Sovereign Wealth Funds ending United States protectionism?

Explaining the US acceptance of foreign governments' investments in US financial institutions at the onset of the subprime mortgage crisis

Author:	Joop Overkamp
Student number:	S4483774
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Specialization:	International Political Economy
Supervisor:	Dr. T.R. Eimer
Faculty:	Nijmegen School of Management
University:	Radboud University, Nijmegen, The Netherlands
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Abstract

For a long time, the United States of America (US) tried to prevent acquisitions of foreign governments into vital economic sectors. This long-held policy seemed to change during the onset of the subprime mortgage crisis when Sovereign Wealth Funds (SWFs) acted as white knight's and provided much-needed liquidity for failing US financial institutions. The US government did not intervene in these investments, which caused politicians to publicly voice their concerns and lengthy congressional hearings. The final governmental response was to accept investments and enact 'best practices' for SWFs and 'guidelines' for SWF investment recipient countries at the IMF and OECD level. Which respectively ensured that SWFs do not invest politically, and SWF investment recipient countries do not discriminate between state owned enterprises or private companies. This research tried to understand this policy decision through the detailed analysis of three policy phases. It finds that neither the Neoclassical Mercantilist nor the Critical Political Economy (CPE) approach can fully explain this decision. Interestingly, a combination between both approaches seems to explain why the US chooses to proliferate neoliberal policies that do not regulate SWFs directly. It seems that the state has more agency than expected by the CPE approach, but, in contrast to the Neoclassical Mercantilist approach, it has to be acknowledged that the state's decision-making is influenced by neoliberal structures. Therefore, that might imply that the proliferation of neoliberal supremacy within international institutions and the government can be explained by the US's seemingly deliberate decisions.

Key words: Sovereign wealth funds, state authority, Mercantilism, New constitutionalism, Structural power, Foreign investment regulations

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1. Introduction

1.1 Research problem

The United States of America (US) is known to be an advocate of open-investment policies around the globe (Travalini, 2009: 779). From the Louisiana Purchase in 1803 onwards, the US accepted and encouraged foreign investments into their lands (ibid: 782). Especially during the liberalization era of Reagan and Thatcher in the 1980s, the idea of free and unobstructed investment flows thrived (Cohen, 2009: 721). On the other hand, when it comes to the foreign direct investments (FDIs) into vital economic sectors of national interest and security, the US is also known as a fierce protector (Hasnat, 2015: 186).

In 1975 President Ford creates the Committee on Foreign Investment in the United States (CFIUS) to review national security implications of FDI (Travalini, 2009: 784). CFIUS's power expands in 1988 due to the Exon-Florio act, which is enacted to prevent the acquisition of a US semiconductor company by a Japanese company (ibid.: 784). Thereafter, acquisitions by Chinese (1988, 2005) and Abu Dhabian (2006) entities into US key national security industries are halted by US authorities (Hasnat, 2015: 188; Cohen, 2009: 721). Interestingly, the US government changed its long-held strategy and does not intervene when sovereign wealth funds (SWFs) invest billions of dollars in US financial companies somewhat later in 2007 and 2008. Despite the financial sector being labeled as a US "critical infrastructure/key resource" (Hasnat, 2015: 192). Even the enactment of the Foreign Investment and National Security Act by the Congress – which increases the monitoring power of the CFIUS and thus enables more legal ways to stop investments - did not lead to any domestic intervention (Cohen, 2009: 722).

The recipients of these SWF investments are struggling US banks such as Citigroup, Merrill Lynch, and Morgan Stanley, whose capital is depleted by consumer mortgage failings and a bursting US housing bubble (Gilson & Milhaupt, 2008: 1348). The big bags of money originate from Chinese, Emirati, Qatari, Singaporean, and Kuwaiti SWFs (Pistor, 2009: 554). The capital injections provide some air for US banks as they soften the effects of the crisis, however, at the price of foreign government stakeholdership and thus possible national security issues (Gilson & Milhaupt, 2008: 1351). These national security concerns spark a new academic debate among international relations scholars. According to Drezner (2008a) and many other scholars these concerns about SWFs are 'overblown', and they mainly emphasize the economic advantage. Indeed, SWFs provide access to a pool of money that can be used as a much-needed inflow of capital. However, other scholars point out that national security issues stem from SWF's secrecy, huge amount of quickly transferable assets, and potential politically motivated investments (SWFI, 2020; Cohen, 2009: 719; Hemphill, 2009: 556; Helleiner & Lundblad, 2008; Knill et al., 2011).

These negative side-effects are picked up by US politicians and attract a lot of political coverage through lengthy and repeated hearings in the US Senate (Das, 2009: 90; Cohen, 2009: 720). Moreover, US Senators Hillary Clinton and Joe Biden, National Intelligence Director John McConnell, and Treasury Deputy Secretary Robert Kimmitt publicly voice their concerns over potential political goals of SWF investments in the US (The Economist, 2008; Helleiner & Lundblad, 2008: 70; Cohen, 2009: 720). As a response, the US initiates to enact internationally formed codes of conduct for SWFs (the 'Santiago Principles') and recipient countries (OECD guidelines) through the IMF and OECD (Helleiner & Lundblad, 2008: 70-71). These principles include that SWFs should solely invest with a commercial or economic motive - rather than (geo)political motive - and that recipient countries should not discriminate between SWF investments or other investments (ibid: 71). However, in the meantime, President George W. Bush publicly voices that SWF investments are great for the US and that these investments are totally 'fine' (The Telegraph, 2007). This indicates that the US wants these foreign investments, therefore, changing a long-lasting strategy of stopping these investments into vital economic sectors.

This thesis examines why the US government accepts SWF investments into the financial sector at the onset of the subprime mortgage crisis. Especially when considering that many US politicians and high-ranking civil servants seem to be quite wary of 'major national security issues' (Cohen, 2009: 720). The decision to not intervene in these investments seems to be at odds with the ancient strategy of the US to defend its national interests against foreign owned enterprises. This leads to the following research question:

> *Why did the US government accept investments from several sovereign wealth funds into struggling US financial institutions during the subprime mortgage crisis?*

1.2. Theoretical framework

To answer this question, two competing International Political Economy (IPE) approaches are scrutinized. The first theory entails a mercantilist approach derived from influential writers such as Drezner (2008b) and Gilpin (2001), which is enhanced by Rose's (1998) neoclassical realist framework. The second theory compromises a Critical Political Economy (CPE) theory that combines the new constitutionalism theory by Gill & Cutler (2014) with the structural power analysis of Susan Strange (1988; 1996).

The mercantilist approach of Drezner (2008b) and Gilpin (2001) argues that states try to maximize economic power and protect domestic industrialized economic sectors. States act in an anarchic international system where their only objective is to further the state's public well-being. Ultimately, this safety and prosperity can be achieved through economic sacrifices in the interest of long-run prosperity (Viner, 1948: 10). Regarding international bargaining, powerful states can force international rules, agreements, and regimes upon smaller states (Drezner, 2008b: 6). A state bases its foreign and domestic policies upon the outcome of a cost-benefit analysis that in the long-run stabilizes and increases economic prosperity (Drezner, 2008b; Gilpin, 2001).

This mercantilist approach is subsequently enhanced with a foreign policy executive (FPE) approach determining the FPE's effectiveness derived from the Neoclassical realism theory. Neoclassical realism combines the liberal 'Innenpolitik' school of thought– which stresses the influence of domestic variables on foreign policy decisions – and 'neorealist' theories – which emphasize the pressure of international systems on foreign policy decisions (Rose, 1998: 146). Neoclassical realism maintains that pressures from society, domestic institutions, culture, and leader images affect the efficacy of foreign policy decision making (ibid.: 147). For instance, political decision-makers need to appease these domestic or societal pressures, before enacting certain policies (ibid.). Both theories are combined to increase the understanding of US decision-making regarding SWF investments. This leads to the following synthesis: the US government deliberately chooses to accept the investments based on a cost-benefit analysis.

The new constitutionalism theory is part of the CPE school of thought. This approach questions how a certain order of social relations or society came about (Cox, 1981). It therefore does not take institutions and existing social power relations for granted but questions them by investigating their origins and whether they could be in a process of change (ibid.). The new constitutionalist approach argues that entrenchment of neoliberal ideology (e.q. free markets, free-flowing capital, and deregulation) leads to the demise of governmental power to regulate financial institutions (Gill & Cutler, 2014: 3). Neoliberal thought consists of commodification processes where the nature of social reproduction, welfare, society, and governance is reconstituted (e.g. hospitality is not a social gift but bought/sold on Airbnb) (ibid.: 11). The supremacy of neoliberal ideology within governments has furthermore been elevated to the international sphere. This increases the power of financial institutions towards governments as they can ensure their patterns of accumulation at the international sphere. This subsequently is described by the new constitutionalism as the process in which governments are becoming toothless, due to international institutions increasingly enacting flexible and legal standards in which financial institutions can shop for their own preferred laws (ibid.: 6).

To enhance this idea that power shifts away from national governments to non-state actors Strange's analytical framework of structural power is scrutinized. Strange shows that the above-mentioned power shifts are structural. Examining Strange's works provides insight into where structural power actually lies and whether governments are still the owner of their policies or that they accommodate the preferences of the holders of structural power. Strange acknowledges actors, such as SWFs, as world players and argues that states have lost their political authority over society and economy to these financial corporations (Strange, 1996: 4). Structural power is the power that shapes the rules of the game of the global political economy which other states/actors have to adhere to (ibid.: 68). It is the power that can make actors adhere to preferences without having to coerce them (ibid.: 25). The possessor of structural power – whether it is a government, non-state actor, or multinational corporation - dictates the rules of the game (ibid.: 77). To find out who the possessor of structural power is, Strange advises to pay attention to bargains: who gets what in which situation (ibid.: 94). Therefore, from this perspective, the decision to accept SWF investments is explained by structural capitalist pressures and the hegemony of the neoliberal paradigm.

Methodologically, in order to test the theories' explanatory power, a process-tracing method is used to create a structured understanding of the case (Beach & Pedersen, 2019). The case description consists of three phases, providing evidence on the decision-making process. Evidence is retrieved from Congressional records, interviews, newspaper articles, and academic articles. Moreover, a great deal of information is retrieved from WikiLeaks, which provides a unique insight. In the concluding chapter, theoretical implications retrieved from the evidence are discussed and theoretical recommendations are proposed.

1.3. Scientific relevance

At the onset of the subprime mortgage crisis, the US is seen as the sole superpower, especially because of its military capabilities (Strange, 1996; Drezner, 2008b: 36). The structural power analysis of Strange (1998; 1996), however, hypothesizes that despite the high US military capabilities, its power to decide upon its preferred policies will diminish in the field of finance if non-state actors hold structural power (ibid.). The power of non-state financial institutions has only increased since Strange's work, which makes it even more likely that the ability of the US government to dictate its policy is diminished (Krippner, 2005). It would be academically relevant to assess whether empirical findings backing the CPE theory can demonstrate that even the most powerful country in the world cannot protect itself from free-flowing capital hurting its domestic economy. Furthermore, it would mean that the theoretical underpinning of the neoclassical mercantilist theory - the state is a unitary actor and other actors do not matter - does not hold in practice.

1.4. Societal relevance

This thesis can contribute to societal insights on whether states can(not) protect themselves against foreign investments. As previously described, in a 2006 poll Americans oppose the overtaking of American companies by foreign entities (Pew Research Center, 2006). Furthermore, in a 2008 poll, US citizens oppose SWF investments from all countries other than Australia or Norway in the US economy (The Wall Street Journal, 2008). In addition to the people disliking these investments, politicians also publicly oppose them (The Economist, 2008; Helleiner & Lundblad, 2008: 70; Cohen, 2009: 720). This thesis could give insights for civil groups, civil servants, and government agencies into the governments' playing field and why it struggles to create policy according to the people's wishes.

1.5. Structure of research

This thesis continues with Chapter 2 which lays out the ontological foundations of the mercantilist theory enhanced by a neoclassical realist framework, and a CPE perspective which combines theoretical underpinnings of new constitutionalism and Strange's structural power analysis. In chapter 3 the neoclassical mercantilist theory and the CPE approach are operationalized to form hypotheses and the designated methods are discussed. Chapter 4 provides empirical findings from many sources including academic papers, official US governmental and international organizational documents, and Wikileaks which are structured in three policy phases. Chapter 5 concludes this thesis with a discussion of the results and areas further research could focus upon.

2. Theoretical Chapter

This chapter will describe the two theories that are used in this research. For the neoclassical mercantilism theory, first the philosophical roots are described, then the theory itself is illustrated, where after a major drawback to the theory is discussed. This leads to the addition of the neoclassical realist theory, which when combined, constitutes the neoclassical mercantilist theory. The CPE perspective starts with a description of its philosophical roots. After which the new constitutionalist branch of CPE is discussed, showing the trend of neoliberal ideology causing power to shift from governments to the private sector. This power is subsequently linked to the idea of structural power within the financial sector as described by Strange (1998).

2.1. Neoclassical mercantilism

2.1.1. Theoretical underpinnings

The ontological foundations of mercantilist thinking in IPE originates from ancient realist thinkers such as Thucydides, Cicero, Machiavelli, and Thomas Hobbes. The latter visions the world as an anarchy where inhabitants violently compete with one another for status and material goods until they agree upon a social and a political contract (Hobbes, 2016). The social contract entails that inhabitants of a territory accept individual and property rights in return for the concession of certain liberties, such as the government's ability to use force (ibid.). These concessions result in the government of the state becoming the protagonist in increasing the inhabitant's well-being and the sole authority to use force (ibid.). Thus, through these contracts (violent) competition among inhabitants and anarchy are put to a halt (ibid.). However, states do not have such arrangements in place in the international sphere (ibid.). Therefore, (violent) competition for wealth and other objectives contributing to the state's well-being still dominates the anarchic international system (ibid.). This mechanism is used as a starting point for the realist theory.

From this starting point, two different interpretations of international anarchical affairs are created – state-centric and systemic realism. State-centric realists argue that the behavior of states is generated by states primarily assessing their power (Gilpin & Gilpin, 2001: 16). Systemic thinkers oppose this as they argue that the distribution of power between states and relative power determines states' objectives in international affairs (Waltz, 2010). Both strands do not agree with a constant level of fighting in international relations as argued by Hobbes, but expect that international cooperation between states is possible, if it is in their interests to do so (Gilpin & Gilpin, 2001: 17).

The neorealist branch builds further on systemic realism and holds that the state's principal concern remains their national security in a "self-help" international Hobbesian system – with continuous threats to its political and economic independence (Waltz, 2010). The neorealist approach knows two different fields: defensive and offensive realism. Offensive realism argues that states pursue as much power as possible and that violent conflict should be used to gain more power - if benefits outweigh costs (Mearsheimer, 2002). Defensive realism, however, holds that countries try to balance themselves against each other and thus create a balance of power (Waltz, 2010). Neomercantilism argues that balancing of states is done internally and externally (Waltz, 2010). Internally, states find balance through increasing military capabilities, externally, they find balance by creating alliances or taking advantage of less powerful states (ibid.). States act 'predictable' according to Waltz (2010) because they are in the same Hobbesian system and want to achieve the same thing: national security. Therefore, foreign policy is based upon this one objective, making other objectives – such as cooperation or values - of second-order importance.

