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Perspective

Households, Sovereign Wealth Funds, and the Stock Market

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DESCRIPTION

A sovereign wealth fund is a government-owned investment fund that invests money generated by the government, typically from a country's excess reserves. SWFs assist both a country's economy and its residents. A SWF's funding might come from a variety of sources. Excess reserves from state-owned resource revenues, trade imbalances, and bank reserves accumulated from budget excesses, foreign exchange operations, money from privatizations, and government transfer payments are all popular sources. In general, sovereign wealth funds serve a specific purpose. Some countries have sovereign wealth funds, which are analogous to private-sector venture capital. SWFs, like any other sort of investment fund, have their own set of goals, terms, risk tolerances, liability matches, and liquidity problems. Some funds may prioritize returns above liquidity, while others may prioritize liquidity over returns. Risk management in sovereign wealth funds can range from extremely conservative to extremely aggressive, based on the assets and goals [1].

Under certain conditions, a sovereign wealth fund that primarily invests in the global stock market and whose profits are intended for a social dividend can promote both equity and efficiency. A basic overlapping generation model with a proportion of hand-to-mouth agents is created, in which the government creates such a fund using public debt. The fund's social optimum size is strictly positive and defined by an empirical formula. While this strategy is similar to popular capitalism in that it seeks a more equitable distribution of capital revenue, it is based on a distinct conception of what constitutes a desirable society. This paper revisits the premise that partial public ownership of capital can be an efficient strategy for attaining more equal income distribution in mature economies without sacrificing efficiency. I examine a debt-financed Sovereign Wealth Fund (SWF) that primarily invests in the global stock market and refunds its net profits to citizens through a social dividend. I refer to it as a "progressive SWF." This institution would ensure that every person benefits from the high rates of return on capital investment that come with globalization and automation. Because it is linked to capital profits, which are frequently expected to expand faster than labour incomes, the social dividend given by a progressive SWF would result in long-term reductions in poverty and inequality [2].

Some empirical findings may help in understanding the potential of public stock ownership as a redistributive instrument. First, in many nations, the labor share of national revenue is declining. This tendency shows that the potential redistributive effect of public ownership of capital is growing. The impending robot revolution is likely to accelerate this movement in the functional distribution of income, possibly dramatically. Second, younger generations of employees face a significantly more unequal distribution of lifetime wages than their ancestors. The bottom quartile even shows a drop in absolute real lifetime earnings, as reported in the United States and Germany. Third, trade unions' ability to promote workers' welfare has been eroding: union membership has been declining in the private sector in most advanced economies over the last three decades; union wage coverage has similarly declined, and collective wage bargaining, where it still occurs, has increasingly been decentralized to the firm level. It is difficult to see these patterns changing very soon. They were fuelled by structural economic changes and a weakening of societal norms that encourage people to join labor unions [3].

The stock market and households

The most important finding from an examination of household equity allocations is that a large proportion of the population simply does not own any stocks. Despite the high mean return on stocks and other hazardous assets, more than half of households in industrialized economies do not invest in them. In Germany, for example, only around one-fifth of households own shares, either directly or indirectly through mutual funds, exchange-traded funds, and retirement accounts. This type of violation of the participation principle is more widespread among the comparatively poor in the United States, only a small percentage of households in the lowest half of the wealth distribution own public equity. Another strong finding in the household finance literature is a breach of the

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diversification principle: Among households who do invest in stocks, many hold only a few of them. Given the high financial risk they face, many households obtain an insufficient return. Diversity is a basic fact of household finance worldwide [4].

Institutional aspects

Modern SWFs should be democratically legal autonomous agency, similar to the central banks, competition authorities, and regulatory entities to which many governments have delegated the responsibility of tackling some complicated problem in pursuit of a publicly accepted long-run aim. Existing SWFs are frequently incorporated in a framework known as the "management model." The government, generally the ministry of finance, is the legal owner of the SWF's assets. In turn, the owner transferred investment authority to an asset manager, often the central bank or a government-owned independent fund management firm. Additional governance criteria are expected to be required in order to ensure efficient management of public wealth *via* progressive SWFs.

Investment terms

The funds in an SWF are typically large. These allowed investments included in each SWF differ by fund and by country. Countries can establish or dissolve SWFs to meet the demands of their people. Funds concerned about liquidity may limit their investments to particularly liquid public debt securities. Sovereign wealth funds may invest directly in domestic industries in specific situations. In terms of investment, liquidity, debt, and allocation balances might be important issues. There may be concerns that SWFs wield political power. Some of the world's largest sovereign wealth funds are not completely open about their investments and corporate governance policies [5].

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