MINISTRY OF FINANCE

Meld. St. 9

(2021–2022)

Report to the Storting (white paper)

The Government Pension Fund 2022

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(Government Støre)

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Responsible long-term investment

Executive summary

The Government Pension Fund is an intergenerational fund. The Fund is owned by the State and comprises the Government Pension Fund Global (GPFG) and the Government Pension Fund Norway (GPFN). The purpose of the Fund is stipulated in the Government Pension Fund Act . The savings shall support the funding of pension expenditure under the National Insurance Scheme and further long-term considerations in the spending of government petroleum revenues, thus ensuring that the petroleum wealth benefits both current and future generations.

The Ministry of Finance holds the formal responsibility for the management of the Government Pension Fund under the Act. Norges Bank and Folketrygdfondet carries out the operational management of the GPFG and the GPFN, respectively, within management mandates stipulated by the Ministry. The investment objective of the two Funds is to achieve the highest possible return, given an acceptable level of risk. Within the scope of this objective, the Funds shall be managed responsibly. A clear financial objective, together with responsible, long-term fund management, ensures that the Government Pension Fund will benefit both current and future generations.

Norges Bank and Folketrygdfondet make decisions about individual investments and exercise the ownership rights of the Funds independently of the Ministry of Finance. The investment strategy for the Funds and the investment framework are defined by the Ministry, with key choices having been endorsed by the Storting. A clear division of roles highlights responsibilities. The governance structure ensures that key decisions affecting risk and return, as well as decisions regarding the responsible investment framework, are endorsed by the Fund's owners; the people of Norway, represented by the Government and the Storting. At the same time, there must be sufficient delegation of responsibility to ensure that operational management decisions are made close to the markets and companies in which the Funds are invested. Transparency and broad endorsement of the investment strategy and the investment management framework support understanding of the risk assumed. This establishes a foundation for remaining committed to the chosen strategy, also during periods of considerable financial market turbulence.

The investment management framework for the Government Pension Fund is established by the Government and the Storting, but the Fund is not a policy tool. However, withdrawals from the GPFG contribute to the funding of welfare schemes and political priorities. The financial objective of the Fund and the ability to fund public expenditure are closely related. Over time, the GPFG has become an ever more important source of public expenditure funding. In 2021, about one quarter of fiscal budget expenditure was funded from the GPFG.

According to the fiscal policy guidelines, annual withdrawals from the GPFG shall over time correspond to the expected long-term annual real rate of return on the Fund capital; estimated at 3 percent. The guidelines further stipulate that petroleum revenue spending in any given year shall be adapted to the economic situation. This implies that one may spend more than the expected real rate of return during periods of economic setback, but also that spending should be less in economic upturns. Persistently running large fiscal deficits would impair the long-term sustainability of public finances.

Large increases in the Fund capital over the last two decades have offered scope for a significant increase in petroleum revenue spending. Historically, large petroleum revenue transfers into the Fund have increased the Fund value, even during periods of stock market decline. In coming years, periods without increase, or periods of decline, in the Fund value must be expected. The Fund value will increasingly be determined by the development in the international financial markets. As the Norwegian welfare state has increasingly been funded by transfers from the GPFG, public finances have become more vulnerable to market fluctuations. Increased vulnerability and reduced Fund growth prospects suggest that caution should be exercised in the continued phase-in of Fund revenues into the Norwegian economy.

The investment strategy

The Ministry of Finance emphasises the importance of an investment strategy that is professionally acknowledged and tailored to the distinctive characteristics and purpose of the Fund. The strategies for the GPFG and the GPFN have been developed over time, based on thorough assessments, professional recommendations and practical experience. The investment strategy is defined in the management mandates for the two Funds and reflected in, inter alia, the composition of the benchmark indices established by the Ministry. The strategic benchmark index defines a capital allocation between equities and fixed-income securities, and reflects the owner's investment preferences and risk tolerance. The equity share for the GPFG is 70 percent, while it is 60 percent for the GPFN. Fixed-income securities account for the remainder.

