

Annual Report **2011**



# 1986 2011

In 2011, a quarter century had passed since Norges Bank moved into its new headquarters at Bankplassen. The new building's inauguration on 13 October 1986 marked the end of a long and complicated construction process. The architectural firm Lund & Slaatto won the competition to build Norges Bank in 1973, with groundwork beginning in 1979.



## 1973

Design competition for new headquarters for Norges Bank. The entry by the architectural firm Lund & Slaatto was used as the basis for extensive design and planning work. The project was guided by consideration for the local urban milieu, indoor working environment, security and capacity for future expansion. In the period 1976-79, the essentials relating to the structure, design, details and use of materials were approved.

## 1980

Construction began at the turn of the year 1979-80 and involved more than 100 individual contractors. In the most intensive period, over 100 architects and engineers were engaged full-time in planning in addition to the property consultancy OPAK's staff of project and construction managers.

## 1982

On 17 August 1982, the president of the Storting, Per Hysing Dahl, laid the cornerstone at a ceremony held at the foundation pit.

## 1986

Building occupancy took place on 29-31 August, though extensive work continued after that. Approx. 750 employees, including the Printing Works' staff, moved in during autumn 1986 and spring 1987. The building has 60,000 m<sup>2</sup> of floor space, a third of which is underground. The official opening took place on 13 October 1986, with HM King Olav V as guest of honour.

## 1990

In May, Fritz Røed's sculpture *Gateteater* (Street Theatre) was installed in the outdoor space *Rådhushaven*. This was the last of the works purchased as part of the building's public art programme. Since then, paintings, sculptures, textile artworks and prints by Norwegian artists have been regularly added to the Bank's art collection.

1970 1971 1972 1973 1974 1975 1976 1977 1978 1979 1980 1981 1982 1983 1984 1985 1986 1987 1988 1989 1990



## 1991

On 14 June 1991, the Bank marked the 175th anniversary of the Storting's first Norges Bank Act. The Bank's headquarters were decorated to celebrate the occasion. A book commemorating people and events in the period 1816-1991 was published. The ground floor hall and renovated buildings housed an anniversary exhibition, and an open day was held for employees and their families.

## 1998

NBIM (Norges Bank Investment Management) manages the Government Pension Fund Global on behalf of the Ministry of Finance. NBIM was established as part of Norges Bank on 1 January 1998. NBIM grew quickly, and the need for office space along with reorganisations in the rest of the Bank resulted in extensive reconstruction and internal relocations. The original canteen on the fifth floor was converted to offices and the canteen is now on the ground floor. Reception has been moved closer to the entrance, as one of several measures to enhance security.

## 2001

On 1 July, parts of the Bank's cash handling operations were spun off into NOKAS, a limited company. When NOKAS was established, Norges Bank owned 33.5% of the shares, with the remainder owned by Norwegian banks. NOKAS's operations occupied a large part of the ground floor.

## 2007

Norges Bank's Printing Works was closed down in June 2007. As from 2008, Norwegian banknotes are printed abroad. The first banknotes were delivered the year after the founding of Norges Bank in 1816 and banknotes were thus printed in-house for 190 years.

## 2010

The space vacated by the Printing Works was converted to rental office space. In autumn 2009, Finanstilsynet moved into the renovated space. The minister of finance, Sigbjørn Johnsen, was the main speaker at the inauguration ceremony on 20 January 2010. A new fitness room was also built, available to employees of both Norges Bank and Finanstilsynet.

## 2011

The Bank's shares in NOKAS were transferred to other owners on 6 January 2006. NOKAS vacated the building in October 2011, and the premises will be converted to space for Norges Bank. In 2011, several other technical modifications were made to the building, including combining private offices into open-plan offices and multipurpose spaces.

1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011





# Annual Report **2011**

 **NORGES BANK**

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# Highlights in 2011

- Norges Bank's key policy rate was raised by 0.25 percentage point to 2.25% in May and was left unchanged up to December. At the monetary policy meeting in December, the key policy rate was reduced by 0.5 percentage point to 1.75%.
- Underlying inflation ranged between 1% and 1.5% through 2011, and measured by the CPIXE, inflation averaged 1.1%.
- In the course of spring, both Greece and Portugal had to request assistance from the EU and IMF crisis fund. Government bond yields rose in several countries. The sovereign debt crisis in Europe had contagion effects on international financial markets and the growth outlook for the world economy weakened. Expectations concerning future key rates fell markedly.
- In autumn 2011, the European Banking Authority announced that all the large European banks were required to increase their Core Tier 1 capital ratio to 9% as from 1 July 2012. The requirement entails the establishment of a higher required minimum ratio. Norges Bank responded by urging Norwegian banks to recapitalise.
- In Norway, a new liquidity management system for banks was introduced as from October. Under the new system, banks will receive interest on a defined portion of deposits – a quota – at the key policy rate. Deposits exceeding the quota will receive interest at the reserve rate, which is one percentage point lower than the key policy rate.
- Against the background of international financial market turbulence and weakened growth prospects abroad, Norges Bank assessed the financial system to be somewhat more vulnerable at the end of 2011 than at the beginning of the year. However, Norges Bank's stress tests showed that the increase in capital adequacy ratios since 2009 had strengthened the resilience of the Norwegian banking sector to a severe international downturn.
- Norges Bank decided to withdraw the 50-øre coin as legal tender with effect from 1 May 2012.
- Norges Bank made its first property investments for the Government Pension Fund Global through the acquisition of 25% leasehold interest in Regent Street in London in partnership with The Crown Estate. Investments were also made in seven properties in the Greater Paris Region.





Annual Report  
of the Executive Board **2011**

# Norges Bank's Executive Board



The Executive Board supervises the executive and advisory activities of the Bank and comprises seven members, all appointed by the King-in-Council. Two employee representatives attend meetings when the Executive Board deals with administrative matters.

<b>Øystein Olsen</b>	Appointed governor of Norges Bank as from 1 January 2011 for a term of six years. Postgraduate degree in economics (Cand. oecon) from the University of Oslo (1977). His work experience includes positions as director general, Economic Policy Department, Ministry of Finance, and director general, Statistics Norway.
<b>Jan F. Qvigstad</b>	Appointed deputy governor of Norges Bank from 1 April 2008 for a term of six years. Postgraduate degree in economics (Cand. oecon) from the University of Oslo (1975). His work experience includes posts as principal officer and assistant director, Economics Department at the Ministry of Finance, and as executive director of Norges Bank Monetary Policy.
<b>Brit K. Rugland</b>	Appointed 1 January 2004–31 December 2005. Reappointed 1 January 2006–31 December 2009 and 1 January 2010–31 December 2013. General manager and owner of the investment company Rugland Invest. Chairman of the board of the state-owned gas company Gassco AS. Has broad experience from the petroleum, financial and shipping industries.
<b>Liselott Kilaas</b>	Appointed 1 January 2004–31 December 2007. Reappointed 1 January 2008–31 December 2011. Managing director, Aleris Norge. Graduate of the University of Oslo and Institute for Management Development (IMD) in Lausanne. Member of the board of directors of Telenor and has broad experience from the ICT sector, petroleum industry and consultancy.
<b>Ida Helliesen</b>	Appointed 1 January 2010–31 December 2013. Retired. Helliesen has held several executive positions at Norsk Hydro, including CFO. She is a business economist and has been a member of several government commissions, including on energy and on telecommunications. She has also held directorships at Aker Solutions, Skagerak Energi, Statistics Norway, Storebrand Bank and served as a member of the Norwegian Ministry of Finance's Investment Strategy Council.
<b>Eirik Wærness</b>	Appointed 1 January 2010–31 December 2013. Chief analyst, energy market research, Statoil. Wærness is an economist with Norwegian and international qualifications and research experience. Has work experience from the Norwegian Ministry of Finance, Total E&P Norge and Econ Pöyry.
<b>Egil Matsen</b>	Appointed 1 January 2012–31 December 2015. Professor, Department of Economics, NTNU, research in the areas of macroeconomics and finance. Also has work experience from Norges Bank. Doctorate in economics (Dr. oecon) from the Norwegian School of Economics and Business Administration.

## EMPLOYEE REPRESENTATIVES

<b>Jan Erik Martinsen</b>	Appointed 1 January 2001–31 December 2012. Employee representative. Employee of Norges Bank since 1975. Chief safety delegate in the period 1 January 1994–31 December 2000. Deputy chairman of Norges Bank's Staff Association from 2001 to 2006 and chairman since 1 January 2007.
<b>Gøril Bjerkhol Havro</b>	Appointed 1 January 2011–31 December 2012. Employee representative. Employee of Norges Bank since 2008. Has a BA from the University of Oxford, a master's degree in development studies from Nelson Mandela Metropolitan University in South Africa, and a business economics degree from HEC Paris. Work experience from the OECD, Paris.

# Annual Report of the Executive Board 2011

**N**orges Bank's activities are regulated by the Norges Bank Act. In addition, the Bank manages the Government Pension Fund Global in accordance with the Act relating to the Government Pension Fund and the mandate for managing the Government Pension Fund

Global issued by the Ministry of Finance.

Norges Bank is managed from the head office in Oslo. The Bank also has offices in London, New York, Singapore and Shanghai.

Pursuant to Section 5 of the Norges Bank Act, executive and advisory authority in Norges Bank is vested in the Executive Board, which manages its resources. The Executive Board comprises seven members, all appointed by the King-in-Council. The Governor and Deputy Governor of Norges Bank are chairman and deputy chairman, respectively, of the Executive Board. The other five members are not permanent employees of the Bank. Two alternates have also been appointed for the five external members. They attend Executive Board meetings on a regular basis with the right to be present and to speak. Two employee representatives supplement the Executive Board when matters are discussed that primarily concern the Bank's internal operations and conditions for the staff.

The Executive Board works to attain the Bank's objectives and values, with particular emphasis on promoting price stability, financial stability and prudent and effective asset management. The Executive Board attaches importance to high standards and low costs in the Bank's performance of its responsibilities.

The Executive Board is responsible for ensuring sound organisation of, and establishing a satisfactory framework, objectives and principles for, the Bank's operations. The Executive Board shall ensure that financial reporting and asset management are subject to adequate control and supervision and shall oversee the Bank's administration and operations in other respects. The Executive Board shall also ensure that the Bank's risk management and internal control are satisfactory in all parts of the Bank's operations.

The Executive Board has two subcommittees, the audit committee and remuneration committee. The audit commit-

tee comprises three of the external members of the Executive Board, and prepares business for and advises the Executive Board. The committee's task is to strengthen and streamline the Executive Board's management and follow-up work related to financial reporting, risk management, internal control and internal audit.

The remuneration committee comprises two of the external members of the Executive Board. It is a preparatory body, responsible for matters concerning pay and remuneration arrangements at the Bank.

In 2011, 14 Executive Board meetings were held, and 144 items of business were discussed. Most of the business concerned core activities in the area of investment management, monetary policy and financial stability. The number of items of business has been declining in recent years, as the Executive Board has delegated executive responsibility to the Governor of Norges Bank and the Chief Executive Officer of Norges Bank Investment Management (NBIM). This has enabled the Executive Board to focus more attention on governance, follow-up and control of operations, with particular emphasis on issues of strategic importance related to core activities.

## Monetary policy and financial stability

The conduct of monetary policy and work on financial stability in Norway in 2011 was marked by the sovereign debt crisis in Europe. High and rising government debt in many countries resulted in increasing turbulence and weakened prospects for the global economy. Capacity utilisation in the Norwegian economy was assessed to be close to a normal level through the year, and unemployment was low and stable. Growth held up, with a sharp increase in petroleum investment and high levels of building activity, but towards year-end, growth prospects in Norway also became somewhat weaker.

In the first half of 2011, inflation was expected to pick up further ahead. In May, Norges Bank's key policy rate was raised by 0.25 percentage point to 2.25%. During the summer and autumn, market turbulence resumed and intensified. The euro area debt crisis made access to whole-

sale funding more expensive and less accessible to European, and also Norwegian, banks. In the October *Monetary Policy Report*, the forecast for the key policy rate was revised down. Higher risk premiums in market and lending rates and a weaker outlook for the Norwegian economy led to a 0.5 percentage point reduction in the key policy rate to 1.75% in December.

Inflation is low and stable. For a number of years, inflation has remained somewhat below, but fairly close to, the 2.5% target. Consumer price inflation varies considerably from month to month, partly as a result of short-term fluctuations in energy prices. Excluding these fluctuations, the underlying rise in consumer prices was low through 2011. Underlying inflation was 1.1%, as measured by the CPIXE.

The new system for managing bank liquidity approved by the Executive Board in 2010 was implemented in October. Banks receive interest at the key policy rate on only a specific portion of bank reserves – a quota. Reserves in excess of the quota bear interest at the reserve rate, which is one percentage point lower than the key policy rate. The volume of loans from Norges Bank to banks declined, and the interest rate for overnight interbank deposits, the NOWA rate, remained close to the key policy rate after the system went live.

Owing to turbulence in international financial markets and a weaker growth outlook abroad, Norges Bank assessed the financial system as somewhat more vulnerable at end-2011 than at the beginning of the year. The risk of international turbulence spreading to Norwegian banks increased. The Executive Board noted that banks' borrowing in foreign countries may pose a short-term challenge. At the same time, banks' losses on loans and securities may grow, if developments abroad eventually substantially weaken Norwegian business sector profits. Challenges to the financial system in Norway may also arise further ahead. The household debt burden is high, and house prices are rising quickly. This may make many households vulnerable when interest rates return to a more normal level, or if prospects for the real economy weaken. Such developments will also adversely impact the rest of the real economy and the financial sector.

Norges Bank's stress tests of banks showed that due to the increase in capital adequacy ratios since 2009, the Norwegian banking sector is better equipped to weather a severe international downturn. The tests also showed that banks need more capital to be able to maintain lending in bad times. Against this background, Norges Bank recommended that the largest Norwegian banks raise their Core Tier 1 ratios.

New quantitative liquidity requirements (Basel III) will be introduced between 2015 and 2018. Until then, Norwégi-

an banks will have to increase their liquidity buffers and obtain more long-term wholesale funding.

Sound and credible plans for managing banking crises are important for ensuring financial stability. The Norwegian crisis resolution system should also be improved. Norges Bank has also argued that it should be easier for the authorities to split up a bank to maintain essential public services performed by the bank without the use of public funds. Furthermore, Norges Bank has stated the view that partial conversion of a bank's debt to equity can be a tool for dealing with a troubled bank.

Norwegian payment systems functioned effectively in 2011. There were no serious interruptions in the settlement system's technical operations. Norges Bank decided in 2011 that the 50-øre coin would no longer be legal tender as from 1 May 2012.

## Investment management

Investment management was also affected by the turmoil in global capital markets in 2011. Equity prices fell, especially in Europe, while returns on fixed income instruments were positive, since rising bond prices reflected falling yields.

At end-2011, Norges Bank managed NOK 3 575bn in international capital markets, in the form of foreign exchange reserves and assets in the Government Pension Fund Global.

The market value of foreign exchange reserves after deducting borrowing in foreign currency was NOK 262bn at end-2011, an increase from NOK 258bn the previous year. Norges Bank's foreign exchange reserves are managed in a money market portfolio of investments in short-term fixed income instruments and in a long-term portfolio of fixed income instruments and equities. In addition, a "petro" buffer portfolio is used for regular transfers of foreign exchange to the Government Pension Fund Global.

In 2011, the Executive Board revised the guidelines for investing the long-term portfolio. The primary purpose of the changes was to bolster liquidity. Changes include simplifying the benchmark index for the fixed income portfolio and introducing a requirement for at least 50% of investments in this portfolio to be held in liquid government bonds.

In addition, a requirement was added specifying that no more than 20% of the fixed income portfolio may be invested in corporate bonds and collateralised bonds. Lending of fixed income securities was eliminated, since these investments need to be available as liquidity reserves.

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## *Norges Bank shall promote economic stability in Norway*

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The investment portfolio of the Government Pension Fund Global accounts for most of Norges Bank's assets under management. The market value of the portfolio was NOK 3 312bn at end-2011, an increase of NOK 234bn over the previous year. Transfers from the government accounted for NOK 271bn, while the return on the portfolio was NOK -86bn before foreign exchange gains. The krone depreciated against several of the currencies the portfolio is invested in. In isolation, this increased the market value by NOK 49bn.

In 2011, the investment portfolio of the Government Pension Fund Global earned a return of a negative 2.5%, measured in a currency basket that corresponds to the composition of the benchmark index. The return on the portfolio was 0.13 percentage point lower than the return on the benchmark index. Since 1998, the average excess return from equity and fixed income instrument management has been 0.28 percentage point.

After Norges Bank received a mandate in 2010 to gradually invest up to 5% of portfolio assets in real estate outside of Norway, the first transactions were carried out in 2011. In spring 2011, an agreement was completed to purchase 25% of net income from The Crown Estates' portfolio of properties in Regent Street in London. A few months later, the Fund invested in seven properties in Paris. In 2011, Norges Bank established subsidiaries as part of the management of the real estate asset class in the investment portfolio. For a detailed discussion, see Note 24 to the financial statements, GPF Note 15, "Subsidiaries and jointly controlled entities".

In 2011, the Executive Board revised the structure and content of the governance documents for the management of the investment portfolio of the Government Pension Fund Global. The investment mandate and job description for the CEO of NBIM delegates responsibility for management of the investment portfolio. Other documents stipulate principles for risk management, corporate governance, organisation and management, and employee remuneration. The documents have been published on the NBIM website.

Norges Bank engages in active ownership to maintain and increase financial wealth for future generations. The Bank promotes shareholders' rights and works to improve social and environmental conditions related to the companies the Bank invests in. Corporate governance at Norges Bank is based on the principles of the UN Global Compact and the OECD Principles of Corporate Governance and multinational companies. Norges Bank votes at the annual general meetings of approximately 90% of the companies in the portfolios.

The Executive Board also refers to the annual report on the management of the Government Pension Fund Global published by Norges Bank.

## **Organisation and personnel**

### **Expertise and resources**

Norges Bank's vision is to be a transparent and well run central bank. The Bank's employees shall be professionally competent with a high level of integrity. The Bank shall achieve results through effective cooperation, focusing on both day-to-day operations and innovation. Developing personnel policy measures that ensure the proper skills at all levels of the Bank's operations is a priority task. The Bank's personnel policy shall foster employee skills enrichment and personal development over an employee's entire career. At end-2011, there were 629 employees in Norges Bank, compared with 589 at end-2010. In NBIM, the number of employees increased by 37, to a total of 315 at year-end. Growth in this part of operations is expected to continue in 2012. The number of employees in central banking operations is approximately unchanged. The Bank has a very diverse workforce, with employees from a total of 31 nations.

In the investment management area, the emphasis in 2011 was on boosting analysis capacity. The leader group was also reorganised to improve follow-up of the investment area. The Executive Board issued new guidelines and policies for remuneration of employees of NBIM that are in line with the Ministry of Finance's Regulation of 1 December 2010 relating to remuneration arrangements in financial institutions, investment firms and firms that manage securities funds.

In central banking operations, the emphasis is on developing Norges Bank as a transparent and well run central bank. A reorganisation project has been launched to realise synergies in core functions and to facilitate more effective solutions between policy areas and administrative services.

### **Gender equality and diversity**

Norges Bank focuses on gender equality and diversity. The Bank shall give women and men the same opportunities for salary, professional and personal development and advancement. Pay systems are non-discriminatory and offer equal opportunities to all.

The Bank's gender equality programme sets targets for the proportion of women in various job categories. At end-2011, the proportion of women employees in Norges Bank as a whole was 35%. The target is 40%. Under the Bank's action plan for equality and diversity, there is a systematic effort to attract and recruit more women. Career development and management programmes are aimed at increasing the number of women in managerial posts. Flexitime ar-

rangements at the Bank are intended to make the job situation easier for parents of young children.

Norges Bank has a zero-tolerance policy towards all forms of discrimination. The Executive Board follows the progress of gender equality efforts at Norges Bank through regular reports from the administration.

### Health, safety and environment

Norges Bank attaches considerable importance to ensuring a high level of safety in all areas of the Bank's operations. The objective is to protect the lives and health of employees and associates, while securing the considerable assets managed by the Bank.

At year-end, no workplace accidents or injuries during working hours had been recorded, or accidents/injuries of a serious nature while travelling to or from work. No injuries or accidents have been reported to the Norwegian Labour Inspection Authority as occupational injuries.

The quality of the physical working environment is measured regularly by various climate surveys. Norges Bank's health service provides aids and equipment as needed. The building has been evaluated in the light of universal design requirements. New guidelines for universal design will be applied for new reconstruction projects.

The Bank's psychosocial working environment is measured primarily through employee health appraisal interviews and the annual working environment survey. In 2011, the survey revealed generally high job satisfaction among Bank employees, and the Bank's Working Environment Committee assesses the working environment and social climate as satisfactory.

### Sickness absence and an inclusive workplace

Sickness absence at the Bank is at a low, stable level. It is the Bank's aim for this figure not to rise. In 2011, sickness absence accounted for 2.7% of the total number of working days, unchanged from 2010. Of this, long-term absences (16 days or more) constituted 1.5%, compared with 1.4% in 2010. Employees with long-term absences are followed up individually and preventive measures implemented, in compliance with new rules.

Norges Bank is an inclusive workplace enterprise. This means that the Bank is committed to working to maintain sickness absence at a stable, low level, accommodating employees with needs for special adaptations and enabling older employees to extend their professional careers in line with national objectives.

### Ethical rules

For Norges Bank to be able to fulfil its responsibilities, the general public must have confidence that the Bank is well run and focuses on performing its duties in a proper manner. It is particularly important to the Executive Board that the Bank's employees in all areas conduct themselves with the necessary ethical awareness and that their loyalty is to Norges Bank as their employer.

In line with this, the Executive Board has established ethical principles for employees. These ethical principles are intended to create common attitudes towards ethical issues among all employees of Norges Bank. The principles serve as the basis for further rules and procedures laid down by the management of central banking operations and investment management, respectively.

Employees who normally have access to or work in investment services or management of financial instruments on behalf of the Bank or one of its customers are covered by special rules regarding own-account trading in Chapter 8 of the Securities Trading Act. Special ethical rules have also been laid down for members of the Executive Board.

In addition, the Executive Board has issued principles for internal reporting of censurable conditions at Norges Bank.

### External environment

Norges Bank's direct environmental impact is primarily related to greenhouse gas emissions and office waste. The Bank's indirect environmental impact derives from procurement of goods and services and standards for customers, suppliers and investment properties. Efforts to reduce power consumption continued in 2011, including from efficient control of lighting and ventilation systems. The Bank is working diligently to make its operations greener through a long-term building maintenance programme, including plans to replace the chillers in 2012/2013, with a focus on energy consumption and the proper type of refrigerant.

### Internal control and risk management

The Ministry of Finance has issued a regulation on risk management and internal control in Norges Bank, corresponding to a similar regulation for entities licensed by Finanstilsynet.

The Executive Board has issued general risk management policies for Norges Bank, and detailed risk management policies for central banking operations and investment



management, respectively. The two operational areas each have in place a unit to coordinate and follow up risk management and internal control. In addition, they each have a unit to ensure compliance with legislation and internal rules.

The Executive Board uses the audit committee to follow up risk management and internal control. In addition, internal audit supports the Executive Board in its follow-up of risk management and internal control by providing advice and independent assessments.

Risk management and internal control in Norges Bank are based on the management model that describes the organisational structure, management processes and internal policy documents. The governance structure for investment management has been defined in a separate document.

Reporting on the risk situation is an integral part of management processes and corporate governance. Central banking operations report on their risk situation twice a year, and investment management four times a year. Each year, the governor assesses whether internal control was implemented in a satisfactory manner. The internal audit submits an annual independent report on internal control at the Bank to the Executive Board. On the basis of reporting from management and internal audit, the Executive Board submits to the Supervisory Council an annual assessment of the risk situation in the Bank.

## More about financial risk

Norges Bank's primary exposures to financial risk involve market risk, credit risk, counterparty risk and foreign exchange risk through the management of foreign exchange reserves. In addition, the Bank is exposed to credit risk associated with lending to banks. The Bank's borrowings primarily comprise deposits from banks and the government.

The composition of the foreign exchange reserves portfolios and associated risk is primarily determined by the benchmark index defined by the Executive Board. The Executive Board's investment mandates for the portfolios contain a number of guidelines and restrictions. These restrictions regulate the extent to which active management may be engaged in, in addition to rule-based capital allocations. The portfolios primarily contain equities and government and government-related bonds, but also corporate and securitised bonds. In addition, they contain forward exchange contracts, futures contracts and equity swaps. Norges Bank measures the absolute and relative market risk related to management of the portfolios.

Norges Bank's market risk is the risk of changes in the value of the portfolios due to movements in interest rates and equity prices. Norges Bank's credit risk is the risk of losses if issuers of fixed income instruments default on their payment obligations to Norges Bank. Norges Bank performs credit assessments of interest-bearing securities and counterparties. Loans to banks are provided against collateral in the form of approved securities. Norges Bank's counterparty risk is the risk of incurring loss if a counterparty is declared bankrupt or cannot otherwise perform its contractual obligations. Counterparty risk includes risk associated with the bankruptcy of a counterparty, default risk and settlement risk. Counterparty risk is controlled and countered as far as possible given the investment strategies. Norges Bank's currency risk is the risk of changes in foreign exchange rates. Norges Bank is not hedged against foreign exchange rate fluctuations. As the central bank, Norges Bank is not exposed to liquidity risk.

Norges Bank has no exposure to financial risk in the management of the Government Pension Fund Global. For further discussion, see Note 1, Section 2 in Part II.

## Report on the financial statements

### Report on the annual financial statements

As from 2011, the annual financial statements of Norges Bank are prepared in accordance with the Norwegian Accounting Act and the Regulation relating to annual financial statements for Norges Bank. The regulation is in force as from the 2011 accounting year and requires Norges Bank to prepare its financial statements in accordance with the International Financial Reporting Standards (IFRSs) that have been endorsed by the EU, but lays down specific requirements for the presentation of the investment portfolio of the Government Pension Fund Global and subsidiaries, which exclusively comprise investments in the investment portfolio. The regulation requires Norges Bank's financial statements to include the financial reporting of the investment portfolio of the Government Pension Fund Global, which shall also be prepared in accordance with IFRS. The adoption of a new financial reporting framework for Norges Bank has entailed transition effects, which are discussed in Note 1 to the annual financial statements.

