

Ida Wolden Bache: Norges Bank's management of the Government Pension Fund Global

Introductory statement by Ms Ida Wolden Bache, Governor of Norges Bank (Central Bank of Norway), to the public consultation on the Government Pension Fund in the Storting's Standing Committee on Finance and Economic Affairs, Oslo, 30 April 2024.

* * *

Thank you for the opportunity to talk about Norges Bank's management of the Government Pension Fund Global.

The objective of the investments made by the Government Pension Fund Global is to achieve the highest possible return, given an acceptable level of risk. The fund is to be managed responsibly. A financial objective and long term management permit both current and future generations to benefit from our national petroleum wealth.

In recent years, the global economy has been characterised by significant and unexpected events. The COVID-19 pandemic and then Russia's full-scale invasion of Ukraine led to substantial increases in both energy prices and the prices of other goods and services. To combat inflation, central banks raised interest rates quickly and significantly. Now, inflation is on the decline in most countries, and so far, it seems that the global economy may experience a softer landing than many have feared. However, there is still considerable uncertainty about future developments.

Significant disruption and uncertainty have caused major fluctuations in the financial markets in recent years. These fluctuations are reflected in the returns in the Government Pension Fund Global.

At last year's public consultation, we looked back on a year characterised by clearly negative returns in the fund. The equity markets had experienced their worst year since the 2008 financial crisis, and rising interest rates had led to a decline in the value of fixed income investments. In 2023, the opposite was the case. Both the equity and fixed income markets contributed to historically strong growth in the fund's market value. While 2022 returns were higher than the benchmark index, last year's returns were somewhat lower as a result of the decline in the value of the fund's investments in unlisted real estate.

The fund has a long-term time horizon and results must be measured over time. From 1996 until year-end 2023, the accumulated return on the fund constituted more than NOK 8,500 billion, representing over half of the fund's market value. And the return was more than NOK 300 billion higher than the return on the benchmark index.

The fund's investment strategy has been developed over time and has served us well. The fund is managed close to its benchmark. The strategy emphasises broad diversification of investments. The proportion of equities is currently at 70 per cent. In addition to stocks and bonds, Norges Bank invests in unlisted infrastructure for renewable energy and unlisted real estate.

The Ministry of Finance is responsible for determining the investment strategy and the benchmark index. Significant changes are embedded here in the Storting. This broad political support is crucial for the confidence in Norges Bank's management of the fund and is one of the key success factors for the fund's long-term success.

Last November, Norges Bank's Executive Board advised the Ministry of Finance to permit investments in unlisted equities on a general basis. Comparable sovereign funds and pension funds already make significant investments in unlisted equities. However, this does not necessarily mean that we should do the same.

The Government Pension Fund Global has a unique governance structure and a special role in Norwegian society. Transparency, accountability and cost-effectiveness are crucial for ensuring the public's confidence in the fund. These are aspects that the Executive Board carefully considered in its work on its recommendation. In this process, we also drew on the knowledge accumulated through the fund's investments in unlisted real estate and unlisted infrastructure for renewable energy. After taking several factors into account, we recommended permitting investments in unlisted equities, the main reason being that we believe, given the fund's particular characteristics, it would lead to higher returns for the fund over time. After costs. And without a significant increase in risk.

We also believe it is possible to set requirements for private equity funds in order to invest in a manner that sufficiently addresses issues relating to transparency and responsible investment.

Based on current information, the Ministry of Finance does not generally consider it desirable to invest in unlisted equities and would like to gather more knowledge on the subject. We have naturally taken this under advisement. Allowing for investments in unlisted equities will be a long-term decision, requiring broad support.

Last week, there were demonstrators outside Norges Bank, demanding that the fund withdraw from investments related to the war in Gaza. We understand the seriousness behind such demands. What is unfolding in Gaza is a humanitarian disaster.

There are many challenging questions related to what the fund should and should not invest in. These issues have been thoroughly investigated in recent years, as documented in the reports published by the Mestad Commission and the Sverdrup Commission in 2020 and 2022, respectively.

The criteria for excluding companies from the fund are anchored in the Storting. When companies are excluded from the fund, the aim is not to improve returns or to impact those companies but to avoid investing in companies that cause or contribute to serious violations of fundamental ethical norms.

The Council on Ethics for the Government Pension Fund Global assesses individual companies based on ethical guidelines. Norges Bank's Executive Board makes decisions on observation and exclusion based on recommendations from the Council on Ethics. At year-end 2023, a total of 164 companies were excluded from the fund.

The seriousness associated with increased geopolitical tensions not only influences the assessments that fall under the purview of the Ethics Council but also the work we do at Norges Bank based on the fund's financial objective. Managing geopolitical risk is an integral part of the fund's risk management strategy and is something to which Norges Bank Investment Management (NBIM) and the Executive Board increasingly devote time. Our stress tests show that geoeconomic conflicts may cause large declines in the value of the fund.

In line with its mandate, Norges Bank places great emphasis on being a responsible investor. Sustainable economic development and well-functioning markets are in the long-term interest of the fund.

Being an active owner enables us to influence companies in a more sustainable direction. We let companies know what we expect and are in dialogue with them. We exercise our voting rights at general meetings.

In 2023, Norges Bank published expectations for companies on consumer interests and views on the responsible use of artificial intelligence. We also published our sharpened expectations for the way in which companies should manage climate risk.

In recent years, we have raised our ambitions for responsible investment. However, there are issues that must be addressed. We don't want the fund to be perceived as a political actor. However, when we seek to influence companies, it could be perceived in this way. In a world characterised by increasingly more conflict and unrest, this balancing act will be more challenging.

In exercising our ownership rights, we place great emphasis on acting responsibly ourselves. We strive to be predictable, transparent and reliable. Our expectations and views are knowledge based and rooted in internationally recognised standards and principles. We are clear that we conduct our active ownership in pursuit of the fund's long-term financial objective. We believe that this will best help preserve the legitimacy of the fund both within and beyond Norway's borders and to fostering its growth and sustainability.

With that, I yield the floor to Nicolai.