The choice of equity share is the decision with the greatest impact on overall risk in the Fund. A larger equity share entails higher expected return, but also increased volatility in the value of investments and a higher risk of loss. By endorsing the chosen equity share, the Fund's owners; the people of Norway, represented by the Government and the Storting, have expressed what is considered an acceptable level of risk. The investment strategy further entails the Fund capital being primarily invested in listed markets.

A key premise underpinning the strategy is that overall risk can be reduced by broad diversification of investments across asset classes, regions, countries, industries, companies and issuers. The composition of the equity and fixed-income benchmarks implies that investments are diversified across a large number of equities and bonds. The benchmarks have been designed to facilitate close replication at a low cost and are also used to measure the investment management performance of Norges Bank and Folketrygdfondet.

Most of the Fund risk is determined by general equity and bond market developments. Norges Bank and Folketrygdfondet may deviate somewhat from the benchmark indices in their operational investment management, within risk limits stipulated in the mandates. The intention behind this is to ensure cost-effective adoption of the benchmark indices, as well as to exploit distinctive Fund characteristics or advantages to generate excess return. The GPFG management mandate further allows some limited scope for investments in unlisted real estate and unlisted renewable energy infrastructure. The investment strategies for the GPFG and the GPFN are discussed in chapters 2.2

and 4.2, respectively (in Norwegian only). Potential implications of increased inflation for developments in the value of the GPFG are addressed in chapter 2.6 (in Norwegian only).

Strong performance in 2021

Market developments in 2021 reflected that the global economy was rebounding from the coronavirus pandemic, with robust growth in many countries. Expansionary monetary and fiscal policy served to boost overall demand. Moreover, higher commodity and energy prices have contributed to a steep increase in consumer prices. Higher inflation and a positive economic growth outlook created expectations of monetary policy normalisation in many countries, with an increase in key policy rates. This development caused long-term interest rates to increase during the year, and led to weak returns on fixed-income securities globally. At the same time, company earnings reverted to pre-pandemic levels during 2021, and high equity returns were registered globally. However, new virus outbreaks, inflationary pressure and monetary policy normalisation caused stock market uncertainty over the course of the year. The second half of the year, in particular, was characterised by considerable share price volatility. There were also major differences between sectors and countries. The energy, finance and technology sectors delivered the strongest performance, while interest rate-sensitive sectors such as telecommunications, power and water utilities accounted for the weakest performance. Geographically, returns were highest in North America.

The market value of the GPFG increased by NOK 1,432 billion in 2021, to reach NOK 12,340 billion. The increase is primarily the result of positive financial market returns. The return on the GPFG in 2021 was 14.5 percent, measured in the currency basket of the Fund and before the deduction of investment management costs. The market value of the GPFN at year-end 2021 was NOK 333 billion, which represents a NOK 41 billion increase over the course of the year. The return on the GPFN last year was 14.0 percent, measured in NOK and before the deduction of investment management costs.

Norges Bank and Folketrygdfondet seek to achieve the highest possible return, net of costs and given an acceptable level of risk, within the limits stipulated in the mandates from the Ministry of Finance. In 2021, Norges Bank achieved a return on the GPFG that was 0.74 percentage points higher than the return on the benchmark index, while Folketrygdfondet achieved an excess return of 0.97 percentage points in the management of the GPFN. The Ministry emphasises the overall performance achieved in the GPFG and the GPFN over time. The average annual return on the GPFG over the last 20 years has been 0.2 percentage points higher than the return on the benchmark index. The average excess return on the GPFN has been 1.0 percentage point per year since 2007. The Ministry is satisfied with this performance, given the level of risk assumed. Measured as a proportion of assets under management, investment management costs last year were 4.0 basis points for the GPFG and 5.4 basis points for the GPFN.

The performance of the GPFG and the GPFN is discussed in chapters 2.4 and 4.4, respectively (in Norwegian only).