Foreign exchange reserves constitute Norges Bank's main assets (excluding the Government Pension Fund Global, which has no effect on the Bank's results). Norges Bank holds interest-free liabilities in the form of notes and coins

in circulation. In addition, the Bank holds domestic deposits from the government and other banks. This balance sheet composition normally generates a positive return over time. The Bank's assets are invested primarily in foreign currency, whereas its liabilities are primarily in NOK. This gives rise to a currency risk that requires sufficient equity. As from 2011, Norges Bank is presenting separate columns in the income statement, balance sheet and statement of cash flows showing the Bank's foreign exchange reserves. Cash flows at Norges Bank are primarily of an operational nature.

Norges Bank's income primarily comprises net income from financial instruments related to foreign exchange reserves. Gains and losses arise from changes in foreign exchange rates, changes in equity prices and changes in interest rates that affect bond prices. Norges Bank's results depend on developments in these parameters, which can cause substantial yearly fluctuations in net income.

For 2011, Norges Bank income statement shows a profit of NOK 9.5bn, compared with a profit of NOK 12.6bn for 2010. Total comprehensive income for 2011 is a profit of NOK 8.4bn, compared with a profit of NOK 13.0bn for 2010.

Net income from financial instruments in the international money markets related to the Bank's foreign exchange reserves was a gain of NOK 11.9bn in 2011, compared with NOK 13.1bn in 2010. A portion of this net income is due to the depreciation of the Norwegian krone against most of the principal currencies in the foreign exchange reserves, which, when translated into NOK, resulted in a foreign exchange gain of NOK 6.2bn in 2011. In 2010, the appreciation of the krone resulted in a foreign exchange loss of NOK 3.9bn for the foreign exchange reserves. Gains and losses arising from changes in the krone exchange rate have no effect on the international purchasing power of the foreign exchange reserves.

Interest payments to the Treasury amounted to NOK 2.1bn in 2011. In 2010, total interest expenses to the Treasury amounted to NOK 1.7bn.

Changes in actuarial gains and losses for the Bank's pension benefit obligations amounted to NOK 1.1bn in 2011, and NOK 0.4bn in 2010.

The Adjustment Fund stood at NOK 64.0bn at end-2010. After year-end allocations for 2011, the Adjustment Fund amounted to NOK 72.6bn. The Ministry of Finance has stipulated the amount that Norges Bank may allocate to the Adjustment Fund as a buffer against changes in exchange rates and securities prices (see "Distribution of profit", below). The size of the foreign exchange reserves and domestic claims at year-end provide a basis for allocating up to NOK 110.2bn to the Adjustment Fund.

Norges Bank's total assets were NOK 3 652bn at end-2011. Norges Bank's financial statements include the krone account and investment portfolio of the Government Pension Fund Global, which accounts for approximately 91% of the balance sheet. The Government Pension Fund Global's krone deposit is a liability item on Norges Bank's balance sheet and at year-end was NOK 3 309bn. The equivalent amount of the krone deposit is invested abroad by Norges Bank in an earmarked investment portfolio. The return earned on the investment portfolio is transferred to the krone account of the Government Pension Fund Global. Costs incurred by Norges Bank in connection with management of the Government Pension Fund Global are reimbursed by the Ministry of Finance up to a limit. Financial reporting for the investment portfolio is presented in Note 24 pursuant to the provisions of Chapter 3 of the Regulation relating to annual financial statements for Norges Bank.

### Distribution of profit

Pursuant to the Norges Bank Act of 24 May 1985, guidelines for allocation and distribution of Norges Bank's profit were originally approved by the Council of State on 7 February 1986.

1. Allocations shall be made from Norges Bank's profit to the Adjustment Fund until the Fund has reached 5% of the Bank's holdings of Norwegian securities and 40% of the Bank's net foreign exchange reserves, excluding the immunisation portfolio and capital managed for the Government Petroleum Fund (now called the Government Pension Fund Global), other claims/liabilities abroad or any other commitments that the Executive Board considers to involve a not insignificant exchange risk.

The immunisation portfolio is that part of Norges Bank's foreign exchange reserves that is included in a separate portfolio. The return on this portfolio will be credited to/debited from the Treasury in the accounts of the same year. The same applies to the Government Petroleum Fund portfolio.

If the size of the Adjustment Fund exceeds the levels specified in point 1, first paragraph, the surplus shall be reversed to profit or loss.

2. If the Adjustment Fund falls below 25% of the Bank's net foreign exchange reserves excluding the immunisation portfolio and capital managed by the Government Petroleum Fund and other claims/liabilities abroad at the end of

the year, available capital shall be reversed from the Transfer Fund to Norges Bank's financial statements until the Adjustment Fund reaches full size according to point 1.

3. Any profit after provisions to or transfers from the Adjustment Fund shall be allocated to the Transfer Fund.
4. Any loss following the allocations described in point 2 shall be covered by transfers from the Adjustment Fund.
5. In connection with the closing of the books each year, an amount equal to one third of the capital in the Transfer Fund shall be transferred to the Treasury.<sup>1</sup>

In accordance with the guidelines and the transition to IFRS, the Executive Board proposes the following transfers and allocations:

All remaining other reserves, NOK 205m, are to be transferred in their entirety to the Adjustment Fund as required by the adoption of IFRS. In accordance with point 1, the profit after other allocations, NOK 8 376m, is to be transferred to the Adjustment Fund. As there are no funds in the Transfer Fund, no transfer will be made to the Treasury.

Oslo, 29 February 2012

Øystein Olsen  
*(Chair)*

Jan Fredrik Qvigstad  
*(Deputy Chair)*

Ida Helliesen

Liselott Kilaas

Egil Matsen

Brit K. Rugland

Eirik Wærness

Jan Erik Martinsen  
*(Employee representative)*

Jens Olav Sporastøyl  
*(Alternate employee representative)*

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<sup>1</sup> The Government Petroleum Fund has been renamed the Government Pension Fund Global. The immunisation portfolio was eliminated in 2003

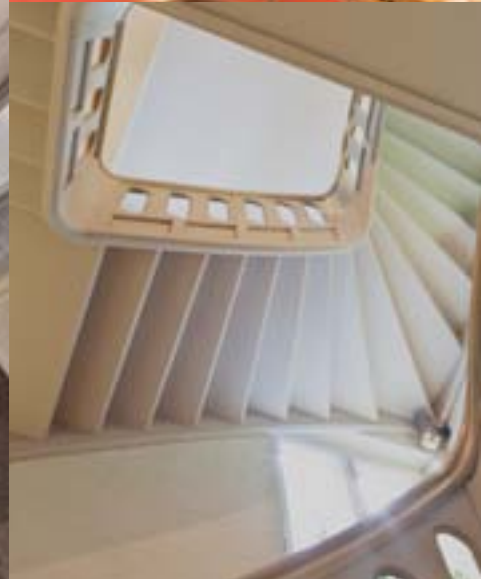
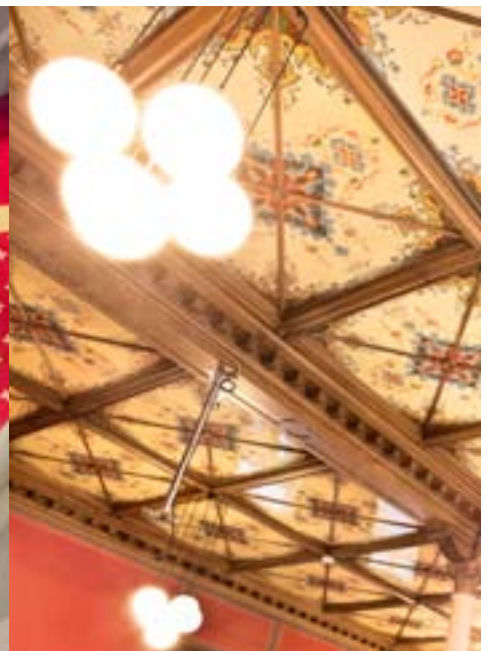


**PRESERVING  
RÅDHUSGATA 10, 12 AND 14  
AND KIRKEGATEN 6**

The buildings in Rådhusgata date from the reconstruction of the town after the fire in 1624. That same year, King Christian IV planned the new town Christiania, and the urban core was moved from Bjørvika to Kvadraturen.

Rådhusgata 10, 12 and 14 were purchased to be incorporated into the new headquarters along with Kirkegata 6 (from 1850–60), which previously housed Andresens Bank. All four buildings are listed.





Extensive restoration work began in 1978–80 in collaboration with the national and local cultural heritage offices. Today, Rådhusgata 10 and 12 and Kirkegata 6 are used for offices, while Rådhusgata 14 is used for the Bank's receptions.

The gable end of Rådhusgata 14, which owing to its architectural significance was almost the only element to remain intact during restoration, can be seen abutting the new building.

The contour of the building's original gable, the covered gallery and a rear structure are visible.

1986  
2011

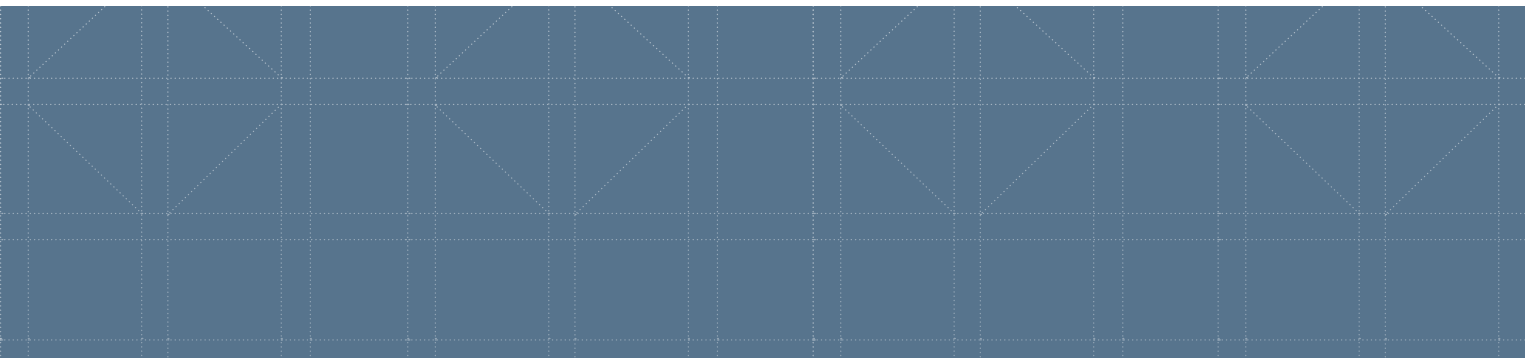


## GEOMETRIC FORMS

The building typifies the architectural style called structuralism, with a substantial content of prefabricated elements. Characteristic of the building's design is a structure based on a 90 cm x 90 cm construction module.

The octagonal form was adopted early for the column sections for functional reasons in order to accommodate ventilation ducts. The octagon became an aesthetic element, which along with the square creates variety and a wealth of form and gives





rise to a leitmotif – a molecular structure – that is the building's signature stamp. The octagon is consistently applied and reflected in bearing columns, stone paving, lifts, outdoor plantings and flower pots.



1986  
2011



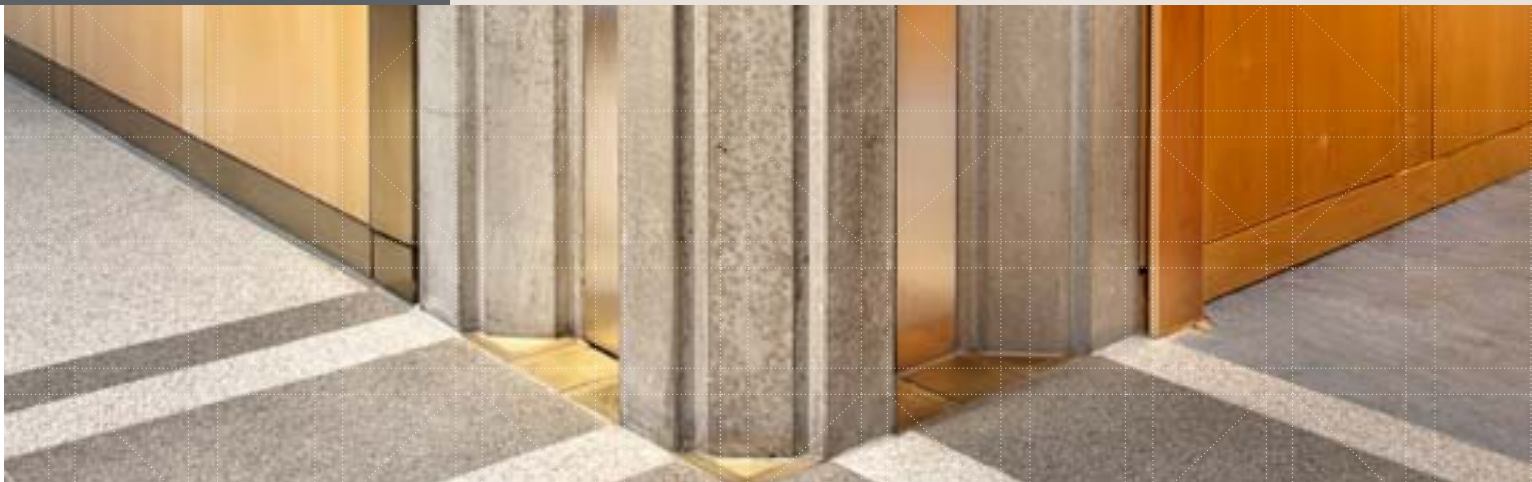
## CHOICE OF MATERIALS

An important criterion for the building was quality. This was expressed in the choice of materials.

These include stone (Carrarra marble and granite in three colours: pink Røyken granite, white Støren granite and dark Hauge granite),

concrete, metal (copper, brass and steel) and wood (beech, white laminate and merbau parquet).

Outside, the façade is composed of Røyken granite combined with copper. Inside, stone is the primary material for stairways and corridor zones. Beech and







white laminate are used in offices as a contrast with the stark marble stairwells. Inside, the copper is replaced by brass, which is supplemented with steel. Stainless steel is a recurring element accenting concrete columns and beams in walls and ceilings, while brass marks the position of

load-bearing structures. Concrete columns are visible throughout the interior.

The interplay of materials creates contrasts between hot and cold, while marking the different zones in the building.





## EXTERIOR SPACES

The open spaces between the arms of the building are designed as gardens. They create a pleasant atmosphere and are intended to help people orient themselves in the block. The gardens can be enjoyed by strolling about in them, but are also visible

from inside: from the storey the garden is located on or from the galleries, stairwells and offices on higher floors. The gardens are composed of graphical elements and are variations on the building's geometric theme.





The garden spaces differ in character according to function, location, light conditions and size and represent different combinations of the main components water, rock, vegetation and light. To distinguish south from north and east from west, the motifs of some of

the gardens occur in mirror-image pairs. The gardens are in and of themselves an essential part of the building's ornamentation.

1986  
2011

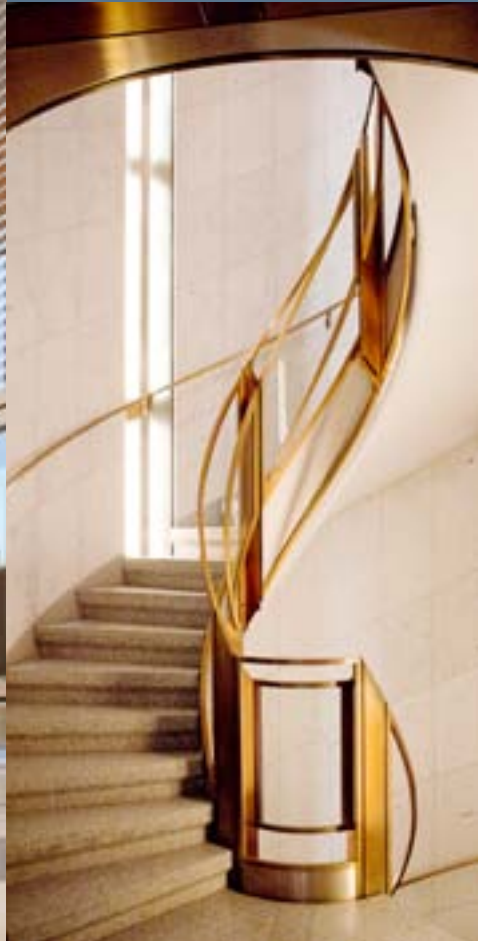


## STAIRWELLS AND CORRIDORS

The floor tiles in the corridors are composed of light and dark granite, with the dark granite signalling an intersecting corridor or access to a different level.

The design of the stairs is important. There are two kinds of stairwells in the building: rectangular main stairs in the middle of the block, and spiral staircases in the outer corners of the block.

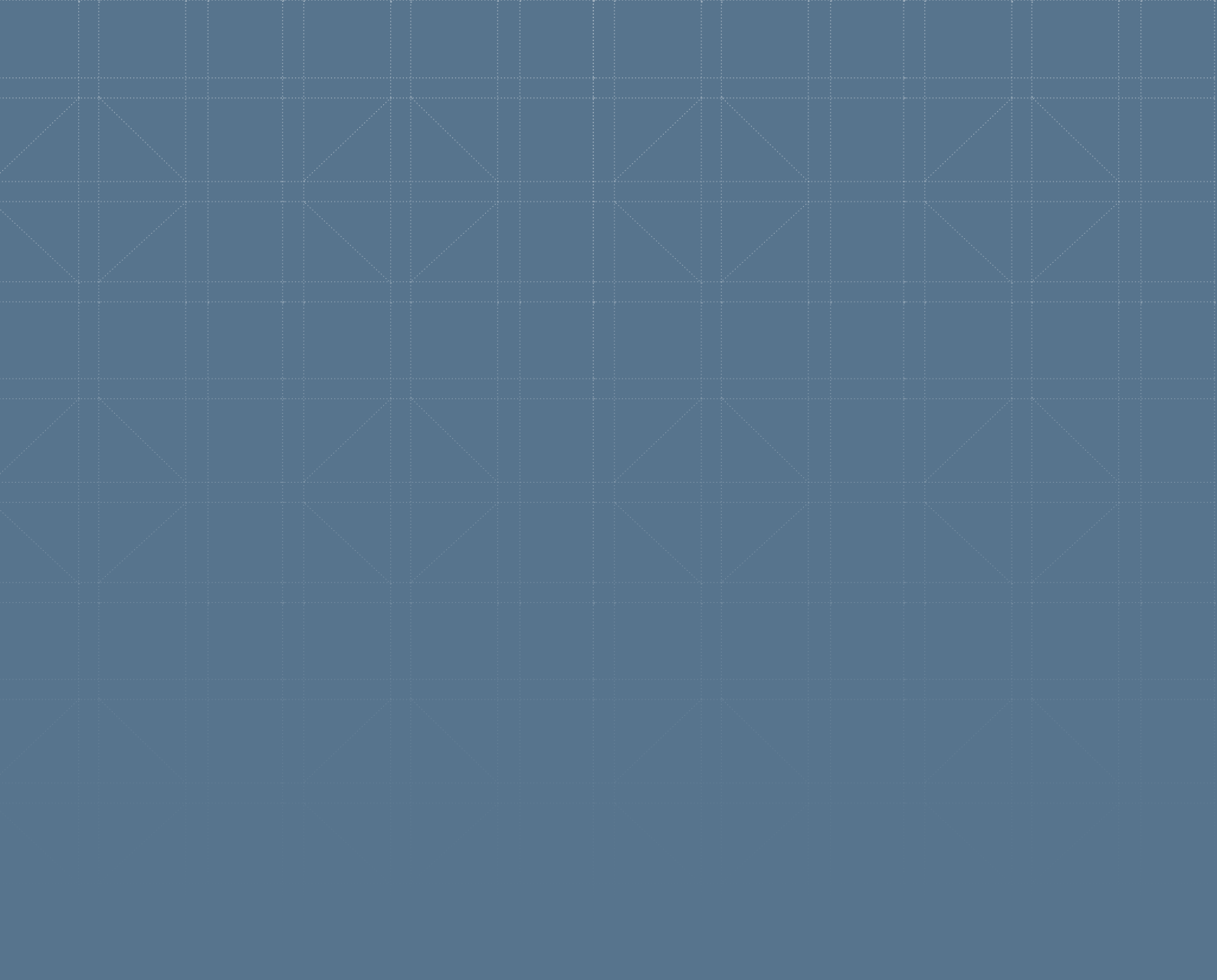


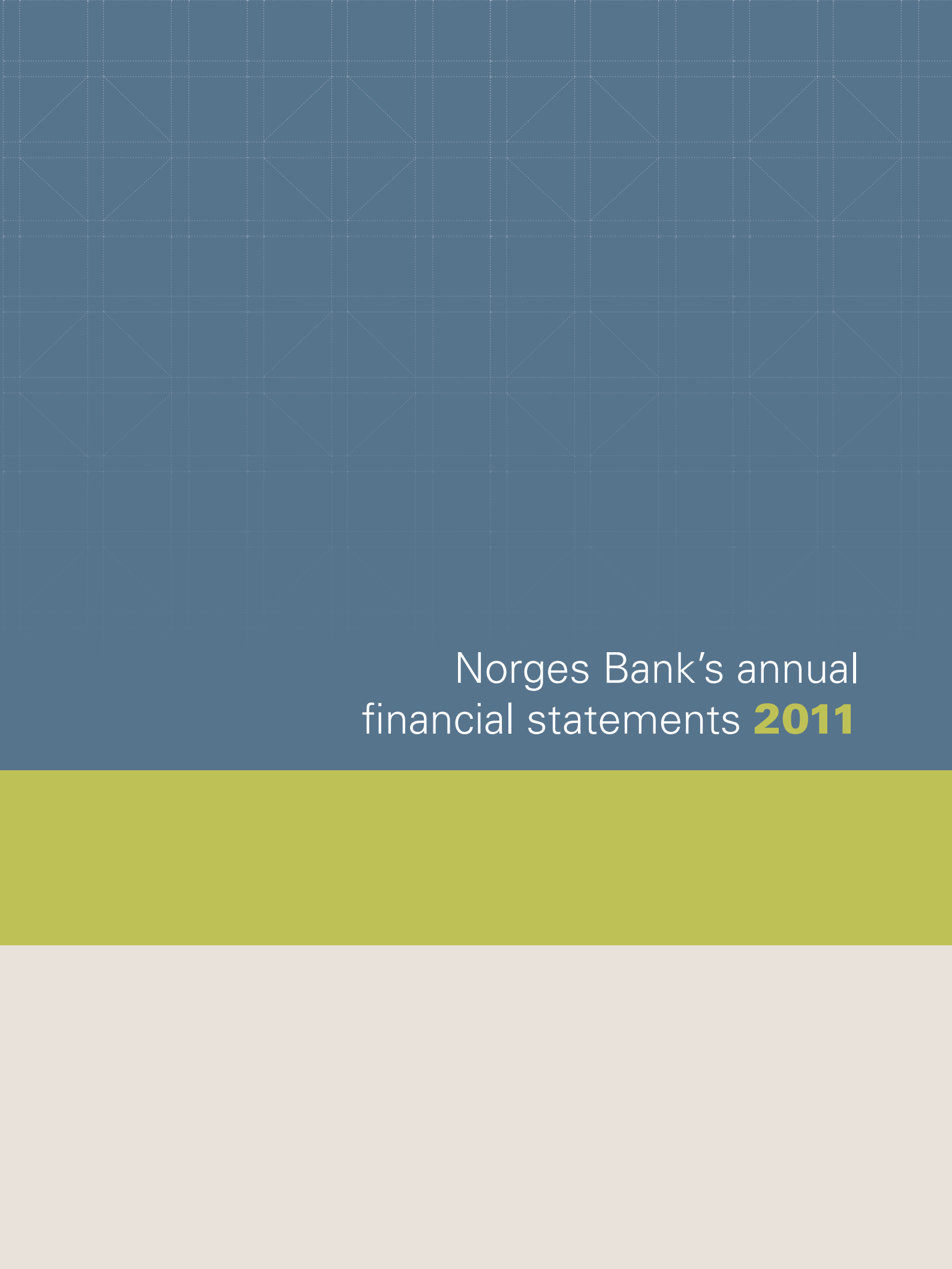


The materials in the stairwells are marble, granite and brass. The marble work in the spiral staircases is precision work, and in order to accommodate the spiral stairs, no two tiles are alike.