2.1.2. Mercantilism

Mercantilism builds further on the neorealist theoretical underpinnings: The state is the absolute rational decision-maker, acts in an anarchic international system, and therefore tries to shift international politics into its favor. Mercantilists regard economic welfare, instead of security relations between states as the most important objective. Therefore, mercantilists search for the interaction between economic markets and important actors, such as states, multinationals, and international organizations. They examine how production and distribution of wealth are associated with political intervention (Gilpin, 2016: 9). Viner, an important mercantilist thinker, describes eloquently what mercantilism entails in the following quote:

> *"(1) wealth is an absolutely essential means to power, whether for security or for aggression; (2) power is es- sential or valuable as a means to the acquisition or retention of wealth; (3) wealth and power are each proper ultimate ends of national policy; (4) there is long-run harmony between these ends, although in particular circumstances it may be*

necessary for a time to make economic sacrifices in the interest of military security and therefore also of long-run prosperity." (Viner, 1948: 10).

Neomercantilism builds on these theoretical underpinnings and believes that, in the modern globalized economy, nation-states are still the most important actors (Gilpin & Gilpin, 2001: 21-23; Drezner, 2008b: 3-5). Nation-state governments choose their foreign and domestic policy decisions in a "self-help" anarchic Hobbesian international system with only one goal: increase national (economic) interest and thus, further the public well-being. Because of the "self-help" system, states are constantly in a fight and need to react to pressures from other countries to ensure their sovereignty. To find the right policy approach to events altering the status quo, states calculate without interference from domestic or international powers, in a cost-benefit way, all policy prospects and choose the policy prospect that increases national economic interest most.

Neomercantilism also knows a divide in offensive and defensive branches, however, in neomercantilism, those are named: malevolent and benign mercantilism (Gilpin, 2016.: 32). The first branch focusses on a state using aggressive behavior – economic warfare – against other states to advance its economy (ibid.: 33). The latter focusses on protecting the economy against the influences of other states (ibid.: 33). Herein relative gains are more important than objective gains, meaning that states always want to ensure that their gain is relatively higher than other states' gains (ibid.: 33). In this thesis, the defensive and offensive strand are equally useful due to the US objective to protect the financial sector against SWF investment domestically and to ensure a profitable environment internationally. The foremost objective of states in mercantilism is to protect its economy against foreign economic and political forces, and further ensure the proliferation of the economic well-being (ibid.33). A state can protect its economy and further the public well-being by taking policy action in the domestic sphere or international sphere.

In the domestic sphere, states value economic sectors with a high level of industrialization as these generate great economic wealth (ibid.: 33). Industrialization causes self-sufficiency and political autonomy over the state's economy (ibid.: 33). This is more important than economic interdependence or cooperation, as the latter leads to insecurity because the real objectives of partnering states are never clear (ibid: 33-34). Lastly, military industries and the means to set up military power – which enables national security - can only be accomplished by economic means generated partly from highly industrialized industries (ibid.: 33). Therefore, states protect their domestic technologically advanced industries against the influence of external economic or political forces and foreign meddling to preserve key industries. By maintaining key industries, countries can increase their relative material capabilities and thus, increase their national (economic) prosperity.

In the international sphere, dominant states establish the economic rules of the game for smaller states, multinational corporations, and other (international) economic actors, by forcing policies upon them which shape the structure and functioning of the world economy (Gilpin & Gilpin, 2001: 23). A relatively more powerful state can force even non-state actors into compliance with rules that are in favor of the powerful state – in exchange for access to its internal markets or by threatening to use its economic power (Drezner, 2008b: 35). In this endeavor, powerful states use their power to set up international regimes and organizations to shape the world economy into their favor (Drezner, 2008b: 6). The relationship between economics and politics is therefore interactive (Gilpin & Gilpin, 2001: 23). (Inter)national markets are - in this view - subordinate to the interest of the most powerful state, which actively tries to influence (inter)national market forces to increase its domestic economic wealth and power (Gilpin, 2016: 31-32). This is possible because market size is translated into government power, which in turn, facilitates economic coercion of other actors (Drezner, 2008b: 32). States hereby continuously use their power in order to implement policies that channel economic forces in favor of their own national interest and interests of the people (Gilpin, 2016: 31-32). Drezner (2008b) argues that - in this highly integrated global economy - states use domestic, as well as international policies to increase their own national economic interests. Due to globalization, domestic policies affect international markets and vice versa (ibid.). Therefore, domestic and international policies are intertwined and can be used to substantiate the same goal (ibid.). In other words, states use their power in the international sphere to achieve domestic control and states use their power domestically to influence international markets in their favor. Powerful states choose whether they pursue expansionist international policies or domestic policies, by assessing which benefits the public well-being the most in a cost-benefit analysis.

2.1.3. "Opening" the black box

The theoretical underpinnings provided by neorealist thinkers for the neomercantilism theory receive critiques from constructivist and neoliberal scholars. Wendt (1999), a main constructivist thinker, argues that the social interpretation of anarchy, state's identity, and state's interest is not the same in every situation – as neorealism assumes with their use of rational choice theory. Therefore, it is important to analyze human volition and interpretations when researching a state's decision-making (ibid.). Furthermore, neoliberal scholars such as Moravcsik (1997), critique the neorealist understanding of a state's decision making by noting that internal factors influence the behavior of states in an international anarchic system. Internal factors entail internal politics, the socioeconomic structure of the state, and political and economic ideology (ibid.). These internal factors determine the preferences and configurations of key domestic actors - who in the end determine foreign policy for the government. Neorealism disregards those internal domestic factors and social interpretation of policy choices with its static rational choice assumption. Therefore, many scholars advise to 'open the black box' or 'open the mind of the decision maker'. These critiques of mercantilism have not yet contributed to a new IPE theoretical field that enhances 'opening the black box'. Even though Drezner (2008b:6) acknowledges that "domestic factors account for preference formation"; there is no theoretical framework for understanding the effects of domestic factors included in neomercantilism. In the field of international relations, however, such a theory exists. Therefore, to enhance the theory of mercantilism: a neoclassical realist analysis of the domestic factors affecting the Foreign Policy Executive (FPE) by Rose (1998) and Ripsman et al (2016) is added.

2.1.4. Adding FPE analysis

The neoclassical realist FPE fills the gap that arose from the 'black box' critiques on neorealist assumptions. Neoliberal theories suggest that decision making is influenced foremost by domestic factors. Neoclassical realism combines the two schools by using domestic factors as the determining factors of the efficacy of the foreign policy decision made by the FPE (Rose, 1998). Rose's (1998) neoclassical analysis focusses on two aspects determining foreign policy decision making. First and foremost, the state's behavior is determined by the state's goal of achieving economic prosperity within an anarchic international system – which complies with neo-mercantilist thinking (ibid: 146). However, in obtaining this objective of economic prosperity, certain variables such as politicians' perceptions and bureaucratic conditions influence the efficacy of decision-making (ibid.: 146). This aspect contains the influence of neoliberal "*Innenpolitik*" factors on foreign policy formulation (ibid.: 146). The theory thus deviates from neo-mercantilist thought which assumes that the leader is absolute (e.g. Hobbes' Leviathan) and not restrained by domestic factors. Therefore, the new equation entails the effect of the independent variable "cost-benefit analysis by the FPE" on the dependent variable "foreign policy" as formulated by the FPE - whose room to maneuver is determined by "domestic factor" variables (for a detailed description see chapter three). Four domestic factors and the framework of analysis will be outlined hereafter according to the work of Ripsman et al. (2016).

By combining schools of thought, neoclassical realism is often accused of cherry-picking variables from existing theories and purposely choosing a vague scope and domain of research to gain explanatory power (Ripsman et al., 2016: 9; Rathbun, 2008; Kitchen, 2010). Ripsman et al. (2016) overcome this problem by introducing two systemic variables: clarity and permissiveness/restrictiveness of strategic environments. These two systemic variables determine which of the four domestic level clusters influence the efficacy of the decision-making. The problems surrounding the cherry-picking of variables are resolved by providing theoretical background. Clarity entails the degree of transparency leaders encounter, regarding information on opportunities and threats, during a particular time horizon (ibid.: 46-52). The level of clarity determines the level of uncertainty in which decision-makers operate. More uncertainty creates room for personal interpretation, personal preferences, and cultural background - which influence decision making processes. Therefore, a high degree of clarity on the nature of a state's threats and opportunities leads to predictable policy outcomes. This enhances the already existing theory of Waltz (2010) that states are like-units that act upon systemic pressures in the same way.

The permissiveness or restrictiveness of strategic environments is another systemic variable that Ripsman et al. (2016: 52-56) introduce. Permissive and restrictive strategic environments show the imminence and magnitude of the opportunities and threats presented to states (ibid.). When a threat or opportunity is imminent and big: a state's possible reaction is restricted and with it the options of the FPE to maneuver in the international system are small. Whereas when opportunities or threats are not big and imminent; a more permissive strategic environment exists (ibid.). Permissiveness and restrictiveness of strategic environments thus show the options available for decision-makers.

2.1.5. Adding intervening variables

The four domestic variables presented here are an impressive addition to the current literature on neoclassical realism. The authors build on articles and books from scholars such as Dueck (2014), Kitchen (2010), Rose (1998), and Schweller (2004) to formulate four new domestic variables that influence the efficacy of the decision-making of the FPE (ibid.: 59).

Firstly, leader images entail the beliefs or interpretations of FPEs (ibid.: 61). These cognitive constraints stem from FPE's personalized values and beliefs – created through prior experiences (ibid.: 62). These prior experiences contribute to how FPEs process information. FPEs can ignore certain parts of information or focus more on other parts or understand information and signals differently due to cognitive constraints (ibid.: 62). Leader images influence the interpretation and classification of policy prospects within a cost-benefit analysis.

Secondly, cultural aspects create indications of the degree of support for a policy prospect by the people (ibid. 66). This strategic culture variable includes norms, beliefs, and collective cognitive expectations that are deeply entrenched in society. These norms shape the strategic understanding of the FPE on topics such as the acceptability of policy (ibid: 67). The acceptability of actions directly influences the FPE's freedom of decision-making. As Dueck (2014) shows: decision-makers frame, modify, and adjust strategic choices to comply with cultural preferences to keep popular support. This problematizes achieving objectives for the FPE when policies do not comply with domestic culture.

The third cluster entails state-society relations, which consist of interactions between state institutions and various economic and societal groups (ibid.: 71). Key attributes of this cluster are the degree of harmony between the state and society, and level of political and social cohesion within a state (ibid.). An important factor here is the degree of influence society has on actual policy formation and implementation. Furthermore, Ripsman et al. (2016) argue that the FPE will be restrained when encountering competition or societal pressure towards enacting legislation (ibid.: 72). However, when the FPE has a dominant coalition of support within society it will be easier to enact expansionist international objectives such as freer trade and international cooperation on the global level (ibid.: 72).

Fourthly, domestic institutions consist of formal institutions, such as bureaucratic oversight and bureaucratic rules (ibid.: 75). Institutions determine who contributes to policy formation and what power those players have to either stop or create policies (ibid.). For democratic regimes, these institutions decide the degree of autonomy of the FPE (ibid.). Therefore, the amount of legislation, bureaucracy, and decision-making procedures requiring consent from other governmental departments determines the FPE's effectiveness of intervention.

These four variables differ in their effectiveness in explaining policy outcomes in different situations. This depends on the clarity and strategic environment in where the FPE acts (ibid.: 91). For example, leader images are less important when the FPE could extensively discuss certain details with its advisors before deciding upon a definitive policy (high clarity). Furthermore, regarding state-society interactions: bureaucracies, key interest groups, and societal actors have more time to mingle in the process when there is less clarity and a longer time horizon. The intervening variables are thus not chosen in an ad-hoc manner as many critics of neorealism argue. The systemic variables clarity and strategic environment determine which cluster is most useful in what situation, as portrayed in Table 1.

Table 1: Intervening variable clusters by the degree of systemic clarity and strategic environment

		Degree of Systemic Clarity (High to Low)	
		High Clarity	Low Clarity
Nature of Strategic Environment (Restrictive to Permissive)	Restrictive Environment	*Leader images and Strategic culture*	*Leader images and Strategic culture*
	Permissive Environment	*Strategic culture, Domestic institutions, and State-society relations*	*Indeterminate—all four clusters could be relevant.*

(Source: Ripsman et al. (2016): 95).

2.1.6. Summary

A Hobbesian international system forces the state to act in an environment of constant competition and insecurity. Therefore, a state tries to increase its economic strength, maintain key industries, and increase self-sufficiency to achieve their ultimate goal: optimal national (economic) public well-being. The state bases its policy to achieve this goal on a cost-benefit calculation in which different policies - domestic and foreign - are weighted. As a powerful state, the US can coerce other countries to agree with its foreign objectives. Domestically it has the sovereign power to intervene in foreign investments. The efficacy of the policy prospects from the cost-benefit analysis are subsequently determined through domestic factors such as cultural background, working of institutions, state-society relations, and its leader images. Which domestic factors intervene in the relationship is retrieved from the degree of clarity and strategic environment. Therefore, the policy outcome and the efficacy of these outcomes need to be explained by including domestic variables to the cost-benefit analysis.

2.2. Constitutionalizing structural power

2.2.1. Critical Political Economy

The realm of the international political economy consists of three main strands, namely: Mercantilism, Liberalism, and CPE. Critical political economic thought develops upon the assumptions of Karl Marx about the international political economy. The ideas of Marx stem from the concept of dialectics as described by Hegel (Lukacs, 1972). This concept describes that inherent contradictions within society create tensions, described as a socially formed thesis and antithesis. When tensions between societal groups grow out of control, these inherent contradictions will be canceled out, stored and brought to a higher level - a new form of society (ibid.). Thus, the inherent contradictions within society lead to a situation where this contradiction is taken to a higher level. Then at this higher level, a new inherent contradiction within society is found. Marx agrees with this dialectical process and argues that history and society can be researched through this process, by stepping out of the investigated society and observe this society as if the researcher had no part in it (ibid.). Marx goes beyond that and argues that, during his time – the aftermath of the industrial revolution -, current inherent contradictions – such as continuous crises and ongoing worker exploitation- are part of capitalist society. Consequently, the capitalist society is expected to fail and turn into a socialist society when these inherent contradictions are resolved. Joseph Schumpeter argues that Marxist thinking can be approached in three different manners: Marxist philosophy, Marxism as social science, or Marxism as a social praxis (Elliott, 1980). CPE theories combine these three approaches to explain why capitalism survives in current societies despite the inherent contradictions. Marxist philosophy entails Hegel's dialectic process, Marxism as social science could be seen as a critical 'antithesis' to the current thesis within society, and Marx's political praxis argues Marx's prediction that transforms society for the better. This thesis will use these Marxist perspectives to describe Gill & Cutler's (2014) CPE branch: New Constitutionalism - which builds further on the Neo-Gramscian branch –, and Strange's CPE analysis on structural power.