Responsible investment

The Government Pension Fund Act requires the Fund to be managed responsibly within the scope of its financial objective. Environmental, social and corporate governance considerations form an integral part of the management of the GPFG and the GPFN, in line with the mandates laid down by the Ministry of Finance. The mandates require Norges Bank and Folketrygdfondet to adopt responsible investment principles in accordance with internationally recognised standards. By advocating long-term value added and responsible business conduct, responsible investment serves to further the objective of achieving the highest possible return, given an acceptable level of risk.

Norges Bank and Folketrygdfondet make decisions about individual investments and exercise the ownership rights of the Funds independently of the Ministry. The responsible investment framework comprises, inter alia, advocacy of good corporate governance and responsible business conduct principles, as well as contributing to the development of international standards, company dialogue on relevant topics and issues, as well as voting in annual general meetings of investee companies.

Norges Bank has, as part of its responsible investment efforts, prepared expectation documents on several issues, including, inter alia, climate, human rights, children's rights, as well as tax and transparency. The documents are directed at the boards of directors of investee companies, and are used as, inter alia, a basis for the Bank's ownership dialogue with the companies. Folketrygdfondet has prepared expectation documents for companies on, inter alia, strategy, capital structure and financial objectives, anti-corruption, remuneration, human rights, climate and the environment.

The Ministry of Finance has adopted Guidelines for Observation and Exclusion of Companies from the GPFG (the ethical guidelines). The guidelines feature both *product-based* exclusion criteria, which encompass the production of tobacco, cannabis, coal and certain weapon types, and *conduct-based* exclusion criteria, which encompass, for example, serious or systematic human rights violations and severe environmental damage. An independent Council on Ethics appointed by the Ministry of Finance makes recommendations on the observation or exclusion of companies under the ethical guidelines. Decision-making authority rests with the Executive Board of Norges Bank . For the coal criterion, the Bank may make decisions without any prior recommendation from the Council on Ethics. Before exclusion is decided, the Bank shall consider whether other measures may be suited for reducing the risk of continued violation of ethical norms, or may be more appropriate for other reasons. The Bank shall consider the various tools at its disposal in relation to each other and use these in an integrated manner. Active ownership may be effective in reducing the risk of violating ethical norms by influencing companies to change their conduct. What is the most appropriate tool must be considered on a case-by-case basis.

The investments of the Fund attract considerable attention. Even a strong framework for risk management, responsible investment and ethically motivated guidelines cannot serve as a guarantee against blameworthy situations in Fund portfolio companies. It is neither feasible, nor appropriate, to organise investment management with a view to preventing the Fund from ever being exposed to unwanted situations.

Responsible investment is a rapidly evolving field in which new knowledge is gained and new practices are established. The Government wants to make the GPFG world leading in responsible investment and the management of climate and nature risks. The Government's ambition will be addressed through continual development of the responsible investment framework for the Government Pension Fund in view of, inter alia, developments in internationally recognised principles and best practices. In this white paper, the Ministry is further proposing that the responsible investment framework for the GPFG is to be reviewed on a regular basis; see the discussion in chapter 3.1 (in Norwegian only).

The responsible investment of the GPFG and the GPFN is discussed in more detail in chapter 2.3 and 4.3, respectively (in Norwegian only).

Review of active management in the GPFG

The Ministry of Finance conducts regular reviews of Norges Bank's management of the GPFG at the beginning of each term of the Storting. The purpose is to contribute to transparency and insight into Norges Bank's management of the Fund. The reviews are important to ensure confidence in the investment management and may strengthen the ability to adhere to long-term investment strategies, also during periods of weak performance. The Ministry is presenting a new review in this white paper.

The mandate from the Ministry of Finance permits Norges Bank to deviate from the benchmark index defined by the Ministry. A key issue considered in the regular reviews is whether the limit on such deviations, measured by expected tracking error, should be adjusted. The tracking error limit expresses by how much the annual percentage difference in return between the GPFG's actual investments and the benchmark index can be expected to vary. The limit has been held at 1.25 percentage points since 2016.

As part of the review, the Ministry of Finance appointed an expert group comprised of Professors Rob Bauer of Maastricht University, Charlotte Christiansen of Aarhus University and Trond Døskeland of NHH Norwegian School of Economics. The Ministry has also received analyses and assessments from Norges Bank. In addition, an open seminar on the Bank's active management of the GPFG was held in March 2022.