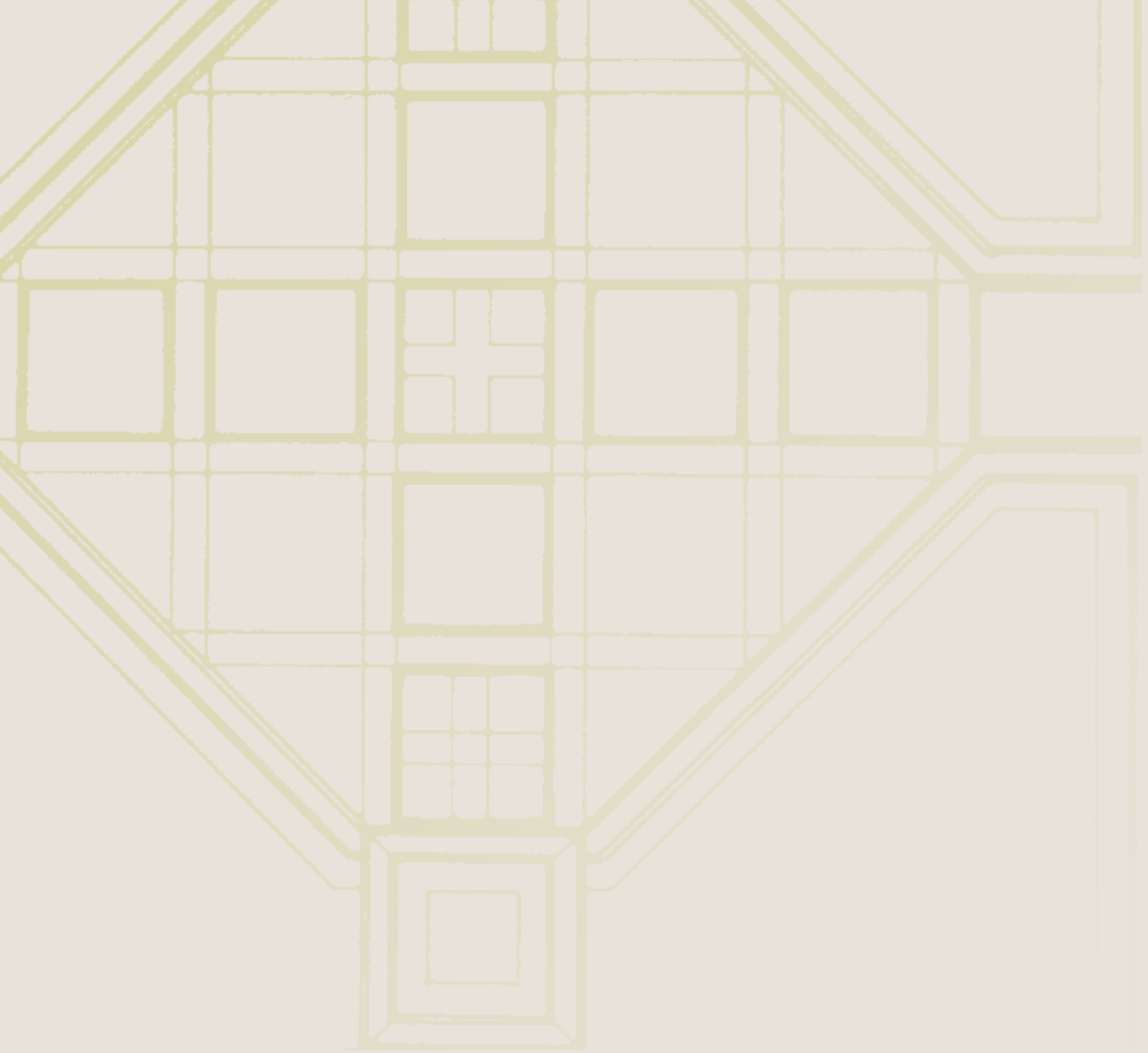


1986  
2011





Norges Bank's annual  
financial statements **2011**





# Income statement

Amounts in NOK million

	Note	2011	2010	2011 Of which foreign exchange reserves	2010 Of which foreign exchange reserves
<b>NET INCOME FINANCIAL INSTRUMENTS</b>					
Interest income from deposits and claims	3	111	22	11	22
Interest income from lending to banks	3	946	1 935	-	-
Interest income, lending associated with reverse repurchase agreements	3	105	129	105	129
Net income/expenses and gains/losses from:					
Equities	3	-6 247	10 150	-6 247	10 150
Bonds and other fixed income securities	3	11 773	6 990	11 773	6 990
Financial derivatives	3	91	-263	91	-263
Interest expense repurchase agreements	3	29	41	22	41
Interest expense paid on deposits from banks and Treasury	3	2 081	1 702	-	-
Share dividends from BIS	3	22	56	-	-
Net interest income from claims on/liabilities to the International Monetary Fund	14	31	13	-	-
Interest income from long-term lending	3	91	58	-	-
Foreign exchange gains/losses	3	5 414	-3 951	6 169	-3 895
<b>Net income from financial instruments</b>		<b>10 227</b>	<b>13 396</b>	<b>11 879</b>	<b>13 092</b>
<b>MANAGEMENT OF THE INVESTMENT PORTFOLIO OF THE GOVERNMENT PENSION FUND GLOBAL</b>					
Total comprehensive income, investments for Government Pension Fund Global (GPF)	24	-39 583	252 416	-	-
Withdrawn from/Transferred to krone account GPF	24	39 583	-252 416	-	-
Of which management fees GPF	4	2 539	2 959	-	-
<b>Management of the investment portfolio of the Government Pension Fund Global</b>		<b>2 539</b>	<b>2 959</b>	-	-
<b>OTHER OPERATING INCOME</b>					
Other operating income	5	112	151	-	-
<b>Total other operating income</b>		<b>112</b>	<b>151</b>	-	-
<b>OTHER OPERATING EXPENSES</b>					
Personnel expenses	6	870	909	-	-
Other operating expenses	7	2 411	2 944	-	-
Depreciation, amortisation and impairment losses	17	93	77	-	-
<b>Total other operating expenses</b>		<b>3 374</b>	<b>3 930</b>	-	-
<b>Profit for the period</b>		<b>9 504</b>	<b>12 576</b>	<b>11 879</b>	<b>13 092</b>
<b>STATEMENT OF COMPREHENSIVE INCOME</b>					
Profit for the period		9 504	12 576	11 879	13 092
Change in actuarial gains/losses	21	-1 128	416	-	-
<b>Total comprehensive income</b>		<b>8 376</b>	<b>12 992</b>	<b>11 879</b>	<b>13 092</b>

# Balance sheet

Amounts in NOK million

ASSETS	Note	2011	2010	2011 Of which foreign exchange reserves	2010 Of which foreign exchange reserves
<b>FINANCIAL ASSETS</b>					
Deposits in banks		11 790	952	11 713	895
Lending associated with reverse repurchase agreements	10	15 964	53 760	15 964	53 760
Unsettled trades		162	1 972	162	1 972
Equities	11	90 778	92 324	90 778	92 324
Equities lent	12	0	1 567	0	1 567
Bonds and other fixed income instruments	11	153 736	117 412	153 736	117 412
Bonds lent	12	71	24 834	71	24 834
Financial derivatives	13	3	26	3	26
Claims on the International Monetary Fund	14	36 113	32 328	-	0
Lending to banks	15	25 241	60 057	-	-
Other financial assets	16	7 052	9 960	42	67
<b>Total financial assets</b>	<b>8,9</b>	<b>340 910</b>	<b>395 192</b>	<b>272 469</b>	<b>292 857</b>
<b>INVESTMENTS, GOVERNMENT PENSION FUND GLOBAL</b>					
Investments, Government Pension Fund Global	24	3 309 033	3 074 461	-	-
<b>Total investments, Government Pension Fund Global</b>		<b>3 309 033</b>	<b>3 074 461</b>	-	-
<b>NON-FINANCIAL ASSETS</b>					
Other non-financial assets	17	1 855	1 912	-	-
<b>Total non-financial assets</b>		<b>1 855</b>	<b>1 912</b>	-	-
<b>TOTAL ASSETS</b>		<b>3 651 798</b>	<b>3 471 565</b>	<b>272 469</b>	<b>292 857</b>

Amounts in NOK million

LIABILITIES AND EQUITY	Note	2011	2010	2011 Of which foreign exchange reserves	2010 Of which foreign exchange reserves
<b>FINANCIAL LIABILITIES</b>					
Short-term borrowing		-	-	-	-
Borrowing associated with repurchase agreements	10	137	14 432	137	14 432
Cash collateral received	12	72	17 893	72	17 893
Unsettled trades		9 722	470	9 722	470
Short-sale bonds	11	0	1 492	0	1 492
Financial derivatives	13	51	213	51	213
Other financial liabilities	18	2 684	405	3	2
Liabilities to the International Monetary Fund	14	26 720	25 808	-	-
Deposits from banks, etc.	3,19	92 134	79 898	-	-
Deposits from the Treasury	3	81 673	136 851	-	-
Notes and coins in circulation	20	54 766	53 928	-	-
<b>Total financial liabilities</b>	<b>8,9</b>	<b>267 959</b>	<b>331 390</b>	<b>9 985</b>	<b>34 502</b>
<b>DEPOSITS IN KRONE ACCOUNT GOVERNMENT PENSION FUND GLOBAL</b>					
Deposits in krone account Government Pension Fund Global	24	3 309 033	3 074 461	-	-
<b>Total deposits in krone account Government Pension Fund Global</b>		<b>3 309 033</b>	<b>3 074 461</b>	-	-
<b>NON-FINANCIAL LIABILITIES</b>					
Pensions	21	1 609	674	-	-
Other liabilities		632	851	-	-
<b>Total non-financial liabilities</b>		<b>2 241</b>	<b>1 525</b>		
<b>Total liabilities</b>		<b>3 579 233</b>	<b>3 407 376</b>	<b>9 985</b>	<b>34 502</b>
<b>EQUITY</b>					
Equity		72 565	64 189	-	-
<b>Total equity</b>		<b>72 565</b>	<b>64 189</b>	-	-
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>3 651 798</b>	<b>3 471 565</b>		
<b>TOTAL FOREIGN EXCHANGE RESERVES</b>				<b>262 484</b>	<b>258 355</b>

Oslo, 29 February 2012

Øystein Olsen  
(Chair)

Jan Fredrik Qvigstad  
(Deputy Chair)

Ida Helliesen

Liselott Kilaas

Egil Matsen

Brit K. Rugland

Eirik Wærness

Jan Erik Martinsen  
(Employee representative)

Jens Olav Sporastøyl  
(Alternate employee representative)

# Statement of cash flows

Amounts in NOK million (inflows +) / outflows (-)

	2011	2010	2011 Of which foreign exchange reserves	2010 Of which foreign exchange reserves
<b>Operating activities</b>				
Interest received on deposits in banks	3 421	15	3 421	15
Net cash flows received in connection with reverse repurchase agreements	44 059	-3 601	44 059	-3 601
Net cash flows arising from purchases and sales of equities	-2 855	-2 858	-2 855	-2 858
Net cash flows arising from purchases and sales of bonds and other fixed income instruments	-1 432	-18 854	-1 432	-18 854
Net cash flows arising from financial derivatives	-50	-128	-19	-139
Net cash flows related to claims on and liabilities to the International Monetary Fund	-2 658	-2 543	-	-19
Net cash flows arising from lending to banks	34 830	14 828	-	-
Dividends received from investments in equities	2 272	2 384	2 271	2 384
Interest received on bonds and other fixed income instruments	4 423	5 257	4 423	5 257
Fees received in connection with equity and bond lending	73	107	73	107
Interest received on lending to banks	932	2 493	-	-
Outflows associated with borrowing	-	-7	-	-7
Net cash flows related to repurchase agreements	-14 033	5 557	-14 033	5 557
Net cash flows related to deposits in banks	12 216	-406	-	-
Inflows from the Treasury to the Government Pension Fund Global	-274 155	-165 392	-	-
Net cash flows from the Treasury excl. inflows to the Government Pension Fund Global	218 978	164 207	-	-
Interest paid on banks' deposits	-1 137	-901	-	-
Interest paid on government's deposits	-917	-780	-	-
Net cash flows related to notes and coins in circulation	813	-393	-	-
Cash collateral received/paid related to securities lending, derivatives and repurchase agreements	-17 822	1 160	-17 822	1 160
Cash flows related to other financial assets and other financial liabilities	4 027	-2 292	5 885	-1 132
Management fee received from the Government Pension Fund Global	2 960	3 228	2 960	3 228
Other operating income received	145	193	-	-
Cash outflows related to personnel and other expenses	-3 393	-3 591	-	-
<b>Net cash outflows from operating activities</b>	<b>10 697</b>	<b>-2 317</b>	<b>26 931</b>	<b>-8 902</b>
<b>Investing activities</b>				
Net cash flows related to non-financial assets and liabilities	-337	-185	-	-
<b>Net cash flows from investing activities</b>	<b>-337</b>	<b>-185</b>	<b>-</b>	<b>-</b>
<b>Financing activities</b>				
Net inflows to foreign exchange reserves	-	-	-16 592	6 446
<b>Net cash flows from financing activities</b>	<b>-</b>	<b>-</b>	<b>-16 592</b>	<b>6 446</b>

Amounts in NOK million (inflows (+) / outflows (-))

	2011	2010	2011 Of which foreign exchange reserves	2010 Of which foreign exchange reserves
<b>Net change in cash and cash equivalents</b>				
<b>Cash and cash equivalents at 1 January</b>	<b>952</b>	<b>4 143</b>	<b>895</b>	<b>4 040</b>
Net cash payments in the period	10 360	-2 502	10 339	-2 456
Foreign exchange gains/losses on cash and cash equivalents	478	-689	479	-689
<b>Cash and cash equivalents at 31 December</b>	<b>11 790</b>	<b>952</b>	<b>11 713</b>	<b>895</b>
<b>Cash and cash equivalents comprise:</b>				
Deposits in banks	11 790	952	11 713	895
Short-term borrowing	-	-	-	-
<b>Total</b>	<b>11 790</b>	<b>952</b>	<b>11 713</b>	<b>895</b>

## Statement of changes in equity

Amounts in NOK million

	Adjustment Fund	Transfer Fund	Other reserves	Total equity
31 December 2009*	51 298	-	983	<b>52 281</b>
Transition effects (IFRS)	-	-	- 1 047	<b>- 1 047</b>
<b>1 January 2010 (IFRS)</b>	<b>51 298</b>	<b>-</b>	<b>- 64</b>	<b>51 234</b>
Charge to Revaluation Fund 2010	-	-	- 37	<b>- 37</b>
Total comprehensive income	-	-	12 992	<b>12 992</b>
Transfers to Adjustment Fund	12 686	-	- 12 686	-
<b>31 December 2010</b>	<b>63 984</b>	<b>-</b>	<b>205</b>	<b>64 189</b>
1 January 2011	63 984	-	205	<b>64 189</b>
Total comprehensive income	8 376	-	-	<b>8 376</b>
Transfers to Adjustment Fund	205	-	- 205	-
<b>31 December 2011</b>	<b>72 565</b>	<b>-</b>	<b>-</b>	<b>72 565</b>

\* In accordance with the accounting policies for Norges Bank that were previously adopted by the Supervisory Council.

# Notes

## **Note 1** **Transition to International Financial Reporting Standards (IFRS) and accounting policies**

### **1. INTRODUCTION**

Norges Bank is Norway's central bank. The Bank shall promote economic stability in Norway. Norges Bank has executive and advisory responsibilities in the area of monetary policy and is responsible for promoting robust and efficient payment systems and financial markets. Norges Bank manages Norway's foreign exchange reserves and the Government Pension Fund Global.

Pursuant to Section 30 second paragraph of the Norges Bank Act, the annual financial statements of Norges Bank have been prepared in accordance with the Accounting Act and the Regulation concerning annual financial reporting for Norges Bank, which has been laid down by the Ministry of Finance. The regulation applies as from the 2011 accounting year and requires that Norges Bank's financial statements are prepared in accordance with International Financial Reporting Standards as endorsed by the EU (IFRS), but sets certain specific requirements for the presentation of the investment portfolio of the Government Pension Fund Global and subsidiaries that exclusively constitute investments as part of the management of the investment portfolio. The regulation requires Norges Bank's financial statements to include the financial reporting of the investment portfolio of the Government Pension Fund Global, which shall also be prepared in accordance with IFRS.

Norges Bank prepares annual financial statements with a closing date of 31 December that includes financial reporting for the investment portfolio of the Government Pension Fund Global. In addition, Norges Bank prepares interim financial statements, which solely comprise the quarterly financial reporting of the investment portfolio of the Government Pension Fund Global, with closing dates of 31 March, 30 June and 30 September.

The annual financial statements of Norges Bank for 2011 were approved by the Executive Board on 29 February 2012 and adopted by the Supervisory Board on 15 March 2012.

## **2. NORGES BANK AND THE GOVERNMENT PENSION FUND GLOBAL**

The Government Pension Fund Global is invested in its entirety outside Norway. The Storting has established the legal framework in the Government Pension Fund Act, and the Ministry of Finance has formal responsibility for investment management. The Government Pension Fund Global shall support saving to finance future government expenditure and underpin long-term considerations relating to the use of Norway's petroleum revenues.

The Ministry of Finance has deposited funds for investment in a krone account in Norges Bank specified for this purpose. The corresponding value of the krone account constitutes an investment portfolio managed by Norges Bank in accordance with the Act relating to the Government Pension Fund and management mandate for the Government Pension Fund Global issued by the Ministry of Finance. The Executive Board has delegated day-to-day asset management to the Bank's asset management area, Norges Bank Investment Management (NBIM).

Norges Bank is not exposed to financial risk from its management of the Government Pension Fund Global. The return on the portfolio is transferred in its entirety to the krone account and does not affect total comprehensive income or equity in Norges Bank. The net value of the investment portfolio is recognised as an asset on a separate line in the Norges Bank balance sheet. The krone account is recognised as a liability in the same amount to the Ministry of Finance in the Norges Bank balance sheet.

### **3. TRANSITION TO IFRS**

#### **3.1 Transition effects for the investment portfolio of the Government Pension Fund Global**

Adoption of IFRS has not required any changes in recognition, measurement or classification for assets and liabilities or changes in the IFRS income statement for the investment portfolio of the Government Pension Fund Global for comparative periods in 2010. Accordingly, owners' capital has remained unchanged in all periods. In accordance with IAS 1 Presentation of Financial Statements, a separate statement of comprehensive income is included, and as at the reporting date, comprises only foreign exchange translation differences that arise upon consolidation of foreign subsidiaries in Norwegian kroner. Also included is a statement of changes in equity in accordance with IAS 1, in that this information has now been moved from a note disclosure to a separate statement as required by the adoption of IFRS. The previous financial reporting framework

did not require presentation of a statement of cash flows for the investment portfolio of the Government Pension Fund Global. As part of the transition to IFRS, such a statement has been presented, along with comparative amounts for 2010.

### 3.2 Transition effects for Norges Bank

Adoption of IFRS has entailed changes in recognition and measurement and classification of income, assets and liabilities for Norges Bank. Amounts in the financial statements for 2010 have been restated accordingly. The transition also requires Norges Bank to present statements of comprehensive income, cash flows and changes in equity.

Adoption of IFRS has resulted in a transition effect for Norges Bank's pension benefit obligation on account of a change in method for determining the discount rate and a change in method for recognition of actuarial gains and losses. The discount rate was previously set as the yield on government bonds plus a risk premium, but after the adoption of IFRS the yield on government bonds is used. Further-

more, Norges Bank has recognised assets related to the Bank's collection of art and numismatic objects. This collection had not been recognised under the previous accounting policies and with the adoption of IFRS has been recognised at appraised cost.

All transition effects have been recognised as at 1 January 2010 and comprise the following items:

Amounts in NOK million	
1 Jan. 2010	
Increase in the pension benefit obligation related to a change in the discount rate	491
Recognition of actuarial loss	638
Recognition of collection of art and numismatic objects	- 82
<b>Total reduction in equity as a consequence of transition effects</b>	<b>1 047</b>

Effect of transition on equity in Norges Bank as at 1 January 2010:

Amounts in NOK million				
	Adjustment Fund	Transfer Fund	Other reserves	Total equity
31 December 2009*	51 298	-	983	52 281
Transition effect (IFRS)	-	-	- 1 047	- 1 047
<b>1 January 2010 (IFRS)</b>	<b>51 298</b>	<b>-</b>	<b>- 64</b>	<b>51 234</b>
Charge to Revaluation Fund 2010	-	-	- 37	- 37
Total comprehensive income	-	-	12 992	12 992
Transfers to Adjustment Fund	12 686	-	- 12 686	-
<b>31 December 2010</b>	<b>63 984</b>	<b>-</b>	<b>205</b>	<b>64 189</b>

\* In accordance with the accounting policies for Norges Bank that were previously adopted by the Supervisory Council.

### 3.3 Other changes related to adoption of IFRS

In connection with the adoption of IFRS, Norges Bank has chosen to implement a change in accounting policies related to recognition of pension benefit obligations. Under previous accounting policies, cumulative actuarial gains and losses that exceeded the greater of 10% of the benefit obligation or 10% of the fair value of plan assets may be unrecognised in profit or loss for the year in order to smooth the effects. As from 1 January 2011, changes in the obligation are fully recognised in total comprehensive income, with comparative amounts restated accordingly.

Norges Bank has also chosen to recognise all transition effects in other reserves. At the same time, this solution requires elimination of the Revaluation Fund under other reserves. The residual amount of other reserves has been transferred, in connection with the allocation of total comprehensive income, to the Adjustment Fund as at 31 December 2011.

Norges Bank has also chosen to use the liquidity presentation format. The result of this change is that international reserves may no longer be presented as a term directly in the balance sheet. As in previous years, international reserves are presented in the notes. At the same time, Norges Bank has chosen to include separate columns in its presentation format that specify Norges Bank's foreign exchange reserves.

### 3.4 Opening balance 2010

The opening balance for 2010 for Norges Bank appears below. Comparative amounts have been restated for the notes for the opening balance at 1 January 2010 for the accounting items for which there are transition effects. This pertains to Note 21 Pension benefit obligation and Note 17 Other non-financial assets.

Amounts in NOK million

ASSETS	Previous GAAP* in accordance with new presentation format 31 Dec. 2009	Reclassification effects	Transition effects IFRS	IFRS 1 Jan. 2010
<b>FINANCIAL ASSETS</b>				
Deposits in banks	4 415			4 415
Lending associated with reverse repurchase agreements	50 430			50 430
Unsettled trades	802			802
Equities	74 618			74 618
Equities lent	8 449			8 449
Bonds and other fixed income instruments	107 392			107 392
Bonds lent	18 138			18 138
Financial derivatives	364			364
Claims on the International Monetary Fund	18 145	12 214		30 359
Lending to banks	75 442			75 442
Other financial assets	7 857			7 857
<b>Total financial assets</b>	<b>366 052</b>	<b>12 214</b>	<b>-</b>	<b>378 266</b>
<b>INVESTMENTS FOR THE GOVERNMENT PENSION FUND GLOBAL</b>				
Investments for the Government Pension Fund Global	2 636 815			2 636 815
<b>Total investments for the Government Pension Fund Global</b>	<b>2 636 815</b>	<b>-</b>	<b>-</b>	<b>2 636 815</b>
<b>NON-FINANCIAL ASSETS</b>				
Other non-financial assets	2 170	-247	82	2 005
<b>Total non-financial assets</b>	<b>2 170</b>	<b>-247</b>	<b>82</b>	<b>2 005</b>
<b>TOTAL ASSETS</b>	<b>3 005 037</b>	<b>11 967</b>	<b>82</b>	<b>3 017 086</b>

\*In accordance with the accounting policies for Norges Bank that were previously adopted by the Supervisory Council.



Amounts in NOK million

LIABILITIES AND EQUITY	Previous GAAP* in accordance with new presentation format 31 Dec. 2009	Reclassification effects	Transition effects IFRS	IFRS 1 Jan. 2010
<b>FINANCIAL LIABILITIES</b>				
Short-term borrowing	272			272
Borrowing associated with repurchase agreements	8 633			8 633
Cash collateral received	16 734			16 734
Unsettled trades	1 528			1 528
Short-sale bonds	340			340
Financial derivatives	297			297
Other financial liabilities	368			368
Liabilities to the International Monetary Fund	14 155	12 214		26 369
Deposits from banks, etc.	80 312			80 312
Deposits from the Treasury	138 036			138 036
Notes and coins in circulation	54 303			54 303
<b>Total financial liabilities</b>	<b>314 978</b>	<b>12 214</b>	<b>-</b>	<b>327 192</b>
<b>DEPOSITS IN KRONE ACCOUNT GOVERNMENT PENSION FUND GLOBAL</b>				
Deposits in krone account Government Pension Fund Global	2 636 815			2 636 815
<b>Total deposits in krone account Government Pension Fund Global</b>	<b>2 636 815</b>	<b>-</b>	<b>-</b>	<b>2 636 815</b>
<b>NON-FINANCIAL LIABILITIES</b>				
Pensions	226	-247	1 129	1 108
Other liabilities	736			736
<b>Total non-financial liabilities</b>	<b>962</b>	<b>-247</b>	<b>1 129</b>	<b>1 844</b>
<b>Total liabilities</b>	<b>2 952 755</b>	<b>11 967</b>	<b>1 129</b>	<b>2 965 851</b>
<b>EQUITY</b>				
Equity	52 282		-1 047	51 235
<b>Total equity</b>	<b>52 282</b>	<b>-</b>	<b>-1 047</b>	<b>51 235</b>
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>3 005 037</b>	<b>11 967</b>	<b>82</b>	<b>3 017 086</b>

\*In accordance with the accounting policies for Norges Bank that were previously adopted by the Supervisory Council.

### 3.5 Restated income statement 2010

A restated income statement for Norges Bank for 2010 appears below

Amounts in NOK million

INCOME STATEMENT	Previous GAAP* in accordance with new presentation format 2010	Transition effects IFRS**	IFRS 2010
<b>NET INCOME FINANCIAL INSTRUMENTS</b>			
Interest income from deposits in banks and claims	22		22
Interest income from lending to banks	1 935		1 935
Interest income, lending associated with reverse repurchase agreements	129		129
Net income/expenses and gains/losses from:			-
Equities	10 150		10 150
Bonds and other fixed income securities	6 990		6 990
Financial derivatives	-263		-263
Interest expense repurchase agreements	41		41
Interest expense paid on deposits from banks and Treasury	1 702		1 702
Share dividends from BIS	56		56
Net interest income from claims on/liabilities to the International Monetary Fund	13		13
Interest income from long-term lending	58		58
Foreign exchange gains/losses	-3 951		-3 951
<b>Net income from financial instruments</b>	<b>13 396</b>	<b>-</b>	<b>13 396</b>
<b>MANAGEMENT OF THE INVESTMENT PORTFOLIO OF THE GOVERNMENT PENSION FUND GLOBAL</b>			
Total comprehensive income investments for Government Pension Fund Global (GPFG)	252 416		252 416
Withdrawn from/Transferred to krone account GPFG	-252 416		-252 416
Of which management fees GPFG	2 959		2 959
<b>Management of the investment portfolio of the Government Pension Fund Global</b>	<b>2 959</b>	<b>-</b>	<b>2 959</b>
<b>OTHER OPERATING INCOME</b>			
Other operating income	151		151
<b>Total other operating income</b>	<b>151</b>	<b>-</b>	<b>151</b>
<b>OTHER OPERATING EXPENSES</b>			
Personnel expenses	799	110	909
Other operating expenses	2 944		2 944
Depreciation, amortisation and impairment losses	114	-37	77
<b>Total other operating expenses</b>	<b>3 857</b>	<b>73</b>	<b>3 930</b>
<b>Profit for the year</b>	<b>12 649</b>	<b>-73</b>	<b>12 576</b>
<b>STATEMENT OF COMPREHENSIVE INCOME</b>			
Profit for the year	12 649	-73	12 576
Change in actuarial gains/losses	-	416	416
<b>Total comprehensive income</b>	<b>12 649</b>	<b>343</b>	<b>12 992</b>

\*In accordance with the accounting policies for Norges Bank that were previously adopted by the Supervisory Council.

\*\* Differences in income comprise pension expense, change in actuarial gains and reversal of previous Revaluation Fund.

## 4. ACCOUNTING POLICIES

### 4.1 Income statement, statement of comprehensive income and balance sheet

The income statement, statement of comprehensive income and the balance sheet have been prepared in accordance with IAS 1 Presentation of Financial Statements. The liquidity presentation format is used for the balance sheet. In addition, the share of total amounts in NOK related to foreign exchange reserves is presented in separate columns in Norges Bank's income statement and balance sheet. Foreign exchange reserves are to be used for foreign exchange market intervention as part of the implementation of monetary policy or to promote financial stability, and are divided between a long-term portfolio, a money market portfolio and a "petro" buffer portfolio.