2.2.2. Neo-Gramscian approach

Antonio Gramsci builds on Marx' ideas as he tries to explain why capitalism survived many crises, even though capitalism is creating a situation where many people are worse off in comparison to a socialist system. He theorizes a tactic of appeasement of the people (Anderson, 1981). In his research, Gramsci first examines how a state deals with the appeasement of its (former) elites. He states that these elites are appeased with gifts of profitable niche markets so that these elites will support the capitalist structure (ibid.). Furthermore, new elites, such as the new bourgeoisie, are consequently appeased by providing them with cooptation in governmental institutions and a controlled environment where they can criticize the capitalist structure, but not change it (ibid.). Thirdly, the workers in a capitalist structure are appeased by the state which limits exploitation through providing welfare regulations and ideology (ibid.). The ideology of 'hard work pays off' is used to motivate people to accept poverty today because they can become rich tomorrow – which takes away the need to fundamentally oppose the capitalistic structure (ibid.).

Robert Cox (1983) takes the Gramscian idea of the appeasement of the people to the realm of international relations. Cox (1983) argues that international organizations and international relations appease people in return for accepting capitalistic structures. Furthermore, Cox (1981) takes a Marxist view arguing that research entailing CPE should acknowledge historical evolvements and how certain power structures came about – adhering to the process of dialectics by Hegel (Bieler & Morton, 2004). Therefore, it does not take current power and social relations for granted but tries to question them (ibid.). By taking Gramscian ideas to the international level, Cox (1981) identifies important power configurations beyond the state and introduces the concept of hegemony. To make the argument that capital has now reached hegemony, Cox (1981) states that in the 1970s a structural change occurred in production creating the conditions for the hegemony of transnational capital. This led to a situation where states became tools for neo-liberalism to spread the logic of structural capitalist competition (Cox, 1992).

2.2.3. New constitutionalism

New constitutionalists build further on Cox's critical understanding of the world by looking from an outside-in perspective to the origins and form of the current world order and international relations (Gill & Cutler, 2014: 3). New constitutionalism as we currently know it is formed in the 'neoliberal era' in the 1980s (ibid.: 5). In that period, Fukuyama claimed that neoliberalism would be the final polity at the 'end of history' and British Prime-Minister Thatcher argued that there is 'no alternative' to neoliberalism (Fukuyama, 2006; Gill & Cutler, 2014: 5). Since the '80s, neoliberal policies are implemented everywhere: from international regulation and governance structures to a person's daily life (Gill & Cutler, 2014). Neoliberal policies are associated with laissez-faire economic liberalism: policies of economic liberalization, privatization, deregulation, free trade, austerity, and reductions in government spending in order to increase the role of the private sector in the economy and society. Important to note here is that new constitutionalism scrutinizes neo-liberal policies, not the earlier described neoliberal theory of international relations.

The new constitutionalism theory builds on Gramscian understanding of collective mentalities that dominate society (Gill & Cutler, 2014: 30). It argues that through commodification processes everything within society is perpetrated as a tradeable commodity. This results in market-thinking processes in every sector of public life, even in sectors that were previously managed by the welfare state such as education, healthcare, etc. (ibid.). People accept this because they are taught to believe in neoliberal concepts such as market thinking. This belief in neoliberal values is so embedded in people's minds, that they generally think that every situation in life should be solved or approached by concepts of efficiency and incentives. Because of the supremacy of neoliberal ideology within people's minds and the academic world, the ideology is also integrated within governmental decision-making. This paves the way for 'market civilizations' where every aspect of society can be neoliberalized, disregarding the social effects. This contains the commodification of political, civic, and societal phenomena and a shift toward flexible accumulation –where capital generates profits instead of profit being created out of real production (ibid.: 34). This understanding builds further on Harvey's (2004, 2010) financialization theory, where overaccumulation in all economic sectors leads to a turn to financial products to create the desired profits. This neoliberal turn thus leads to neoliberal ideological supremacy within society and penetration of neoliberal thinking in every sector of human life, paving the way for flexible capital accumulation.

This neoliberal discourse was eventually also enacted in international affairs through the formation of international agreements, regimes and treaties. This is a direct result of the domination of neoliberal thinking at the domestic level (Gill & Cutler, 2014). These international agreements, regimes and treaties subsequently constitute a globalized new world order of neoliberal regulations and laws (ibid.). These international organizations subsequently take over legislative power from states to enact political-legal – including hard and soft law - and regulatory mechanisms (Gill & Cutler, 2014). These regulatory mechanisms in the international sphere in turn further institutionalizes the supremacy of neoliberal thought in the world. First, an ideology is shaped for the people, which consequently will be institutionalized in the international realm.

Subsequently, neoliberal thinking can get locked-in within various international agreements and international organizations. Through neoliberal reforms power and sovereignty of governments shifts towards the private realm as market interference by governmental institutions is seen as destructive (ibid.). Subsequently states cannot challenge corporate decisions or capital movements anymore as neoliberal principles of capital and market freedom are locked-in by international agreements and international organizations (ibid.). Locked-in means, in this case, that states multilaterally enact agreements, which cannot be overturned by states once enacted because it is now part of the 'international realm'. Therefore, states lose power – as they have to adhere to the rule of law created within the (international) system.

Thus, New Constitutionalism argues that neoliberal thought is central to the rise of the power of the capital market (ibid. 23). Furthermore, this neoliberal thought at the domestic level paves the way for soft, neoliberal international laws at the international sphere. This constitutes a new world order, which entails – according to new constitutionalism - a structure of laws and agreements that locks in neoliberal free market principles (ibid.: 23). This situation lays bare a clash named by Marx as 'inherent contradictions within society' (ibid.: 23-24). The inherent contradiction is that states cannot regulate multinational corporations anymore as those corporations can 'shop' for more convenient laws in other countries.

2.2.4. Bringing in Strange's integrated analytical framework

A fruitful contribution to this theoretical framework is the structural power analysis of Strange's (1988) integrated analytical framework. Strange's analytical framework shows that the dominance by multinational corporations over governments (new constitutionalism theory), actually entails a structural power relationship. Therefore, to better understand the relationship between governments and private institutions, Strange's structural power analysis is added to the new constitutionalist approach.

Strange argues that scholars of international relations and economics do not properly understand the international political economy because they emphasize their research wrongly. Whereas economists do not take power relations into account, international relations scholars wrongly focus upon the state as the sole source of policy outcomes (ibid.). Therefore, she develops her own analytical framework to understand the field of international political economy properly, by integrating perspectives from both economics and political science. Strange acknowledges – as new constitutionalists do – that states are losing power to multinational corporations and other actors. However, Strange envisions power relations to be different than just purely relational (A forces B to do something). In her analytical framework, she focusses on structural power, which encompasses the power to influence decisions with merely the existence of the actor holding structural power. Structural power is defined by Gwynn (2019: 204) as follows:

> *"Structural power characterizes a situation in which the institutional context shapes actor preferences or incentives in such a way that one actor (B) conforms its behavior to (A)'s preferences, independent of any specific attempt by (A) to affect their relationship."*

Structural power is one of the two types of power next to relational power that Strange distinguishes in her framework (ibid. 65). The first type, structural power, is the most important as it constitutes relationships between economic enterprises and states within the international political economy (ibid.). It entails a form of power that can – in the long term - shape and determine the playing field that other actors have to adhere to (ibid.: 66). This means that structural power can form the rules, customs, and norms that govern international economic relations. Strange finds that structural power can be achieved in four different structures, namely: control over security, control over production, control over credit or finance, and control over knowledge, beliefs, and ideas. Strange (1988) states that only when scholars comprehend the relationship and ownership of these structures in certain cases, the international political economy can be examined rightfully. An important question according to Strange to examine these relationships and ownerships is: who gets what in which situation (ibid.: 94)?

According to Strange's empirical research on the topic of financial markets, power is shifting away from states towards multinational companies (Strange, 1996). She examined the US to assess whether powers had shifted in the four basic domains. This resulted in a remarkable finding that the US have actually lost power in three out of the four structures – only remaining the most powerful in security (ibid.). These lost powers went to financial institutions and multinational corporations (ibid.). She concurs with the argument made by Gill and Cutler (2014) that these power concessions are due to – among others - deregulation of the US economy (Strange, 1996). She argues furthermore, that due to technological advancements in economic industries, structural power is expected to shift away further towards international financial markets (ibid.). That means that governments will now merely be able to accommodate to the preferences of international financial institutions. This is counterintuitive, especially when taking into account that a democracy gives the right to the people to give away power to a certain actor – which, in the end, might be a futile thing to do.

Since Strange's argument of excelling power loss of governments in finance sectors and the onset of the subprime mortgage crisis, a lot has happened (Strange, 1996). Since then, structural power of financial institutions has increasingly taken over societal aspects (Van der Zwan, 2014; Harvey, 2010; Krippner, 2005). Therefore, Strange (1996) argues that scholars should pay attention to untangling the complex web of overlapping, symbiotic or conflicting authority in bargaining situations within the domain of finance. The question on who gets what is important as states can no longer unilaterally set their policies without having to consult with other powers in the finance structure due to their increasing importance (ibid: 43). For example, financial corporations and institutions can leverage additional policy conditions to make countries comply with loans (Larmour, 2002). Moreover, capital can freely move across borders and be used to take control of foreign financial institutions. The power of the financial sector is ever-growing due to the need for capital and liquidity, creating vulnerabilities for countries setting up high barriers for foreign capital injections. Combining this with processes of new constitutionalism creates a theoretical window of opportunity for financial institutions to force states to enact and promote more hardcore domestic and international neoliberal laws without even having to pressure the states overtly.

The actor holding the power in the financial superstructure can decide the ways in which other actors can spend money today and has the power to (mis)manage floating currencies tomorrow. Therefore, the financial superstructure is defined as "all the arrangements governing the availability of credit plus all the factors determining the terms on which currencies are exchanged for one another" (Strange, 1988; 191). Liberalization opened the door to greater risk-taking in the financial markets and thus brought economic instability (ibid.: 195). Strange argues that not one sole theory can explain IPE processes: thus, researchers should look at processes that can - with common sense – be explained in terms of power (May, 1996; 172). Therefore, power in the financial structure can be explained by the authority to control or create credit in the global economy (ibid.). In this case, the framework offers a way to analyze nonvisible – within the societal context - structural power relationships. Subsequently it can advocate that the inaction of the US government towards the SWF investments in US financial institutions comes from the hegemony of financial institutions over governments.

2.2.5. Summary

The combined CPE approaches lead to a 'constitutionalizing structural power' approach, which argues that through liberalization in all spheres of human life a new constitutional power is created (Gill & Cutler, 2014). This power entails commodification processes, many regulatory institutions, and ideological institutions on the international, as well as the national level (ibid.). This results in a new world order that diminishes state power by demanding more and more neoliberal regulations (ibid.). Therefore, the state has become a puppet of neoliberal ideology in a neoliberal world order where it accepts that power remains at the 'market side'. This theory is enhanced with the analytical framework of structural power by Susan Strange (Strange, 1988; 1996). She presents a framework where scholars can assess these powers and find out where the actual powers of actors reside –the government, multinational actors, corporations, societal groups, etc. (ibid.). Especially when examining the superstructure of finance, Strange finds that the power is flowing away to financial institutions and non-state actors. Finally, it is therefore expected that the US – in the case of SWF investment in financial institutions – cannot stop these investments, because that will go against neoliberal thought and the current holders of the financial superstructure. The structural power of the new constitutionalist world order is compelling the US to accept the investments, even though it could damage the US financial sector through uncertainty by handing over the authority to other states' investment corporations.

3. Methodological Chapter

This chapter will provide information on how the central question in this research is tested. First, hypotheses are drawn from the two theories discussed in the theoretical chapter, where after those hypotheses are operationalized. Second, the epistemological approach will be described. Thereafter, the sources and method of inquiry will be discussed. Fourth, limitations of the sources and the whole case study design will be portrayed.

3.1. Hypotheses and operationalization

3.1.1. Dependent variable

The dependent variable in this thesis is the policy output of the US government towards the investments of SWFs into US financial institutions. According to Alons (2007) the US policy output towards foreign investments could consist of 1. domestic protective (economic) measures, 2. international protective (economic) measures involving international organizations and regimes, and 3. bilateral agreements with foreign governments (Gilpin, 2016; Drezner, 2008b; Gill & Cutler, 2014; Alons, 2007). The policy output of the FPE should be assessed holistically. The dependent variable entails both the domestic acceptance of SWFs and the collateral foreign policy initiatives of the US government. Therefore, the three policy outputs proposed by Alons (2007) will be scrutinized to see the total US policy response to the incoming investments.

3.1.2. Mercantilist theory

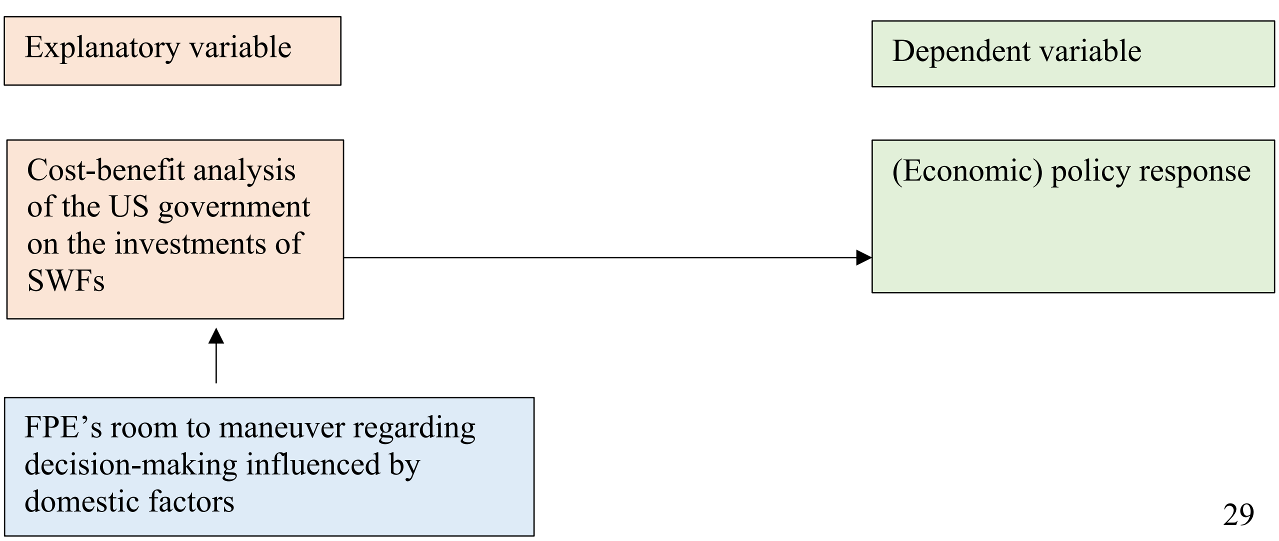
The neoclassical mercantilist approach as described in chapter 2 entails the FPE weighing policy options through a cost-benefit analysis. The main goal of a state is to further the public (economic) well-being (Gilpin, 2016; Drezner, 2008b). In this case, the FPE is furthering the public well-being by choosing the optimal perceived policy prospect. As this case is about the US protecting its economy from other countries' SWF investments, the total policy response of the US – domestic and international – is scrutinized. The expectations derived from the neoclassical mercantilist perspective can be summarized in the following overarching hypothesis:

The US accepts the investments from SWFs in failing US financial institutions because the FPE perceives this as the best outcome in a cost-benefit analysis.