The analysis of the expert group shows that Norges Bank's deviations from the benchmark index explain only a minor part of the historical fluctuations in the overall return on the Fund. Measured in this way, the management of the GPFG may be characterised as close to the benchmark. The expert group has calculated that the Bank's active management over the period from January 1998 to September 2021 has served to increase the market value of the GPFG by an estimated NOK 228 billion before the deduction of investment management costs and NOK 170 billion net of investment management costs.

In its performance evaluation, the expert group has used models to interpret historical performance. The expert group's analysis indicates, inter alia, that parts of the excess return may be explained by somewhat higher market risk in the Fund than in the benchmark index. The findings from the analysis also show that some of the Bank's strategies have achieved significant excess return that can probably be attributed to investment management skill rather than chance.

Since 2017, unlisted real estate has not been included in the strategic benchmark index defined by the Ministry of Finance. Such investments are made within the scope for deviations from the benchmark index. Norges Bank states that investments are made in listed and unlisted real estate within an integrated strategy. The overall real estate investments have since 2017 reduced the return on the Fund somewhat. The Ministry notes that unlisted investments must be evaluated over a time period of more than a few years.

The Ministry's overall assessment is that Norges Bank's active management has been satisfactory and that the GPFG should continue to be managed with a certain element of active management. The Ministry agrees with Norges Bank's assessment that the scope for deviations would appear to be sufficient given the current portfolio and investment strategy, and is therefore not proposing any changes to the tracking error limit at present. If the scope for investment in unlisted assets were to be expanded, it would be appropriate to conduct a new assessment of the scope for deviations and how the framework for deviations from the benchmark index is arranged.

The review of Norges Bank's active management is discussed in more detail in chapter 2.5 (in Norwegian only).

Climate risk management in the GPFG

Climate change affects the global economy and financial markets. In the years to come, company earnings may be influenced by climate policy, technological development, changing stakeholder preferences and physical implications of climate change. Uncertainty with regard to climate change and how companies and the global economy will be affected gives rise to financial risk, which needs to be managed by investors like the GPFG. Such risk is challenging to assess, and is one of several types of risk to which the Fund is exposed.

Climate and environmental considerations have for many years been an important dimension in the ongoing development of the investment strategy, the responsible investment framework and the ethical guidelines for the GPFG. Norges Bank manages climate risk within the limits in the mandate adopted by the Ministry. Climate risk assessments form an integral part of risk management, investment decisions and active ownership. Norges Bank is already devoting considerable resources to this effort. It is important to emphasise that the GPFG has a financial objective, and that it is not a part of the Bank's mandate that the Fund shall contribute to the attainment of specific climate objectives. There is a broad political consensus on this.

An external expert group appointed by the Ministry to assess the significance of financial climate risk and climate-related investment opportunities to the GPFG submitted its report in August 2021. The group's assessment is that the key to reducing climate risk is an effective and predictable climate policy. The GPFG is, according to the group, relatively robust to moderate climate change and a predictable climate policy. In contrast, dramatic climate change or sudden policy shifts may pose major challenges to global financial markets and to the GPFG. The expert group notes that overall climate risk in the financial system is high, but finds no basis for assuming that such risk is systematically mispriced over time. This implies that one cannot expect a better ratio between risk and return for the Fund by excluding investments in specific industries. The experts therefore believe that the principles underpinning the investment strategy for the Fund should remain unchanged.

The expert group is of the view that the mandate from the Ministry of Finance should be premised on a high level of ambition in climate risk management. The group recommends the inclusion of a mandate provision requiring the Bank's responsible investment efforts to be based on a long-term goal of zero greenhouse gas emissions from investee companies, in accordance with the Paris Agreement. This must, according to the group, be combined with regular reporting and the use of targets that are revised on a regular basis. The expert group is of the view that active ownership is the key instrument for managing the GPFG’s climate risk. It is noted that targeted and effective active ownership may influence the robustness of investee companies, and also contribute to strengthening the general ability of financial markets to price climate risk and reduce transition risk.

