Investment Trends Among Sovereign Wealth Funds
Asset Allocation Stable, Returns Less Volatile

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Executive Summary

This is our biennial update on the asset allocation trends of sovereign wealth funds (SWF). The key theme over the last three years has been a structural shift in the macro environment — an end to the era of ultra-loose monetary policy coupled with rising inflation and increasing geopolitical risks. Against this backdrop, markets have been exceptionally volatile, and SWFs have not been immune.

Year 2022 was the first since 2008 when SWFs on average reported a negative return. Still, they outperformed conventional benchmarks. And we find that the outperformance of SWFs remains true over the long term as well, but only when adjusted for risk. Meanwhile, asset allocation has largely remained steady, reflecting slower growth of private market portfolios, due to private markets facing absorption constraints and public markets gaining traction again.
Returns for SWFs

Returns for SWFs have been exceptionally volatile since 2020. Year 2021 was a year of exceptional growth — SWFs returned 17%, the highest since records began in 2008. Against the backdrop of a global pandemic, markets responded to the economic reopening, an unprecedented loosening of fiscal policy and a delayed start to monetary policy tightening. The result was a market boom that drove asset prices to record levels.

By contrast, 2022–2023 was a period of bust and recovery, with markets feeling the effects of the inflationary shock and the sharp policy rate increases that followed, in addition to broader geopolitical shocks, particularly from the Russia-Ukraine war. Returns in 2022 were -11%, the lowest on record, second only to losses during the 2008 Global Financial Crisis. In 2023, markets rebounded and SWFs expect a return of about 12%.²

Over the years, SWFs have built diversified portfolios. But how do their returns compare? Figure 1 juxtaposes a 60/40 portfolio, showing that historical returns of SWFs are similar but notably less volatile.³

Source: Global SWF, Bloomberg, as of 31 December 2023.
The average 10-year return (2012–2022) for SWFs was 6.1% versus 6.7% for the classic 60/40 portfolio. However, risk (measured by standard deviation) was 7.1% for the former versus 10.6% for the latter, supporting the case for greater diversification of assets, particularly into asset classes that show less correlation with the public equity and fixed income markets.

Figure 2 illustrates the ten-year average return for different SWFs in our sample. The Middle East and North Africa region (MENA) leads regionally, which could be partly due to high private market exposure. Large SWFs (AuM above US$50 billions) tend to outperform small SWFs for the same reason.

Figure 2
Ten-Year Unweighted Average Returns for SWFs (2012–2022)

Note: The choice to limit the data as of 2022 was conscious, as the overwhelming majority of 2023 returns were estimates that are subject to considerable adjustments. Source: Global SWF, as of 31 December 2023.
SWFs as Global Market Movers

We estimate that a global portfolio of investable assets was worth US$165 trillion as of 1H 2023. This figure is based on a ground-up aggregation of asset classes available to institutional investors. Within this global market, SWFs are a prominent force. With total assets of US$10 trillion, they account for 6% of the total. This is particularly pronounced in private markets, where we estimate the SWF share to be about 14%.

As Figure 3 illustrates, growth in assets under management (AuM) steadily continued in recent years, with total AuM reaching US$10 trillion by year-end 2023, an increase of US$1.3 trillion from 2020. This was driven by strong market performance in 2021 (internal rate of return of 17%) and fresh capital in the years that followed. New capital materialized as a consequence of the Russia-Ukraine war in early 2022, which led to a sharp rise in energy prices. The unexpected windfall for oil-exporters created pools of surplus capital that could be channelled towards the SWFs of those countries.

As of 2023, the average asset allocation has little changed from 2020, which largely suggests that similar to other asset owner types SWFs are settling into steadier strategic asset allocations (Figure 4).
However, SWFs are not necessarily moving in unison. Between 2010 and 2015, most SWFs were behaving in a similar fashion, largely adding private market exposure at the expense of bonds and stocks. That herding behaviour became less pronounced in the middle of the decade and has now ceased altogether (Figure 5).

In 2020–2023, there was no discernible consistency with regard to any asset class. The macro environment had changed the appeal for fixed income assets, but roughly the same number of funds were adding or reducing their share of bonds in portfolios. Meanwhile, private market investments become more challenging in light of higher inflationary and interest rate shock, which, nevertheless, did not prevent half the funds from increasing exposure.