### 4.2 Statement of cash flows

The statement of cash flows has been prepared in accordance with IAS 7 Statement of Cash Flows using the direct method, whereby major classes of cash receipts and cash payments are disclosed separately. Specific categories of cash flows, primarily arising from the purchase and sale of financial instruments, are shown on a net basis when appropriate. All investment activity is defined as operating activities. The management fee for the Government Pension Fund Global, which is charged to the investment portfolio and paid by the Ministry of Finance to Norges Bank, is also shown as an operating cash flow. Cash transfers to the Government Pension Fund Global's krone account, in the form of a contribution from the owner, are classified as a financing activity and presented as a transfer from the Norwegian government. The investment portfolio of the Government Pension Fund Global has no investing activities as defined in IAS 7. Pursuant to the Norges Bank Act, Norges Bank is responsible for issuing notes and coins and ensuring that society has access to and the necessary confidence in cash as a means of payment. For that reason, issuance of notes and coins is deemed an operating activity and not a financing activity.

Cash and cash equivalents comprise Deposits in banks and Short-term borrowing.

The statement of cash flows for Norges Bank shows no items for financing beyond equity transactions, if any.

### 4.3 Statement of changes in equity and owner's capital

Norges Bank presents a statement of changes in owner's capital (Government Pension Fund Global) and changes in equity. The statements have been prepared in accordance with IAS 1 Presentation of Financial Statements.

Owner's capital for the Government Pension Fund Global comprises contributed capital in the form of transfers from the Norwegian government and retained earnings in the form of total comprehensive income.

Norges Bank's equity comprises the Adjustment Fund, the Transfer Fund and Other reserves. The Adjustment Fund comprises the Bank's restricted equity, and the Transfer Fund comprises the basis for transfers to the Treasury. Norges Bank's capital is governed by guidelines for provisions and allocations laid down by the Council of State on 7 February 1986, most recently amended by Royal Decree of 6 December 2002.

### 4.4 Currency

Norges Bank's functional currency is the Norwegian krone (NOK). Transactions in foreign currency are recognised in the financial statements at the exchange rate prevailing on the transaction date. Assets and liabilities in foreign currencies are translated into Norwegian kroner using the exchange rate at the balance sheet date. The presentation currency for financial reporting is the Norwegian krone.

In the income statement, the foreign exchange element linked to realised and unrealised gains and losses on assets and liabilities is disaggregated and presented on a separate line. Foreign exchange adjustments for the period are estimated based on the cost in foreign currency and changes in exchange rates between the time of purchase, or the previous balance sheet date for financial instruments purchased in earlier periods, and the balance sheet date. At realisation the exchange rate at the transaction date is used.

Foreign subsidiaries that are consolidated into the investment portfolio's financial reporting and have a functional currency different from the one of Norges Bank are translated into Norwegian kroner. Income statements are translated at an average exchange rate for the period, and balance sheets are translated at the reporting period's closing rate. Any translation differences are included in Total comprehensive income and presented as Translation reserve arising from consolidation of foreign subsidiaries.

See also Note 2 Significant estimates and critical accounting judgements.

#### 4.5 Income and expenses

Interest income from deposits in banks, interest income from lending associated with reverse repurchase agreements and investments in bonds and other fixed income instruments is recognised when the interest is earned and classified in each of the respective lines in the income statement.

Dividends from investments in equity instruments are recognised as income when the dividends are formally approved by the shareholders' meeting or comparable responsible party. Dividends are included in the line Net income/expenses and gains/losses from equities and units.

Income from securities lending is presented as a net income comprising securities lending fees, expenses related to cash collateral received, reinvestment income, and the deduction of the security lending agents' fees connected to the handling of the transaction. Net income is calculated and classified in accordance with the type of security that is lent as either Net income/expenses and gains/losses from equities and units or Net income/expenses and gains/losses from bonds and other fixed income instruments.

Rental income related to investment property, less direct expenses incurred in connection with the signing of lease agreements, is recognised as income straight-line over the lease term. Incentive schemes related to signing lease agreements are recognised straight-line over the lease term, even if payment streams deviate from this basis.

For a description of accounting using the equity method, see 4.12 Jointly controlled entities and jointly controlled assets.

Interest expense is measured and recognised as incurred in the income statement and presented as either Interest expense repurchase agreements or Other interest expense.

Transaction costs are defined as all costs directly attributable to the completed transaction. For investments in equities and fixed income instruments, this includes normal commission fees and stamp duties. Commission fees include an amount paid as part of the commission fee to cover analytical research services through CSAs (commission sharing agreements; agreements to allocate commission between transaction commission and research commission). For investments within the investment asset class real estate, transaction costs will also typically include fees to advisors, typically lawyers and valuation experts, and stamp duty. Transaction costs are expensed as incurred and classified in accordance with the type of investment as either Net income/expenses and gains/losses from equities

and units, Net income/expenses and gains/losses from bonds and other fixed income instruments, or Net income/expenses and gains/losses from Financial assets real estate. For investment property and jointly controlled entities, directly attributable transaction costs are recognised in the balance sheet as a portion of the cost at initial recognition. For financial instruments that at initial recognition are measured at amortised cost, transaction costs are recognised in the balance sheet as part of the instrument's cost.

The management fee comprises the Ministry of Finance's reimbursement of Norges Bank's expenses connected with the management of the Government Pension Fund Global, which is recognised in the income statement for the investment portfolio of the Government Pension Fund Global as an expense, and recognised as revenue in the Norges Bank income statement. Operating expenses are reimbursed by the Ministry of Finance within an agreed limit. The management fee accrues during the financial year, but is cash-settled in the year following.

Other operating income in the Norges Bank income statement primarily comprises services for banks, services for the government and rental income that is recognised as earned.

#### 4.6 Taxation

Norges Bank's activities in Norway are not subject to tax. In some foreign markets, Norges Bank is liable to tax, in the form of withholding tax on dividend and interest income and corporate tax paid by foreign subsidiaries for operations in other countries.

#### 4.7 Classification and presentation of financial instruments

At initial recognition all financial assets are classified in one of the following categories depending on the type of instrument and purpose of the investment:

- Financial assets held for trading,
- Financial assets designated as at fair value through profit or loss (fair value option), or
- Financial assets classified as loans and receivables measured at amortised cost.

At initial recognition, financial liabilities are classified in one of the following categories:

- Financial liabilities held for trading,
- Financial liabilities designated as at fair value through profit or loss (fair value option), or
- Other financial liabilities, measured at amortised cost.

Norges Bank does not engage in hedge accounting, and therefore none of the financial instruments are designated as hedging instruments.

#### ***Financial assets or liabilities held for trading***

All positions in financial derivatives are classified in the category financial assets held for trading or financial liabilities held for trading. Other assets and liabilities are classified as held for trading if the investment is primarily made with the intention of sale or repurchase in the short-term, or at the point of first recognition is part of a portfolio that is managed at the portfolio level and where there is evidence of an actual pattern of short-term realisation of profit. None of the investments in equities or bonds are as at the balance sheet reporting date classified as held for trading.

#### ***Financial assets and liabilities designated as at fair value through profit or loss (fair value option)***

Financial instruments are classified in this category if the following criteria are met: the financial instruments are part of a portfolio that is managed and followed up based on the fair value in connection with a documented risk management strategy or a documented investment strategy. This implies that a fair value business model is used for the portfolio or the asset, and the primary objective is to have gains over the longer term connected to changes in fair value.

All portfolios of equities and bonds under management are as at the balance sheet reporting date classified in this category. Positive holdings of equities and other equity instruments and positive holdings of bonds and other fixed income instruments are presented on separate lines in the balance sheet. Net short positions in similar instruments are presented as Short-sale bonds.

Investments in the asset class real estate in the form of a share in the cash flow from underlying properties are classified in this category and presented on a separate line in the balance sheet.

#### ***Loans and receivables and other financial liabilities, measured at amortised cost***

Financial assets and liabilities that are not held for trading and are not designated as at fair value through profit or loss, and are not listed in an active market, are classified as loans and receivables or other financial liabilities.

Short-term financial assets and liabilities with positions in repurchase and reverse repurchase agreements and deposits/debt in the money market along with cash collat-

eral are classified as loans and receivables or other financial liabilities and measured at amortised cost.

#### ***Earned and accrued interest***

Earned and accrued interest is presented in the balance sheet on the same line as the respective financial asset or liability.

### **4.8 Recognition and derecognition, financial instruments**

Financial assets or liabilities are recognised in the balance sheet when Norges Bank becomes party to the instrument's contractual benefits, or when the risks and rewards of ownership are transferred if this occurs at a different point in time. The transaction is recognised at trade date, in that the purchase or sale of the instrument occurs under normal market conditions. Financial assets are derecognised when the contractual rights to the cash flows expire, or when the financial asset and substantially all the risks and rewards of ownership are transferred. Average acquisition cost is used upon derecognition. Financial liabilities are derecognised when the obligation is extinguished.

#### ***Securities lending***

Securities lending transactions consist of a transfer of securities, either equities or bonds, from Norges Bank to a borrower against collateral in the form of cash or securities. When the loan terminates, identical securities are returned to Norges Bank. The borrower is obliged to compensate the lender for corporate events relating to the securities. In addition the borrower pays a fee to the lender. The borrower holds the voting rights attached to the securities during the lending period.

Securities lent are not derecognised. During the lending period the securities are accounted for in the same way as other securities holdings. Loaned securities are presented on separate lines in the balance sheet, Equities lent and Bonds lent.

Collateral received in the form of cash is recognised as an asset together with a corresponding liability measured at amortised cost, Cash collateral received. Collateral received in the form of securities is not recognised in the balance sheet unless reinvested.

Reinvestments of cash collateral in the form of reverse repurchase agreements and bonds are recognised in the balance sheet and accounted for in the same manner as comparable investments.

### ***Repurchase and reverse repurchase agreements***

In connection with positions in repurchase agreements, the security is not derecognised when the agreement is entered into. During the contract period, the accounting for the underlying securities is in accordance with the accounting policies for investments in securities. Cash received is recognised as a financial asset in the form of bank deposits and the corresponding short-term financial liability is measured at amortised cost and shown in the balance sheet as Borrowing associated with repurchase agreements.

In connection with reverse repurchase agreements, the received underlying security is not reinvested and therefore is not recognised in the balance sheet. The cash paid is derecognised, and a corresponding receivable reflecting the cash amount that will be received in return is recognised as an asset at amortised cost, Lending associated with reverse repurchase agreements.

Income and expenses connected with repurchase and reverse repurchase agreements are presented on separate lines in the income statement, Interest income, lending associated with reverse repurchase agreements and Interest expense repurchase agreements.

## **4.9 Measurement of financial instruments**

### ***Initial recognition***

Financial assets and liabilities classified in categories with subsequent measurement at fair value through profit or loss are recognised at fair value on the trade date. Fair value will normally be the transaction price unless a different value can be justified on the basis of transactions observed in the market.

Financial assets and liabilities that are measured at amortised cost after initial recognition are recognised on the trade date at fair value including directly attributable transaction costs. Transaction costs are described further in 4.5.

### ***Subsequent measurement – fair value***

All equities, bonds and other fixed income instruments, real estate investments and financial derivatives classified as financial assets and liabilities held for trading or designated as at fair value through profit or loss are measured at fair value on the reporting dates after initial recognition. Gains and losses from changes in fair value are recognised in profit or loss in the period in which they arise. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The price quoted by a stock exchange, broker or price provider is used for securities that are traded in active markets.

If the market for a security is not active, fair value is established by using a valuation technique. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, reference to the current fair value of another instrument that is substantially the same, discounted cash flow analysis and option pricing models. If there is a valuation technique commonly used by market participants to price the instrument and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, that technique is used. The chosen valuation technique makes maximum use of market inputs. For further information on valuation techniques, see Note 22 Fair value measurement.

Changes in fair value are recognised in the income statement line related to the relevant instrument type, i.e. Net income/expenses and gains/losses from Equities and units, Net income/expenses and gains/losses from bonds and other fixed income instruments, Net income/expenses and gains/losses from financial derivatives and Net income/expenses and gains/losses from financial assets real estate.

### ***Subsequent measurement – amortised cost***

Financial assets and liabilities classified as loans and receivables or other financial liabilities are measured at amortised cost after initial recognition. The effective interest is recognised in the income statement. The effective interest rate is determined as the rate that discounts contractual cash flows within the agreed maturity to the recognised amount. The cash flows include directly attributable transaction costs.

## **4.10 Netting**

Financial assets and financial liabilities are presented net in the balance sheet if Norges Bank has a legal right to offsetting in addition to the intention to in practice settle on a net basis.

Financial derivatives are not netted, because these criteria are not met. This implies that positions with positive market values are presented as assets and positions with negative market values are presented as liabilities.

## **4.11 Investment property**

Properties held for the purpose of earning rental income or capital appreciation within the real estate asset class are accounted for as investment property in the investment portfolio's balance sheet.

Investment property is recognised as an asset when it is probable that the future rental income and value changes that are associated with the investment property will flow

to Norges Bank and the cost of the investment property can be measured reliably. An investment property is derecognised when sold, i.e. when substantially all the risks and potential for returns related to the property have been transferred to a buyer.

An investment property is measured initially at its purchase price, plus directly attributable transaction costs.

Investment property is measured at fair value at the reporting dates following initial recognition. Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction and is determined without deduction for transaction costs that will incur on sale or other disposal. External appraisals and valuations are regularly obtained as the primary basis for the determination of fair value. See Note 24 GPF Global for further information about valuation. Changes in the fair value of properties classified as Investment property in the balance sheet of the investment portfolio are presented in the investment portfolio's income statement as Net income/expenses and gains/losses from investment properties.

#### **4.12 Jointly controlled entities and jointly controlled assets**

Jointly controlled entities and jointly controlled assets are investments where subsidiaries established as part of the management of the investment portfolio of the Government Pension Fund Global have joint control through an agreement with the counterparty over the entity's strategic, financial and operational decisions, or comparable decisions related to the asset.

Jointly controlled entities are accounted for using the equity method. Investments in jointly controlled entities are recognised as an asset when it is probable that the future economic benefits that are associated with the interest in the entity will flow to Norges Bank and the cost of the investment can be measured reliably. Jointly controlled entities are derecognised when sold, i.e. when substantially all the risks and returns have been transferred to a buyer.

Cost at initial recognition comprises the consideration paid, plus directly attributable transaction costs. Investments in such entities are presented as Investments in jointly controlled entities, real estate in the investment portfolio's balance sheet. All jointly controlled entities report to Norges Bank using the accounting policies of Norges Bank, including measuring investment properties held by a jointly controlled entity at fair value.

In subsequent reporting periods, the carrying amount of the investment will be adjusted by the share of the profit

or loss for the period, which comprises the investment portfolio's share of changes in the investee's equity for the period, adjusted for dividends received and any amortisation of excess value. The investment portfolio's share of the profit or loss for the period is presented as Share of the profit/loss in jointly controlled entities, real estate.

Jointly controlled assets are accounted for using proportionate consolidation. Such investments are recognised on the same basis as for jointly controlled entities. Cost at initial recognition comprises the consideration paid, plus directly attributable transaction costs. Under proportionate consolidation, the investment portfolio accounts for its proportionate share of assets, liabilities, income and expenses, on the basis of their nature. Jointly controlled assets primarily comprise investment property (see above). Income and expenses associated with management of investment property are presented as Net income/expenses and gains/losses from investment properties.

#### **4.13 Consolidation of subsidiaries**

Norges Bank has established subsidiaries that exclusively constitute investments as part of the management of the investment portfolio of the Government Pension Fund Global. Consolidated financial statements are prepared for the investment portfolio. Pursuant to Section 3-4 first paragraph last sentence of the Regulation relating to annual financial reporting for Norges Bank, only consolidated financial statements shall be prepared for the investment portfolio.

The subsidiaries exclusively constitute investments as part of the management of the investment portfolio of the Government Pension Fund Global, and are omitted from consolidation in the financial statements of Norges Bank pursuant to Section 2-3 fourth paragraph of the above-mentioned regulation.

The accounting policies are applied consistently when consolidating ownership interests in subsidiaries. Intra-group transactions and intercompany balances are eliminated in the preparation of consolidated financial statements. Intra-group items comprise loans and equity financing from the investment portfolio to subsidiaries to finance property investments in subsidiaries. Loans are made at market interest rates and are issued in the subsidiary's functional currency. Except for the above-mentioned items, all items recognised in subsidiaries' financial statements are included in the investment portfolio's statement of comprehensive income, balance sheet and statement of cash flows. This includes subsidiary operating expenses and management costs, presented as Other expenses.

#### 4.14 Related parties

Norges Bank is owned by the Norwegian government and under IAS 24.25 is exempt from the disclosure requirements in relation to related party transactions with the government.

#### 4.15 Notes and coins

Notes and coins in circulation are recognised in the balance sheet at face value when they are placed into circulation. Notes and coins are derecognised when they are withdrawn from circulation and no later than the expiry of the ten-year deadline for redemption. Notes and coins not redeemed by the ten-year deadline are recognised as income in profit or loss. Notes and coins redeemed after the ten-year deadline are recognised as an expense in profit or loss. Expenses for the production of notes and coins are recognised in profit or loss as incurred.

#### 4.16 Pension and other benefit obligations

Accounting treatment of pension and other benefit obligations is in accordance with IAS 19 Employee Benefits. Norges Bank has several pension plans, a funded plan for Bank employees financed by the Bank's pension fund, in addition to unfunded plans for a number of other employees. The Bank's other benefit obligations are related to restructuring measures in the form of early retirement and termination benefits. Calculations for fund-based plans through Norges Bank's pension fund are based on actuarial assumptions regarding life expectancy, expected wage growth and adjustment of the National Insurance basic amount (G). The economic assumptions on which the calculation of the benefit obligations is based may change over time. The net benefit obligation is the difference between the present value of the benefit obligation and the fair value of plan assets.

Plan assets are measured at fair value. Benefit obligations and plan assets are measured on the balance sheet date. Employers' National Insurance contributions are included and are estimated on the basis of actual net underfunding. Pension expense is calculated on the basis of a straight-line attribution of benefit over the period of service and consists of the current service cost, less the return on plan assets. Changes in actuarial gains and losses are recognised in total comprehensive income.

#### 4.17 Deposits from the government

Deposits from the government are recognised as a liability at amortised cost.

#### 4.18 Presentation of the investment portfolio of the Government Pension Fund Global

Income from the investment portfolio of the Government Pension Fund Global and income attributed to the Government Pension Fund Global's krone account are presented on separate lines in the statement of comprehensive income. The net value of the investment portfolio and the balance of the Government Pension Fund Global's krone account are presented on separate lines on the asset and liability side of the balance sheet, respectively. Deposits and withdrawals from the Government Pension Fund Global's krone account are presented on separate lines in the statement of cash flows.

Financial reporting for the investment portfolio of the Government Pension Fund Global is presented in a separate note in accordance with IFRS.

#### 4.19 International Monetary Fund

##### *Norges Bank and the IMF*

Pursuant to Section 25 of the Norges Bank Act, Norges Bank shall administer Norway's financial rights and fulfil the obligations ensuing from participation in the International Monetary Fund (IMF).

##### *Allocated Special Drawing Rights*

Allocated Special Drawing Rights (SDRs) are recognised as an asset in the balance sheet. The value of SDRs is calculated on the basis of a currency basket comprising USD, EUR, GBP and JPY. The equivalent value of allocated SDRs in the IMF shows Norges Bank's total allocations of SDRs since the scheme entered into force in 1970 and is recognised as a liability in the balance sheet. SDRs are measured at amortised cost.

##### *Reserve position*

Norges Bank's reserve position in the IMF is recognised in the balance sheet as a net outstanding account with the IMF. This consists of Norges Bank's allocated quota in the IMF less holdings in the Fund of constant SDRs, which the IMF holds as a krone deposit with Norges Bank. The reserve position is measured at amortised cost.

##### *Loans to the IMF*

Loans to the IMF are recognised at fair value at initial recognition. Loans to the IMF are subsequently measured at amortised cost.



#### **1.4.20 Lending to banks, etc.**

Loans to banks are recognised at fair value at initial recognition. There are no establishment fees or other directly attributable transaction costs. If there is an indication that an impairment loss has been incurred, the amount of the loss is measured as the difference between the carrying amount and the present value of estimated future cash flows. The carrying amount of the engagement is reduced, and the amount of the loss for the period is recognised in profit or loss.

#### **1.4.21 Other assets**

##### ***Non-current assets***

Non-current assets are recognised at cost, less accumulated straight-line depreciation or amortisation over their expected useful life. An impairment test is performed if there is an indication of impairment. If the carrying amount exceeds fair value, the carrying amount will be written down to fair value.

##### ***Gold***

Norges Bank has holdings of gold coins and gold bars as part of the Bank's historical collections. The holdings were measured at fair value on the date the gold was reclassified from international reserves to non-current assets. An impairment test is performed if there is an indication of impairment. If the carrying amount exceeds fair value, the carrying amount will be reduced to fair value. In the event the metallic value of gold rises, the holdings are not revalued.

##### ***Art and numismatic collections***

Norges Bank has a substantial collection of art, gifts and numismatic objects such as medals, banknotes and coins. The collection has been recognised in connection with the transition to IFRS at estimated cost on the basis of earlier appraisals. The collections are not expected to be subject to impairment.

## **5 STANDARDS, AMENDMENTS AND INTERPRETATIONS NOT APPLICABLE IN 2011**

### **5.1 IASB final standards and IFRS and IFRIC interpretations with application dates after 2011**

#### ***Amendments to IAS 12 Income Taxes***

Under the amended IAS 12, if a deferred tax asset or liability arises from investment property that is measured using the fair value model in IAS 40 Investment Property, there is

a rebuttable presumption that the carrying amount of the investment property will be recovered through sale (rather than through use). The presumption is rebutted if two criteria are met. The amendments also incorporate SIC 21 Income Taxes – Recovery of Revalued Non-Depreciable Assets into IAS 12. As a result, IAS 12 will require that measurement of a deferred tax asset or liability that arises from a non-depreciable asset measured using the revaluation model in IAS 16 Property, Plant and Equipment reflect the tax consequences of recovering the carrying amount through sale (rather than through use).

The amended IAS 12 is effective for annual periods beginning on or after 1 January 2012, but the standard has not yet been endorsed by the EU. Norges Bank expects to apply the amended standard as from 1 January 2012, under the assumption that it will be endorsed by the EU. Norges Bank does not expect any material effect on other comprehensive income or the fair value of investment property in the balance sheet upon adoption.

#### ***Amendments to IFRS 7 Financial Instruments – Disclosures***

The amendments relate to disclosure requirements for financial instruments that are derecognised in their entirety, but where the entity has a continuing involvement. The amendments will give users a clearer picture of the potential risks that remain with the transferor.

The amended IFRS 7 is effective for annual periods beginning on or after 1 July 2012, but the standard has not yet been endorsed by the EU. Norges Bank expects to apply the amended standard as from 1 January 2012, under the assumption that it will be endorsed by the EU. Application is not expected to have any material effect on Norges Bank's note disclosures.

#### ***Amendments to IAS 19 Employee Benefits***

The amendments to IAS 19 require full recognition of all changes in the defined benefit obligation and plan assets. The amendments also entail less flexibility with regard to presentation of changes in value. The amendments also introduce more extensive disclosure requirements.

The amended IAS 19 is effective for annual periods beginning on or after 1 January 2013, and is expected to be endorsed by the EU in 2012. Norges Bank expects to apply the amended standard as from 1 January 2013, under the assumption that it will be endorsed by the EU. Norges Bank applies the principle of full recognition of actuarial gains and losses in total comprehensive income under the current IAS

19. The amendments to IAS 19 are thus not expected to have a material impact on Norges Bank's recognition of its pension benefit obligation. The amendments may entail additional note disclosures.

### ***IFRS 9 Financial Instruments***

IFRS 9 replaces the classification and measurement rules for financial instruments in IAS 39 Financial Instruments – Recognition and Measurement. In accordance with IFRS 9, financial assets with basic loan features shall be carried at amortised cost, unless the business model indicates that they should be carried at fair value. All other financial assets shall be measured at fair value.

Classification and measurement of financial liabilities under IFRS 9 is a continuation of IAS 39, with the exception of financial liabilities designated as at fair value through profit or loss (fair value option), where changes in fair value relating to own credit risk shall be separated and be presented in other income and expenses.

All portfolios of equities, bonds and financial derivatives have as at the date of transition to IFRS a business model that is also consistent with the classification measured at fair value under IFRS 9. In Norges Bank's judgement, should the business model change to an extent that requires reclassification to measured at amortised cost in accordance with IFRS 9, classification under the categories loans and receivables or held to maturity for financial assets, or other liabilities, will become applicable under IAS 39 Financial Instruments – Recognition and Measurement.

IFRS 9 is effective for annual periods beginning on or after 1 January 2013, but the standard has not yet been endorsed by the EU. Norges Bank expects to apply IFRS 9 as from 1 January 2013, under the assumption that it will be endorsed by the EU. Application of IFRS 9 is not expected to result in material changes in classification, recognition or measurement for Norges Bank's financial reporting.

### ***IFRS 10 Consolidated Financial Statements***

IFRS 10 Consolidated Financial Statements (IFRS 10) supersedes IAS 27 Consolidation and Separate Financial Statements and SIC-12 Consolidation – Special Purpose Entities. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements; defines the principle of control, and establishes control as the basis for consolidation; sets out how to apply the prin-

ciple of control to identify whether an investor controls an investee and therefore must consolidate the investee and sets out the accounting requirements for the preparation of consolidated financial statements.

IFRS 10 is effective for annual periods beginning on or after 1 January 2013, with early application permitted if adopted as part of the "package of five" standards issued by the International Accounting Standards Board (IASB) in May 2011. The standards that must all be adopted simultaneously are IFRS 10 Consolidation and Separate Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in Other Entities, IAS 27 Separate Financial Statements (as amended in 2011), and IAS 28 Investments in Associates (as revised in 2011). IFRS 10 is expected to be endorsed by the EU in 2012.

Norges Bank does not expect that the adoption of IFRS 10 will have a significant impact on the consolidated financial statements of the investment portfolio of the Government Pension Fund Global or Norges Bank's financial statements. Norges Bank expects to apply IFRS 10 as from 1 January 2013, under the assumption that the standard will be endorsed by the EU.