Norges Bank is of the opinion that the expert group’s recommendations provide a solid basis for the Bank’s continued follow-up of climate risk and climate-related investment opportunities and takes the view that many of the recommendations represent a formalisation and evolvement of the Bank’s current efforts. The Bank notes that the management of climate risk in the Fund has developed over time and will continue to develop on the basis of new insights. The management mandate should therefore be general and based on principles. The Bank agrees with the expert group that climate risk management must be premised on the Fund’s role as a financial investor and that the main features of the investment strategy and the benchmark index should remain unchanged, including the principle of broad investment diversification. The Bank also agrees with the expert group’s view that there is no basis for assuming that climate risk is systematically mispriced.

The Ministry of Finance agrees with the expert group’s and Norges Bank’s assessment that there is no reason to assume that climate risk is systematically mispriced over time. Nor is there any reason to assume that the Fund has any advantage or systematically better information on climate risk than other investors. This means that although overall climate risk in the financial system is high, one cannot expect a better ratio between risk and return by changing the composition of the benchmark index. The Ministry emphasises that the Fund is not managed with a view to the attainment of any other objective than the highest possible return. The principles underpinning the investment strategy for the Fund should therefore remain unchanged, as recommended by both the expert group and the Bank.

As a long-term global investor, it is in the interest of the GPFG that the goals under the Paris Agreement are attained and that the transition to a zero-emission economy takes place in an orderly manner. An effective and predictable climate policy and a gradual decarbonisation of the economic system would reduce the risk of financial instability and abrupt changes in the value of the Fund’s investments.

As owner, the GPFG has a financial interest in companies managing the transition to a zero-emissions economy and adequately reporting thereon. Improved climate-related corporate reporting would strengthen the ability of financial markets to price climate risk. This may contribute to an orderly transition to global net zero emissions and thereby to a gradual reduction in financial market risk associated with that transition.

The Ministry shares the view of both the expert group and Norges Bank that responsible investment and active ownership will be of key importance in climate risk management in the GPFG due to, inter alia, the long-term and systemic nature of such risk. In its dialogue with companies, the Bank should continue to set expectations that companies plan for different climate scenarios, including at least one scenario in which the goals under the Paris Agreement are attained, and assess the climate risk associated with their own activities. It is in the financial interest of the Fund that Norges Bank set expectations on companies’ strategies and plans for managing the transition. It is, at the same time, important for companies’ strategy and activities to be assessed in a real-world context, including the regulatory and climate policy framework in which companies operate. Companies' strategy must in any event support their long-term profitability. The key to reducing climate risk is, as noted by the expert group, an effective and predictable climate policy. This falls outside the responsibilities of the GPFG as a financial investor. However, the climate risk in the Fund will be affected by what climate policy is being pursued.

The Ministry emphasises that Norges Bank's reporting on its climate risk management must be in conformity with recognised principles and standards, and evolve to reflect new knowledge and practises over time.

The Ministry is in this white paper proposing to strengthen the GPFG efforts on climate risk. This will require Norges Bank to establish principles for the management and measurement of climate risk and to use various measurement methods, including stress tests based on future development scenarios, one of which is a scenario consistent with global warming of 1.5 degrees. Moreover, the Bank's responsible investment shall be based on the long-term goal that investee companies align their activities in a way that is consistent with global net zero emissions in accordance with the Paris Agreement. This long-term goal shall be supplemented by regular reporting on, inter alia, companies' forward-looking decarbonisation pathways, in accordance with leading frameworks for such reporting. The Bank must report on what principles and assessments underpin decisions on participation in various climate-related initiatives. The Bank must also report on climate risk in conformity with recognised principles and standards. The Bank's reporting should be considered in relation to the EU taxonomy, but it is too early to consider the potential application of that framework at present. The responsible investment framework for the GPFG shall be reviewed on a regular basis.