To test this hypothesis, the independent variables should be identified. Therefore, the use of a cost-benefit analysis on the consequences of US government interventions regarding the case of SWF investments into US financial institutions should be examined. The use of this seems plausible when speeches from the highest executive in the US – the President – are assessed. In these speeches, Bush acknowledges that protecting US citizens against investments jeopardizing national security and accepting capital investments into vital US economic markets that need the liquidity are ways of dealing with this issue (The White House: President George W. Bush, 2008). This quick test shows that the US FPE at least acknowledges two policy options to respond to this case.

Furthermore, empirical research must find evidence on the existence of considerations and discussions at the governmental level. More specifically, whether the FPE gets information from politicians or experts and whether societal actors play a part in the decision-making. Restraining or enabling domestic factors that should be accounted for are: Leader images, state-society relations, domestic institutions, and strategic culture. In other words, domestic factors influence FPE decision-making processes – which in turn affect the cost-benefit analysis. According to Ripsman et al. (2016: 95), the degree of clarity and nature of the strategic environment in a case determines what kind of domestic factors are important. Therefore, to test the hypotheses, evidence should be found that supports the existence of the domestic variables that, according to Ripsman et al.'s (2016) theory, affect the decision-making process of the FPE. When these domestic variables are in the government's favor, the FPE will not be restrained and can freely and quickly implement its policy. The theoretical chain of events described above can be summarized in the conceptual model 1:

Figure 1: Conceptual model 1 Neoclassical Mercantilism



According to the theory, the policy response that will be chosen should optimally further the public well-being of American citizens and companies in the perception of the FPE. Therefore, the hypothesis is confirmed when the perceived result of the FPE's cost-benefit analysis supports the acceptance of SWF investments into US financial institutions. Therefore, it is important that the US tackles the problem they acknowledge and subsequently achieve economic prosperity. This confirmation also entails the expectation that domestic factors will either enable or restrain the FPE from acting quickly due to their acceptance of the government's policy stance. This hypothesis will be rejected when the FPE agrees that SWF investments can have negative impacts but has no ability to counter the agreed negative effects of the investments. In this case, the state is not the ultimate powerful actor as described by the neoclassical mercantilist theory.

3.1.3. 'Constitutionalizing structural power' theory

The CPE approach 'constitutionalizing structural power' entails a holistic approach to the decision-making process of the US government. The theory argues that the US government cannot defend its domestic interests against the powerful interests of capital freedom and the structural power of the multinational financial institutions (Gill & Cutler, 2014; Strange, 1988; 1996). This stems from the neoliberal hegemony that constituted international regimes and rules that ensure open markets and neoliberal reforms. Thus, the new constitutionalist world order of liberal regimes and financial institutions indirectly force countries to stay open to foreign investments, through their structural power (Gill & Cutler, 2014). Therefore, the build up towards the policy response of the US is scrutinized, which starts with examining ideological aspects within the US government. The expectations of the CPE perspectives boil down to the following overarching hypothesis:

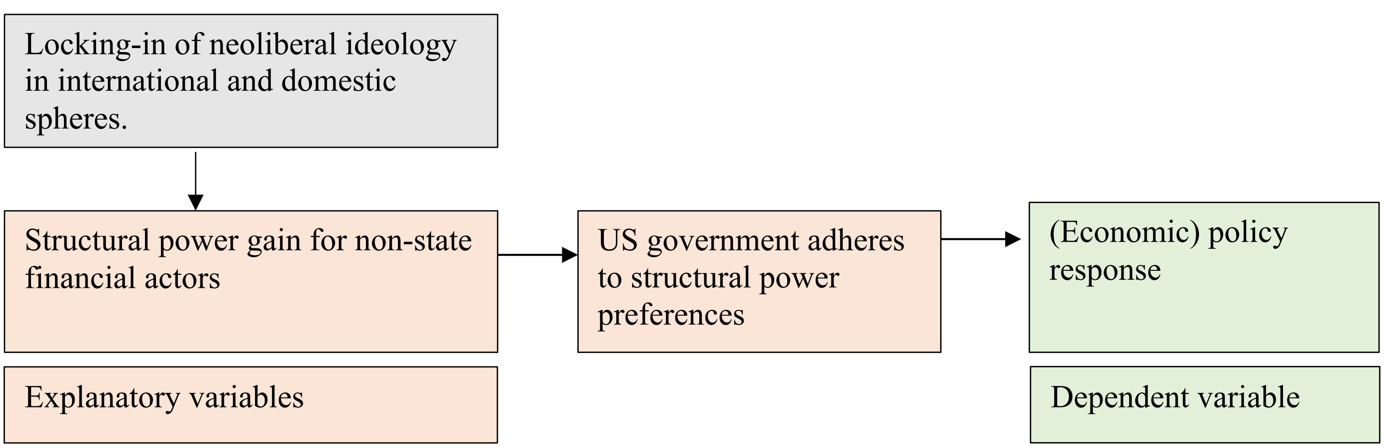
The US accepts the investments from SWFs in failing US financial institutions because it is structurally forced by a neo-liberalized world order to adhere to neoliberal practices.

Before the hypothesis can be tested, the independent variables have to be operationalized. The two independent variables are: the existence of neoliberal ideological supremacy causing loss of formal accountability for multinational corporations and the acknowledgment of structural power of the finance sector vis-à-vis the US government (Gill & Cutler, 2014; Strange, 1988; 1996). Strange's (1988) research papers and the new constitutionalist theory both argue that the (structural) power of governments - to decide upon the rules of the game of capital markets - is lost to multinational financial corporations (Gill & Cutler, 2014).

After acknowledging neoliberal commodification and financialization shifts in the domestic sphere, the neoliberal reshaping of the international sphere through legal means has to be examined. Evidence should be found on the effect of these neoliberal regimes, laws, and rules at the international level - which subsequently cause locking-in mechanisms of neoliberal patterns of accumulation. This entails ambiguous laws and regimes that de facto give corporations and non-state actors more freedom. Finally, the proliferation of soft, self-regulatory standards for multinational corporations must be scrutinized.

The loss of government authority over financial markets due to a new world order of locked-in neoliberal standards is related to Strange's (1988) idea of a shift in structural power from the government towards multinational corporations. Structural power determines the most likely policy outcome of the US as it indirectly forces the state to adhere to the preferences of financial institutions (ibid.). This means that a liberalized world order exists and that the US government is subject to its will even without directly forcing it. Therefore, the degree of neoliberal hegemony and the way the US government assesses the investments should be scrutinized as the independent variable. When the policy preference of the government collides with the neoliberal discourse, as protagonized by the new constitutionalist approach, this is caused by financial institutions holding structural power over the US government. This phenomenon is anecdotally supported through theories and has to resemble the evidence found in this research. To confirm this hypothesis, empirical evidence should support the theoretical framework underlying the effect shown in the conceptual model 2, seen below:

Conceptual model 2



According to the theory, the hypothesis is confirmed when the US adheres to the wishes of non-state actors and a neoliberalized world order and thus accepts the investments of SWFs. Neoliberal ideology within the US and at the international sphere provides a better bargaining position for non-state actors as this causes deregulations of private entities. It is therefore expected that multinational corporations lose formal accountability through newly initiated laws and regulations in the international sphere. This means that the US loses structural power in the financial sector to non-state actors. Subsequently, the structural power of financial institutions will force the US government to accept that the only way to handle this crisis: is to enact even more neoliberal standards and ambiguous laws. This hypothesis will be rejected if the US government enacts policies that go against the neoliberal ideology or against the preferences of financial institutions. Thus, the US government has to resist the preferences of SWFs and successfully enact policies that go against their interests.

3.2. Epistemological approach

The ontological foundations of case study designs stem from a debate between positivist thinkers – who believe that knowledge is objective and something we can observe in the open world - and Popper's critique – which argues that knowledge is only fallible by theory and that falsification is the only way to provide knowledge (Adorno & Adey, 1976). This debate has been refuted by an anti-foundationalist approach which states that reality is a relative object and that everything is socially constructed, therefore truth cannot be found but merely be 'interpreted' (Wollin, 1992). Positivist thinking is fundamental to the epistemologies of the old traditional realist schools (associated with the mercantilist approach) – as it provides methodologies for finding a general set of rules and answers to questions. In other words, positivist thinkers argue that there is an observable realistic world where inferences can be drawn. Anti-foundationalist approaches, which mainly consist of critical realists (associated with the new constitutionalist approach) reject these positivist elements by arguing that social activity consists of historical and social context (Dean et al., 2006: 6). Thereby, providing the basis for critical theories that aim to examine underlying works of social interactions and things that cannot be observed 'objectively' in reality. Positivist thinkers compensate for this loss of 'observable reality' with the instrumentalism approach – which contains the idea that theoretical assumptions facilitate predictions rather than that it represents a realistic observable truth (Wight, 2007: 379-381).

Political scientists have frequently used positivist thinking as the basis for research on realist theories (Dunne & Kurki & Smith, 2013: 15). As Gerring (2007: 39) argues: although social scientists are on a quest to find new theories, they also test existing theories by conjectures and refutations. This combines the positivist thinking with Popper's critique and creates the mainstream case study methods within political science. This mainstream positivist approach to human interaction is a behavioralist approach towards doing research (Halperin & Heath, 2012: 27). The behavioralist approach allows political scientists to study and – in Weber's (2002) words - "erklären" the observable behavior of governments and actors (Halperin & Heath, 2012). Weber's positivist "erklären" definition entails an approach in where law-governed explanations for political situations are created that can be inferred to other situations (Weber, 2002). However, in this case study of SWF investments, it is not merely the objective to know why these investments into the US are accepted, but also what causal mechanisms led to this acceptance and whether it can be generalized to other situations. Therefore, the social ontology of the anti-foundational approach is derived and added to this study. This means that this research will aim to understand which causal mechanisms of social interaction resulted in the dependent variable – the acceptance of the investments (Weber, 2002). This is a method of "verstehen" (ibid.). Through "verstehen", the social world can be explored and subsequently understood through interpretable perspectives, beliefs, norms, and meanings (Bevir & Rhodes, 2006). These interpretable social variables are an addition to the behavioristic "erklären" approach and therefore, this method will combine the two epistemological approaches. This way neither a purely interpretative anti-foundational approach – which argues that social research is merely interpretable and not prove able – nor a purely positivist approach – which emphasizes that social activities can be objectively proved - is used. Therefore, this study aims to find and understand the causal mechanism that led to the Y variable through an inductive case study approach (Weber, 2002). When using an inductive approach, the case can be studied holistically instead of atomistically, because this approach starts with specific social observations and moves on towards identifying patterns and regularities which through hypothesis can be drawn into general conclusions or theories (Halperin & Heath, 2012: 29; Blanche et al., 2006: 47). This particular case study focusses on testing the theories and therefore cannot be called purely inductive – as this approach also entails theory creation.

3.3. Case design

This research can be typified as a single-case study on the response of the US government towards SWF investments. This single-case study can be described as a single diachronic case study as it has no spatial variation as only the US is investigated (Gerring, 2007: 27-29). The case does involve temporal variation as it looks at developments regarding the decision-making process of the US government from US protectionist history towards the enactment of the OECD guidelines (ibid.: 27-29). The decision on these investments is crucial because this is a special case in history as it constitutes a change in US policy towards foreign investment (ibid.). This case is special because the US has – historically – prevented equivalent investments into their economy. Therefore, scrutinizing this case could cast doubt on either the rationale behind previous decisions by the US government or this decision. Moreover, this case is a crucial case because the US represents the most powerful state in the world at that moment in time (Drezner, 2008b).

Testing potential crucial breaking points in history – like the one investigated in this case – must follow extensive and rigorous theory formulation (Odell, 2001: 163). To find possible improvements for already existing theories, first, a thorough description of the theories has to be provided (Eckstein, 1975: 103). Furthermore, particular pieces applying to this case should be highlighted in the theoretical chapter to gain the right focus. However, by doing this, problems occur with cherry picking of pieces of the theory that explain the case. Furthermore, a theory could be written towards the case because it is preferred by the writer of this thesis at forehand (Odell, 2001: 164). Therefore, to prevent these problems - and to install more discipline – a very convincing and powerful alternative theory should be included (ibid.). By answering the research question in y-centered research design the theories will not merely be tested upon their relative predictability of this case but also on their relative predictability of governmental decision-making as a whole. This will lead to general conclusions about the applicability of these theories in modern-day situations (ibid.). Moreover, this investigation could lead to suggestions to improve these theories based on this case (ibid.).

3.4. Sources and method of inquiry

As this study consist of a single case - the US response towards SWF investments - the central mode of inference consists of a within-case analysis via process tracing (Mahoney & Goertz, 2012: 89; Beach & Pedersen, 2019). This process-tracing approach helps with "verstehen" and tries to diagnose the causal mechanism of the X towards the Y variable through two competing theories (George & Bennett, 2005). In academic terms, process-tracing opens up the ‘black box’ of the causal mechanism by focusing on pathways and combinations of causes that lead to the policy outcome of the US government (Bennett, 2008; Beach & Pedersen, 2019). Therefore, the above-stated hypotheses will be examined through the method of process tracing using a detailed case description with phases of policy creation in the empirical chapter. This helps in confronting spuriousness problems in case studies - when a researcher might find a correlation that has nothing to do with the real causal mechanism, also known as a type 1 error (ibid.). By describing the case in detail, different probable causes can be identified and subsequently tested for the direction of the mechanisms (Bennett, 2010: 210). This also tackles the main critique on process-tracing – which constitutes of ‘infinite regress’ – which entails that it is possible to add infinite variables on a small case to explain every case (ibid.). This problem is solved because in this research the variables are retrieved from theories and therefore their “probative value” is already determined (ibid.). Thus, there is a limited choice of variables due to the theoretical background.

Evidence to substantiate the process-tracing method on the US case comes from an analysis of a variety of sources. These sources entail key decision-maker speeches, policy notes, legislations, domestic debates in the Congress and House of Representatives, think tank reports, reports from governmental organizations, newspaper articles, and academic research. To optimally test the causal mechanism, this research focusses on collecting as much primary source material as possible. However, a big amount of data will come from secondary sources as the inner workings of governments and documents thereabout are often not openly available. A way to work around this problem is to investigate leaked governmental dossiers and communications from Wikileaks. These documents were not meant to be made public, and therefore the actors and their statements are described naturally in those documents. This increases the validity of the document (Michael, 2015). However, it is not possible to authenticate the messages from WikiLeaks, as the messages are illegally obtained. As a reference, the author of this thesis acknowledges that the WikiLeaks articles that are used in this thesis might represent the truth as they are written in the same structure as diplomatic records the author has seen in person when he worked at the embassy of the Netherlands in Riyadh. Ethical problems are dismissed as the documents are already out there and using them will not change the outcome of the leakages (ibid.). As secondary sources have the advantage of being analytical on the event itself, numerous news articles, commentary articles in quality papers, and academic papers on this case are scrutinized. After combining these sources, patterns and workings of the causal process can be systematically assessed (Beach & Pedersen, 2019: 75).

3.5. Limitations

The abovementioned research design contains weaknesses and limitations, mainly due to time and resources problems. The limitations can be divided into three issues: case study method issues, issues regarding sources and governmental black-box issues, and documentational completeness issues. Firstly, the limitations of the use of a case study stem from the freeform of this research design (Maoz, 2002: 164-165). It is not as structured as quantitative research, leading to potential problems of non-structured thinking. This is reduced by using theories as a structural ground for the research. However, the interpretation of the writer is still an important caveat in this research. This in turn adds to the problem of oversimplifying theories and outcomes in research to explain certain phenomena more easily. Moreover, certain pieces of the theories could be neglected even though they influence the case or the theory itself (Hodkinson & Hodkinson, 2001). Furthermore, problems of representativeness occur due to small N research (Gerring, 2007: 43). The higher internal validity compensates for the small generalizability caused by the small N research and thorough investigation of one case (Ibid.; Stake, 2005).

