

# Management of the Government Pension Fund Global

Introductory statement by CEO Yngve Slyngstad before the Standing Committee on Finance and Economic Affairs of the Storting.

*Please note that the text below may differ from the actual presentation.*

I would like to thank the Chair of the Committee for the invitation to speak on the management of the Government Pension Fund Global (GPFG) in 2016.

*Chart: 7 867 billion kroner in the fund*

At the end of 2016 the GPFG had a market value of NOK 7 510 billion. Last week the fund's value passed NOK 8 000 billion following a very good start of the year. First quarter 2017 return came to 3.8 percent, or NOK 297 billion. Measured in Norwegian kroner, this was the third best quarter in the history of the fund.

The return on the GPFG came to 6.9 percent in 2016 measured in international currency, equivalent to NOK 447 billion. The annual return has averaged 5.7 percent since 1998. The rate of return on the first krone, after inflation and costs, has been 3.8 percent.

*Chart: Returns exceed inflows*

The total return is now larger than the total inflow to the fund. Since its inception in 1996, to the end of the first quarter this year, NOK 3 375 billion has been transferred to the GPFG. The total return amounts to NOK 3 420 billion.

The increase in the fund's market value stems to a great extent from an exceptionally high return over the past five years. Four out of every five kroner of the fund's return come from this five-year period. The fund's market value has also risen in recent years as a result of the depreciation of the krone. This does not affect the fund's international purchasing power.

*Chart: NOK 199 billion kroner in cash flow in 2016*

In pace with the rise in the value of the fund, the cash flow from the fund's investments has also increased. This cash flow consists of share dividends, interest income and rental income. This current income amounted to nearly NOK 200 billion in 2016 alone. With falling international interest rates, the largest contribution now comes from dividend payments from investee companies.

*Chart: Large fund – large expected value fluctuations*

We have seen exceptionally high return over the past five years. Looking ahead, we must be prepared for periods of substantial declines in value.

A notable consequence of the fund's size is that we can expect large fluctuations in the fund's market value. At the end of the first quarter this year, the expected volatility of the fund was estimated at approximately 11 percent, or NOK 860 billion. A decline in value of this magnitude is to be expected. In particularly challenging market situations, the decline in value could exceed NOK 1 000 billion.

*Chart: Recommendation on equity share*

The equity share decision is the best expression of the risk-bearing capacity of the fund owner. Assessments have been made every ten years. First in 1997, when the equity share was set to 40 percent, next in 2006 when it was set to 60 percent, and now in 2017. In 2016 Norges Bank recommended the Ministry of Finance to increase the equity share of the fund's strategic benchmark index to 75 percent. The considerable growth of the fund increases the capacity to tolerate substantial losses.

*Chart: Share of equities in the benchmark index*

At the turn of the year, the long-term target equity share was increased from 60 percent to 62.5 percent. The reason for the adjustment was that the fund's unlisted real estate investments are no longer included in the Ministry's strategic benchmark index. The Bank decides the size of the total real estate allocation, within a 7 percent limit.

As global equity markets have recently delivered solid returns, the equity share of the *actual* benchmark index is somewhat higher than that of the strategic benchmark index, which is the long-term target. The actual benchmark index currently has an equity share of close to 65 percent.

*Chart: Expectation documents*

Our mission is to safeguard and build financial wealth for future generations. Responsible investment management supports the investment objective of the highest possible return with a moderate level of risk.

Our ownership strategies are premised on good corporate governance and well-functioning boards. As a shareholder, we have an interest in understanding the companies' corporate governance and sustainability frameworks, as well as operational and financial strategy issues.

Expressing clear expectations towards the companies in our investment portfolio, based on internationally recognised principles, is part of our work in this area. Our expectations are aimed primarily at company boards and are a starting point for dialogue. We have previously issued expectation documents on children's rights, water management, climate change and human rights.

Earlier this year, we issued a new expectation document on tax and transparency. We expect multinational enterprises to exhibit appropriate, prudent and transparent tax behaviour.

*Chart: Decreasing management costs*

Management costs continue to fall, sustaining the downward trend of recent years. Internal management costs amounted to 0.04 percent of assets under management in 2016. We have realised significant economies of scale in recent years. At the same time, we have built up a real estate investment division, where costs per krone of assets under management are higher than for equity and fixed income investments.

Norges Bank has adopted a strategic plan for the period 2017 to 2019. Our aim is to keep internal management costs below 0.05 percent of assets under management, even with expected changes in asset allocation.

*Chart: Public information available on our website*

In addition to our annual report, we publish extended information on responsible investment, the unlisted real estate investments, and the return and risk of the fund.

All public information about the fund is available on our website, which includes a range of publications, data and background information. We submit letters to the Ministry of Finance concerning investment strategies. Our advice is underpinned by Discussion Notes. We also publish a series we call Asset Manager Perspective, which contains our suggestions for the development of well-functioning financial markets. In our communication with companies, we use Expectation Documents, and we present our views on key ownership issues in the form of Position Papers. As an example, we issued a Position Paper on CEO remuneration earlier this year.

Together, these documents provide a high level of transparency on the management of the fund. Our responsibility is to manage the financial wealth of the Norwegian people in a responsible, efficient and transparent manner.