These initiatives will contribute to an integrated approach to climate risk management, which is premised on the Fund's financial objective. This approach encompasses both framework, management and reporting, with climate risk being integrated in risk management, investment decisions and active ownership across all investment management activities.

Climate risk in the GPFG is discussed in more detail in chapter 3.1 (in Norwegian only).

The GPFG environmental investment mandates

The Ministry of Finance has in the management mandate for the GPFG required Norges Bank to establish specific environmental investment mandates. These mandates are subject to separate reporting requirements. The environmental investment mandates form part of the Bank's active management and count towards the limit on deviations from the benchmark index. The Ministry announced, in the white paper on the Government Pension Fund in 2021, that it in view of international sustainability reporting developments would assess whether the reporting requirements for the environmental investment mandates should be expanded somewhat. Such assessment would be based on the premise that the GPFG, including the environmental investment mandates, shall contribute to the highest possible long-term return, given an acceptable level of risk. As a basis for the Ministry's assessments, Norges Bank was requested to consider a potential expansion of the reporting requirements, as well as to provide an account of developments in the market for environmentally-related investments. The expert group that examined climate risk management in the GPFG has also discussed the environmental investment mandates.

Norges Bank is of the view that it would not be appropriate to expand the specific reporting requirements to include climate and environmental effects or the mandates' overall exposure to environmentally-related activities. The Bank states that this needs to be considered in the context of the Ministry's assessment as to how the recommendations of the expert group that examined climate risk should be follow up on, that sustainability reporting standards are still at an early stage of development, as well as the financial objective of the environmental investment mandates.

The expert group that examined climate risk management in the GPFG noted, inter alia, that it may introduce ambiguity in the division of responsibilities if the owner (the Ministry of Finance) includes instructions in the management mandate as to how the investment manager (Norges Bank) shall deviate from the benchmark index. The group recommends that the Ministry consider a different solution for regulating the environmental investment mandates and make the Fund's environmentally- and sustainability-related investments more apparent. A potential alternative outlined by the group is to replace the NOK 30–120 billion range by a reporting requirement for all investments within specific categories in the Fund. If a more ambitious climate risk management and reporting arrangement is contemplated for the Fund as a whole, the expert group would deem it appropriate to consider whether there is still a need for separate environmental investment mandates.

The Ministry is in this white paper proposing to remove the management mandate requirement for the establishment of specific environmental investment mandates. This needs to be considered in the context that the Ministry is now proposing to strengthen and develop the framework for, and follow-up of, climate risk in the management of the GPFG, cf. the discussion in chapter 3.1 (in Norwegian only). The Ministry is proposing, inter alia, more comprehensive and integrated climate risk management and reporting, including the assessment of potential future use of the EU taxonomy.

The Ministry emphasises that it is the management mandate *requirement* for environmental investment mandates that it proposes to remove. This does not mean that the Fund's investments in climate- and environmentally-related activities *must* be reduced. Norges Bank may still invest more in environmentally-related companies than would be implied by the benchmark index, if deemed appropriate by the Bank. It is for Norges Bank to assess how the active management should be structured, in accordance with the established division of responsibilities.

The Fund may still be invested in unlisted renewable energy infrastructure, within the current cap of 2 percent of the Fund. Removing the requirement for specific environmental investment mandates will imply, in somewhat simplified terms, that the cap on unlisted renewable energy infrastructure investments is increased from NOK 120 billion to just over NOK 240 billion, based on the market value of the GPFG at the beginning of 2022.

The environmental investment mandates are discussed in more detail in chapter 3.2 (in Norwegian only).

Amendments to the ethically motivated guidelines

The Guidelines for Observation and Exclusion of Companies from the GPFG (the ethical guidelines) were amended in certain respects in 2021. The background was the Ethics Commission's report NOU 2020:7; *Values and Responsibility*. The amendments included the introduction of a criterion for the exclusion of companies that produce cannabis for recreational use, a new criterion targeting sales of weapons that are used in ways that constitute serious and systematic violations of international law, and an expansion of the corruption criterion to also encompass «other serious financial crime». In addition, some provisions of the guidelines were clarified. Furthermore, the mandate of Norges Bank was amended, by including the UN Guiding Principles on Business and Human Rights (UNGP) among the standards on which the Bank's responsible investment shall be based. It was also specified in the mandate that Norges Bank shall have procedures for the approval of markets in which the Fund is invested, and that such approval shall take place on a regular basis. The amendments to the ethical guidelines are discussed in more detail in chapter 3.3.1 (in Norwegian only).