There are also limitations regarding the sources. First and foremost, regarding inner workings of governments: full information on their motives and thoughts is not available. It is furthermore not possible to reconstruct the FPE's policy discussions nor the context in which these discussions were held (Pfiffner, 2005: 222). Therefore, the first problem regarding sources occurs with getting data on how the FPE thinks. Second, it is not possible to get in touch with decision-makers on the ground because of limited resources at the researcher's disposal. Therefore, interviews are not possible. Third, sources – such as oval office meetings – that could indicate the attitude of the President and his staff towards the subject are classified and therefore not available for this research. These source access problems are partially solved by leaked document databases such as Wikileaks. However, the WikiLeaks source also presents limitations. Whereas it is known that documents on WikiLeaks are solid, it still does not paint a full picture on the case, as there might be information that refutes or complements the Wikileaks documents in 'unreachable' documents (Michael, 2015).

Finally, there are problems regarding the completeness of the documents that are used. There might be information that is not reachable for this research because of their 'classified denotation'. Therefore, it is not known whether the data that is presented here from senate hearings, committee discussions, house discussions, etc. can be seen as the exhaustible truth in this case. Furthermore, there might be indicative data that is overlooked or subject to selection bias by the researcher who chooses the documents that provide the quickest answer (Heath & Halperin 2012: 330-331). Another possibility is that documents were overlooked as search engines do not give a full list of government documents on the subject that is searched for.

4. Case analysis

This chapter will describe the events concerning SWF investments in US financial institutions. To assess the investments of SWFs into the US financial sector in a structured manner, the case will be described in a manner similar to the policy process model outlined by Public Administration scholar Birkland (2019: 26). The first phase consists of an arising problem for the US government, the second phase describes governmental preparations and discussions to handle this problem, and the third phase outlines how the US responds to this problem.

4.1. First Phase: Problem arises

4.1.1. Legislative history of US foreign investment

To get a full picture of the US decision towards SWF investments, a historical account of US regulations and policies towards foreign investments is outlined in this phase. This historical approach will show cultural characteristics and explain the developments that led towards the Foreign Investment and National Security Act of 2007 (FINSA) – which had a significant regulatory effect on investments by SWFs (Rose, 2015).

From the Louisiana Purchase onwards, the US has welcomed foreign investment and thrived under the loans that foreign nations facilitated (Travalini, 2009: 782). However, the US also came to understand that foreign ownership potentially hurts national security. Therefore, over time, the US has developed certain strategies to stop potentially harmful investments into its economy (ibid.: 783). In the 1970 foreign investments increased due to globalization and the devaluation of the Dollar, which led to increased legislation (ibid.). Initially, the US Congress enacted the Foreign Investment Study Act of 1974 (Study Act) to review legislative power to monitor foreign investments – which was found to be shortcoming (ibid.). In response to the Study Act report, President Ford created the Committee on Foreign Investment in the United States (CFIUS) (ibid.). The CFIUS' duty is to monitor the impact of foreign investment and fulfill a coordinating role in US policy formation regarding this subject (ibid.). At first CFIUS was seen as toothless, however its authority changed due to the Exon-Florio Act of 1988 (ibid.: 784). The Exon-Florio act was a response on the attempted acquisition of a US semiconductor company by a Japanese company, which was seen as a threat to national security by the US government (ibid.). This act allowed the US government to monitor the effects of foreign investments on national security: it determined that CFIUS will report results of their investigation and impact analysis to the President, including choices to take no action, stop the transaction, or order divestiture (ibid.). A CFIUS investigation can be started either voluntarily by companies that are part of the investments or by a member of the CFIUS (ibid.). After the 9/11 terrorist attacks national security standards increased, including on foreign investments (ibid.:787). Furthermore, citizen opposition towards foreign investments – especially those from SWFs – increased according to multiple polls (Pew Research Center, 2006; The Wall Street Journal, 2008).

The requirements for approval of foreign investments and acquisitions gained even more attention due to multiple cases of foreign investment into the US (ibid.). Firstly, in 2005, the acquisition of a US oil and gas company by a Chinese company was called off due to a CFIUS review that subsequently led to political oppression from the US politicians towards the Chinese government (ibid.: 789). Secondly, the acquisition by a United Arab Emirates (UAE) company of a company that ran operations in six US ports was stopped, even though it successfully passed a CFIUS review, by a House vote in 2006 (ibid.). These cases resulted in concerns over the role and powers of the CFIUS. Because not the CFIUS' review process, but the political actions by the US government were the reason the investments were halted. Thirdly, in 2006 a Venezuelan company tried to acquire a US voting equipment company, which led to CFIUS review that was not completed due to the early withdrawal of the Venezuelan company from the acquisition (ibid.: 791). As a response towards these cases, President Bush started the 'Invest in America Initiative' to express continued support towards foreign direct investment (ibid.). It was a direct commitment to the principles of free and fair trade (ibid.). However, on the background, the Congress was busy with increasing CFIUS powers due to the UAE port case where the CFIUS review did not create the results the Congress hoped for. Subsequently, both the 'National Security Foreign Investment Reform and Strengthened Transparency Act of 2007' and the 'Foreign Investment and National Security Act of 2007 (FINSA)' were enacted (ibid.). These two legislations broadened the CFIUS's power, obligated CFIUS to inform the Congress on their investigations on companies, and increased the required scrutiny applied to the review of investments (ibid.: 794). However, an important loophole remained: CFIUS only reviewed cases in which the acquisition entails a stake of 10% or more (Rose, 2014: 18).

4.1.2. Subprime mortgage crisis

In the beginning of 2007, real economic indicators showed the occurrence of a housing bubble in the US that could threaten the, at that time, highly indebted US financial institutions (Tancer, 2007; Demyanyk & van Hemert, 2011). The housing bubble, however, covered up the real problem in US mortgage markets: 'the occurrence of toxic loans' (Demyanyk & van Hemert, 2011). Very risky loans were provided by US financial institutions to borrowers that had very low credit scores. This is also known as loans with deteriorating quality. Banks hoped that people could repay the loans with the profits retrieved from the increased housing prices. Even though, in the meantime, banks sold these mortgages as securities to other naïve investors to get rid of the credit risk. The first problems appeared when the people with low credit scores could not pay back their mortgage. On top of that, housing prices started to fall, because the houses of those people were directly put on the market by the banks (Holt, 2009). This increased the risk of moderate risk house owners to fail on their loans, due to lower returns on their house (ibid.). Especially because it is possible in the US to deliver the home keys back to the bank to be exonerated of the mortgage, causing more and more houses to be listed on the market and house prices to decline. This eventually resulted in a high delinquency rate on mortgages by US consumers in 2007, causing banks to accept lower returns on foreclosed homes and liquidity problems to rise (ibid.). When even low risk consumers failed on their loans, the US financial institutions were extremely indebted and in need for liquidity (Bolton et al. 2012; Gomes, 2008). US banks were very desperate, as almost no investors were willing to provide capital due to extreme risks of US bank failings (Hatton & Pistor 2011: 10). The problems got worse and the 'toxic loans' were slowly demolishing the US banks. These banks, however, were eventually considered to be 'too big to fail' and received an astonishing $700 billion bailout from the US government – in this way the US government nationalized banks and bought the 'toxic assets' (US department of the Treasury, 2008a; The New York Times, 2008). The bailout eventually created a stable environment for the US financial institutions and prevented them from failing, at the price of transferring ownership to the US government (Culpepper & Reinke, 2014). Moreover, the bailout was at the price of moral hazard as bankers were saved without being held accountable for their mistakes.

4.1.3. Investments of SWFs

Approximately a year before the government bailout, as the banks reported heavy losses, SWFs provided the first round of relief (Helleiner and Lundblad, 2008). These investments entailed acquisitions from Middle Eastern and Asian SWFs towards Citigroup, Carlyle Group, Blackstone, Morgan Stanley, Merrill Lynch and other US financial institutions (Pistor, 554: 554). The investments demanded extra scrutiny from US regulators, as the department of Homeland security had marked the financial sector of the US as 'critical infrastructure/key resource' (Hasnat, 2015). Bank failings were – temporarily - avoided due to SWF investments and with it the problem of US citizens losing jobs and the crisis spreading towards other sectors in the US economy. Meanwhile, the Bush administration worried about the increased leverage of foreign governments towards the US (The New York Times, 2007). Foreign ownership of US companies raised the possibility of foreign nations disrupting stock prices, hijacking stakeholder meetings and pressuring for relocation of US jobs (Shabbir, 2009). In response, the US government applied pressure on the International Monetary Fund (IMF) to review 'best practices' for SWFs (ibid.). The US government, in the meantime, openly stated that it supported and welcomed all kinds of investments into the US economy, stating that they: are 'fine' with the SWF investments (ibid.; The Telegraph, 2007). However, behind the scenes, the US government was busy with diplomatic endeavors to ensure that SWFs remained non-activist shareholders (Wikileaks, 2007; Wikileaks, 2008e; Wikileaks, 2009b).

Interestingly, all investments of SWFs acquired a stake of 10% or less in the targeted company – which is, according to a Chinese diplomat, strategically chosen because of the threshold of the CFIUS review process as explained above (ibid.; Wikileaks 2009a). Importantly, Wikileaks reports of US meetings with Chinese diplomats suggest that the Chinese tried to acquire a 49% stake in Morgan Stanley in 2008. However, they were unsuccessful due to – in their own words – intervention from US New York Federal Reserve Bank President Tim Geithner (Wikileaks, 2008a). In this time other nations, such as Qatar, Singapore, and Kuwait also reached out to the US via diplomatic channels to offer money from their SWFs (Wikileaks, 2008b; Wikileaks, 2008c; Wikileaks, 2008d). These SWF investments, in the period of May 2007 until mid 2008, were not stopped. This presented US policy makers with a difficult situation: the thin line between the foreign state and their SWF sparked lengthy discussion in the media and political establishment of the US (Das, 2009).

4.1.4. Analysis first phase

Neoclassical Mercantilism

The neoclassical mercantilist theory hypothesizes that the government has an active role in channeling the investments to benefit the US economy most, is strongly confirmed by analyzing phase one. By setting up a legislative network, the US has given itself the power to act and shape global economic capital flows in their advantage. The US is clearly actively channeling investments as it, even without the right legislation in place, is accepting or denying investments according to their contribution to the US' welfare. The main focus of the government remains the financial sector in New York, which is seen as a critical industry to US national security. Moreover, the US will defend that financial sector due to its highly industrialized nature, as it is, together with London, the center of the global financial world in 2007 (Long finance, 2007). By accepting the investments, the banks finally received their much-needed capital and could remain their powerful position in the world, even during a financial crisis. Interestingly, the US reportedly stopped an acquisition of 49% of a US bank, showing that they accept smaller investments (up to 10% of the stakes), but not big ones (Wikileaks, 2008a). The US government remains the autonomous actor for accepting investments and plays a huge role in the perseverance of its vital economic sector and public well-being with the bailout.

This decision to accept the investments depends – aside from the cost benefit analysis– on how the FPE perceives the problem created by the investments. The FPE acts in a high clarity and high permissiveness of strategic environments system where the investments come in through proper channels and with a full legislative system to potentially block them when they enhance acquisitions of higher than 10%. Therefore, the FPE's decision is influenced by the strategic culture of the US, domestic institutions, and state-society relations (see table 1 in Chapter two).

First, the US strategic culture can be typified as semi resilient against foreign investments in the US economy. Citizen polls show that people dislike the idea of foreign ownership – especially SWF ownership – of US companies. The US has also stopped investment into strategic sectors over the past decades. However, as these SWF investments mainly carry stakes of less than 10% the effect on real ownership of US companies by foreign nations is not that high. Therefore, constraining effects of strategic culture on the FPE are limited. Second, state-society relations in the US were, due to the special circumstances and the sheer size of the US market, in favor of the FPE. Third, the FPE was not stopped by societal or economical groups such as banks and unions because it was trying to save those groups by preventing inevitable failing of US Banks. Moreover, due to the CFIUS process, the FPE had no obstruction from domestic institutions as it could unilaterally start a review process on every investment by the SWFs. Therefore, the US FPE had some negative effect of strategic culture, but ample prospects to act quickly with no obstruction to intervene in these investments. As a result, by not intervening, the FPE had in mind that these investments are beneficial to the US and could act quite unconstrained in order to preserve a vital and leading US financial sector.

Critical political economy perspective

The 'constitutionalizing structural power' hypothesis, that the US is forced by international capital markets to accept the investments of SWFs, is partly confirmed and partly disconfirmed by analyzing phase one. SWFs in this case represent newly found state-led institutions that influence the financialization of the world's economy. Income from sources such as trade surpluses and natural resources is accumulated by the government and consolidated in a sovereign wealth fund to gain new ways of financial profit accumulation.

The global markets can be typified as highly liberalized at the time of the investments and capital was (and still is) freely flowing around the globe. Liberalization of the global economy made it possible for a SWF to act as a 'normal investor' but with the incentives of the host country potentially deeply embedded within its strategy. This is revealed when assessing the investments of SWFs into a sector of viable national interest to the US with very little interference from their government. Reportedly, the US merely stopped one investment from the Chinese SWF. This would mean that the US did have some say in the acceptance of the investments and was not forced by the liberalized international system. For years, the US tried to find the right policy to deal with foreign investments. Finally, a policy including a 10% loophole was enacted because of the need to adhere to neoliberal 'free market' ideology, as the US wanted to stay open to foreign investment. Because of the 10% loophole, the US had to accept investments from other nations without starting a CFIUS review immediately. Indicating, that they were either uninterested in losing 10% stakes in US companies to foreign nations, or they were leveraged by the financial sector to remain open to investments.

This attitude of the US government towards the US financial institutions seems to be a direct result of the effects of the subprime mortgage crisis. The financial sector has the structural power to set the priorities of the US government: prevent US bank failing by allowing foreign stakeholdership. As the financial sector is marked as critical for US economic interests, this is a threat to national security. US government officials clearly see this threat, as they approach other nations diplomatically in order to ensure that the investments are 'in good faith' and do not harm US interests. This is a damage control tactic of a country that feels vulnerable to the effects of the investments it could not stop. This resentment towards the investments is also visible in their reaction towards the subprime mortgage crisis. As the US cannot stop the investments, it has to comply with the neoliberal standard of free-flowing capital which is forced upon the US by the neoliberalized world order system. Therefore, the US government's only policy that could intervene in the loss of authority in the financial sector was to buy its influence in the financial institutions - in which SWFs bought stakes - by buying stakes on their own. Thus, by preventing a devastating loss to the US economy, the US government complies with the rules set by financial institutions that caused these problems in the first place. All in all, the hypothesis is partly confirmed and partly disconfirmed because the US was able to subdue the structural power of the financial sector once by stopping an investment of the Chinese SWF into a US financial institution.