### ***IFRS 11 Joint Arrangements***

IFRS 11 Joint Arrangements (IFRS 11) supersedes SIC-13 Jointly Controlled Entities – Non-Monetary Contributions by Venturers. A joint arrangement is an arrangement over which two or more parties have joint control, and has the following characteristics, that the parties are bound by a contractual arrangement and the contractual arrangement gives two or more of those parties joint control over the arrangement. A joint arrangement is either a joint operation (the parties that have joint control over the arrangement have rights to the assets, and obligations for the liabilities) or a joint venture (the parties that have joint control of the arrangement have rights to the net assets). While IFRS 11 specifies two primary accounting methods, it clearly indicates when a particular method must be used, unlike the choice of accounting method permitted currently. Unless the fair value exception is used, jointly controlled entities shall be accounted for using the equity method as described in IAS 28 Investments in Associates (as revised in 2011).

IFRS 11 is effective for annual periods beginning on or after 1 January 2013, with early application permitted if adopted as part of the "package of five" standards issued by the IASB in May 2011. See above under IFRS 10 for a list of these five standards. IFRS 11 is expected to be endorsed by the EU in 2012.

Norges Bank does not expect that the adoption of IFRS 11 will have a material impact on the financial reporting for the investment portfolio of the Government Pension Fund Global or other areas of Norges Bank. Norges Bank expects to apply IFRS 11 as from 1 January 2013, under the assumption that the standard will be endorsed by the EU.

#### ***IFRS 12 Disclosure of Interests in Other Entities***

IFRS 12 Disclosure of Interests in Other Entities (IFRS 12) requires the disclosure of information that enables users of financial statements to evaluate the nature of and risks associated with interests in other entities as well as the effects of those interests on the entity's balance sheet, income and cash flows. IFRS 12 is required to be applied by an entity that has an interest in subsidiaries, joint arrangements (joint operations or joint ventures), associates, or unconsolidated structured entities.

IFRS 12 is effective for annual periods beginning on or after 1 January 2013, with early application permitted if adopted as part of the "package of five" standards issued by the IASB in May 2011. See above under IFRS 10 for a list of these five standards. IFRS 12 is expected to be endorsed by the EU in 2012.

Norges Bank does not expect that the adoption of IFRS 12 will have a material impact on the financial reporting for the investment portfolio of the Government Pension Fund Global or other areas of Norges Bank. Norges Bank expects to apply IFRS 12 as from 1 January 2013, under the assumption that the standard will be endorsed by the EU.

#### ***IFRS 13 Fair Value Measurement***

IFRS 13 Fair Value Measurement (IFRS 13) defines fair value and sets out a single IFRS framework for measuring fair value and disclosures about fair value measurement. IFRS 13 applies when another IFRS requires or permits fair value measurement or disclosures concerning fair value measurement.

IFRS 13 is effective for annual periods beginning on or after 1 January 2013, with early application permitted. IFRS 13 is expected to be endorsed by the EU in 2012. Norges Bank does not expect that the adoption of IFRS 13 will have a significant impact on its financial reporting. Norges Bank expects to apply IFRS 13 as from 1 January 2013, under the assumption that the standard will be endorsed by the EU.

## **Note 2**

### **Significant estimates and critical accounting judgements**

The preparation of the financial statements of Norges Bank, which includes the financial reporting for the investment portfolio of the Government Pension Fund Global in accordance with the accounting policies in Note 1, involves the use of estimates and judgements that may affect assets, liabilities, income and expenses. Estimates and judgements are based on historical experience and expectations about future events that are considered probable at the time the financial statements are presented.

Estimates are based on best judgement; however, actual results may deviate from estimates. In cases of particularly uncertain estimates, this is described in the respective notes.

#### **SIGNIFICANT ESTIMATES**

Below is an overview of significant estimates on the reporting date.

#### **Fair value of securities, financial assets, financial derivatives and investment property not traded or quoted in an active market**

Some of the holdings within the investment portfolio of the Government Pension Fund Global are not traded in active markets, i.e. they have been allocated to the Level 2 or 3 pricing categories. This is primarily the case for bond holdings, OTC financial derivatives and real estate investments, while nearly all equities are allocated to Level 1 (traded in active markets).

Level 2 and 3 holdings are priced using models, and the resulting value is defined as an estimate. The resulting values of holdings allocated to Level 3, with significant use of non-observable inputs, are regarded as particularly uncertain estimates. Generally, widely accepted, standard pricing models are used. For further information on pricing models and control environment, see Note 22 Fair value measurement.

Valuation of investment properties relies on external appraisals and valuations. The determination of fair value in such appraisals requires the use of estimates such as future cash flows from assets (based on assumptions regarding tenant occupancy rates, tenant profiles, future revenue streams, the capital value of property, plant and equipment and the overall physical condition of the property) and discount rates applicable to those assets. These estimates are based on local market conditions on the reporting date.

Other instruments in Norges Bank not included in the investment portfolio of the Government Pension Fund Global are allocated exclusively to Level 1.

### **Gains/losses on securities before foreign exchange gains and losses, and Foreign exchange gains and losses**

Gains and losses on securities and financial derivatives resulting from changes in the price of the security/instrument (before foreign exchange gains and losses) and gains and losses resulting from changes in foreign exchange rates (foreign exchange gains and losses) are presented separately in the income statement. The method of allocating total gains and losses in Norwegian kroner for a holding for a period to a security element and foreign exchange element is an estimate, as different methods will result in different allocations.

#### ***Foreign exchange element:***

Norges Bank calculates unrealised gains and losses due to changes in foreign exchange rates based on the cost in local currency of the holding and the change in the foreign exchange rate from the time of purchase until the balance sheet date. If the holding has been purchased in a previous period, gains and losses from previous periods that have already been recognised in profit or loss are deducted to arrive at the gain or loss for the current period. Accordingly, for realised gains or losses, the foreign exchange rate on the date of sale is used instead of the closing rate at the end of the reporting period, and previously recognised unrealised gains or losses for the holding are reversed in the current period.

#### ***Security element:***

Unrealised gains and losses from changes in the security price are calculated based on the change in the security price from the purchase date to the balance sheet date and the closing rate at the balance sheet date, and gains and losses recognised in the income statement in previous periods are deducted to arrive at the gain or loss from security prices for the current period. Realised gains and losses from changes in security prices are based on the selling price as opposed to the price on the balance sheet date and previously recognised unrealised gains or losses for the holding are reversed in the current period.

### **Krone account of the Government Pension Fund Global**

The underlying estimate uncertainty in the Government Pension Fund Global is reflected in the accounting policies used in the accounting of the Government Pension Fund

Global. The most significant items with sources of estimate uncertainty are discussed above. Changes in the policies or assumptions will also change the amount in the krone account, since it contains cash transfers and fair value changes in the underlying instruments. For further information regarding, risk, valuation and sensitivity, see Note 24.

### **Pension benefit obligation**

Norges Bank has several pension plans, a funded plan for Bank employees financed by the Bank's pension fund, in addition to unfunded plans for a number of other employees, as well as employees in foreign countries. Unfunded plans are funded through operations and primarily comprise defined contribution plans. The funded plan is a defined benefit plan. Measurement of the pension benefit cost and the pension benefit obligation for these plans requires determining a number of assumptions and estimates, including future salaries, discount rates, early retirement frequency and return on plan assets. The discount rate used to determine the pension benefit obligation and pension benefit cost is calculated on the basis of returns on a portfolio of long-term bonds. Norges Bank's pension benefit obligation (PBO) pertains exclusively to Norway. The discount rate used as at 31 December 2011 is 2.6%, calculated on the basis of government bond yields in accordance with IAS 19 Employee Benefits. This is consistent with Norwegian Accounting Standards Board (NASB) guidelines concerning determination of pension benefit assumptions for use as at 31 December 2011. Plan assets are tied to Norway. The expected return on plan assets in also consisted with NASB guidelines, and at 31 December 2011 is 4.1%. Assumed wage growth for the remaining period of service is also consistent with NASB guidelines and at 31 December 2011 is 3.5%.

Changes in these assumptions may affect the pension plans' financial position, in addition to the net periodic pension benefit cost for the period. The pension benefit obligation (PBO) is significantly affected by changes in the discount rate and expected salary and pension benefit adjustments. The PBO is also materially affected by demographic assumptions. Changes in the aforementioned parameters and changes in the PBO will affect the net pension benefit cost in subsequent periods, both the service cost for the year and the effect of discounting.

### **Lending to banks and the International Monetary Fund (IMF)**

When there are indications that loans are impaired, the present value of estimated future cash flows is calculated.

There is uncertainty connected with the estimated future cash flows. This uncertainty is reduced by only providing loans to banks against collateral in the form of approved securities. Using different assumptions, the result of the calculation may yield different outcomes and appurtenant adjustment of the need to recognise impairment losses.

Norges Bank's loans to the IMF have been made to bolster the IMF General Arrangements to Borrow (GAB), which follow IMF guidelines. Norges Bank is not directly exposed to risk in the loan portfolio managed by the IMF. The IMF has never realised a loss on its loans under the GAB. The IMF has preferred creditor status, which means that the IMF has priority over all other creditors. If the IMF should incur a loss on its loans, this will initially affect the Fund's own assets and, if necessary, paid-in quota subscriptions. In Norges Bank's assessment, the risk related to IMF loans is minimal, and no loan loss provisions have been recognised with regard to these loans.

#### **Notes and coins in circulation**

Notes and coins are derecognised when they are withdrawn from circulation and no later than the expiry of the ten-year deadline for redemption. It is Norges Bank's experience that this assumption does not provide precise estimates of expected returns of notes and coins. Since it is also the Bank's experience that a substantial portion of remaining notes and coins outstanding are rarely redeemed after the ten-year deadline, on the basis of an accounting judgement the Bank has chosen to recognise them as income in their entirety.

#### **Significant critical accounting judgements related to the application of accounting policies**

The following are the judgements made by management related to the application of accounting policies regarded to have the greatest impact on the amounts recognised in the financial statements.

#### **Choice of functional currency**

The management of Norges Bank judges the Norwegian krone to be the functional currency in the bank, as this is the dominant currency with regard to the underlying activities of the bank. The owner's capital in the Government Pension Fund Global, in the form of the Government Pension Fund Global krone account, is denominated in Norwegian kroner, and a significant share of the costs related to the management of the assets is in Norwegian kroner.

The financial reporting of the investment portfolio of the Government Pension Fund Global is part of the financial

statements of Norges Bank, and on this basis the judgement is that the investment portfolio's functional currency is also the Norwegian krone. The bank's and the investment portfolio's results are measured and reported internally and to the owner in Norwegian kroner, while the percentage return for the investment portfolio is reported both in Norwegian kroner and in the currency basket specified in the investment mandate given by the Ministry of Finance. Furthermore, no single investment currency stands out as dominant in the area of asset management.

When subsidiaries are established or acquired in connection with the management of the real estate asset class within the investment portfolio of the Government Pension Fund Global, an assessment is made concerning the appropriate functional currency for use in the subsidiary's financial reporting, and for use in the consolidation into the consolidated financial statements of the investment portfolio. Normally the local currency will be indicative of the appropriate functional currency for the company, given that this is the currency of the economic environment in which the entity operates, and the currency for all of its transactions.

In cases where there is doubt related to which currency is the functional currency or whether the entity has operations, then the currency of its financing activities and the denomination of any income and expenses will be considered, together with the consideration of whether the entity is merely an extension of Norges Bank into the local market.

#### **Assessment of degree of control**

In relation to investments in entities or assets made by Norges Bank on behalf of the investment portfolio of the Government Pension Fund Global, through wholly-owned holding companies, together with a partner and where the bank has a substantial ownership interest, an assessment is made to establish whether the bank has control over the entity or the asset. This assessment is necessary to establish whether the investment should be accounted for as an investment in a financial asset, an associate, a jointly controlled entity/asset or a consolidated subsidiary. In connection with the assessment of the degree of control, the ownership interest will be given significant consideration, along with the contractual terms in the shareholder and joint venture agreements that may suggest a greater or lesser degree of control than that based on an observation of the ownership interest taken in isolation. A total assessment of all relevant elements in each specific case forms the basis for a conclusion concerning whether or not the bank has control over the investment.

### Note 3 Net income from financial instruments

Amounts in NOK million

2011						
	Interest income/ expense	Dividends	Net income/ expense	Realised gains/ losses	Unrealised gains/ losses	Total
Interest income from deposits and claims	111	-	-	-	-	111
Interest income from lending to banks	946	-	-	-	-	946
Interest income, lending associated with reverse repurchase agreements	105	-	-	-	-	105
Net income/expense and gains/losses from:						
- Equities	-	2 289	43	246	-8 825	-6 247
- Bonds and other fixed-income securities	4 180	-	24	275	7 294	11 773
- Financial derivatives	-20	-	-	-18	129	91
Interest expense repurchase agreements	29	-	-	-	-	29
Interest expense on banks' and Treasury deposits:						2 081
- Of which interest expense paid to Treasury	917	-	-	-	-	
- Of which interest expenses paid on sight deposits from banks	996	-	-	-	-	
- Of which interest expenses paid on F-deposits from banks	144	-	-	-	-	
- Of which interest expenses paid on depots operated by banks	24	-	-	-	-	
Share dividend from BIS	-	22	-	-	-	22
Net interest income, from claims on/liabilities to the International Monetary Fund	31	-	-	-	-	31
Interest income from long-term lending	91	-	-	-	-	91
Foreign exchange gains/losses				-7 840	13 254	5 414
<b>Net income from financial instruments</b>	<b>3 334</b>	<b>2 311</b>	<b>67</b>	<b>-7 337</b>	<b>11 852</b>	<b>10 227</b>

#### Interest terms for deposits from banks

Up until 3 October 2011, banks' sight deposits with Norges Bank bore the key policy rate. From 3 October 2011, banks receive interest only on a specific portion of sight deposits – a quota – at the key policy rate. Sight deposits in excess of this quota bear a lower interest – the reserve rate. For the period 3 October to 31 December 2011, the reserve rate was fixed at 100 basis points lower than the key policy rate. Banks have been divided into three groups, with all banks in a particular group allocated the same quota, except for settlement banks, which are allocated larger quotas.

Norges Bank reduces the quantity of reserves in the banking system by providing banks with fixed-rate deposits (F-deposits). As in the case of fixed-rate loans, the interest rate is normally determined by multi-price auction. Banks submit bids for a desired amount and interest rate. Norges Bank decides the aggregate amount of the allotment. The banks' interest rate bids are ranked in ascending order. Banks that place bids within the aggregate amount will be

awarded an amount at the interest rate submitted. The maturity on F-deposits is determined by Norges Bank and varies depending on the projection of structural liquidity. Norges Bank can provide F-deposits at a floating rate, i.e. the interest rate on the F-deposits depends on the benchmark rate in the money market. Average maturity for F-deposits from banks was 0.1 month in 2011.

#### Interest terms for deposits from the Treasury

Interest terms for deposits from the government are set in a special agreement between Norges Bank and the Ministry of Finance. The interest on deposits is calculated on the basis of money market rates weighted between Norwegian and foreign rates in proportion to investments in Norges Bank's balance sheet (excl. Investment for and Deposits krone account Government Pension Fund Global).

Interest on Treasury deposits in 2011 was paid at an annual rate of 0.50% in Q1 and Q2, and 0.75% in Q3 and Q4. The same interest rates apply to deposits from public sector account holders who receive interest on their deposits.

Amounts in NOK million

	2010					
	Interest income/ expense	Dividends	Net income/ expense	Realised gains/ losses	Unrealised gains/ losses	Total
Interest income from deposits and claims	22	-	-	-	-	22
Interest income from lending to banks	1 935	-	-	-	-	1 935
Interest income from lending associated with reverse repurchase agreements	129	-	-	-	-	129
Net income/expense and gains/losses from:						
- Equities	-	2 290	63	-1 799	9 596	10 150
- Bonds and other fixed-income securities	5 122	-	40	2 241	-413	6 990
- Financial derivatives	-89	-	-	80	-254	-263
Interest expense repurchase agreements	41	-	-	-	-	41
Interest expense on banks' and Treasury deposits:						1 702
- Of which interest expense paid to Treasury	780	-	-	-	-	
- Of which interest expenses paid on sight deposits from banks	902	-	-	-	-	
- Of which interest expenses paid on Fdeposits from banks	-	-	-	-	-	
- Of which interest expenses paid on depots operated by banks	20	-	-	-	-	
Share dividend from BIS	-	56	-	-	-	56
Net interest income, from claims on/liabilities to the International Monetary Fund	13	-	-	-	-	13
Interest income from long-term lendings	58	-	-	-	-	58
Foreign exchange gains/losses	-	-	-	-2 143	-1 808	-3 951
<b>Net income from financial instruments</b>	<b>5 447</b>	<b>2 346</b>	<b>103</b>	<b>-1 621</b>	<b>7 121</b>	<b>13 396</b>

### Interest terms for deposits from banks

In 2010, banks' deposits in Norges Bank bore interest at the key policy rate.

### Interest terms for deposits from the Treasury

Interest on Treasury deposits in 2010 was paid at an annual rate of 0.50% in Q1, 0.25% in Q2, and 0.50% in Q3 and Q4. The same interest rates apply to deposits from public sector account holders who receive interest on their deposits.

## Note 4 Management fee, Government Pension Fund Global

Norges Bank's operating income and operating expenses include income and expenses of NOK 2 539m related to the management of the Government Pension Fund Global. The expenses are reimbursed by the Ministry of Finance up to a set limit. Expenses related to management also include

allocated indirect and imputed costs. The management fee covers these components, which are included in the Bank's operating expenses, including personnel expenses, depreciation and other operating expenses.

Amounts in NOK million

	2011	2010
Salaries, employer's National Insurance contributions and other personnel-related costs	447	389
IT, information and decision support systems	214	224
Custody and settlement costs	406	382
Outsourced IT and analysis costs	254	214
Consulting and legal fees	73	116
Base fees to external managers	371	452
Other costs	107	81
Allocated common costs Norges Bank	121	115
<b>Management fee excluding performance-based fees</b>	<b>1 993</b>	<b>1 973</b>
Performance-based fees to external managers	546	986
<b>Total management fee</b>	<b>2 539</b>	<b>2 959</b>

## Note 5 Other operating income

Amounts in NOK million

	2011	2010
Services, banks	56	71
Services, government	16	28
Rent, external	32	29
Other income	8	23
<b>Other operating income</b>	<b>112</b>	<b>151</b>

### Services for banks

Norges Bank performs settlement services for banks through Norges Bank's settlement system (NBO). To promote efficient and robust settlement of payments in Norges Bank, expenses for account maintenance and settlement services are covered by the annual fees for NBO. The assumption is that revenues will cover two-thirds of the overall cost of implementing and operating the settlement system. A third of expenses is attributable to central bank functions and covered by Norges Bank. Recharging of fees related to VPS settlement is recognised in 2011 as a refund of expenses. Comparative amounts for 2010 have not been restated; the amount for 2010 totalled NOK 14m.

### Services for the government

The Ministry of Finance is responsible for managing the government's debt securities and cash holdings. Pursuant to agreements between Norges Bank and the Ministry of Finance, some responsibilities associated with the management of the government's debt and cash holdings have been assigned to Norges Bank. In accordance with these agreements, Norges Bank shall perform a number of services relating to government debt management in Norway. Norges Bank's responsibilities are related to market operations in government bonds and Treasury bills. The Ministry of Finance covers Norges Bank's expenses for these services. In 2010, Norges Bank received remuneration for management of the Government Petroleum Insurance Fund.



## Note 6 Personnel expenses

Amounts in NOK million

	2011	2010
Salaries and fees	600	575
Employer's National Insurance contributions	85	66
Pension expense (see Note 21)	95	191
Restructuring costs (see Note 21)	2	5
Other personnel expenses	88	72
<b>Total personnel expenses</b>	<b>870</b>	<b>909</b>

Norges Bank had 629 permanent employees on 31 December 2011, corresponding to 624.7 full-time equivalents (FTEs).

### Benefits to governing bodies and senior management

#### Supervisory Council

The chair of the Supervisory Council receives annual remuneration of NOK 43 000, the deputy chair receives NOK 27 000 and the other members of the Council receive NOK 21 000. Alternates receive annual remuneration of NOK 3 500. Members of the Permanent Committee receive annual remuneration of NOK 43 000. Total remuneration to members and alternates of the Permanent Committee and the Supervisory Council totalled NOK 646 000 in 2011.

Expenses for Norges Bank's Supervisory Council and the Office of the Supervisory Council amounted to NOK 12 180 655 in 2011. With regard to remuneration to members of the Supervisory Council and the director of the Office of the Supervisory Council, reference is made to the Supervisory Council's report to the Storting for 2011.

#### Executive Board – external members

Remuneration to members and alternates of the Executive Board is determined by the Ministry of Finance.

2011				
Name	Total remuneration paid	Executive Board	Audit Committee	Remuneration Committee
Liselott Kilaas	248 000	182 000	66 000	-
Asbjørn Rødseth	237 000	182 000	55 000	-
Ida Helliesen	237 000	182 000	55 000	-
Eirik Wærness	207 000	182 000	-	25 000
Brit K. Rugland	207 000	182 000	-	25 000

2010				
Name	Total remuneration paid	Executive Board	Audit Committee	Remuneration Committee
Liselott Kilaas	248 000	182 000	66 000	-
Asbjørn Rødseth	237 000	182 000	55 000	-
Ida Helliesen	237 000	182 000	55 000	-
Eirik Wærness	197 000	182 000	-	15 000
Brit K. Rugland	197 000	182 000	-	15 000

Alternates received a fixed annual remuneration of NOK 120 000. Total remuneration to members and alternates

of the Executive Board, Audit Committee and Remuneration Committee was NOK 1 376 000.

### ***Governor and deputy governor***

The salaries of the governor and deputy governor of Norges Bank are determined by the Ministry of Finance. In addition, they have a company car at their disposal, a free telephone and insurance covered by their employer. Governor Øystein Olsen is a member of Norges Bank's pension fund. The terms and conditions of his retirement benefits are the terms and conditions for the pension fund in force on the date in question. A full retirement pension for Deputy Gov-

ernor Jan F. Qvigstad is 2/3 of final salary adjusted in line with pensions in the National Insurance scheme. Retirement benefits are payable from the date of retirement, albeit not before the age of 65. The period of service for full benefit is 12 years. The pension plan will be coordinated with other public pension plans, but this is not taken into account in the calculation of current earned pension benefits. Deputy Governor Qvigstad has a pension entitlement from his previous period of service at Norges Bank. Coordination of this entitlement would offset current estimated earned pension benefits.

**2011**

Executive	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
Governor	Ø. Olsen	1 768 349	147 264	539 835	-
Deputy Governor	J.F. Qvigstad	1 587 482	165 801	2 691 170	1 890 000

**2010**

Executive	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
Governor	S. Gjedrem	1 743 086	134 716	1 059 512	-
Deputy Governor	J.F. Qvigstad	1 555 039	166 029	1 214 033	1 890 000

### Salaries and retirement benefits for other directors at Norges Bank

Norges Bank's directors are entitled to the same employment benefits and have the same borrowing rights as the Bank's other employees. Pension plans are discussed in Note 21 and loans to employees are discussed in Note 16.

### Benefits to senior executives in Norges Bank's central banking activities

The Executive Board sets a salary interval for area directors in central banking operations. The governor determines annual salary within this interval.

2011					
Director	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
Norges Bank Financial Stability	K. Gulbrandsen	1 402 644	27 947	309 115	2 196 475
Norges Bank Monetary policy	J. Nicolaisen	1 402 932	20 452	307 819	250 000
Norges Bank Administration	J. Ebbesen	1 329 918	13 337	256 160	-
Legal Department	M. Ryel	1 403 062	21 887	324 002	-
Communications Department.	M. Beyer <sup>1)</sup>	337 500	4 738	352 868	-
Internal Audit	I. Valvatne	1 372 014	36 889	321 895	1 274 000

<sup>1)</sup> M. Beyer is serving as acting communications director, substituting for S. Meisingseth, who is on leave.

2010					
Director	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
Norges Bank Financial Stability	K. Gulbrandsen	1 334 063	27 241	292 639	564 200
Norges Bank Monetary policy	J. Nicolaisen	1 336 511	15 199	275 114	60 000
Norges Bank Administration	J. Ebbesen	1 363 803	13 573	232 422	-
Legal Department	M. Ryel	1 342 612	32 682	285 533	-
Communications Department.	S. Meisingseth	1 152 878	30 100	283 317	1 711 400
Internal Audit	I. Valvatne	1 310 682	21 193	279 541	1 302 000

## Benefits to senior executives in Norges Bank Investment Management (NBIM)

The Executive Board sets a salary interval for the chief executive officer (CEO) of NBIM. The governor determines annual salary within this interval. Salaries for other members

of the NBIM management team are determined by the CEO of NBIM in consultation with the Executive Board and following annual assessments.

2011					
	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
CEO	Yngve Slyngstad	5 751 162	25 620	382 809	805 328
Deputy CEO and Chief of Staff	Trond Grande <sup>1</sup>	3 609 575	23 676	292 331	-
CIO Equities	Petter Johnsen <sup>2</sup>	3 228 750	50 587	322 875	-
CIO Real Estate	Karsten Kallevig <sup>3</sup>	2 812 500	23 965	214 821	-
Chief Treasurer	Jessica Irschick	4 520 250	38 789	452 025	-
Chief Risk Officer	Jan Thomsen <sup>4</sup>	3 296 924	17 656	303 120	-
Chief Operating Officer	Age Bakker	2 760 630	16 382	345 161	-

Benefits disclosed pertain to the period during which the employee was a member of the leader group.

<sup>1)</sup> Trond Grande became Deputy CEO on 1 February 2011 and Chief of Staff on 1 April 2011 after serving as chief risk officer.

<sup>2)</sup> Petter Johnsen became CIO Equities on 1 April 2011.

<sup>3)</sup> Karsten Kallevig became CIO Real Estate on 1 April 2011.

<sup>4)</sup> Jan Thomsen became Chief Risk Officer on 1 April 2011, after serving as Chief Compliance Officer.