The Ethics Commission proposed that lethal autonomous weapons should be added to the list of weapons that are encompassed by this product criterion under the guidelines. The Ministry agrees with the Commission's assessment that such weapons raise several issues, as stated in last year's white paper on the Government Pension Fund. However, the Ministry concluded that there must be a reasonable and agreed understanding of what autonomous weapons are before such a criterion can be applied. It was proposed, against that background, to await the international process that Norway is participating in on the ethical and legitimate use of, inter alia, autonomous weapons, and to revert to this issue when such process has resulted in clarification. The Standing Committee on Finance and Economic Affairs stated in Innst. 445 S (2020–2021) that it expects a product criterion for lethal autonomous weapons to be introduced when a sufficiently precise definition is available. The Standing Committee requested an update on the status of this effort in the next white paper on the Government Pension Fund.

The Ministry notes that several processes are taking place internationally in relation to autonomous weapons, in which Norway also participates, including, inter alia, under the UN Convention on Certain Conventional Weapons (CCW). The expert group under CCW held a number of meetings in the autumn of 2021, but has yet to reach agreement on substantive recommendations. Consequently, the backdrop is fundamentally the same as when the Storting deliberated last year's white paper on the Government Pension Fund. There is, however, a broad consensus that this process must continue and that the CCW is the appropriate framework for this. This process may admittedly take some time. The Ministry of Finance will revert to the Storting when relevant clarifications and a sufficiently precise definition is available. See chapter 3.3.2 for further details (in Norwegian only).

Experience with the coal criterion and the climate criterion

It was announced in last year's white paper on the Government Pension Fund that the Ministry of Finance would in this year's white paper provide an account of experience with both the climate criterion and the coal criterion under the ethical guidelines. Feedback has been obtained from Norges Bank and the Council on Ethics as a basis for the Ministry's assessments.

According to Norges Bank, 95 percent of coal extraction and 80 percent of coal-based power production has been excluded from the Fund or placed under observation under the product-based coal criterion. The Bank is of the view that this shows that the criterion is largely functioning as intended. Norges Bank points to several considerations which suggest, in the view of the Bank, that one should exercise caution when it comes to reducing the threshold values established for the criterion. According to the Bank, a potential reduction of the threshold values would mean, inter alia, greater challenges in relation to data and analysis, while at the same time increasing the risk that companies that should have been subject to such criterion are not captured by said criterion, or of incorrect exclusions. The Ministry agrees with Norges Bank's assessments of the product-based coal criterion and proposes that this criterion remain unchanged.

A total of four companies have been excluded from the GPFG under the conduct-based climate criterion. All of these have significant production of oil from oil sands. The Council on Ethics reports that the Council has devoted considerable resources to examining companies under the climate criterion, without this having resulted in a corresponding volume of recommendations for the exclusion or observation of companies. The Council on Ethics notes that the scope of the Council's efforts in relation to the climate criterion and the Bank's climate risk efforts means that the Council and Norges Bank are to a large extent examining the same industries and companies. The Council on Ethics has experienced company being sold through risk-based divestment, before the Council on Ethics has completed its assessment. Moving forward, it is the assessment of the Council on Ethics that the efforts of the Council are unlikely to result in any significant exclusion or observation of companies. The Council on Ethics is therefore of the view that it should be considered whether the Bank's climate-related efforts should also include the assessment of companies under the climate criterion, in the same way as how the coal criterion is applied.