4.2. Second phase: Governmental discussions

4.2.1. Domestic political discussion

The lack of transparency, potential political grounds of the investments, and the magnitude of the investments – topped by an unfolding crisis - sparked concerns among representatives and government officials (Weiss, 2009). An official report by the Department of the Treasury in June 2007 concerning these threats spurred discussions in the US Congress (U.S. department of the Treasury, 2007a). In the meantime, more concerns were voiced by the Chairman of the Securities and Exchange commission, Cristopher Cox, through a speech at the Harvard University in October 24, 2007 (Das, 2009: 30). As a political reaction, several congressional hearings were planned in the Senate and House committees from November 2007 until June 2008. Congressional hearings are an important step towards government action, as it is the principal formal method for US congressional committees to collect and analyze information in the early stages of policy creation (Galloway, 1959: 25-26). In addition, US Senator Shelby requested a formal study from the Government Accountability Office (GAO) regarding the legal possibilities to monitor SWF investments. The actions from Congressional members and governments officials on this issue indicated the political concerns regarding these investments.

In the first congressional hearing senators expressed their concerns about SWF activity in the US (U.S. Government Publishing Office, 2007). Senator Evan Bayh summarized these concerns in his opening statement as follows:

> *"The lack of transparency that characterizes many sovereign wealth funds undermines the theory of efficient markets at the heart of our economic system. In addition, unlike private investors and their representatives--pension funds and mutual funds, for example--government-owned entities may have interests other than and that occasionally will take precedence over profit maximization." (Ibid.).*

In the remainder of the first congressional hearing economic and financial experts and politicians were questioned in order to capture the magnitude of the problem and the possible regulation prospects. Furthermore, the potential threats to the US economy were analyzed and concretized. In response to this hearing, a lot of media attention was generated that forced public officials to speak out on the subject (Das, 2009: 30). The Department of the Treasury, in December 2007, officially raised two major concerns regarding SWF investments (ibid.). These are: 1. On the investment side, the investments of SWFs could spur protectionism which potentially damages the global economy, 2. Investments of SWFs could raise legitimate national security concerns (U.S. Department of the Treasury, 2007b). In addition, US Treasury deputy secretary Robert Kimmitt argued that SWFs could have political intentions and that the US has to make sure that SWFs intentions are based solely on economic grounds (New York Times, 2007). This indicates that the US government worried about the national security issues and the development of protectionist sentiments in other countries. Somewhat later, opposition politicians also started calling for protective measures against SWF investments by the name of Hillary Clinton as she was preparing to become a presidential candidate (the Economist, 2008; CNN Politics, 2007).

In the following congressional hearings on February 14, 2008 and March 5, 2008 the effect of SWF investments on the US (economy) was further scrutinized (Govinfo, 2008; U.S. Senate, 2008). In the opening statement of the Congressional hearings, US Senator Charles E. Schumer (New York) identified that these meetings will function to concretize the problem of SWF investments (ibid.). Furthermore, during these meetings the first indications of a potential outcome were formulated. In the hearing, US senators acknowledged that the problems concerning SWF investments could be mitigated by 'best practices' – which were to be formulated by the IMF instead of the Federal government (U.S. Senate, 2008: 1-3). Furthermore, the senators acknowledged the current financial crisis that was unfolding and saw that US financial institutions could not raise capital from normal investors. This absence of capital investments could lead to a dramatic shrink in US financial institutions and the loss of thousands of jobs (ibid.). Senator Schumer summed this up in the following statement:

> "*there may only be two options, neither of which is very attractive: We can allow a dramatic contraction of our economy, or we can allow foreign investment, in a measured way, to stave off further job loss and keep the economy humming*." (U.S. Senate, 2008: 2).

The invited experts – by name of Dr. Paul - backed the economic argument that the financial situation of US banks would have been far worse if SWFs had been halted from investing (Govinfo, 2008). Furthermore, experts argued that when the US enacts extra protective measures, it would discourage further foreign investments into their economy and could start a protectionist domino-effect among other countries (Govinfo, 2008). Therefore, SWFs should be pushed towards mutually agreed self-restraining ‘best practices’ – formulated by the IMF – to stop politically motivated investments (ibid.). To sum up the problems of SWF investments, senators and experts cooperatively came up with four concerns that should be addressed: 1. The lack of transparency of SWFs, 2. The potential use of SWFs to invest politically or strategically 3. The possible increase of protective measures worldwide, and 4. The potential loss of US tax gains (Govinfo, 2008; U.S. Senate, 2008).

After formulating and concretizing the problems of SWF investments, the rhetoric of the US government against SWFs sharpened (Cohen, 2009: 720). The director of US National Intelligence declared openly that:

> *“Concerns about the financial capabilities of Russia, China, and OPEC countries and the potential use of their market access to exert financial leverage to achieve political ends represents a major national security issue” (Ibid.: 720).*

In the following months, three more congressional hearings were held on March 24, May 21 and June 11 to formulate the right policy objectives to combat investments from SWFs (US Senate foreign relations committee, 2008; U.S. Printing office, 2008a; U.S. Printing Office, 2008b). The concerns of the US National Intelligence Director were backed in these hearings by several senators such as Joe Biden, then Chair of Senate Foreign Relations committee:

> “*I think there is a subtle impact on our conduct of foreign policy when investments in the United States affect the powerful groups in which the investments are made, for them to determine and put impact on the Congress and the President ought curtail and/or enhance a certain foreign policy action*.” (US Senate foreign relations committee, 2008: 23).

The calls for regulations of SWFs intensified as other important senators such as Bayh (Indiana) and Schumer (New York) resonated the call from Biden (US Senate foreign relations committee, 2008; U.S. Printing office, 2008a; U.S. Printing Office, 2008b). Clearly, domestic or international action by the US government was now inevitable. Interestingly, during that period, President Bush did not speak out on the concerns regarding SWFs and showed no sign of concern regarding these investments. When the President actually did openly talk about SWFs, he stressed that the US will always welcome foreign investments, deemphasizing the national security threats (Reuters, 2008; White House archives, 2008). This indicated a relaxed attitude towards the investments from the government; the President even labelled the investments of SWFs in the US financial institutions as 'fine' (The Telegraph, 2007).

4.2.2. International efforts US government

As early as October 2007, after the first investments of SWFs reached US financial institutions, the G7 agreed that the IMF, World Bank, and OECD should explore 'best practices' and guidelines for SWFs in areas such as institutional structure, risk management, transparency, and accountability (G8, 2007). The US seemed to be the main protagonist of these 'best practices' and guidelines as these policies are a logical step from the advice of the Treasury and experts during congressional hearings (U.S. Government Publishing Office, 2007). Furthermore, the Secretary of the Treasury, Henry Paulson, stated that the US reached out to other countries to develop consensus on pushing the IMF, World Bank and OECD towards 'best practices' and guidelines:

> *"Our fundamental premise is that open financial markets and investment policies are beneficial to our well-being and SWFs (...). That said, the growing importance of SWFs merits cautious, well-considered public policy responses. (…) Last night's G7 outreach dinner with countries that have sovereign wealth funds was an important initial step in the process of developing consensus and collaboration around this important issue." (IMF, 2007).*

Moreover, in an internal letter of the US Congressional Research Service (2008) to Congress, it becomes clear that the Bush administration had been pushing IMF representatives to develop a system of 'best practices' for SWFs. The leading role of the US is also highlighted when assessing Treasury documents about meetings between 25 SWF countries and the IMF in Washington (U.S. Department of the Treasury, 2008b). In this document, plans were suggested to create 'guidelines' for recipient countries of SWF investments in return for self-restraining SWF 'best practices' (ibid.). This concession was necessary, according to SWFs, because of the rise in investment protectionism around the globe and the need to maintain open markets (ibid.). As early as June 2007, Under Secretary for International Affairs Clay Lowery suggested that national authorities around the globe should maintain domestic legal mechanisms to review investments, in a manner that preserved national security without creating unnecessary and counterproductive financial barriers (U.S. department of the Treasury, 2007c). Therefore, the US urged the OECD to come up with guidelines to stop protectionist measures of SWF investment recipient countries (ibid.). These guidelines for recipient countries, according to Lowery, should:

> *"strengthen open and transparent investment regimes and fight tendencies that restrict them" (ibid.).*

Interestingly, in a diplomatic meeting, Kimmitt - then Deputy Secretary of the Treasury – noted towards President Barroso of the European Commission (EC), that in order to not undermine SWF abilities to operate according to market principles, both actors (US and EU) should be careful to seek "appropriate levels of transparency" within 'best practices' for SWFs (Wikileaks, 2007b). The Bush administration sticks to its message and keeps advocating liberalization on the global scale through official channels:

> "*My Administration is committed to ensuring that the United States continues to be the most attractive place in the world to invest" (Congressional research service, 2013).*

In the meantime, the US quite actively promoted the ideas of guidelines for recipient countries as well as 'best practices' for SWFs through their diplomatic channels (Wikileaks, 2007c;d;e;f; Wikileaks, 2008f;g;h;i;j;k;l;m;n). These diplomatic efforts were mainly focused on European, Gulf, and Eastern Asian countries and were led by the Treasury's Deputy Secretary Kimmitt (ibid.). Some meetings were also held with Russia and China (ibid.). In these conversations the US encouraged these countries to either adopt, help promote or help improve the 'best practices' framework proposed by the IMF (ibid.). Some SWF home countries explicitly mentioned protectionist sentiments. Their willingness to help promote 'best practices' for SWFs was conditioned by US international action combatting those protectionist sentiments (ibid.). In the following months, the US actively searched for allies to promote 'best practices' for SWFs and guidelines for recipient countries. As these diplomatic efforts were fulfilled by high government officials, this approach can clearly be seen as an active response from the US government towards the investments of SWFs.

4.2.3. Analysis second phase

Neoclassical Mercantilism

The hypothesis of the neoclassical mercantilist approach is partly confirmed and partly disconfirmed. As the discussion on the SWF investments unfolds, it becomes clear that the government has to deal with an extraordinary situation. The US knows – as a superpower - that it can establish the economic and regulatory rules of the game for smaller states and other economic actors. The US also knows that the economy requires SWFs investments to soften the impact of the crisis for US financial institutions and American citizens. The protection of this high-level industry is very important for the economic welfare of the state. To find the best policy output the FPE does a cost-benefit analysis.

This cost-benefit analysis is subsequently determined through the FPE's perception of state-society relations and domestic institutions. In this phase, we see that senators from both parties, bureaucrats from different ministries, and experts from outside politics agree with each other that action against these investments from SWFs is compulsory – being a national security issue -. Therefore, the FPE can formulate its own response and will not be constrained in its decision-making by state-society relations nor domestic institutions.

Even without consensus on the policy response, it is clear that the FPE - in its cost-benefit analysis – saw the need for the acceptance of investments to protect financial institutions. Moreover, the FPE found a diplomatic way to tackle the problem of potential politically motivated investments. By acting internationally, the FPE made sure that the administration's agenda – promoting and ensuring free trade around the globe – was safeguarded. Therefore, in this case, the US government is clearly the most important actor which is not influenced by non-state actors. It is actively lobbying for their agenda worldwide, protecting their technological advanced industries against failings, and ensuring the idea of open and free trade which – according to the government – is in benefit of the US. However, the US cannot force other smaller states to adhere to their own suggested 'best practices' for SWFs, without accepting their wish to also create guidelines for SWF investment recipient countries. Furthermore, the US agrees with the EU that they will not search for the ‘harshest’ ‘best practices’ for SWFs. This clearly indicates that the power of the US to coerce other actors – as suggested by the neoclassical mercantilist theory - is partly confirmed and partly disconfirmed as, in reality, the US gets what it wants but also needs to concede other policy objectives.

Critical political economy perspective

The hypothesis of the ‘constitutionalizing structural power’ approach is strongly confirmed. The investments in the US financial sector rang bells all over the country and sparked intensive debates in the Congress about national security implications. During these debates, however, the side effects of protectionist measures (stopping the investments) were mainly seen as damaging to the economy by making it harder for US companies to attract investments in the future. Also, protective measures potentially hurt US companies trading internationally, especially when other countries follow suit with protective barriers to free trade. These considerations of US congressional members and experts are based on the idea that free trade and neoliberalized rules all over the world are ‘holy’ and should not be tempered with. In their minds it is the only way to achieve economic prosperity. Oppositional members of Congress, interestingly, reason from neoliberal standards too as they agree with ‘best practices’ - which do not enforce anything - to safeguard the US economy. This indicates the entrenchment of neoliberal thought. These ‘best practices’ are another form of soft, self-regulatory, and flexible standards in which SWFs can freely move their capital - on the condition that they ‘vow’ that these investments are made on economic grounds -. Moreover, as the US is promoting these principles on an international scale, power to change these principles once enacted is forfeited, as those are formalized in the international realm. This leaves structural power at the side of financial institutions, as they do not have to adhere to national governments but to their own designed terms. The US is pushing for this policy objective because of their neoliberal ideology and thereby loses regulatory power to international regimes. Furthermore, it adheres to the standard economic strategy - perpetuated by SWFs - of deregulation and private company freedom.

This loss of power by the US was possible because the SWFs made themselves important by providing much needed liquidity to failing US banks when no one else would. In the end that gave them leverage over the US government, as denying them now potentially means that they refuse to invest in future US crises. This leverage resulted in discussions about rules, in favor of

SWFs – a concession by the US. Moreover, this leverage and structural power is clearly visible through the diplomatic meeting of the US with the EU. In this meeting, the US accommodates to the preferences of financial institutions by urging the EU to promote less strict 'best practices' for SWF to not anger SWFs. As credit has become important for the perseverance of financial institutions, the US is bound to accept concessions (OECD guidelines for recipient countries) to be guaranteed of capital injections from SWFs by the next financial downfall. Therefore, the US is structurally forced by the financial sector to think in neoliberal policy solutions to this problem and to internationally proceed with solutions that benefit the SWFs.

4.3. Third phase: Policy Response

4.3.1. Domestic policy output

In May 2008 the Department of the Treasury reported that policy objectives towards SWFs were drafted by the US political leadership, in cooperation with the Department of the Treasury (U.S. Department of the Treasury, 2008b). These policy objectives entailed 'best practices' for SWF and guidelines for recipient countries of SWF investments. In Paulson's words, these voluntary 'best practices' and guidelines serve as a strong incentive among SWFs and recipient countries to hold themselves to high standards. Both the IMF and OECD supported these investment regimes for countries either owning or receiving SWF (investments) (ibid.). Policy principles for SWFs and recipient countries were later on formalized as an official US policy objective by a statement by the Department of the Treasury on the 20th of March 2008 (U.S. department of the Treasury, 2008c):

"Policy principles for SWFs include:

> *1. SWF investment decisions should be based solely on commercial grounds, rather than to advance, directly or indirectly, the geopolitical goals of the controlling government. SWFs should make this statement formally as part of their basic investment management policies.*
>
> *2. Greater information disclosure by SWFs, in areas such as purpose, investment objectives, institutional arrangements, and financial information – particularly asset allocation, benchmarks, and rates of return over appropriate historical periods – can help reduce uncertainty in financial markets and build trust in recipient countries.*
>
> *3. SWFs should have in place strong governance structures, internal controls, and operational and risk management systems.*
>
> *4. SWFs and the private sector should compete fairly.*
>
> *5. SWFs should respect host-country rules by complying with all applicable regulatory and disclosure requirements of the countries in which they invest.*

Policy principles for countries receiving SWF investment include:

1. Countries receiving SWF investment should not erect protectionist barriers to portfolio or foreign direct investment.

2. Recipient countries should ensure predictable investment frameworks. Inward investment rules should be publicly available, clearly articulated, predictable, and supported by strong and consistent rule of law.