The table above shows the NBIM leader group at year-end 2011. Dag Dyrdal was a member of the leader group as Chief Strategic Relations Officer until 1 April 2011. Remuneration received for this position in 2011 was NOK 569 709 in salary paid, NOK 6 977 in other benefits and NOK 86 452 in earned pension benefits. Mark Clemens was a member of the leader group as Chief Administrative Officer until 1 April 2011. Remuneration received for this position in 2011

was NOK 582 900 in salary paid, NOK 4 642 in other benefits and NOK 76 542 in earned pension benefits. Mark Clemens also had a employee loan in the amount of NOK 766 668. Bengt Ove Enge was a member of the leader group as Chief Investment Officer until 30 June 2011. Remuneration received for this position in 2011 was NOK 2 202 763 in salary paid, NOK 6 459 in other benefits and NOK 234 027 in earned pension benefits.

2010					
	Name	Salary paid	Value of other benefits	Pension benefits earned	Employee loan
Chief Executive Officer	Yngve Slyngstad	4 181 678	27 929	345 792	905 944
Deputy CEO (until 1 Oct. 2010)	Stephen Hirsch	5 306 396	145 181	769 502	-
Chief Risk Officer	Trond Grande	2 681 654	26 723	241 591	-
Chief Operating Officer	Age Bakker	2 384 688	20 192	299 660	-
Chief Compliance Officer	Jan Thomsen	2 766 665	66 594	259 640	-
Chief Strategic Relations Officer	Dag Dyrdal	2 165 563	35 746	302 746	-
Chief Administrative Officer	Mark Clemens	2 237 125	29 609	239 701	260 000
Chief Treasurer	Jessica Irschick	4 903 500	13 319	490 350	-
Chief Investment Officer	Bengt Ove Enge	4 526 286	20 690	202 939	81 336

## Note 7 Other operating expenses

### SPECIFICATION OF OTHER OPERATING EXPENSES

	Amounts in NOK million	
	2011	2010
IT, information and decision support systems	343	359
Base fees to external managers	369	461
Performance-based fees to external managers	546	978
Custody and settlement costs	426	406
Outsourced IT and analysis costs	272	231
Consulting and legal fees	141	176
Other expenses	314	333
<b>Total other operating expenses</b>	<b>2 411</b>	<b>2 944</b>

### AUDITING EXPENSES

	Amounts in NOK thousand, exclusive vat	
	2011	2010
Statutory audit*	8 414	9 883
Other assurance services**	3 484	11 521
Tax advice	595	-
Other services	1 317	24
<b>Total fees, external auditor</b>	<b>13 810</b>	<b>21 428</b>

\* Statutory audit includes fees for discussions of financial reporting issues related to IFRS.

\*\* Includes limited reviews of the Government Pension Fund Global's quarterly financial reporting and other assurance services. 2010 amounts include NOK 5.9m related to auditing the Government Pension Fund Global's financial reporting for 2009 invoiced in 2010.

### Audit expenses in subsidiaries

Norges Bank has established subsidiaries whose activities exclusively constitute investments as part of the management of the investment portfolio of the Government Pension Fund Global.

	Amounts in NOK thousand	
	2011	2010
Statutory audit	186	-
Other assurance services	-	-
Tax advice	-	-
Other services	93	-
<b>Total fees, external auditors subsidiaries</b>	<b>279</b>	<b>-</b>

## Note 8 Foreign exchange reserves – Financial assets and financial liabilities by portfolio and currency

Norges Bank's foreign exchange reserves are divided between a long-term portfolio managed by NBIM and a money market portfolio managed by Norges Bank Monetary Policy (NBMP). The portfolios are managed under different mandates and have different risk profiles.

In addition, a buffer portfolio is used for regular transfers of foreign exchange to the investment portfolio of the Government Pension Fund Global. This portfolio receives funds from the State's Direct Financial Interest in petroleum activities (SDFI) and from Norges Bank's foreign exchange purchases in the foreign exchange market. The buffer portfolio is managed by NBIM.

Amounts in NOK million

31 Dec. 2011				
PORTFOLIOS				
	Long-term	Money market	Buffer	Total
<b>FINANCIAL ASSETS</b>				
Deposits in foreign banks	69	11 618	26	11 713
Lending associated with reverse repurchase agreements	1 313	11 231	3 420	15 964
Unsettled trades	162	-	-	162
Equities	90 778	-	-	90 778
Equities lent	0	-	-	0
Bonds and other fixed income instruments	132 023	21 713	-	153 736
Bonds lent	71	-	-	71
Financial derivatives	2	1	-	3
Other financial assets	42	-	-	42
<b>Total financial assets</b>	<b>224 460</b>	<b>44 563</b>	<b>3 446</b>	<b>272 469</b>
<b>FINANCIAL LIABILITIES</b>				
Short-term borrowing	-	-	-	-
Borrowing associated with repurchase agreements	137	-	-	137
Cash collateral received	72	-	-	72
Unsettled trades	-	9 722	-	9 722
Short-sale bonds	-	-	-	-
Financial derivatives	50	1	-	51
Other financial liabilities	3	-	-	3
<b>Total financial liabilities</b>	<b>262</b>	<b>9 723</b>	<b>-</b>	<b>9 985</b>
<b>Net foreign exchange reserves</b>	<b>224 198</b>	<b>34 840</b>	<b>3 446</b>	<b>262 484</b>

Amounts in NOK million

31 Dec. 2010				
PORTFOLIOS				
	Long-term	Money market	Buffer	Total
<b>FINANCIAL ASSETS</b>				
Deposits in foreign banks	422	461	12	895
Lending associated with reverse repurchase agreements	28 231	16 809	8 720	53 760
Unsettled trades	1 972	-	-	1 972
Equities	92 324	-	-	92 324
Equities lent	1 567	-	-	1 567
Bonds and other fixed income instruments	110 410	7 002	-	117 412
Bonds lent	24 834	-	-	24 834
Financial derivatives	21	5	-	26
Other financial assets	67	-	-	67
<b>Total financial assets</b>	<b>259 848</b>	<b>24 277</b>	<b>8 732</b>	<b>292 857</b>
<b>FINANCIAL LIABILITIES</b>				
Short-term borrowing	0	-	-	0
Borrowing associated with repurchase agreements	14 432	-	-	14 432
Cash collateral received	17 893	-	-	17 893
Unsettled trades	470	-	-	470
Short-sale bonds	1 492	-	-	1 492
Financial derivatives	212	1	-	213
Other financial liabilities	2	-	0	2
<b>Total financial liabilities</b>	<b>34 501</b>	<b>1</b>	<b>0</b>	<b>34 502</b>
<b>Net foreign exchange reserves</b>	<b>225 347</b>	<b>24 276</b>	<b>8 732</b>	<b>258 355</b>

Amounts in NOK million

31 Dec. 2011

	USD	CAD	EUR	GBP	CHF	JPY	Other	Total
<b>FINANCIAL ASSETS</b>								
Deposits in foreign banks	6 796	12	4 853	57	0	-18	13	11 713
Lending associated with reverse repurchase agreements	10 581	-	5 383	-	-	-	0	15 964
Unsettled trades	25	-	0	-	-	137	0	162
Equities	46 879	4 473	10 893	8 037	3 076	7 889	9 531	90 778
Equities lent	0	-	-	-	-	-	-	0
Bonds and other fixed income instruments	73 145	-	52 640	14 053	-	13 897	1	153 736
Bonds lent	71	-	-	-	-	-	-	71
Financial derivatives	2	-	1	0	-	-	-	3
Other financial assets	2	0	35	4	1	-	0	42
<b>Total financial assets in foreign currency</b>	<b>137 501</b>	<b>4 485</b>	<b>73 805</b>	<b>22 151</b>	<b>3 077</b>	<b>21 905</b>	<b>9 545</b>	<b>272 469</b>
<b>FINANCIAL LIABILITIES</b>								
Short-term borrowing	-	-	-	-	-	-	-	-
Borrowing associated with repurchase agreements	-	-	-	-	-	137	-	137
Cash collateral received	72	-	-	-	-	-	-	72
Unsettled trades	2 924	-	6 799	-	-	-	-	9 722
Short-sale bonds	-	-	-	-	-	-	-	-
Financial derivatives	47	-	1	3	-	-	-	51
Other financial liabilities	3	-	-	-	-	-	-	3
<b>Total financial liabilities in foreign currency</b>	<b>3 046</b>	<b>-</b>	<b>6 799</b>	<b>3</b>	<b>-</b>	<b>137</b>	<b>-</b>	<b>9 985</b>
<b>Net foreign exchange reserves</b>	<b>134 455</b>	<b>4 485</b>	<b>67 006</b>	<b>22 148</b>	<b>3 077</b>	<b>21 768</b>	<b>9 545</b>	<b>262 484</b>



Amounts in NOK million

31 Dec. 2010

	USD	CAD	EUR	GBP	CHF	JPY	Other	Total
<b>FINANCIAL ASSETS</b>								
Deposits in foreign banks	694	2	43	34	1	54	67	895
Lending associated with reverse repurchase agreements	24 427	-	28 421	455	-	430	27	53 760
Unsettled trades	1 500	-	386	-	-	86	0	1 972
Equities	44 814	3 780	13 367	9 100	3 325	7 824	10 114	92 324
Equities lent	0	-	0	0	-	-	1 567	1 567
Bonds and other fixed income instruments	63 922	44	51 571	14 835	-	11 870	-24 830	117 412
Bonds lent	1	-	3	0	-	-	24 830	24 834
Financial derivatives	1	-	-482	5	-	502	0	26
Other financial assets	1	0	12	3	51	-	0	67
<b>Total financial assets in foreign currency</b>	<b>135 360</b>	<b>3 826</b>	<b>93 321</b>	<b>24 432</b>	<b>3 377</b>	<b>20 766</b>	<b>11 775</b>	<b>292 857</b>
<b>FINANCIAL LIABILITIES</b>								
Short-term borrowing	-	-	-	-	-	-	0	0
Borrowing associated with repurchase agreements	6 664	-	6 391	831	-	546	-	14 432
Cash collateral received	7 292	-	10 146	455	-	-	-	17 893
Unsettled trades	150	-	57	-	-	263	0	470
Short-sale bonds	1 492	-	-	-	-	-	-	1 492
Financial derivatives	1	-	1 215	191	-	-1 194	0	213
Other financial liabilities	2	-	0	-	-	-	-	2
<b>Total financial liabilities in foreign currency</b>	<b>15 601</b>	<b>-</b>	<b>17 809</b>	<b>1 477</b>	<b>-</b>	<b>-385</b>	<b>0</b>	<b>34 502</b>
<b>Net foreign exchange reserves</b>	<b>119 759</b>	<b>3 826</b>	<b>75 512</b>	<b>22 955</b>	<b>3 377</b>	<b>21 151</b>	<b>11 775</b>	<b>258 355</b>

## Note 9 International reserves

Together with claims on the International Monetary Fund (IMF), foreign exchange reserves constitute Norges Bank's international reserves.

Norges Bank regularly reports International reserves to Statistics Norway and the International Monetary Fund (IMF).

The statement below shows a comparison of Norges Bank's foreign exchange reserves with its international reserves at the balance sheet date:

Amounts in NOK million

ASSETS	2011 Foreign exchange reserves	2010 Foreign exchange reserves	2011 International reserves	2010 International reserves
<b>FINANCIAL ASSETS</b>				
Deposits in banks	11 713	895	11 713	895
Lending associated with reverse repurchase agreements	15 964	53 760	15 964	53 760
Unsettled trades	162	1 972	-	-
Equities	90 778	92 324	90 778	92 324
Equities lent	0	1 567	0	1 567
Bonds and other fixed income instruments	153 736	117 412	153 736	117 412
Bonds lent	71	24 834	71	24 834
Financial derivatives	3	26	3	26
Claims on the International Monetary Fund	-	0	31 300	29 624
Other financial assets	42	67	-	-
<b>Total financial assets</b>	<b>272 469</b>	<b>292 857</b>	<b>303 565</b>	<b>320 442</b>
<b>TOTAL ASSETS</b>	<b>272 469</b>	<b>292 857</b>	<b>303 565</b>	<b>320 442</b>

LIABILITIES	2011 Foreign exchange reserves	2010 Foreign exchange reserves	2011 International reserves	2010 International reserves
<b>FINANCIAL LIABILITIES</b>				
Short-term borrowing	-	-	-	-
Borrowing associated with repurchase agreements	137	14 432	-	-
Cash collateral received	72	17 893	-	-
Unsettled trades	9 722	470	-	-
Short-sale bonds	0	1 492	0	1 492
Financial derivatives	51	213	51	213
Other financial liabilities	3	2	-	-
Liabilities to the International Monetary Fund	-	-	12 361	11 615
<b>Total financial liabilities</b>	<b>9 985</b>	<b>34 502</b>	<b>12 412</b>	<b>13 320</b>
<b>TOTAL LIABILITIES</b>	<b>9 985</b>	<b>34 502</b>	<b>12 412</b>	<b>13 320</b>
<b>TOTAL FOREIGN EXCHANGE RESERVES</b>	<b>262 485</b>	<b>258 356</b>		
<b>TOTAL INTERNATIONAL RESERVES</b>			<b>291 153</b>	<b>307 122</b>

## Note 10 Repurchase and reverse repurchase agreements

### Portfolio distribution, lending associated with repurchase agreements

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Lending associated with the long-term portfolio	1 313	28 231
Lending associated with the money market portfolio	11 231	16 809
Lending associated with the buffer portfolio	3 420	8 720
<b>Total lending associated with repurchase agreements</b>	<b>15 964</b>	<b>53 760</b>

### Portfolio distribution, lending associated with reverse repurchase agreements

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Borrowing associated with the long-term portfolio	137	14 432
Borrowing associated with the money market portfolio	0	0
Borrowing associated with the buffer portfolio	0	0
<b>Total borrowing associated with repurchase and reverse repurchase agreements</b>	<b>137</b>	<b>14 432</b>

Norges Bank uses the markets for repurchase and reverse repurchase agreements in its financing activities internally and through securities lending programmes (See Note 12 External agency securities lending). At any time the Bank will have lent portions of its holdings in bonds through repurchase agreements, against receiving a corresponding amount in cash (repos and sell buy backs). This may be a form of financing asset management (borrowing of cash), or lending securities with the aim of reinvesting received cash at a higher interest rate and thus creating additional income or returns. In addition, the Bank is a party to reverse

repurchase agreements where the counterparty has transferred bonds or equities to the Bank and where the Bank has transferred cash to the counterparty (reverse repo, buy sell backs and triparties). Such contracts are used in connection with placing liquidity and also through agency securities lending as reinvestments of cash collateral received related to lent securities. Rules have been laid down regarding the types of securities eligible as collateral. To be eligible as collateral, bonds shall have a credit rating of at least A or the equivalent from at least one of the rating agencies Fitch, Moody's or Standard & Poor's.

For repurchase agreements, the lent security is not derecognised. Received cash is recognised as Deposits in banks, with a corresponding liability to pay back the cash, recognised as Borrowing associated with repurchase agreements. For reverse repurchase agreements, the security received as collateral is not recognised in the balance sheet, while transferred cash is derecognised from Deposits in banks. A corresponding receivable is recognised as an asset, Lending associated with reverse repurchase agreements.

In the second half of 2011, the volume of outstanding repurchase and reverse repurchase agreements was reduced significantly, especially in EUR-denominated securities, as part of a reduction in exposures due to high financial market risk.

The following table shows total outstanding repurchase and reverse repurchase agreements at year-end 2011, with comparative amounts for 2010, and corresponding securities collateral or lent securities. In order to show the total exposure for the contracts, unsettled trades have been shown separately and are included under received and posted collateral/lent securities. This securities collateral has not yet been transferred and therefore is not included in the lines Bonds posted as collateral or lent and Bonds/Equities received as collateral in the table, while the corresponding cash amount to be transferred is included in Borrowing associated with repurchase agreements and Lending associated with reverse repurchase agreements.

Amounts in NOK million

Repurchase and reserve repurchase agreements	2011		2010	
	Carrying amount	Fair value	Carrying amount	Fair value
<i>Repurchase agreements</i>	-	-	-	-
Borrowing associated with repurchase agreements (cash borrowed or received as collateral)	137	137	14 432	14 432
Bonds posted as collateral or lent (asset)	-	-	14 180	14 180
Unsettled trades (asset)*	137	137	-	84
<b>Net overcollateralisation (undercollateralisation) repurchase agreements</b>	<b>-</b>	<b>-</b>	<b>252</b>	<b>168</b>
<i>Reverse repurchase agreements</i>				
Reverse repurchase agreements outside of securities lending programme	15 916	15 916	39 534	39 534
Reverse repurchase agreements through securities lending programme (reinvestment of cash collateral)	48	48	14 226	14 226
<b>Lending associated with reverse repurchase agreements (cash lent or invested)</b>	<b>15 964</b>	<b>15 964</b>	<b>53 760</b>	<b>53 760</b>
Bonds received as collateral	-	9 939	-	55 339
<b>Total collateral received reverse repurchase agreements</b>	<b>-</b>	<b>9 939</b>	<b>-</b>	<b>55 339</b>
Unsettled trades (liability)**	-	6 323	-	-
<b>Net overcollateralisation (undercollateralisation) reverse repurchase agreements</b>	<b>-</b>	<b>298</b>	<b>-</b>	<b>1 579</b>
<b>Net overcollateralisation (undercollateralisation) repurchase and reverse repurchase agreements</b>	<b>-</b>	<b>298</b>	<b>-</b>	<b>1 747</b>

\* Cash not yet received, securities not transferred to counterparty. Repurchase agreement transaction has been recognised.

\*\* Cash not yet transferred, securities not received from counterparty. Reverse repurchase agreement transaction has been recognised.

Outstanding repurchase agreements in the long-term portfolio were reduced by 99% from year-end 2010 to year-end 2011, while outstanding reverse repurchase agreements were reduced by 95% in the same period. The change was implemented in the fourth quarter and was due to high risk in the financial markets.

The long-term portfolio and money market portfolio had zero in net overcollateralisation with regard to repurchase agreements at year-end 2011. This is because all outstanding contracts in the long-term portfolio were unsettled at year-end. However, the long-term portfolio is overcollateralised with regard to reverse repurchase agreements in the amount of NOK 23m, since the Bank had an excess of

received securities collateral relative to cash placed in this amount. The corresponding overcollateralisation as at year-end 2011 was NOK 23m for the long-term portfolio and NOK 298m in total for Norges Bank.

Outside of securities lending programmes, Norges Bank had lent a net amount of NOK 1.1bn for the long-term portfolio at year-end. This comprises the net effect of cash borrowed of NOK 137m and cash lent of NOK 1.3bn. See also a further description of leverage in Note 23 Risk and in Note 12 External agency securities lending, which discuss the leverage effect of the activity in securities lending programmes.

## Note 11 Equities, bonds and other fixed income instruments

The table below shows a specification of equities and units:

	31 Dec. 2011			31 Dec. 2010		
	Fair value excluding dividends	Accrued dividends	Fair value including dividends	Fair value excluding dividends	Accrued dividends	Fair value including dividends
Equities:						
Listed equities	90 620	158	90 778	93 774	117	93 891
<b>Total equities</b>	<b>90 620</b>	<b>158</b>	<b>90 778</b>	<b>93 774</b>	<b>117</b>	<b>93 891</b>
<i>Of which equities lent</i>			-			1 567
<i>Of which equities</i>			90 778			92 324

The table below shows a specification of bonds and other fixed income instruments:

Amounts in NOK million

31 Dec. 2011	Nominal value*	Fair value excluding accrued interest	Accrued interest	Fair value including accrued interest
Government bonds:				
Government bonds issued in local currency	120 029	131 221	1 103	132 324
<b>Total government bonds</b>	<b>120 029</b>	<b>131 221</b>	<b>1 103</b>	<b>132 324</b>
Government-related bonds: Sovereign bonds**				
Bonds issued by local authorities	99	58	4	62
Bonds issued by international organisations	-	-	-	-
Bonds issued by federal agencies	74	34	1	35
<b>Total government-related bonds</b>	<b>192</b>	<b>97</b>	<b>5</b>	<b>102</b>
Inflation-linked bonds:				
Inflation-linked bonds issued by government authorities	-	-	-	-
<b>Total inflation-linked bonds</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Corporate bonds:				
Bonds issued by utilities	-	-	-	-
Bonds issued by financial institutions	389	114	2	116
Bonds issued by industrial companies	36	41	-	41
<b>Total corporate bonds</b>	<b>425</b>	<b>155</b>	<b>2</b>	<b>157</b>
Securitised bonds:				
Covered bonds	16 325	15 201	310	15 511
Mortgage-backed securities	4 107	1 184	7	1 191
Asset-backed securities	875	749	1	750
Commercial mortgage-backed securities	73	53	-	53
<b>Total securitised bonds</b>	<b>21 380</b>	<b>17 187</b>	<b>318</b>	<b>17 505</b>
<b>Total Treasury bills</b>	<b>3 719</b>	<b>3 719</b>	<b>-</b>	<b>3 719</b>
<b>Total bonds and other fixed income instruments</b>	<b>145 745</b>	<b>152 379</b>	<b>1 428</b>	<b>153 807</b>
<i>Of which bonds lent</i>				71
<i>Of which short-sale bonds</i>				-
<i>Of which bonds and other fixed income instruments</i>				153 736

\* Nominal values have been translated into NOK at the closing rate at the balance sheet date. The nominal value comprises the face value of the instrument or principal.

Amounts in NOK million

31 Dec. 2010	Nominal value*	Fair value excluding accrued interest	Accrued interest	Fair value including accrued interest
Government bonds:				
Government bonds issued in local currency	87 303	89 154	851	90 005
<b>Total government bonds</b>	<b>87 303</b>	<b>89 154</b>	<b>851</b>	<b>90 005</b>
Government-related bonds:				
Sovereign bonds**	948	950	20	970
Bonds issued by local authorities	1 082	1 063	32	1 095
Bonds issued by international organisations	3 659	3 844	54	3 898
Bonds issued by federal agencies	3 414	3 600	90	3 690
<b>Total government-related bonds</b>	<b>9 102</b>	<b>9 457</b>	<b>196</b>	<b>9 653</b>
Inflation-linked bonds:				
Inflation-linked bonds issued by government authorities	3 327	3 308	3	3 311
<b>Total inflation-linked bonds</b>	<b>3 327</b>	<b>3 308</b>	<b>3</b>	<b>3 311</b>
Corporate bonds:				
Bonds issued by utilities	1 427	1 513	28	1 541
Bonds issued by financial institutions	6 968	6 463	128	6 591
Bonds issued by industrial companies	3 421	3 680	79	3 759
<b>Total corporate bonds</b>	<b>11 816</b>	<b>11 656</b>	<b>235</b>	<b>11 891</b>
Securitised bonds:				
Covered bonds	19 079	18 285	361	18 646
Mortgage-backed securities	8 062	2 302	20	2 322
Asset-backed securities	2 331	2 043	2	2 045
Commercial mortgage-backed securities	2 123	260	7	267
<b>Total securitised bonds</b>	<b>31 595</b>	<b>22 890</b>	<b>390</b>	<b>23 280</b>
<b>Total Treasury bills</b>	<b>1 744</b>	<b>2 614</b>	<b>-</b>	<b>2 614</b>
<b>Total bonds and other fixed income instruments</b>	<b>144 888</b>	<b>139 079</b>	<b>1 675</b>	<b>140 754</b>
<i>Of which bonds lent</i>				24 834
<i>Of which short-sale bonds</i>				1 492
<i>Of which bonds and other fixed income instruments</i>				117 412

\* Nominal values have been translated into NOK at the closing rate at the balance sheet date. The nominal value comprises the face value of the instrument or principal

\*\* As from 1 January 2011, sovereign bonds are included in government related bonds. Comparative amounts have been restated.

## Note 12 External agency securities lending

For the long-term portfolio, Norges Bank has entered into securities lending agreements with external agents, giving these agents the right to lend securities held by the investment portfolios managed by Norges Bank to other market participants with borrowing needs. Both equities and bonds are lent through the securities lending programmes. The purpose of the lending activity is to create additional returns for the Bank from its securities holdings. When a security is lent, the borrower transfers collateral to the agent in the form of cash or securities. The collateral is held on behalf of Norges Bank. Agreements with agents have provisions reducing the bank's counterparty risk in cases where collateral has been received in the form of cash or government bonds. These provisions ensure the bank will be compensated if the counterparty is unable to return the borrowed securities or if the collateral posted for the loan is insufficient to cover any losses in the event of borrower default. Norges Bank bears this risk itself in cases where collateral has been received in the form of equities. Reinvestments by the agent of cash collateral received take the form of positions in the repo market: reverse repurchase agreements, buy sell backs and triparties (see Note 10 Repurchase and reverse repurchase agreements); and in the form of bonds. At 31 December 2011, bonds accounted for 31% of total reinvestments. By comparison, bonds accounted for 19% of total reinvestments at year-end 2010. See the discussion of the change in total volume below.

Securities lent are presented on separate lines in the balance sheet. Cash collateral received is recognised in the

balance sheet as part of Deposits in banks with a corresponding liability Cash collateral received, since Norges Bank has the right to dispose of this cash. Collateral received in the form of securities is not recognised in the balance sheet, because these are not reused (rehypothecated), but are left in custody. Reinvestments in the form of reverse repurchase agreements and bonds are recognised in the balance sheet in the same manner as ordinary investments. Due to increased risk in financial markets in the second half of 2011, Norges Bank reduced its lending programme towards year-end. Exposure has been reduced in general, and specifically with regard to securities lending and collateral denominated in euro and collateral in the form of US securitised bonds.

Norges Bank earns a net income from these securities lending programmes. The net income comprises the pure lending fee, from which costs related to cash collateral received are subtracted, as well as interest income and realised returns from reinvestments. The agent's portion, which is a consideration for carrying out the transactions, is also deducted. Net income from securities lending is presented on the income statement line Net income/expenses and gains/losses from equities and Net income/expenses and gains/losses from bonds and other fixed income instruments. Net income related to equities lending within the long-term portfolio amounted to NOK 44m in 2011, while the corresponding income from bond lending amounted to NOK 24m in 2011 (see also Note 3 Net income from financial instruments). Corresponding amounts for year-end 2010 were NOK 66m and NOK 40m, respectively.



