countries, the weight of transactions in emerging countries is increasing, with new formulas of joint investment with other operators also being explored for these transactions. At the same time, the increasing development of Islamic finance has led to more and more resources being channelled into this alternative.
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SWFS IN THE ISLAMIC BANKING
(Stake in percentage)

*The non-oil arm of UAE sovereign wealth fund IPIC.

Source: In-house based on Annual Reports (2015).
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**Halal food: arousing the appetite of sovereign wealth funds**

Nearly all countries with Muslim majorities currently import much of the food they consume. They are net importers of food, the vast majority of it Halal. In 2013, Muslims spent $1.2 trillion on food and drink, the equivalent of 17.7% of total world expenditure on food in that year. Of this, $1 trillion was spent on Halal food by the Muslim communities in the 57 member countries of the Organisation of Islamic Cooperation (OIC)⁴.

There are three main factors explaining this dependency: adverse climate, the lack of the know-how and technology needed in order to boost food productivity, and the rapid growth of populations with increased disposable income who are starting to adopt Western patterns of consumption.

Even still, there are considerable disparities. According to the latest estimates of the World Integrated Trade Solution (WITS), a joint project of the World Bank, the United Nations and the World Trade Organisation (WTO), the most dependent countries in 2013, and therefore the most vulnerable to changes in food prices (which, lest we forget, were the detonator for the popular uprisings in the Maghreb known as the Arab Spring) were: Saudi Arabia, United Arab Emirates (UAE), Algeria and Egypt. These countries run food trade balance deficits of close to $21 billion, $11 billion, $10 billion and $7 billion respectively. As can be seen in Chart 3, other countries with Muslim majorities such as Qatar, Morocco and Kazakhstan, also had deficits, albeit much more modest ones.

At the other extreme, we find Southeast Asian majority-Muslim countries Indonesia and Malaysia, net food exporters, with trade surpluses in 2013. Outside Southeast Asia, only Turkey is comparable with these two. Compared with Indonesia’s $15.57 billion and Malaysia’s $9.50 billion, Turkey’s trade balance for 2013 showed a surplus of $5.86 billion.

This dependence on imports seen in many Islamic economies has led their governments to take new measures. The objective is two-fold: on the one hand, to develop the necessary internal capacity to supply the growing domestic demand for food and thus gradually reduce the degree of dependence; and on the other hand, to seize the excellent opportunity presented by the boom in food in general, and Halal food in particular, in order to generate wealth. In order to attain these objectives, the governments of many of these countries, particularly those of the Middle East, have turned to their sovereign wealth funds.

The most representative case is without a doubt that of the Qatar Investment Authority, Qatar’s sovereign wealth fund, which manages assets worth $304 billion. In 2008, the fund spent $1 billion on acquiring an investment arm specialising in the agriculture and livestock sector: Hassad Food. With an investment horizon of 50 to 100 years, the vehicle’s mandate is to make investments in the agriculture sector so as to secure the supply of the country’s Halal food in the long term and to obtain juicy returns.

Active since 2009, it set up Hassad Qatar, its domestic arm, with the initial aim of securing the supply of food for the animals of Qatar’s livestock operations by producing and buying fodder. Through this subsidiary it also signed an agreement worth $68 million with Oman’s A’Saffa Foods to establish a poultry operation in the south of Qatar with the capacity to produce 17,000 metric tons a year of Halal chicken and 90 million eggs, approximately 20% of Qatar’s demand for these foods.

Hassad Food also announced the setting up of a joint venture with the Sudanese government. With capital of approximately $100 million, the new company, 75% held by Hassad Food, intended to form 250,000 hectares in the north of Sudan to secure the supply of Halal food for both countries.

In 2010, it spent $500 million on setting up its Australian subsidiary, Hassad Australia. Through this company it has acquired poultry and agricultural operations in New South Wales, Queensland, Victoria and Western Australia worth more than $200 million⁵. It currently owns more than 287,000 hectares, with the capacity to produce 125,000 metric tons of grain and 100,000 heads of Halal lambs a year.

Highlights of its recent activity include its intention of investing $500 million in poultry operations in Turkey, the possibility of entering the Brazilian market, and the acquisition, for $100 million, of a 33.25% stake in the aforementioned A’Saffa Foods, the sultanate’s leading producer of Halal chicken.

However, Hassad Food is not the only Gulf fund to have decided to enter this attractive market segment. The Investment Corporation of Dubai holds a significant stake in Emirates Rawabi, the leading producer of Halal poultry products in the UAE. In 2011 one of Bahrain’s sovereign wealth funds, the Future Generations’ Reserve Fund, launched a $265 million fund to invest in Halal food companies in the country and beyond. In 2005, the Kuwait Investment Authority (KIA), together with Kuwait’s Alghanim Industries and the National Investment Company, set up Kuwait

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China Investment Corporation, a fund with more than $340 million in assets at the end of 2013, one of the objectives of which is to invest in poultry operations in Asia. Similarly, Gulf Investment Corporation, the sovereign wealth fund set up in 1982 by the six member countries of the Gulf Cooperation Council (GCC), managing assets of $2.7 billion, recently invested $196 million in the Gulf Japan Food Fund, created jointly by Japan’s Mizuho Bank and Norinchukin Bank. This vehicle, with $426 million, aims to facilitate access to financing for Japanese companies exporting or seeking to export Halal food to countries in the Gulf.

In Southeast Asia, Singapore’s two sovereign wealth funds, GIC and Temasek, have also seized this opportunity. The city-state’s proximity to both Malaysia and Indonesia (280 million Muslims between the two nations) gives it a certain advantage in seeking markets and finding reasons to invest in the sector. In mid-2014, GIC increased its shareholding in BRF (formerly Brasil Foods) by 0.6% to 4.4%—an expected move. BRF, the result of the merger of Brazilian companies Sadia and Perdigão in 2009, is one of the world’s ten biggest food companies and one of the biggest producers of Halal meat. Proof of this giant’s interest in capturing the Halal meat market is the $160 million investment it made in 2013 to set up a Halal food processing plant in the Khalifa Industrial Zone of Abu Dhabi11.

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At the same time as increasing its holding in BRF, GIC acquired 11% of Century Pacific Food, in the Philippines, for $76 million. With this transaction the fund was following the same logic: positioning itself in a Halal food producer with strong growth potential and a strategic location.

Temasek, for its part, decided to go for domestic food companies, since Singapore serves as a distribution hub for ASEAN. In 2006 it invested $584 million in acquiring 15% of Singaporean company Fraser & Neave Limited. This company has a long tradition of producing and selling Halal food, and at the end of 2011 it opened a new Halal dairy products factory in Malaysia’s Selangor Halal Hub, investing $150 million in the transaction. Three years later, in 2009, it made another domestic investment, this time of $305 million, buying 13.76% of the multinational Olam International.

Western sovereign wealth funds such as Norway’s GPFG, the Australia Future Fund and the Alaska Permanent Fund, unlike those from the Gulf or Southeast Asia, have accessed this growing market by means of their holdings in multinationals with wide exposure, such as Nestlé, which has 150 Halal-certified plants and produces more than 300 Halal items, Mondelēz International, one of the leading producers of Halal chocolate, which recently invested $90 million in setting up a Halal biscuit plant in Bahrain, and Tesco, 27 of whose supermarkets in the UK sell Halal meat.

In short, no-one is willing to forego this mouth-watering market, which is expected to reach $2.5 trillion a year in 2019. Therefore, and also as a result of global agrifood tensions, it will become increasingly common to see these giants investing in Halal food companies.