3. Recipient countries should not discriminate among investors. Inward investment policies should treat like-situated investors equally.

4. Recipient countries should respect investor decisions by being as unintrusive as possible, rather than seeking to direct SWF investment. Any restrictions imposed on investments for national security reasons should be proportional to genuine national security risks raised by the transaction.".

(U.S. Department of the Treasury, 2008b: 1-2).

This report was published a couple of months before the enactment of the Santiago principles. It provided the ideological and legal basis for the principles. Therefore, it is a good sample of US government policy objectives. It summarized the final policy output, stating that the US remains open for investment and acts on a multilateral account to ensure that SWF investments are economically, not politically, motivated.

In the meantime, the investments of SWFs into US financial institutions found no official government policy response. The US government did not act and therefore accepted the investments coming into the country. This is in line with the policy principles for countries receiving SWF investments described above and could be seen as a precedent for other countries to not move into protectionist measures when encountering SWF investments (U.S. department of the Treasury, 2007c). Furthermore, as government officials felt the heat of the financial crisis and the liquidity problems of the banks, accepting the investments of SWFs seemed like an easy way out (U.S. Senate, 2008: 2). An important note here is that allegedly the US had stopped one acquisition of a 49% stake in Morgan Stanley by the CIC (Chinese SWF), even though it did not stop any other investments (Wikileaks, 2008a; Pistor, 554: 554). In this way, as Schumer (US Senator) noted, the US government could accept foreign meddling in a measured way (by accepting acquisitions below 10%), to prevent US financial institutions to fall and thereby prevent job losses in the US economy (U.S. Senate, 2008: 2). The assumption that the US sees a <10% stake as a measured way could be retrieved from the fact that the US CFIUS review process is triggered by acquisitions above 10% (Rose, 2014: 18). When deliberately setting the barrier at that height US lawmakers probably acknowledged investments under that barrier as small, less harmful acquisitions. Therefore, in line with the policy principles the US laid out in their report to Congress, the US did not try to stop the investments from SWFs in the US economy.

4.3.2. International policy output

On the international level, US government officials kept seeking aid from SWFs countries for their plans to enact a voluntary code of conduct written by the IMF and OECD ((Wikileaks, 2007c;d;e;f; Wikileaks, 2008f;g;h;i;j;k;l;m;n). In March 2008 a big step towards a common set of principles was taken by the US when it agreed with Abu Dhabi and Singapore on clauses requiring the investment of SWF's to be solely based on commercial grounds and other 'best practices' (Helleiner & Lundblad, 2008: 71). In return, the US promised not to discriminate against state owned entities or private entities when assessing investments (ibid.). The agreement was initiated by the US to seek international support from SWF countries in order to increase the chances of multilateral 'best practices' for SWFs (U.S. Department of the Treasury, 2008c). This support-seeking is resonated in a speech by Paulson, then Treasury Secretary, who argued that the principles in the agreement further the efforts for the IMF Santiago Principles for SWFs and the OECD guidelines for recipient countries (ibid.). By allying with these important SWF-side states, the US found the needed allies to implement these principles, although the US and allies have to concede guidelines regarding the acceptation of SWF investments for themselves.

The diplomatic efforts by the US seemed to be successful as in September 2008 a newly formed International Working Group of Sovereign Wealth Funds (IWGSWF) agreed upon voluntary 'best practices' for SWF behavior – also known as the Santiago Principles (See Appendix A for full version of the Santiago principles) (Weiss, 2009; IFSWF, 2008). The principles can be divided in three different categories: 1. a legal framework, objectives, and macroeconomic linkages, 2. An institutional framework and governance, 3. investment policies and risk management frameworks (ibid.). The adherence to the principles is not enforced as the Santiago principles are voluntary and must be ratified by authorities of nation states (ibid.). In reaction to these Santiago Principles, Weiss (2009) notes that:

> *"by committing to financial objectives and guidelines for increased transparency and disclosure of investments, the creation of the Santiago Principles appears to be the beginning of the normalization of SWFs as global institutional investors.". (Weiss, 2009: 15).*

Subsequently in late 2008, the OECD was initiating guidelines for recipient countries of SWF investments (ibid.). In a public briefing with the US council for International Business, OECD's Secretary-General Angel Gurria, state his plans for upcoming guidelines for SWF recipient countries (ibid.). He first congratulated the SWFs for enacting the Santiago Principles and then pointed the attention towards SWF recipient countries (ibid.). He acknowledged that it was essential to think clearly on issues of open markets and the positive effect SWFs have on the global economy (ibid.). He then laid out the guidelines for recipient countries which were made in cooperation with the US government (ibid.). The OECD guidelines for investment policies should be applied to all foreign investors including SWFs and other state-owned enterprises (See appendix B for the guidelines) (OECD Investment division, 2008). These guidelines entail 1. Non-discriminatory rules, 2. progressive liberalization and standstill rules, implying that members should not introduce and gradually eliminate restrictions on capital movements into their countries, and 3. unilateral liberalization; a measure in which the liberalization measures one country takes will not be conditioned on that same country when trading with other OECD members (ibid.: 3). The OECD guidelines and the Santiago Principles both are, according to the CRS report for Congress, a policy response to the concerns around SWFs as stated in phase 2 (Weiss, 2009).

4.3.3. Aftermath

As a response to the Santiago Principles, the non-partisan advisory agency for the Congress – the Congressional Research Service (CRS) – noted that is it not yet clear whether these voluntary codes of conduct will satisfy the restrictive rules that Western governments had hoped for (ibid.). Especially the rules regarding transparency were a contentious issue in the Santiago Principles (ibid.: 15). Even though some Western countries insisted that SWFs should have greater transparency, many of them allowed SWFs to bargain for rules that allow a high degree of secrecy regarding SWF operations in the Santiago principles (ibid.). However, in the end, US officials applaud the Santiago Principles as it is a step forward, towards greater transparency and towards solely economically motivated investments.

Thus, the US finds itself at an ideologically extraordinary uncomfortable place: on the one hand it opposes SWF investments into vital US industries, but on the other hand it wants to promote free flowing commercial investments on a world scale (Beeson, 2009: 735). Beeson (2009: 735) notes that the US response to the investments of SWFs is actually quite muted, considering the explosive growth of SWFs and their power (ibid.). Especially when considering that the Santiago principles are not enforceable on SWFs and do not bring any legal protection against foreign meddling into US institutions (Etlinger, 2010). However, scholars from the University of Chicago, Epstein and Rose (2009) argue that the policy response by the US is enough and that the US should actually welcome SWF investments, as they are 'self-regulated' due to natural incentives. Natural incentives being the preference of SWFs to avoid being perceived as strategic/political investors otherwise other countries will not accept their investments. Therefore, no additional legislation should be imposed, and American policymakers should focus on domestic fiscal policies that helped US growth before (ibid.). This idea of acceptance and openness to SWFs is backed by Behrendt (2008: 19), who acknowledges that the West has to accept the emergence of new rich investors in the name of Arab and Asian SWFs. This implies that bargaining power has shifted away from the US: the West needs the investments for the wellbeing of their financial institutions and must accept that they are not the only dominant player anymore in global financial markets (ibid.: 19). Moreover, Lovery (2012) notes that the Santiago Principles and OECD guidelines have indeed sparked transparency among SWFs and their operations. The transparency increases have taken away the problems that politicians mentioned in previous hearings and debates (ibid.). Therefore, Lovery argues that progress is achieved - which will spark even more confidence and a healthy investment relationship between recipient countries and SWFs (ibid.).

4.3.4. Analysis third phase

Neoclassical Mercantilism

The neoclassical mercantilist hypothesis is softly confirmed by the events in phase 3. By not stopping the SWF investments the US government protected the existence of failing banks. If the US had intervened and stopped the investments, these banks could have bankrupted, losing many jobs and an important industrialized hotspot in the global financial economy. In addition, the alleged stoppage of the acquisition of Morgan Stanley by a Chinese SWF, shows US governmental autonomy and the cost-benefit analysis of allowing controlled investments into vital economic sectors. The US government is hereby clearly stating to other countries where its boundaries lie and what kind of investment it accepts.

There is no evidence concerning domestic institutions intervening in the decision of the FPE, as the Department of the Treasury actually actively cooperates with the administration to find the best policy solution.

The US uses its dominant position on the world stage to implement self-restraining 'best practices', in which SWFs agree to 'solely invest economically' and increase transparency. First, the US agrees with two SWF states to promote the principles, where after an active lobby towards other countries is started. However, for that support it needs to concede OECD guidelines. Later on, the US proposes these OECD guidelines within their bigger strategy of promoting free and fair trade and increasing economic prosperity. This indicates that the US advances its own strategy, however that this strategy is not formed through its own cost-benefit analysis but as a response to the concession, which is needed to bring about the 'best practices' for SWFs. This indicates that bargaining power remains at the side of SWFs, who cannot simply be coerced by the US government. The US sees this as a good alternative to stopping the investments as these 'best practices' still fulfill the policy objectives of stopping further harm to national security. Moreover, through the OECD guidelines the US ensures that more countries start to liberalize on the global scale. This is seen as a benefit to the US industry as they can now create wealth abroad more freely. Therefore, the hypothesis is softly confirmed because the US solves the problem of politically motivated SWF investments with the Santiago Principles. However, the US has to accept that it is not the dominant player anymore and that SWFs can now leverage concessions. However, even though SWFs became regular players on the world scale, the US still tackled the problem and achieved international principles that increased US economic welfare.

Critical political economy perspective

The hypothesis of the 'constitutionalizing structural power' approach is partly confirmed and partly disconfirmed. The US is actively choosing to be more open and liberal towards investments from SWFs, as the US accepts the investments and, allegedly, only stops one big investment. However, this investment was stopped by a state Federal Reserve Bank representative, which could suggest that the government did not intervene, but the State Federal Reserve Bank representative acted on his own to stop the investment. This seems plausible as the US government actively promotes free capital movement with its proposal of OECD guidelines. Furthermore, the US governments attitude towards the SWF investments – as memorized in their policy objectives formulated with the Treasury department – shows support for their operating freedom. Indicating that this specific case is an outlier, but with significant value as it resembles power to go against the will of SWFs.

The US, however, goes on and tries to stop protectionist anti-investment sentiments of other countries, that grew out of anxiety towards SWF investments into their countries. By implementing new rules on a multilateral international organizational basis, the US fall into the everlasting neoliberalization trap that forces countries to lock-in neoliberal thought in the global economy. Experts and government officials are influenced by neoliberal thought, consisting of the idea that free-flowing capital is good for their economy. Therefore, these experts and government officials have no choice but to promote and implement 'best practices' instead of hard domestic laws to fight the possible benign intentions of SWF investments – as neoliberal ideology must be adhered to -.

The sole power to encourage other states and implement 'best practices' on a world scale, does not seem to reside with the US government, as it first has to ally with Abu Dhabi and Singapore to agree on a set of principles. In return for this alliance the US has to support the OECD guidelines for recipient countries, making them more open to SWF investments. As numerous diplomatic records recall, SWF hosting countries lobby for free market access for SWFs with success. This quid pro quo at the international level seems like a big concession made by the US government, especially if the US merely 'got' non-enforceable Santiago Principles in return. Therefore, structural power lies with the new great players of the global financial economy: the SWFs. This becomes ultimately clear when the US has to ask SWFs for input and their approval regarding international legislation that is initiated to tighten their power. In the end, the US has to accept the investments: the failing US financial institutions need the money. The lengthy congressional hearings about the potential harm were just a façade, as the US government will not take domestic legislative action to stop the investments. Moreover, if the US actually wants to tackle these investments from being politically motivated, it has to concede with neoliberal regulation guarantees –the OECD guidelines. This shows that the US government does not have the capacity to regulate SWFs on its own.

The US does however have the capacity to initiate and negotiate several policy options that SWFs have to adhere to, leaving some power at the US government level to go against the structural power of SWFs. From here on out, the US have lost power to regulate SWFs as the SWFs have enacted international agreements that regulate themselves. Furthermore, SWFs have established themselves on the world scale, increasing their power towards national governments. Therefore, as the US can still stop one investment and leverage ‘best practices’ for SWFs, the hypothesis is partly confirmed and partly disconfirmed.

5. Conclusion

5.1. Summary of findings

This case study aimed to understand ('verstehen') the inaction of the US government towards SWF investments into failing US banks at the onset of the subprime mortgage crisis. Process-tracing methods were used to describe the three stages of policy creation, to identify what factors led to the policy response of the US government. The US is chosen because it has proactively fought foreign investments into vital economic sectors in the past. As this case involved new important players in the world financial system, the US had to formulate a new policy response from scratch. The case can be seen as a crucial case, that could provide new insights to already existing international political economy theories. Theoretical explanations to analyze this case are provided by a neoclassical mercantilist approach and a combined CPE approach named 'constitutionalizing structural power'. The central question in this research was:

> *Why did the US government accept investments from several sovereign wealth funds into struggling US financial institutions during the subprime mortgage crisis?*

To test the theories and answer the central research question, two hypotheses were deduced. Broadly speaking, the main contradiction between the theories entails whether the US government proactively directs the policy response (neoclassical mercantilism) or whether the US government is structurally forced by financial institutions ('Constitutionalizing structural power'). These hypotheses are tested through the analysis of three phases that represent the policy developments within the US government. The outcomes of the analysis of every phase are summarized in table 2 below.

Table 2: Summary of analysis chapter 4

		Phase I Problem arises	Phase II Political discussion	Phase III Policy output
Neoclassical Mercantilism	H1	Strongly confirmed	Partly confirmed / partly disconfirmed	Softly confirmed
Constitutionalizing structural power	H2	Partly confirmed / partly disconfirmed	Strongly confirmed	Partly confirmed / partly disconfirmed

From this table it can be concluded that both theories explain parts of the government response towards this case quite well. In this case, (policy) actions by the US government could be logically attributed to one of the two theories. As certain parts can be accounted for by one theory, that cannot be accounted for by the other, a combination of the two theories seems appropriate.

To answer the research question, explanations of both theories are combined, reconstructing the following case. The US government saw the need to intervene in unregulated SWF investments into vital economic sectors and started congressional hearings. Interestingly, in the congressional hearings little is said that is out of line with the supreme neoliberal ideology, which is – apparently – deeply entrenched within the US government. On the international scale, the US tries to tackle the problems that unregulated SWF investments brought by initiating and promoting 'best practices'. In exchange for the support of SWF-owning countries, the US had to concede their signature and lobbying power to OECD guidelines for recipient countries. This further increased neoliberal 'self-regulating' and non-enforcing international agreements and laws. Thus, when answering the research question, it becomes clear that the US is still a powerful actor and determines most of its policies and regulations. However, it soundly adheres to the preferences of financial institutions holding structural power. By accommodating to structural power, the US government is partly subdued to the will of financial institutions. In sum, the US government has agency of its own, as it determines what policy output will be chosen. However, it cannot fully decide upon its own policy objectives, because these policy objectives have to be in line with the preferences of the financial sector holding structural power. Moreover, because it plays in a system where the owner of structural power decides the rules of the game, the US government actually believes that neoliberal reforms further its own policy objectives. Thereby, it actively promotes neoliberal regulations and can be seen as a bounded protagonist of a growing neoliberalized world order.