The tables present an overview of positions within external agent securities lending programmes at year-end 2011 compared with year-end 2010:

Amounts in NOK million

	31 Dec. 2011		31 Dec. 2010	
	Carrying amount	Fair value	Carrying amount	Fair value
Securities lent				
Equities lent	-	-	1 567	1 567
Bonds lent	71	71	24 834	24 834
Total securities lent	71	71	26 401	26 401
<b>Collateral received</b>				
Cash collateral received	72	72	17 893	17 893
Equities received as collateral	-	-	-	1 022
Bonds received as collateral	-	-	-	7 072
<b>Total collateral received related to securities lending</b>	<b>72</b>	<b>72</b>	<b>17 893</b>	<b>25 987</b>
<b>Net overcollateralisation</b>	<b>1</b>	<b>1</b>	<b>-</b>	<b>-414</b>

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
<b>Reinvestment related to securities lending</b>		
Reverse repurchase agreements	49	14 226
Asset-backed securities	-	2 616
Other fixed income instruments	-	779
Total reinvestment in the form of bonds and other fixed income instruments	23	3 395
<b>Total reinvestment of cash collateral</b>	<b>72</b>	<b>17 621</b>
Unrealised loss bonds and other fixed income instruments	-	268

## Note 13 Financial derivatives

The first table is a specification of financial derivative holdings at market value as at 31 December 2011 and 31 December 2010, classified as assets or liabilities. The second table shows the nominal values of positions in finan-

cial derivatives for purchased (long) and sold (short) positions as exposure. Nominal values are the basis for the calculation of any cash flows and gains/losses for the contracts.

Amounts in NOK million

	Fair value					
	31 Dec. 2011			31 Dec. 2010		
	Assets	Liabilities	Net	Assets	Liabilities	Net
<b>Foreign exchange contracts</b>	-	-	-	14	12	2
<b>Listed futures contracts</b>	3	49	-46	7	9	-2
Interest rate swaps	-	-	-	-	185	-185
Credit default swaps	-	-	-	-	-	-
Equity swaps	-	2	-2	5	7	-2
<b>Total swap contracts</b>	-	2	-2	5	192	-187
<b>Options</b>	-	-	-	-	-	-
<b>Total financial derivatives</b>	3	51	-48	26	213	-187

Amounts in NOK million

	Exposure							
	2011		Average 2011		2010		Average 2010	
	Purchased	Sold	Purchased	Sold	Purchased	Sold	Purchased	Sold
<b>Foreign exchange contracts</b>	-	-	2 385	-	5 217	-	12 171	118
<b>Listed futures contracts</b>	2 224	7 050	6 370	3 303	18 061	271	22 689	2 000
Interest rate swaps	-	-	-	1 035	-	1 587	1 248	4 386
Credit default swaps	-	-	-	-	-	-	198	36
Equity swaps	-	5	6	3	38	10	14	14
<b>Total swap contracts</b>	-	5	6	1 038	38	1 597	1 460	4 436
<b>Options</b>	-	-	-	-	-	-	1 135	608
<b>Total financial derivatives</b>	2 224	7 055	8 761	4 341	23 316	1 868	37 455	7 162

For a description of foreign exchange contracts, listed futures contracts, swaps and options, see Note 24 GPFG Note 9.

The table below shows received and posted collateral related to positions in financial derivatives in the investment portfolio:

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
<b>Futures contracts and equity swaps</b>		
Fair value futures contracts	-46	-7
Fair value equity swaps	-2	-2
Deposits with clearing brokers (collateral posted)	55	87
Bonds posted as collateral to clearing brokers	-176	-136

## Note 14 International Monetary Fund

The task of the International Monetary Fund (IMF) is to promote international monetary and financial stability. The IMF gives advice to member countries and provides temporary funding in the event of balance of payments pro-

blems. Norges Bank administers Norway's financial rights and fulfils the obligations ensuing from participation in the IMF.

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
<i>Financial assets</i>		
Special Drawing Rights	13 995	14 470
Quota in the International Monetary Fund	17 304	15 170
Loan to the International Monetary Fund, New Arrangements to Borrow (NAB)	3 708	-
Bilateral loan to the International Monetary Fund,	-	2 458
Loans to the International Monetary Fund's arrangements for low-income countries, the Poverty Reduction and Growth Trust (PRGT)	1 106	230
<b>Claims on the on the International Monetary Fund</b>	<b>36 113</b>	<b>32 328</b>
<i>Financial liabilities</i>		
Krone liability to the International Monetary Fund	12 361	11 623
Equivalent value of allocated Special Drawing Rights	14 359	14 185
<b>Liabilities to the International Monetary Fund</b>	<b>26 720</b>	<b>25 808</b>

### Special Drawing Rights

The Special Drawing Right (SDR) is an international reserve asset created by the IMF in 1969. The value of SDRs is calculated on the basis of a currency basket comprising US dollars, euros, sterling and Japanese yen. The composition of the SDR is evaluated every five years.

### Equivalent value of allocated Special Drawing Rights

SDRs are periodically allocated to IMF member countries, most recently in 2010. The equivalent value of allocated SDRs in the IMF shows total allocations of SDRs since the scheme entered into force. At year-end 2011, SDR 1 563.1 has been allocated to Norway.

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Special Drawing Rights in the International Monetary Fund	13 995	14 470
Equivalent value of Special Drawing Rights in the International Monetary Fund	14 359	14 185

## Reserve position in the IMF

### IMF quotas

The IMF allocates quotas to member countries. The quota determines the member country's financial contribution to the IMF and provides the basis for determining the amount of financing the member can obtain in the event of balance of payments problems. 75% of the quota is paid to the IMF in the country's own currency, while the remainder is normally paid in SDRs or a widely used foreign currency. In 2011, Norway's quota increased from SDR 1 671.7m to SDR 1 883.7m.

### NOK liability

The IMF has deposited its NOK holdings with Norges Bank. The IMF translates all transactions on this account from NOK to SDRs and keeps its account in SDRs. The IMF's claim on Norges Bank is in SDRs, and its NOK holdings with Norges Bank are adjusted to eliminate any foreign exchange rate risk the IMF would have on its NOK holdings with Norges Bank. At 31 December 2011, the NOK liability to the IMF was SDR 1 345.6m.

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Quota in the International Monetary Fund	17 304	15 170
NOK liability to the International Monetary Fund	12 361	11 623
<b>Reserve position in the International Monetary Fund</b>	<b>4 943</b>	<b>3 547</b>

## Lending to the IMF

In 2009, the IMF decided to expand its lending capacity to meet the sharp increase in demand for loans in the wake of the financial crisis. In this connection, Norway concluded a bilateral loan agreement in 2010, which was superseded by the IMF's multilateral New Arrangement to Borrow (NAB). At 31 December 2011, Norges Bank's NAB loans total SDR 403.6m or NOK 3 708m.

Loans to the IMF Poverty Reduction and Growth Trust (PRGT) amount to SDR 120m or NOK 1 106m at 31 December 2011, compared with NOK 2 688m at 31 December 2010. Loan resource commitments to the PRGT are SDR 300m.

## Net interest income on claims on/liabilities to the International Monetary Fund

Amounts in NOK million

	2011	2010
<i>Interest income</i>		
Interest on Special Drawing Rights	54	43
Interest on the quota in the International Monetary Fund	60	42
Interest on loans to the International Monetary Fund, New Arrangements to Borrow	9	3
Interest on bilateral loans to the International Monetary Fund	3	1
Interest on loans to the International Monetary Fund arrangements for low-income countries, the Poverty Reduction and Growth Trust (PRGT)	5	1
<b>Interest income, International Monetary Fund</b>	<b>131</b>	<b>90</b>
<i>Interest expenses</i>		
Interest on NOK liability to the International Monetary Fund	45	35
Interest on equivalent value of allocated Special Drawing Rights	55	42
<b>Interest expenses, International Monetary Fund</b>	<b>100</b>	<b>77</b>
<b>Net interest income, claims on/liabilities to the International Monetary Fund</b>	<b>31</b>	<b>13</b>

## Note 15 Lending to banks

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Fixed-rate loans to banks	25 241	60 057
<b>Lending to banks</b>	<b>25 241</b>	<b>60 057</b>

### Lending to banks

Lending to banks is in the form of fixed-rate loans provided against collateral in approved securities pledged in favour of Norges Bank, or fixed-rate deposits and collateral in the form

of deposits in banks' own accounts with Sveriges Riksbank and Danmarks Nationalbank. Loan maturities averaged 0.9 month in 2011, compared with 2.0 months in 2010.

## Note 16 Other financial assets

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Receivables from, Government Pension Fund Global related to management fee	2 539	2 959
Receivables from, Government Pension Fund Global related to investments	0	4 322
Loan to Seðlabanki Íslands	3 720	1 872
Loans to employees	494	486
Shares in the BIS	94	94
Other financial assets	205	227
<b>Other financial assets</b>	<b>7 052</b>	<b>9 960</b>

### Loan to Iceland

As at 31 December 2011, Seðlabanki Íslands had drawn NOK 3 720m under a bilateral loan agreement with Norges Bank. The loan is guaranteed by the Icelandic and Norwegian governments.

### Loans to employees

The Bank's loan scheme for its employees comprises residential mortgages and consumer loans. Mortgages are provided in accordance with guidelines from the Supervisory Council as first mortgages within 85% of assessed value, limited to NOK 2 360 000 and a maximum term of 30 years. Consumer loans are limited to a maximum of four times the employee's monthly salary. The loan schemes apply to all employees. In 2011, the interest rate was linked to the norm rate (the norm rate for loans on favourable terms from an employer). The Ministry of Finance sets the norm rate up to 6 times a year, and through 2011, the interest rate was 2.75%.

### Shares in the BIS

Norges Bank has been allocated a total of 8000 shares at SDR 5000 in the Bank for International Settlements (BIS). 25% of the shares, valued at NOK 25m, have been paid for. These are recognised under the item Other assets. Norges Bank has not paid up the share capital for 75% of the shares. There is a conditional liability amounting to NOK 291m attached to shares purchased plus previously allotted shares. The portion of the conditional liability corresponding to the value of the shares at the time of allotment, i.e. NOK 23m, is recognised under the item Other financial liabilities. The remainder of the conditional liability, NOK 272m, is not recognised in the balance sheet but shown in the note. In 2011, dividend received on BIS shares amounted to NOK 22m.

## Note 17 Other non-financial assets:

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Non-current assets	1 461	1 516
Gold	373	373
Art and numismatic collections	82	82
Other assets	21	23
<b>Other non-financial assets</b>	<b>1 855</b>	<b>1 912</b>

## IFRS effects for other non-financial assets

Amounts in NOK million

	31 Dec. 2009	Reclassification effects	IFRS effects	1 Jan. 2010
Non-current assets	1 604		-	1 604
Gold	291		-	291
Art and numismatic collections	-		82	82
Other assets	275	-247	-	28
<b>Other non-financial assets</b>	<b>2 170</b>	<b>-247</b>	<b>82</b>	<b>2 005</b>

## Non-current assets

The table below shows a specification of non-current assets broken down into intangible assets and property, plant and equipment in 2011 and 2010.

Amounts in NOK thousand

2011									
	Intang. assets	Property, plant and equipment							Total
	Soft-ware	Vehicles, mach. IT-equip.	Security system	Mach. fixtures	Buildings with install.	Bank-building, Bank-plassen 2	Plant under constr.	Land	
Cost at 1 Jan.	229 341	26 300	67 287	15 971	823 515	1 657 410	7 952	59 881	2 887 657
+ Transfers from plant	6 499	0	0	0	0	0	-6 499	0	0
+Additions	10 124	580	0	4 150	11 302	0	18 745	0	44 901
- Disposals	8 127	292	5 877	1 853	20 627	0	0	0	36 776
-/+Adjustments	0	0	0	0	0	0	0	0	0
<b>Cost at 31 Dec.</b>	<b>237 837</b>	<b>26 588</b>	<b>61 410</b>	<b>18 268</b>	<b>814 190</b>	<b>1 657 410</b>	<b>20 198</b>	<b>59 881</b>	<b>2 895 782</b>
- Accumulated depreciation and impairment	146 537	23 343	47 823	9 947	442 230	765 103	0	0	1 434 983
<b>Carrying amount at 31 Dec.</b>	<b>91 300</b>	<b>3 245</b>	<b>13 587</b>	<b>8 321</b>	<b>371 960</b>	<b>892 307</b>	<b>20 198</b>	<b>59 881</b>	<b>1 460 799</b>
<b>Depreciation for the year</b>	<b>28 569</b>	<b>2 035</b>	<b>8 458</b>	<b>2 316</b>	<b>32 690</b>	<b>18 697</b>	<b>0</b>	<b>0</b>	<b>92 765</b>
<b>Impairment for the year</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Depreciation schedule, no. of years	5-6	5	6-7	5-10	5-27	20-75	none	none	

Amounts in NOK thousand

2010										
	Intang. assets	Property, plant and equipment							Total	
	Soft-ware	Vehicles, mach. IT-equip.	Security system	Mach. fixtures	Buildings with install.	Bank-building, Bank-plassen 2	Plant under constr.	Cabin		Land
Cost at 1 Jan.	231 143	26 702	62 625	13 364	789 619	1 657 410	26 696	436	59 881	2 867 876
+ Transfers from plant	18	0	0	0	24 179	0	-24 197	0	0	0
+Additions	1	0	4 915	2 607	14 380	0	5 453	0	0	27 356
- Disposals	1 821	402	252	0	4 664	0	0	436	0	7 575
-/+Adjustment costs at 31 Dec.	0	0	0	0	0	0	0	0	0	0
<b>Carrying amount at 31 Dec.</b>	<b>229 341</b>	<b>26 300</b>	<b>67 287</b>	<b>15 971</b>	<b>823 515</b>	<b>1 657 410</b>	<b>7 952</b>	<b>0</b>	<b>59 881</b>	<b>2 887 657</b>
- Accumulated depreciation and impairment	125 233	21 498	45 241	8 961	424 558	746 406	0	0	0	1 371 897
<b>Carrying amount at 31 Dec.</b>	<b>104 108</b>	<b>4 802</b>	<b>22 046</b>	<b>7 010</b>	<b>398 957</b>	<b>911 004</b>	<b>7 952</b>	<b>0</b>	<b>59 881</b>	<b>1 515 760</b>
<b>Depreciation for the year</b>	<b>31 371</b>	<b>2 179</b>	<b>8 315</b>	<b>1 830</b>	<b>32 734</b>	<b>950</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>77 379</b>
<b>Impairment for the year</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Depreciation schedule, no. of years	5-6	5	6-7	5-10	5-27	20-50	none	none	none	

### Impairment testing

Plant under construction primarily comprises writing and adapting software. Non-current assets that have not been brought into use and are not included in a depreciation schedule are tested annually for impairment. Impairment will be determined on the basis of cost overruns and project delays. No impairment was identified for 2011.

### Buildings

#### Change in depreciation schedule:

In 2011, the depreciation schedule for Bankplassen 2 was changed. The original depreciation period was 50 years. The depreciation period was extended by 25 years. The change in depreciation schedule does not apply retroactively. A new annual depreciation amount has been included as from 2011.

### Bankplassen 4:

Bankplassen 4 is being leased to the government for 80 years until 21 November 2066 (Museum of Contemporary Art). The contract of lease is dated 21 November 1986. The deadline for non-renewal is 21 November 2065. The building is not recognised in Norges Bank's balance sheet.

### Restatement of comparative amounts:

Amortisation of the Revaluation Fund for 2010 has been reversed in connection with the transition to IFRS. Depreciation for the year 2010 has been reduced by NOK 37.0m from NOK 114.4m to NOK 77.4. The depreciation pertains to the lines Buildings with installations and Bankplassen 2, in the amounts of NOK 0.7m and NOK 36.2m, respectively.

## Note 18 Other financial liabilities

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Share capital in BIS not paid up	23	23
Current liability Norges Bank and the investment portfolio of the Government Pension Fund Global	2 370	-
Other financial liabilities	291	382
<b>Total other financial liabilities</b>	<b>2 684</b>	<b>405</b>
Allocated, unpaid shares in the BIS	272	268

## Note 19 Deposits from banks etc.

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010
Sight deposits from banks	41 524	79 809
Fixed-rate deposits from banks	50 519	-
Other deposits	91	89
<b>Deposits from banks etc.</b>	<b>92 134</b>	<b>79 898</b>

See Note 3 for a description of sight deposits and fixed-rate deposits with associated interest rate terms.

## Note 20 Notes and coins in circulation

Notes and coins in circulation are recognised in the amount of NOK 54.8bn and correspond to the total face value of all notes and coins put into circulation.

Norges Bank is obliged to redeem notes and coins for 10 years following the decision to withdraw them as legal tender. In 2011, redeemed/invalidated banknotes and coins amounting to NOK 3.8m were charged as an expense in Norges Bank's financial statements



## Note 21 Pension benefit obligation

Norges Bank has funded and unfunded pension and other benefit obligations. All funded and unfunded plans are included in the Bank's actuarial settlement and are carried at fair value.

Norges Bank's funded pension benefit obligations are covered by Norges Bank's own pension fund, which is organised as a separate legal entity. Retirement benefits are equal to 2/3 of the employee's salary at the time of retirement. The period of service for full benefits is 30 years. Employees contribute 2% of their gross annual salary into the pension fund. Norges Bank's contribution for 2011 was covered partly by cash payments and partly by capital saved in the premium fund. Benefits from the pension fund are coordinated with benefits from the National Insurance scheme.

The basis for retirement benefits covered by the funded plan is limited to an amount equivalent to 12 times the basic pension (G). An unfunded pension plan funded out of current income was established as from 2007 to cover that portion of pensionable salaries in excess of 12G for those employees who already had an agreement entitling them to pension over and above this limit. For those whose employment began after 1 January 2007, the basis for retirement benefits is limited to 12G. The pension plan complies with public service pension requirements.

The pension benefit obligation of Norges Bank's funded plans is NOK 2 404m. Assumptions concerning mortality and other demographic factors are based on the standard K 2005 basis for group pension insurance. The IR 73 rate is used as a basis for calculating disability provisions. A 3%

supplement for future administration costs is priced into the pension benefit obligation. Retirement benefits pertaining to the individual employee are calculated on the basis of retirement benefits earned or received as at 31 December 2011. The pension benefit obligation is equivalent to the calculated cash value of benefits earned. The Bank's funded pension plan covers 2 349 persons, of whom 988 are drawing retirement benefits, 640 are active members (including all those affected by restructuring) and 721 are members who have left the Bank with vested rights.

### Norges Bank's benefit obligations

Norges Bank applies IFRS for its financial reporting as from 1 January 2011. Comparative amounts have been restated accordingly. Benefit obligations have been calculated in accordance with IAS 19. Implementation effects are described in Note 1. In connection with adoption of IFRS, Norges Bank has chosen to change the accounting policy for recognising the pension benefit obligation.

Norges Bank has funded pension plans associated with membership in Norges Bank's pension fund. In addition, the Bank has unfunded plans funded out of current income. These are special and allocated pensions, the unfunded portions of pensions for employees with salaries higher than 12G earned after 1 January 2007, contractual early retirement pensions calculated on the basis of an expected 15% take-up rate and early retirement pensions and redundancy pay agreements related to restructuring. The benefit obligation related to restructuring is the present value of all agreements, including agreements with disbursements in 2011 or later.

Economic assumptions underlying the calculations:

	2011	2010
Discount rate	2.60%	4.00%
Pension adjustment after the age of 67	2.50%	3.00%
Basic pension rate adjustment and adjustment of vested rights	3.28%	3.75%
Expected wage growth	3.50%	4.00%
Expected return on plan assets	4.10%	5.40%
Expected annual attrition	2% up to age 50, then 0	2% up to age 50, then 0

Demographic assumptions:

Standard FNO/Storebrand Pensjonstjenester with 5% reduction in mortality relative to the Financial Supervisory Authority of Norway's margins of safety.

Specification of benefit obligations in the balance sheet:

Amounts in NOK million

	31 Dec. 2011	31 Dec. 2010	1 Jan. 2010
<b>Funded pension benefit obligation:</b>			
Funded plans through the pension fund	-1 387	-465	-843
<b>Unfunded benefit obligations</b>			
Special pensions and allocated pensions	-94	-80	-66
Benefit obligations associated with restructuring	-49	-66	-93
Unfunded portion of pension, for salaries in excess of 12G	-51	-35	-74
Contractual early retirement expected take-up rate	-25	-21	-20
Norsk Kontantservice AS, part of lump-sum premium	-3	-7	-12
<b>Total benefit obligations</b>	<b>-1 609</b>	<b>-674</b>	<b>-1 108</b>

Benefit obligation specified by funded and unfunded plans:

Amounts in NOK million

	31 Dec. 2011		
	Funded plan	Unfunded plans	Total
Accrued benefit obligations	-4 182	-222	-4 404
Fair value of plan assets	2 795	-	2 795
<b>Net plan assets / (-) benefit obligation</b>	<b>-1 387</b>	<b>-222</b>	<b>-1 609</b>

Amounts in NOK million

	31 Dec. 2010		
	Funded plan	Unfunded plans	Total
Accrued benefit obligations	-3 165	-209	-3 374
Fair value of plan assets	2 700	-	2 700
<b>Net plan assets / (-) benefit obligation</b>	<b>-465</b>	<b>-209</b>	<b>-674</b>

Plan assets in funded plan are allocated as follows:

Allocation of plan assets for funded (defined-benefit) plan	2011	2010
Bonds	75 %	73 %
Equities	25 %	27 %
<b>Total overfunding of benefit obligations</b>	<b>100 %</b>	<b>100 %</b>

#### Pension expense for employees in Norway

Pension expense has been calculated in accordance with IAS 19 Employee Benefits and includes current service cost, interest expense and expected return on plan assets. Norges

Bank's share of the lump-sum premiums for employees of Norsk Kontantservice AS previously employed by Norges Bank is included in pension expense.

The change in special and allocated benefits is included in the Bank's overall pension expense. Pension expense is shown in the table below:

	Amounts in NOK million	
	2011	2010
Pension expense, funded plan, which comprises:	82	181
Current service cost	103	81
Interest expense on benefit obligation	120	141
Expected return on plan assets	-131	-115
Recognised actuarial loss	-	82
Recognised curtailment	-	-
Members' contributions	-10	-8
Administration expenses		
Special pensions and allocated pensions	10	5
Unfunded portion of pension for salaries in excess of 12 G funded out of current income	3	3
Norsk Kontantservice AS, employees previously employed by Norges Bank	-	2
<b>Net pension expense</b>	<b>95</b>	<b>191</b>
<b>Net actuarial (loss) gain pensions</b>	<b>-1 118</b>	<b>413</b>
Restructuring costs	2	5
Actuarial (loss) gain restructuring	-10	3
<b>Total actuarial (loss) gain</b>	<b>-1 128</b>	<b>416</b>

### Pension plans for locally employed staff of foreign offices

Locally employed staff at Norges Bank's offices in London and New York have a defined-contribution pension plan in accordance with local provisions in addition to what has been established by the authorities. As employer, Norges Bank contributes up to 8% of fixed salary for employees in New York and up to 10% of fixed salary for employees in London to the plans in line with market practice. The plans are managed externally, within rules determined by Norges Bank. Recognised expenses for the plans in London and New York amounted to NOK 5.2m in 2011 and NOK 3.8m in 2010. Locally employed staff at Norges Bank's offices in Singapore and Shanghai have no pension plan beyond what has been established by the authorities, which is in line with market practice.

### Restructuring expense

Restructuring expense is related to study packages, redundancy pay and early retirement pensions.

## Note 22 Fair value measurement of financial instruments

### 22.1 Long-term portfolio

For a discussion of the control environment and valuation techniques for long-term reserves, see Note 24 GPF Note 13 Fair value measurement.

#### Valuation uncertainty

All equities, bonds and financial derivatives have been allocated to categories reflecting assessed valuation uncertainty. Level 1 comprises investments that are valued on the basis of observable prices in active markets and are considered to

have very limited valuation risk. Investments allocated to Level 2 are valued using models with observable market data. These holdings have some pricing uncertainty. Holdings allocated to Level 3 are priced using models with considerable use of unobservable inputs, which implies substantial uncertainty regarding the establishment of fair value. These investments too, are valued by external professional price providers who are regarded as giving the best estimate of fair value and where the total valuation from different pricing providers varies only to a limited extent.

The table below groups the investments into categories of assessed pricing uncertainty as at 31 December 2011 and 2010:

Amounts in NOK million

	Level 1		Level 2		Level 3		Total	
	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
<b>Equities</b>	<b>90 769</b>	<b>93 880</b>	<b>3</b>	<b>10</b>	<b>6</b>	<b>-</b>	<b>90 778</b>	<b>93 890</b>
<b>Total bonds</b>	<b>116 153</b>	<b>94 023</b>	<b>15 104</b>	<b>37 058</b>	<b>837</b>	<b>2 667</b>	<b>132 094</b>	<b>133 748</b>
Government bonds	114 281	84 108	49	1 505	-	-	114 330	85 612
Government-related bonds	3	3 685	83	5 964	15	5	101	9 654
Inflation-linked bonds	-	3 311	-	-	-	-	0	3 311
Corporate bonds	-	548	135	11 235	22	108	157	11 891
Securitised bonds	1 869	2 372	14 837	18 354	800	2 554	17 506	23 280
<b>Total financial derivatives</b>	<b>-46</b>	<b>-7</b>	<b>-2</b>	<b>-183</b>	<b>-</b>	<b>-</b>	<b>-48</b>	<b>-190</b>
Assets	2	2	0	19	-	-	2	21
Liabilities	-48	-9	-2	-202	-	-	-50	-211
<b>Total</b>	<b>206 876</b>	<b>187 896</b>	<b>15 105</b>	<b>36 885</b>	<b>843</b>	<b>2 667</b>	<b>222 824</b>	<b>227 448</b>

The table above comprises the balance sheet lines Equities, Equities lent, Bonds and other fixed income instruments, Bonds lent, Short-sale bonds and Financial derivatives (asset and liability). Other balance sheet items are thus not included.

Almost all of the equity holdings are classified as Level 1. Equities classified as Level 2 mainly comprise relatively illiquid holdings, which are priced on the basis of similar more liquid shares issued by the same company. Equities classified as Level 3 comprise a small number of holdings, the valuation of which is particularly uncertain due to a lack of market activity, and equities whose trading has been suspended.

Valuation of bonds is more uncertain and complex than valuation of equities. Norges Bank carries out analyses at each reporting date to identify the extent to which there have been transactions and price transparency with related market liquidity for different types of bonds as well as for a

number of individual securities. Most government bonds and inflation-linked bonds have been allocated to Level 1 and pricing is thus almost entirely based on observable market prices. Government-related bonds are allocated to Levels 1, 2 and 3 on the basis of variation in the degree of trading and price transparency in the markets. Most corporate bonds belong to Level 2, though with some exceptions in Level 3. Covered bonds are mostly categorised in the observable Levels 1 and 2 on the basis of a relatively high degree of liquidity and price transparency. Other securitised bonds are mostly allocated to Level 2, with some in Level 3, on the basis of varied and in part limited price transparency. A minor share of securitised bonds, 4.6%, are thus still allocated to Level 3 owing to limited activity in the market for these instruments and the use of unobservable inputs in their pricing, as well as complex models.