Norges Bank notes that the application of the climate criterion requires complex assessments of relationships at the industry and company level, as well as access to detailed information on the activities and plans of companies. Norges Bank notes, like the Council on Ethics, that the Bank's company-specific climate risk efforts often overlap with the climate criterion efforts of the Council on Ethics, and that such overlap is likely to increase in the time to come. Going forwards, Norges Bank is also of the view that it may over time be appropriate to consider permitting the Bank to make decisions on observation and exclusion under the climate criterion at its own initiative, as under the coal criterion.

The Ministry notes that the application of the climate criterion is complex and requires considerable insight, and is of the view that an arrangement corresponding to that introduced for the coal criterion should also be workable for the climate criterion. The Ministry is proposing, against this background, to give Norges Bank the right to take the initiative for exclusion or observation of companies under the climate criterion.

The coal criterion and the climate criterion are discussed in more detail in chapter 3.4 (in Norwegian only).

Long-term perspectives on the GPFG

A Commission to examine long-term perspectives on the GPFG was appointed in September 2021. The Commission is tasked with examining what developments may be of relevance to the GPFG some years into the future, as well as their potential implications for the management of the Fund. Relevant risks in this context are financial risk, in particular, but also reputational risk for the GPFG and Norway, as well as security and foreign policy risk. The Commission shall examine whether developments may have an impact on the premises underpinning the investment strategy for the Fund, and whether there are circumstances suggesting that some of the changes made to the investment strategy in recent year should be reassessed. The Commission is chaired by Ulf Sverdrup (Director of the Norwegian Institute of International Affairs (NUPI)), and shall submit its report by 1 October 2022. See chapter 3.5 for further details (in Norwegian only).

The GPFN's large ownership stakes on the Oslo Stock Exchange

In 2019, the Ministry of Finance was advised by Folketrygdfondet to consider amending the management mandate for the GPFN as the result of its ownership stakes in the Norwegian equity market having reached levels where there is a risk of breaching the 15-percent ownership stake limit in Norwegian companies.

The Ministry of Finance has not reached a final conclusion on the ownership stake challenge in the GPFN. The Ministry has initiated a new comprehensive assessment of various alternatives for solving the ownership stake issue.

The Government aims to establish a separate unit in Tromsø, which can serve to strengthen central government presence and develop professional investment management centres in Northern Norway. Whether this is going to be a new unit of Folketrygdfondet, a unit subordinated to Folketrygdfondet, a new independent unit or part of another central government investment management body, is among the issues that need to be examined in more detail. See chapter 5.1 for further details (in Norwegian only).

Remarks on Russia

Russia went to war against Ukraine on Thursday 24 February 2022. The Government announced in a press conference on Sunday 27 February 2022 that Norway would be joining the EU sanctions against Russia, that the Ministry of Finance would instruct Norges Bank to immediately freeze all investments in Russia and that the GPFG would divest all of its holdings in Russia.

On Monday 28 February 2022, the Ministry of Finance sent a letter to Norges Bank instructing it to freeze all of the Fund's investments in financial instruments issued by Russian enterprises, the Russian State or entities linked to the Russian State, with immediate effect and until further notice. Notice was also given that the investment universe of the Fund will no longer include Russia, including financial instruments, real estate, infrastructure and cash; see further details on the investment universe of the Fund in chapter 2.2.1 (in Norwegian only). The Ministry of Finance asked, against this background, Norges Bank to prepare a proposal for a plan to execute the divestment, which pays heed to the applicable sanctions and considers the Fund's interests in general.

In its reply letter of 15 March 2022, Norges Bank highlights that the Moscow Exchange has been closed since 28 February 2022. In addition, extensive sanctions that restrict trading have been introduced. Since it is not possible to execute trades in the Russian stock market, Russia was omitted from all FTSE Russell indices at a price of close to zero from 7 March 2022. Russia was also omitted from the Fund's benchmark index from the same date. In its letter, Norges Bank further notes that the divestment cannot be executed a present because the market does not function in a normal manner. The divestment will also have to pay heed to sanctions and to the Fund's interests in general, and will have to be executed over time. The Ministry of Finance will revert to the Storting with an account when the divestment has been completed. Russia is now also encompassed by the government bond exemption for the GPFG; see the discussion in chapter 2.3.4 (in Norwegian only).