Neil Lee Cassandra Chong February 12th, 2025

How to make Labour's National Wealth Fund work

Labour's plans for growth include the creation of a National Wealth Fund. A closer look at the proposals reveals that this is not like other Sovereign Wealth Funds, but is in fact more like a Green Investment Bank, meant to channel investments and funding into infrastructure required to reach net-zero. ***Neil Lee*** *and* ***Cassandra Chong*** *look at other successful green banks and distil four lessons that Labour can learn from them.*

The Labour government's first mission is growth. One of their tools for doing this is a National Wealth Fund (NWF), designed – according to their manifesto – with "a remit to support Labour's growth and clean energy missions, making transformative investments across every part of the country". A quick look at other successful wealth funds – such as Singapore's Temasek – suggests that this is a good idea. In theory at least, smart use of public sector resources can help crowd in private sector funding, and countries are increasingly setting up Sovereign Wealth Funds (SWFs), focused on national economic development. Jumping onto the bandwagon, even Donald Trump has said he wants one. Sovereign Wealth Funds have become the latest policy fad.

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decarbonisation, gigafactories and ports. This makes it, specifically, a green investment bank.

But look a little deeper and the UK's "National Wealth Fund" is actually a different beast. A "classic" Sovereign Wealth Fund is funded by excess government revenues from oil and gas, deposited offshore to avoid the economic distortions this can cause. Yet the UK has a budget deficit and scant oil and gas revenue, so the funding for the NWF essentially comes from government borrowing. Funds such as this are more appropriately called Sovereign Investment Funds, and they are used in countries from France to Nigeria to achieve broader policy goals such as economic growth or sustainability. But because of its focus on infrastructure, the NWF is more like a development bank than a Sovereign Wealth Fund (SWF).

Reflecting this, the government has announced that the NWF would be run by the UK Infrastructure Bank ("UKIB"), the UK's post-Brexit replacement for the European Investment Bank. Then, confusingly, they renamed the UKIB (which is a bank) after the fund (which is also a bank), so we have a National Wealth Fund which is really a development bank.

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Labour's vision for the National Wealth Fund

The proposed NWF aims to invest in 5 strategic sectors – in green hydrogen, steel, industrial decarbonisation, gigafactories and ports. This makes it, specifically, a green investment bank. According to the OECD, green investment banks ("GIBs") are public entities that are established with the specific purpose to channel investments and funding into low-carbon and climate-resilient infrastructure. Usually, the motivation behind a GIB's establishment originates from governments recognising that markets or governments alone are insufficient to raise adequate capital to push forward their transition plans or green objectives, which is likely the vision of the Labour government.

The NWF is timely as governments lack the capital to keep up with their net zero commitments. Yet the private sector is unlikely to fill the gap without government help. Problems in financial markets such as risk aversion, due to imperfect information, and high transaction costs, limit private spending. For instance, the long-term investment horizon and high risk of infrastructure projects may be beyond the risk appetite of private investors. The NWF will, if it works, help mitigate these problems. But it won't be the first GIB, there are many others across the world. So building on this, are there any policy lessons the NWF can learn from other GIBs?

What the government can learn from other green banks

To answer this question, we examined four other GIBs which had similar aims. We know that the NWF aims to achieve a private capital per public investment ratio of 3x. So we selected five green banks which had private capital per public investment ratios above this, and were in countries which were, roughly, comparable to the UK. The Japan Green Fund (which achieves a ratio of private capital to public investment of 11x), the Connecticut Green Bank (6.7x), the Technology Fund of Switzerland (4.1x), and the NY Green Bank (3.29x). Our analysis of these green banks offers four broad lessons for Labour to build an efficient and effective NWF.

1. Tolerate risk

First of all, the NWF needs to take on some risky investments. The key reason for the re-establishment of a GIB is to improve capital access for the five targeted sectors (green hydrogen, green steel, industrial decarbonisation, gigafactories, ports). Each of the sectors faced its own challenges in recent years. Taking ports as an example, global geopolitical instability and changes in international trade have reduced the attractiveness of the sector to investors due to fears over the uncertainty of cash flows and revenues for ports. However, the essential nature of the sector does not change as a result.

In order to attract further private investments, the government, hence, could play the role of de-risking. This could be by providing early-stage funding to nascent technologies such as green hydrogen, or by providing financing solutions to make technologies and projects commercially viable. To achieve this, the government must maintain a higher risk tolerance with good risk management. The NWF plays a significant role here as, compared to the private sector, it does not have quite the same profit-generating motive. But it will also have to manage the difficult politics of some failed investments. Some failures are, paradoxically, a sign of policy success as the fund is taking on the risk it is designed to.

2. Offer a diverse range of instruments

Then, what financing solutions should the Government provide? Grants, subsidies, loans, guarantees or even equity financing could be helpful blended finance solutions to attract private capital and lower the cost of capital for the targeted projects and sectors. Guarantees generally require less state intervention and only affects government spending in the case of a loss, making them helpful for projects which are already at the stage of commercialisation. Other instruments can help de-risk private sector loans, particularly important in early stage markets.

> *Further academic research would be helpful to better understand the potential crowding-out of investments in the context of sustainable investments.*

Grants could play an essential role in kick starting innovation and R&D for early-stage projects. However, it raises the concern of whether the government's provision of grants would lead to the crowding out of investments from the private sector. While that has not been the case in the technology sector, there is a knowledge gap in the realm of sustainability, particularly in the sectors that the NWF plans on focusing on. Hence, further academic research would be helpful to better understand the potential crowding-out of investments in the context of sustainable investments.

3. Build a pipeline

The NWF serves an important role in building a pipeline of future projects. In the long run, de-risking investments and priming allows for capacity building, which is a core part of the activities of the European Investment Bank, which helps local areas identify and work with the private sector to bring investments to the market. Drawing lessons from the uptake of green bonds in the private sector due to the "proof of concept" displayed by multinational development banks, GIBs in general, and the NWF by extension, are able to create an enabling environment by showing a "proof of concept" of green financing. Hence, by identifying the five key sectors, the NWF is on track to deliver like the best development banks.

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national economic goals, as stated in the industrial strategy; the worst way would be to have politicians micromanage investments.

4. Stay independent from politics

Third, the NWF needs to maintain administrative flexibility and be far from government control. The best way to help the NWF serve national goals is to have it report that it is making investments consistent with national economic goals, as stated in the industrial strategy; the worst way would be to have politicians micromanage investments. Placing the NWF in the UKIB helps here, and make it consistent with other similar banks such as the Connecticut Green Bank and the New York Green Bank. This would allow them greater flexibility to make investments at private sector timelines.

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The NWF should also provide standardised contracts for the targeted sectors, such that it removes the administrative barriers and bureaucracies associated with drafting entirely new contracts for the private sector. Private investors could use these standardised contracts as a baseline for underwriting, which reduces the costs and effort required for private investment firms to enter into financing agreements.

Not a "real" Sovereign Wealth Fund, but useful nonetheless

The National Wealth Fund is not a Sovereign Wealth Fund in the classic sense. But this doesn't make it useless. By focusing on risky projects, offering a diverse set of instruments, and building up a pipeline of projects – while, crucially, doing it at some distance from the policy process – it can play a role as part of the industrial strategy. But to do this, it needs to be an independent institution built for the long term, not a policy fad.

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