5.2. Theoretical implications and suggestions

The empirical evidence portrayed in chapter 4 strongly supports a connection of the two theories used in this research. This case suggests that the US government is still a prominent decision-maker, however its decisions are made to favor the preferences of financial institutions as they hold structural power. As companies are globalizing and capital can move more freely around the globe, the influence of governments on multinational corporations fades away. This is set in motion by neoliberal ideology that came up, as governments tried new ways to further their own economies. As multinational companies gain more and more power due to deregulation and market thinking, the government that wants economic prosperity is in ever more need to accommodate these companies and keep them 'happy'. Meaning that the neoclassical mercantilist theory does not suffice, because it sees the state as the sole decider within its decision-making. In addition, the CPE derived theory actually gives too little agency to the state by arguing that the state is merely a puppet of transnational capital. To better understand the structural power of financial institutions and multinational companies, and the role and degree it plays in government decision-making these two theories could be synthesized. Creating a theory that places the sole authority of decision making to states, but also acknowledges that the non-state actors' structural power influences the decision-making of states towards favoring the preferences of non-state actors.

The neoclassical mercantilist theory could find a helpful addition when specifying the FPE analysis. According to Rose (1998), the FPE is the most strategic actor of the state apparatus, meaning the President or other high-ranking members of the central government. Interestingly, in this case, evidence is found that other government officials, such as the local representative of the Federal Reserve Bank of New York, were also able to intervene in foreign meddling in the US economy (Wikileaks, 2008a). This shows that the power of local authority is high in the US. Re-specification of the FPE should, therefore, entail a version where local authorities are placed as another domestic factor to the analysis of the FPE. When re-specified, local politicians and government employees with power to influence decision-making should be added to this analysis.

These lower ranking governmental employees are, according to the neoclassical mercantilist theory, still subject to the supervision and direct orders of the FPE.

Certain parts of the CPE hypothesis were quite well supported by the evidence from the case description. An important addition to this theory can be made when assessing the component of the government. Namely, the legal effects of the interlocked neoliberalized regimes are mainly felt by the national government, which deals with international relations. It can be imagined that a local politician or - in this case a local Federal Reserve Bank President - does not recognize the effects and mostly cares about their state policy instead of the international policy of the US. Lower or local politicians/civil servants are not that exposed to international regimes or international relations and focus themselves on the direct effects of foreign meddling on their state's economy. The constitutionalizing structural power approach cannot explain why governments would stop investments at all - as structural power lays with multinational corporations. Therefore, when adding lower-level analysis to a government's behavior, it could be noted that lower governmental divisions (national vs state) act differently, because they do not have to adhere to international regulations in the way the central government has to.

Thus, as evidence described in this case, it seems that the US government has more agency than is expected by CPE theory, and actually seemingly deliberately chooses the path of neoliberalization. However, in contrast to mercantilism, the US government decision-making is adjusted to adhere to the preferences of neoliberal structures. Especially during US - EU diplomatic meetings the occurrence of the financial sector's structural power becomes visible as the US urges the EU to 'not undermine SWF freedoms' and search for 'appropriate levels of transparency' within the 'best practices' as they are needed to enact the Santiago principles (Wikileaks, 2007b). Moreover, supremacy of neoliberal thought within congressional hearings and in the Presidency shows that the state inherently believes that neoliberal policies are the 'only' way to advance the home economy. In the end, this may imply that the proliferation of neoliberalism can be explained by a state's seemingly deliberate decisions.

5.3. Methodological reflections

In this thesis several limitations had to be accepted to fulfill a research with limited resources. Especially regarding the collection of data serious caveats should be taken into account. As mentioned in chapter 3, this case study uses exclusively open source materials to gain access to a limited comprehension into the workings of the government. Because many documents were classified and thus not able for this research, Wikileaks is used. However, although the validity of these documents seems acceptable, they cannot be verified, and therefore caution should be exercised when taking inferences from these data sources. Furthermore, the notion that the senate hearings function as advice for high ranking government officials, should also be taken with a grain of salt. It is impossible for this research to assess whether the direct advice of the government officials was comparable to these statements in congressional hearings. Especially because the new constitutionalist theory heavily relied on neoliberal thought within the government to explain the policy outcomes of the US President.

Oval office meetings and other classified meetings between the President and advisors/staff could shed more light on the real causal relation between the investments and the Santiago Principles & the OECD Guidelines for recipient countries. As for now, these causal relations are anecdotally formed, as hard evidence for these policy objectives remains absent until the minutes of these meetings are released. This also enhances the point of data misrepresentation. As some sources are verified with many other sources, the opinion of experts and politicians during congressional hearings is documented just once. This decreases the validity of the data as these advisors and politicians could voice different opinions at different moments towards government officials.

As this is a single case study, generalizability might be a problem. Even though the generalizability is increased because the case is approached as an ‘crucial’ case, more evidence is needed to control for ‘confirmation bias’ when analyzing the theories. Moreover, the US, as crucial as it might be, has particular governance structures that other countries do not have, such as high divisions of power between state and national governments. Therefore, caution has to be practiced when using this case to describe other nations’ behavior.

5.4. Recommendations for further research

To build further on the theoretical evaluations described above, new research could investigate whether a synthesis of both theories can explain other cases. This synthesis should entail the idea that the state is still an important actor, who deliberately chooses to enact neoliberal regulations and laws. The state does so because it is structurally forced by multinational financial institutions and also because neoliberal ideology is deeply entrenched within the governments advisory and Presidency. States therefore deliberately – in the name of economic growth - choose to lose power through enacting more and more neoliberal laws and regulations. As repeatability is an important part of research, confirmation of this synthesized theory in other research would build a stronger case for developing a new theory. This would exclude the possibility of this synthesis being an accidental finding.

To overcome certain methodological limitations described above, new research could focus, firstly, upon researching internal documents of presidential meetings, or even better, interviews with people active in the Bush administration. With that information, data in this research can be verified and the information could be used to fill the voids of knowledge between the final decision and congressional hearings.

Empirically, it would be interesting to see whether the two-party system of the US played a role in the neoliberal ideological supremacy that is described by the constitutionalizing structural power theory. The experts and politicians could all be described as favoring neoliberal ideology. This could be a direct result from the two-party system, as other parties do not appear in the political spectrum - due to the dominance of the Republican and Democratic party. Moreover, regarding the neoliberal supremacy within the congressional hearings, it might be interesting to see whether group think contributed to the response of the Bush government. Would the response of the US government be different if experts were invited that would harshly critique free flowing capital and would vocally support to never accept SWF investments?

5.5. Societal relevance

This research shows that the US, even though many politicians and the population saw great problems in them, did nothing to stop SWF investments. For society, it is interesting to see that the US, through neoliberal reforms, gave away structural power to financial institutions. The US government still remains the sole actor in the decision-making process, however, by giving away structural power to firms and banks, the US government, needs to accommodate its policies to the wishes of these financial institutions. This happens because the US is still in need of those firms due to the increased importance within its economy. Financial institutions thus do not need to use any power towards the government, as the US government will deliberately choose the policy option that spreads neoliberal thinking on the global scale. This implicates that the government actually adheres to the wishes of the financial sector without being directly forced to do that. The core theoretical implications of this thesis might also be helpful to understand other governments' behavior. For example, the Dutch initial decision regarding the 'dividend tax'. This decision to neoliberalize and lower taxes was made to create a better business environment in the Netherlands. This seems a deliberate decision by the Dutch government to lower taxes and accommodate big businesses. Moreover, when it receives critiques, the government has the power to stop this policy. Therefore, it shows that governments are still important players, but inherently adhere to corporal structural power and neoliberal incentives and thinking. Evidently, this statement needs more scientific research to substantiate the argument.

Appendix A: Santiago Principles.

Generally Accepted Principles and Practices (GAPP) on Sovereign Wealth Funds "Santiago Principles"

A. Legal Framework, Objectives, and Coordination with Macroeconomic policies

1. Sound legal framework with a clear delineation of responsibilities between the SWF and other government bodies.

2, Clearly defined and publicly disclosed policy purpose

3. Coordination with domestic fiscal and monetary authorities

4. Clear and publically disclosed policies, rules, procedures, or arrangements regarding an SWF's funding, withdrawal,, and spending operations

5. Timely reporting of statistical data

B. Institutional Framework and Governance Structure

6. Sound governance framework to facilitate accountability and operational independence

7. SWF owner should set the objectives, appoint members of the governing bodies, and exercise oversight

8. Governing bodies should have a clear mandate and adequate authorities.

9. Independent operational management with clearly defined responsibilities

10. Clearly defined accountability framework

11. Annual report and financial statements should be prepared in accordance with recognized international or national accounting standards.

12. Operations and financial statements should be audited annually in accordance with recognized international or national accounting standards.

13. Clearly defined professional and ethical standards

14. Third-party dealings regarding SWF management based on economic and financial grounds

15. Respecting and complying with all applicablehost country rules, laws, and regulations

16. Public disclosure of governance framework and objectives, as well as the manner in which the SWF's management is operationally independent

17. Public disclosure of financial information to demonstrate its economic and financial orientation

C. Investment and Risk Management Framework

18. Clear and consistent investment policy based on sound portfolio management principles

19. Investment decisions should aim to maximize risk adjusted financial returns or if investment decisions are subject to other than economic or financial considerations, these should be clearly set out and publically disclosed

20. No seeking advantages of privileged information or government's inappropriate influence

21. Exercising shareholder ownership rights in a manner consistent with its investment policy

22, Transparent and sound operational control and risk management systems

23. Accurate and consistent reporting of investments and investment performance

24. Regular review of GAPP implementation

(Source: Weiss, 2009: 16)

Appendix B: OECD recipient countries guidelines

OECD GUIDELINES FOR RECIPIENT COUNTRY INVESTMENT POLICIES RELATING TO NATIONAL SECURITY*

Non-discrimination – Governments should be guided by the principle of non-discrimination. In general governments should rely on measures of general application which treat similarly situated investors in a similar fashion. Where such measures are deemed inadequate to protect national security, specific measures taken with respect to individual investments should be based on the specific circumstances of the individual investment which pose a risk to national security.

Transparency/predictability – while it is in investors' and governments' interests to maintain confidentiality of sensitive information, regulatory objectives and practices should be made as transparent as possible so as to increase the predictability of outcomes.

- *Codification and publication*. Primary and subordinate laws should be codified and made available to the public in a convenient form (e.g. in a public register; on internet). In particular, evaluation criteria used in reviews should be made available to the public.
- *Prior notification*. Governments should take steps to notify interested parties about plans to change investment policies.
- *Consultation*. Governments should seek the views of interested parties when they are considering changing investment policies.
- *Procedural fairness and predictability*. Strict time limits should be applied to review procedures for foreign investments. Commercially-sensitive information provided by the investor should be protected. Where possible, rules providing for approval of transactions if action is not taken to restrict or condition a transaction within a specified time frame should be considered.
- *Disclosure of investment policy actions* is the first step in assuring accountability. Governments should ensure that they adequately disclose investment policy actions (e.g. through press releases, annual reports or reports to Parliament), while also protecting commercially-sensitive and classified information.

Regulatory proportionality - Restrictions on investment, or conditions on transaction, should not be greater than needed to protect national security and they should be avoided when other existing measures are adequate and appropriate to address a national security concern.

- *Essential security concerns are self-judging*. OECD investment instruments recognise that each country has a right to determine what is necessary to protect its national security. This determination should be made using risk assessment techniques that are rigorous and that reflect the country's circumstances, institutions and resources. The relationship between investment restrictions and the national security risks identified should be clear.
- *Narrow focus*. Investment restrictions should be narrowly focused on concerns related to national security.
- *Appropriate expertise*. Security-related investment measures should be designed so that they benefit from adequate national security expertise as well as expertise necessary to weigh the implications of actions with respect to the benefits of open investment policies and the impact of restrictions.
- *Tailored responses*. If used at all, restrictive investment measures should be tailored to the specific risks posed by specific investment proposals. This would include providing for policy measures (especially risk mitigation agreements) that address security concerns, but fall short of blocking investments.

continued…

* Source: OECD Investment Committee report on recipient country policies and SWFs, approved by governments on 4 April 2008. The text on accountability was finalised by governments at the 8th Roundtable on Freedom of Investment which took place under the auspices of the OECD Investment Committee on 8 October 2008. OECD countries that have SWFs are participants in the roundtables on Freedom of Investment. Non-OECD SWFs are also invited.

OECD GUIDELINES FOR RECIPIENT COUNTRY INVESTMENT POLICIES RELATING TO NATIONAL SECURITY continued…

- *Last resort.* Restrictive investment measures should be used, if at all, as a last resort when other policies (e.g. sectoral licensing, competition policy, financial market regulations) cannot be used to eliminate security-related concerns.

Accountability – procedures for internal government oversight, parliamentary oversight, judicial review, periodic regulatory impact assessments, and requirements that important decisions (including decisions to block an investment) should be taken at high government levels should be considered to ensure accountability of the implementing authorities.

- *Accountability to citizens*. Authorities responsible for restrictive investment policy measures should be accountable to the citizens on whose behalf these measures are taken. Countries use a mix of political and judicial oversight mechanisms to preserve the neutrality and objectivity of the investment review process while also assuring its political accountability. Measures to enhance the accountability of implementing authorities to Parliament should be considered (e.g. Parliamentary committee monitoring of policy implementation and answers or reports to Parliament that also protect sensitive commercial or security-related information).

- *International accountability mechanisms*. All countries share a collective interest in maintaining international investment policies that are open, legitimate and fair. Through various international standards, governments recognise this collective interest and agree to participate in related international accountability mechanisms (e.g. the OECD notification and peer review obligations in relation to restrictive investment policies). In particular, these help constrain domestic political pressures for restrictive and discriminatory policies. Recipient governments should participate in and support these mechanisms.

- *Recourse for foreign investors.* The possibility for foreign investors to seek review of decisions to restrict foreign investments through administrative procedures or before judicial or administrative courts can enhance accountability. However, some national constitutions' allocation of authority with respect to national security may place limits on the scope of authority of the courts. Moreover, judicial and administrative procedures can be costly and time-consuming for both recipient governments and investors, it is important to have mechanisms in place to ensure the effectiveness, integrity and objectivity of decisions so that recourse to such procedures is rare. The possibility of seeking redress should not hinder the executive branch in fulfilling its responsibility to protect national security

- *The ultimate authority for important decisions (e,g, to block foreign investments) should reside at a high political level.* Such decisions require high-level involvement because they may restrict the free expression of property rights, a critical underpinning of market economies, and because they often require co-ordination among numerous government functions. The final decision to prohibit (or block) an investment should be taken at the level of heads of state or ministers.

- *Effective public sector management.* Broader public sector management systems help ensure that the political level officials and civil servants responsible for security-related investment policies face appropriate incentives and controls for ensuring that they exercise due care in carrying out their responsibilities and are free from corruption, undue influence and conflict of interest. ■

FURTHER INFORMATION

OECD work on Freedom of Investment:
www.oecd.org/daf/investment/foi

Requests for information can be addressed to:

Ms Kathryn Gordon, Senior Economist, OECD
Paris, France (kathryn.gordon@oecd.org
Tel: +33-1 4524 9842)

(Source: OECD investment committee report, 2008)

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