We continue to see material differences in asset allocation across funds of varied sizes. Large funds invest more in private markets compared with small funds (28% versus 19%). This can be partially explained by the operational complexity in terms of governance, cost and human resources that larger funds find easier to manage. Larger funds also tend to be older and have had the time to develop the institutional capacity necessary to invest in private markets.
Public Market Investments

With interest rates being structurally higher, fixed income once again offers the possibility of decent returns without high leverage. With rates well above the zero bound, bonds now also offer decent downside protection and diversification benefits. But reflecting more caution, there is a move away from plain vanilla bonds towards asset classes that offer more protection from inflation — for instance, inflation-linked and asset-backed securities.

As noted earlier, smaller funds allocate differently from larger funds, with a notably greater share of allocation towards fixed income. We find that this trend has diverged over time — while larger funds have continued to reduce, smaller funds have continued to increased allocation.

![Figure 6](image)

**Unweighted Average of Fixed Income AuM for Small and Large SWFs**

- Large Funds
- Small Funds

Note: Large funds are designated as those with an AuM of above US$50 billions. Source: Global SWF, as of 31 December 2023.

Similarly, the overall share of assets devoted to public equities has not materially changed and has been stable since the mid-2010s at about 38% of assets, with no meaningful differences between regions, fund size or fund nature. However, how funds think about the asset class reflects the changing nature of risk and opportunity.

This is particularly true of investments in emerging markets. For example, funds have been cautious on China on account of its poor economic performance, regulatory risks and uncertainty arising from the US-China tensions.
Private market investments of SWFs have continued to grow in nominal terms, reaching US$2.6 trillion in our sample, with a net increase of US$556 billion since 2020 (Figure 7).

However, the rate of annual growth has slowed, a function of the limited capacity of private markets to absorb new funds. Growth in private market investments, while still faster, continues to converge with that for public markets (Figure 8).

Indeed, the fundamental drivers of private market investments have changed. Investments into private markets accelerated since the global financial crisis by the ultra-low interest rate environment and the subsequent search for yield. SWFs were particularly well-suited for this trend due to their long-term mandates and low liquidity needs.
Interest rates are now expected to remain structurally higher, which changes the relative attractiveness of the asset class. Moreover, other factors are driving the different sub-asset classes down different paths. For example, commercial real estate is under tremendous pressure from the post-pandemic hybrid working model. In contrast, infrastructure has become a particularly bright spot in light of the global decarbonisation agenda and geopolitically motivated reshaping of global supply chains. Relative to 2020, the share of AuM that is invested in private markets remains unchanged at 25% as of end-2023.

Regionally, as noted before, investment funds from MENA have had a strong tilt towards private markets, specifically private equity. Total private allocation in MENA as of 2023 was about 25% higher than in other well-represented regions.

Comparing sub-asset class choices, private equity is by far the preferred choice comprising 46% of all private market assets. Except for a growing share of hedge fund investments (at the cost of the share of private equity), the split among sub-assets in the private market has been stable over the years (Figure 9).
Conclusion

SWF asset allocation is approaching a steady state of roughly 35–40–25 (fixed income/equities/private markets), with the scope of private market investments being largely a function of an individual fund’s ability to cope with illiquidity. That said, intra-SWF diversity continues to grow as the respective mandates and fund sizes imply different tactical and strategic asset allocation priorities. Finally, long-term returns for the group are robust, though more on a risk-adjusted basis than at a headline level.

Endnotes

1 We source our data from Global SWF, which tracks SWF and public pension fund activity globally. From the database of about 200 names, we have taken a sub-set of 33, located in 26 different countries. This is based on a narrow definition of SWFs as stewards of excess government savings that are unencumbered by explicit liabilities and unconstrained by domestic allocation. We are focused on the ability to deploy capital internationally and, therefore, our sub-set includes the largest SWFs that have material overseas investments. The combined AuM of these funds were US$8.6 trillion as of end-2023, representing an overwhelming majority (85%) of SWF assets globally.

2 However, the 2023 figure should be treated as directional as only a handful of funds had reported returns by the date of publication of this report. For completeness, the 12% result includes results for all 34 funds, of which only 6 are based on reported figures. The rest are estimates.

3 60% equity as proxied by the MSCI World Total Return Index and 40% bonds as proxied by the Bloomberg Global Aggregate Total Return Index. Rebalanced annually.


5 Some of the investments made by SWFs, for instance, infrastructure or holdings of illiquid real estate (part of real estate AuM), fall outside the scope of our estimate of the global portfolio due to their highly illiquid/unique nature. The percentage shares of the global portfolio are therefore best treated as an upper bound.
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* Pensions & Investments Research Center, as of December 31, 2022.
* This figure is presented as of December 31, 2023 and includes approximately $64.44 billion USD of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.