### Movements of Level 3 holdings

The table below shows a reconciliation of changes in balance sheet amounts for all Level 3 holdings in 2011 and 2010.

Amounts in NOK million

	1 Jan. 2011	Net gains/ losses	Purchases	Sales	Settled	Transferred from Level 1 or 2	Transferred to Level 1 or 22	Foreign exchange gains/ losses	31 Dec. 2011
<b>Equities</b>	-	2	2	-	-3	4	-	1	6
<b>Total bonds</b>	2 667	159	1	-1 725	-194	89	-14	-146	837
<b>Total</b>	<b>2 667</b>	<b>161</b>	<b>3</b>	<b>-1 725</b>	<b>-197</b>	<b>93</b>	<b>-14</b>	<b>-145</b>	<b>843</b>

Amounts in NOK million

	1 Jan. 2010	Net gains/ losses	Purchases	Sales	Settled	Transferred from Level 1 or 2	Transferred to Level 1 or 22	Foreign exchange gains/ losses	31 Dec. 2010
<b>Equities</b>	1	-3	3	-	-	-	-1	-	0
<b>Total bonds</b>	4 026	288	41	-1 291	-448	433	-473	91	2 667
<b>Total</b>	<b>4 027</b>	<b>285</b>	<b>44</b>	<b>-1 291</b>	<b>-448</b>	<b>433</b>	<b>-474</b>	<b>91</b>	<b>2 667</b>

Holdings allocated to Level 3 in the valuation hierarchy were reduced by NOK 1 824m to NOK 843m during 2011. The reduction in Level 3 bonds was primarily due to sales, and

US securitised bonds not guaranteed by federal agencies accounted for most of these sales.

### Sensitivity for Level 3 holdings

Amounts in NOK million

	Specification Level 3 at 31 Dec. 2011	Unfavourable changes	Favourable changes
<b>Sensitivities 2011</b>			
<b>Equities and units</b>	<b>6</b>	<b>-1</b>	<b>1</b>
<b>Total bonds</b>	<b>837</b>	<b>-91</b>	<b>83</b>
Government-related bonds	15	-2	1
Bonds issued by local governments	13	-2	1
Bonds issued by federal agencies	2	-	-
Corporate bonds	22	-3	2
Bonds issued by financial institutions	22	-3	2
Securitised bonds	800	-86	80
Mortgage-backed securities (MBS)	800	-86	80
Asset-backed securities (ABS)	-	-	-
Commercial mortgage-backed securities (CMBS)	-	-	-
<b>Total</b>	<b>843</b>	<b>-92</b>	<b>84</b>

Amounts in NOK million

<b>Sensitivities 2010</b>			
	Specification Level 3 at 31 Dec. 2010	Unfavourable changes	Favourable changes
<b>Equities</b>	-	-	-
<b>Total bonds</b>	<b>2 667</b>	<b>-333</b>	<b>273</b>
Government-related bonds	5	-	1
Bonds issued by local governments	5	-	1
Bonds issued by federal agencies	-	-	-
Corporate bonds	108	-12	12
Bonds issued by financial institutions	108	-12	12
Securitised bonds	2 554	-321	260
Mortgage-backed securities (MBS)	2 121	-269	188
Asset-backed securities (ABS)	307	-32	22
Commercial mortgage-backed securities (CMBS)	127	-21	50
<b>Total</b>	<b>2 667</b>	<b>-333</b>	<b>273</b>

Norges Bank's analyses indicate that valuation risk was substantially reduced during 2011. The total exposure regarded as being particularly uncertain in relation to valuation (Level 3) was reduced to around a third of exposure by year-end 2010. The estimated valuation risk of Level 3 holdings was NOK 92m related to unfavourable changes and NOK 84m related to favourable changes at year-end 2011. Valuation risk for Level 3 holdings is expected to be less than this as the valuation of all holdings will not move in the same direction based on a change in a single parameter. The technique used to calculate the sensitivity of bond values is based on the availability of independent price sources and begins with the highest and lowest available price for a specific bond. Where a higher or lower price was not available, a standard sensitivity parameter was used. The level of the resulting valuation change is based on the bond type and the availability, reliability and variation of prices.

US mortgage-backed securities' (MBS) sensitivity to changes to unobservable inputs contributed more than 90% of the overall estimated valuation uncertainty, with a reduction in value of NOK 86m related to unfavourable changes and an increase of NOK 80m related to favourable changes. Approximately 60% of the total MBS exposure of NOK 800m at year-end 2011 stemmed from agency-backed interest-only mortgage-backed securities. The most important unobservable parameter changed in this case was prepayment speed assumptions. The remaining Level 3 MBS exposures primarily comprised MBSs not guaranteed by federal agencies and with particularly high coupons (inverse float-

ers). The most important parameter also in this case is prepayment speed assumptions, although sensitivity is lower for these than for interest-only MBSs.

## 22.2 Money market portfolio

The money market portfolio is the most liquid portion of the Bank's foreign exchange reserves. In accordance with the guidelines, the portfolio is invested in a manner permitting it within a single trading day to be used for foreign exchange market transactions without realising any appreciable losses.

The benchmark portfolio is composed of USD and EUR overnight money market indices and Treasury bill indices for the same currencies. Managers are to seek a reasonable return within the constraints set by liquidity requirements and the risk framework. There are restrictions on the choice of instruments and currencies in the portfolio, and there are guidelines for how much the actual portfolio may deviate from the benchmark.

The money market portfolio comprises short money market instruments and German and US government securities, denominated in EUR and USD, respectively, with a maturity of up to one year.

## Control environment

The control environment for fair value measurement of financial instruments is organised around guidelines which are supported by work and control procedures.

The valuation environment has been established, and is adjusted, in accordance with best market practices for valuation. The operational implementation of best market practice principles is done in a manner to ensure a transparent, scalable and comparable valuation of all holdings on a daily basis through the use of sophisticated processes using both internal and external data solutions.

Prices for financial instruments from independent price providers are based on observable prices. On a daily basis the valuation process is subject to numerous controls, focusing on defined thresholds and sensitivities. The levels of these thresholds and sensitivities are monitored and adjusted in accordance with prevailing market conditions. At each month-end, additional extensive controls are performed to ensure compliance with established pricing procedures and the valuation policy's fair value measurement principles. This includes verifying that the external fund accountant uses external prices as required by the price hierarchy applicable at the time in question and verifying that the resulting prices reflect fair value as at the date concerned, i.e. the amount the holding could be exchanged for between knowledgeable and willing parties in an arm's length transaction.

#### Valuation techniques

Norges Bank has defined hierarchies for the independent price sources that serve as a basis for valuation. Holdings that are included in the benchmark portfolio are normally priced in accordance with the index providers' prices, while the remaining holdings of equities and bonds are priced almost exclusively by reputable independent external price providers. Prices are verified based on comparative analyses of prices in accordance with the established hierarchies with prices from available alternative price sources. When alternative price sources are considered to be more representative of fair value, prices are adjusted to bring the valuation closer to expected fair value.

100% of the money market portfolio's investments as at year-end 2011 comprised highly liquid holdings, and are therefore associated with low valuation risk.

The data used, observable as well as unobservable data, include the following elements:

- Bond and note prices – prices based on price quotes.
- Credit spreads – these are obtained from the credit derivative market.
- Yield curves – benchmark yield curves are often the foundation of the valuation matrix and are obtained from various market sources including Treasury bond markets, interest rate swap markets, futures markets as well as interbank markets.
- Money market and bond futures – official closing prices from exchanges are obtained via clearing brokers.
- Foreign exchange rates – WMFX rates at 16:00 GMT obtained from Reuters for use in determining spot prices and translating amounts into NOK.
- Correlation – this is the extent to which changes in one variable are interdependent with changes in another variable. Positive correlation indicates that the variables move in the same direction while negative correlation means the variables change in the opposite direction. The data source is Barclays POINT.

#### Pricing uncertainty

All government bonds and notes in the money market portfolio have been allocated to categories reflecting assessed pricing uncertainty. Level 1 comprises investments that are valued on the basis of observable market prices in active markets and are considered to have very limited valuation risk. The table below groups the investments into categories of assessed pricing uncertainty as at 31 December 2011 for the money market portfolio.

Amounts in NOK million		
	Level 1	
	31 Dec. 2011	31 Dec. 2010
Government bonds	17 938	4 376
Treasury notes	3 720	2 614
<b>Total</b>	<b>21 658</b>	<b>6 990</b>
Assets	21 658	6 990
Liabilities	-	-
<b>Total</b>	<b>21 658</b>	<b>6 990</b>

All investments in the money market portfolio are classified as Level 1 positions with a low valuation risk, as there are normally official closing prices from a stock exchange based on active market trading that correctly reflect fair value.

## Note 23 Risk

### Norges Bank's foreign exchange reserves

Norges Bank's foreign exchange reserves are divided between a long-term portfolio managed by NBIM and a money market portfolio managed by Norges Bank Monetary Policy (NBMP). The portfolios are managed under different mandates and have different risk profiles.

In addition, a buffer portfolio is used for regular transfers of foreign exchange to the investment portfolio of the Government Pension Fund Global. This portfolio receives funds from the State's Direct Financial Interest in petroleum activities (SDFI) and from Norges Bank's foreign exchange purchases in the foreign exchange market. The buffer portfolio is managed by NBIM.

### 23.1 Long-term portfolio

The composition of the holdings in the long-term portfolio and associated risk is primarily determined by the benchmark portfolio defined by Norges Bank's Executive Board.

In the investment mandate for the portfolio issued by Norges Bank's Executive Board, there are a number of guidelines and restrictions regarding the combined equity and bond asset class, as well as for the individual asset

classes. These restrictions regulate to what degree Norges Bank can engage in active investment management while remaining within the legally established capital allocations.

For a discussion of Norges Bank's and NBIM's governance structure and the framework for investment risk, see Note 24 GPF Global Note 14 Risk.

### Market risk measurement

Market risk is the risk of changes in the value of the portfolio due to movements in interest rates, equity prices, foreign currency exchange rates and credit spreads. Norges Bank measures risk in both absolute terms for the actual portfolio, and the relative market risk for investments in the portfolio.

Continuous monitoring, measurement and assessment of market risk are performed along multiple risk dimensions, employing a number of methodologies and approaches. Combining different and complementary risk measures provides a better insight into the risk profile of the holdings in the portfolio.

### Asset class by region

The long-term portfolio is invested across several asset classes and regions as shown in the table below.

		Market value* in percent per region	Market value* in percent per asset class	Assets minus liabilities
		31 Dec. 2011	31 Dec. 2011	31 Dec. 2011
Equities	Americas and Africa	56.6 %		
	Europe	26.0 %		
	Asia and Oceania	17.4 %		
Total equities			40.9 %	90 720
Bonds	Americas and Africa	43.9 %		
	Europe	45.6 %		
	Asia and Oceania	10.5 %		
Total bonds			59.1 %	131 149



		Market value* in percent per region	Market value* in percent per asset class	Assets minus liabilities
		31 Dec. 2010	31 Dec. 2010	31 Dec. 2010
Equities	Americas and Africa	52.7 %		
	Europe	29.7 %		
	Asia and Oceania	17.6 %		
Total equities			41.8 %	93 835
Bonds	Americas and Africa	43.2 %		
	Europe	46.3 %		
	Asia and Oceania	10.5 %		
Total bonds			58.2 %	130 901

\* As from 1 January 2011, the calculation of market value in the table above has been changed to include all positions in the portfolio, and not only equity and bond holdings. Comparative amounts for 2010 have been restated.

### Concentration risk

The long-term portfolio contains substantial investments in government issued bonds. It is also normal for private companies to issue both bonds and equities.

The table below shows the largest holdings of bonds issued by governments, including government bonds issued in local currency, sovereign bonds and inflation-linked bonds issued in local currency:

			Amounts in NOK million	
			2011	Market value 2010
US			53 723	42 905
Japan			13 897	11 871
UK			14 053	9 710
Germany			18 427	9 224
France			14 181	5 615
Spain			-	3 003
Austria			-	1 718
Italia			-	1 643
Netherlands			-	1 633
Finland			-	635
Greece			51	-
Argentina			3	-

The table below shows the long-term portfolio's largest non-government bonds and equities holdings by issuer. Covered

bonds issued by financial institutions are included in the bonds column.

Amounts in NOK million

2011				
	Sector	Bonds	Equities	Total
Exxon Mobil Corp	Oil & Gas	-	1 404	1 404
Banco Bilbao Vizcaya Argentaria SA	Financials	1 249	146	1 395
Bank of Scotland PLC	Financials	1 344	-	1 344
Apple Inc	Technology	-	1 297	1 297
CaixaBank	Financials	1 153	19	1 172
Ayt Cedulas Cajas Global	Financials	1 152	-	1 152
Caja de Ahorros y Pensiones de Barcelona	Financials	832	-	832
Royal Dutch Shell PLC	Oil & Gas	-	831	831
WM Covered Bond Program	Financials	825	-	825
Banco Santander SA	Financials	555	222	777

2010				
	Sector	Bonds	Equities	Total
European Investment Bank	Government-related	2 646	-	2 646
Bank of Scotland PLC	Financials	2 453	-	2 453
La Caja de Ahorros y Pensiones de Barcelonas	Financials	1 952	-	1 952
Ayt cedulas Cajas Global	Financials	1 947	-	1 947
Kreditanstalt fuer Wiederaufbau	Government-related	1 755	-	1 755
Caja de Ahorros y Monte de Piedad de Madrid	Financials	1 356	-	1 356
Exxon Mobil Corp	Oil & Gas	-	1 173	1 173
Banco Popular Espanol SA	Financials	974	13	987
Apple Inc	Technology	-	941	941
Deutsche Pfandbriefbank AG	Financials	926	-	926

### Volatility and correlation risk

For a discussion of techniques for measuring volatility and correlation risk in the long-term portfolio, see Note 24 GPF Note 14 Risk.

					Expected volatility			
Long-term model	31 Dec. 2011	Min 2011	Max 2011	Average 2011	31 Dec. 2010	Min 2010	Max 2010	Average 2010
Portfolio	8.4 %	8.4 %	11.0 %	10.4 %	10.9 %	10.3 %	11.9 %	10.8 %
Equities	15.4 %	15.4 %	20.3 %	19.0 %	20.3 %	20.2 %	24.7 %	20.9 %
Bonds	12.4 %	12.4 %	14.7 %	13.8 %	14.0 %	11.0 %	14.5 %	13.0 %
<b>Responsive model</b>								
Portfolio	9.1 %	6.7 %	13.1 %	9.3 %	7.8 %	5.2 %	9.9 %	7.5 %
Equities	16.7 %	9.6 %	26.0 %	15.0 %	10.3 %	9.0 %	15.9 %	11.9 %
Bonds	13.0 %	7.5 %	17.9 %	11.8 %	9.5 %	6.3 %	14.3 %	10.3 %

					Expected relative volatility			
Long-term model	31 Dec. 2011	Min 2011	Max 2011	Average 2011	31 Dec. 2010	Min 2010	Max 2010	Average 2010
Portfolio	67.60	27.23	90.02	50.96	54.75	37.94	115.03	69.72
Equities	8.31	6.09	45.98	12.44	44.27	5.67	125.78	48.01
Bonds	47.11	46.17	87.99	62.06	81.10	67.03	139.13	94.46
<b>Responsive model</b>								
Portfolio	68.54	15.94	98.19	46.94	42.74	32.86	107.20	61.30
Equities	10.04	6.08	34.75	11.10	30.29	4.73	159.64	41.19
Bonds	61.87	28.67	90.49	48.57	65.83	53.98	160.71	86.30

Risk measured by the long-term risk model declined for the portfolio as a whole and in both asset classes in 2011. For the portfolio as a whole, measured risk at year-end was 8.4%. This means that for the portfolio, annual fluctuations in value of just above NOK 19bn can be expected under normal market conditions. The reduction over the year is primarily an effect of the model's use of three years' historical data, whereby the historical data from the volatile period in 2008 was no longer included in the data at year-end. The portfolio's expected relative volatility increased during 2011, driven by overweighting in the equity market relative to the benchmark portfolio.

For a discussion of a responsive risk model for the long-term portfolio, see Note 24 GPF Note 14 Risk.

At the end of the fourth quarter of 2011, expected relative volatility for the portfolio according to the responsive model was somewhat higher than at the beginning of the year. This is due to an increase in short-term fluctuations in both the equities and bond markets.

For a discussion of strengths and weaknesses of the model for measuring volatility and correlation risk for the long-term portfolio, see Note 24 GPF Note 14 Risk.

### **Back-testing of models**

For a discussion of back-testing of the models performed to validate the model's ability to estimate risk for the long-term portfolio, see Note 24 GPFG Note 14 Risk.

The table below summarises the total number of observations where actual loss exceeds expected risk, expected

frequency and the ratio between them. Only downside risk has been taken into account. The closer the observed/expected ratio is to 1, the better the model has estimated risk. Three different confidence intervals are considered. A ratio above one indicates that the risk has been underestimated.

2011				
Risk measure	Period	Expected	Observed	Observed/ Expected
Standard deviation	2 years	83	70	0.80
Value-at-Risk 95%	2 years	26	23	0.90
Value-at-Risk 99%	2 years	5	5	1.00

2011				
Risk measure	Period	Expected	Observed	Observed/ Expected
Tracking error	2 years	83	46	0.55
Value-at-Risk 95%	2 years	26	19	0.73
Value-at-Risk 99%	2 years	5	8	1.54

### Credit risk

For a discussion of measuring credit risk for the long-term portfolio, see Note 24 GPFG Note 14 Risk. In the table below, 0.2% of the actual portfolio is categorised as Higher risk at year-end 2011, down from 2% at year-end 2010.

The table below is a breakdown of the actual bond portfolio by credit rating category as at 31 December 2011.

Amounts in NOK million

31 Dec. 2011						
	AAA	AA	A	BBB	Higher risk	Total
Government bonds	100 384	13 897	-	-	49	114 330
Government-related bonds*	-	-	20	2	79	101
Inflation-linked bonds	-	-	-	-	-	0
Corporate bonds	-	-	-	57	100	157
Securitised bonds	10 820	4 194	1 877	614	1	17 506
<b>Total bonds and other fixed income instruments</b>	<b>111 204</b>	<b>18 091</b>	<b>1 897</b>	<b>673</b>	<b>229</b>	<b>132 094</b>

Amounts in NOK million

31 Dec. 2010						
	AAA	AA	A	BBB	Higher risk	Total
Government bonds	70 857	13 522	279	482	472	85 612
Government-related bonds*	8 182	928	270	206	68	9 654
Inflation-linked bonds	-	3 311	-	-	-	3 311
Corporate bonds	215	2 405	4 728	4 100	443	11 891
Securitised bonds	16 041	5 290	152	153	1 644	23 280
<b>Total bonds and other fixed income instruments</b>	<b>95 295</b>	<b>25 456</b>	<b>5 429</b>	<b>4 941</b>	<b>2 627</b>	<b>133 748</b>

\* As from 2011, sovereign bonds are included in government-related bonds. Comparative amounts have been restated.

The table below is a breakdown of the asset class fixed income instruments by credit rating and currency.

						2011
	AAA	AA	A	BBB	Higher risk	Total
EUR	42.7 %	0.0 %	0.0 %	0.0 %	0.1 %	42.8 %
USD	30.9 %	3.2 %	1.4 %	0.5 %	0.1 %	36.1 %
GBP	10.6 %	0.0 %	0.0 %	0.0 %	0.0 %	10.6 %
JPY	0.0 %	10.5 %	0.0 %	0.0 %	0.0 %	10.5 %
<b>Total</b>	<b>84.2 %</b>	<b>13.7 %</b>	<b>1.4 %</b>	<b>0.5 %</b>	<b>0.2 %</b>	<b>100.0 %</b>

						2010
	AAA	AA	A	BBB	Higher risk	Total
EUR	25.6 %	9.0 %	1.7 %	2.2 %	0.1 %	38.6 %
USD	36.1 %	0.8 %	1.6 %	1.7 %	1.3 %	41.5 %
GBP	9.5 %	0.3 %	0.8 %	0.4 %	0.0 %	11.0 %
JPY	0.0 %	8.9 %	0.0 %	0.0 %	0.0 %	8.9 %
<b>Total</b>	<b>71.2 %</b>	<b>19.0 %</b>	<b>4.1 %</b>	<b>4.3 %</b>	<b>1.4 %</b>	<b>100.0 %</b>

During the course of 2011, the use of credit derivatives was reduced considerably.

### Counterparty risk

For a discussion of what counterparty risk is, and how it arises and is measured, managed and reported for the long-term portfolio, see Note 24 GPFG Note 14 Risk. The table below is a breakdown of exposure by type of activity/instru-

ment regarded as having counterparty risk. Securities lending through external agents was reduced during the second half of 2011.

Amounts in NOK million

						31 Dec. 2011
	Carrying amount adjusted for collateral	Gross exposure	Netting effects	Collateral and guarantees	Net exposure	
Time deposits and unsecured bank deposits	67	56	-	-	56	
OTC derivatives including foreign exchange contracts	1	1	-	-	1	
Repurchase and reverse repurchase agreements*	-23	44	8	-	36	
Securities lending transactions**	-1	1	-	1	0	
Bonds posted as collateral for futures trades	176	178	-	-	178	
<b>Total</b>		<b>280</b>	<b>8</b>	<b>1</b>	<b>271</b>	

Amounts in NOK million

31 Dec. 2010					
	Carrying amount adjusted for collateral	Gross exposure	Netting effects	Collateral and guarantees	Net exposure
Time deposits and unsecured bank deposits	381	396	-	-	396
OTC derivatives including foreign exchange contracts	-141	224	66	84	74
Repurchase and reverse repurchase agreements*	-973	833	149	-	684
Securities lending transactions**	-142	1 370	-	1 301	69
Bonds posted as collateral for futures trades	136	133	-	-	133
<b>Total</b>		<b>2 956</b>	<b>215</b>	<b>1 385</b>	<b>1 356</b>

\* The column Carrying amount adjusted for collateral takes into account all positions in the repurchase market, including reinvestments of cash collateral. The internal measurement and controls of counterparty risk for these types of instruments do not include these reinvestments.

\*\* The column Carrying amount adjusted for collateral includes securities lent and collateral received and is adjusted for unrealised losses connected to reinvestments in the form of bonds.

31 Dec. 2011		
	Norges Bank counterparties (excl. brokers)	Brokers
AAA	3	3
AA	50	43
A	39	43
BBB	4	14
BB	-	2
B	-	12
<b>Total</b>	<b>96</b>	<b>117</b>

31 Dec. 2010		
	Norges Bank counterparties (excl. brokers)	Brokers
AAA	3	3
AA	55	57
A	23	36
BBB	-	21
BB	-	6
B	-	3
<b>Total</b>	<b>81</b>	<b>126</b>

### Leverage

For a discussion of leverage in the long-term portfolio, see Note 24 GPF Note 14 Risk.

At the beginning of 2011, the portfolio had leverage of 1.9%. During 2011, the holding of cash increased and at year-end 2011 the portfolio had no leverage.

	31 Dec. 2011	2011 Q3	2011 Q2	2011 Q1	31 Dec. 2010
Leverage	0.0 %	0.0 %	1.7 %	1.4 %	1.9 %

### Sale of securities Norges Bank does not own

Sale of securities not owned by Norges Bank (short sales) can only be done if the Bank has established borrowing agreements to cover a negative position. Such transactions

are very rarely undertaken, and at year-end 2011, no securities had been sold in this manner.

## 23.2 Risk in the money market portfolio managed by Norges Bank Monetary Policy (NBMP)

### Purpose of the portfolio

The money market portfolio is to be invested in such a way that it can be used at short notice as a monetary policy instrument or to promote financial stability. The portfolio is also used to meet Norges Bank's international obligations, including transactions with the IMF and loans to individual countries.

Pursuant to the decision of the Executive Board in 2010, the size of the portfolio was to be between SDR 2bn and SDR 3bn and investments in government securities are to have residual maturity of less than one year. The decision also states that the benchmark portfolio is to comprise USD and EUR overnight money market indices and Treasury bill indices for the same currencies. In view of developments in financial markets through summer 2011, a decision was made to transfer SDR 1.5bn (NOK 12.9bn) from the long-term portfolio to the money market portfolio, with effect from end-August. As from the same date, the benchmark portfolio comprises 75% USD and 25% EUR.

### Market risk

Market risk is risk related to changes in the value of the portfolio due to changes in interest rates and/or foreign exchange rates. Norges Bank measures the money market portfolio's absolute and relative market risk.

### Absolute market risk

Absolute risk is estimated on the basis of the actual portfolio, as the standard deviation of the return. The model uses expected standard deviation, based on the composition of the portfolio and assumptions regarding sensitivities to fluctuations in relevant market factors and correlations between these factors. A parametric weighted method is employed. The standard deviation is a statistical term that indicates the magnitude of variation that can be expected in the return on the portfolio. The expected annual standard deviation in the actual portfolio was 0.08% in local currency at year-end 2011. This means that in two out of every three years the value of the portfolio is expected to fluctuate within +/-0.08% of total market value (one standard deviation) at that time.

Market risk was at the same level as at year-end 2010, which is low compared with the historical market risk for comparable portfolios.

### Relative market risk

Market risk in the money market portfolio is also measured by expected relative volatility. This is a statistically defined risk measure that indicates the size of the expected deviation that can normally be expected between the return on the benchmark portfolio and the return on the actual portfolio. Corresponding estimates of absolute market risk are parametrically weighted using a method of estimating relative market risk.

The Executive Board has issued guidelines for how much the actual portfolio may deviate from the benchmark portfolio. The limit for expected relative market volatility has been set at 1.0%, and the Bank uses a model that takes into account market fluctuations. Average expected relative volatility was measured at 0.03% in 2011.

Risk	Limits	Actual	
		31 Dec. 2011	31 Dec. 2010
Market risk	Maximum 1.0% relative volatility	0.03	0.05
	Alternative measurement technique	0.04	0.08
Asset allocation	Cash (Minimum 10%)	25.28	10.46
	Securities	74.72	89.54
Currency allocation	USD	75.72	49.85
	EUR	24.18	50.15
	JPY	0.06	-
	GBP	0.05	-
Duration, benchmark portfolio		0.19	0.29



### Credit risk

Credit risk is the risk of losses if issuers of fixed income instruments default on their payment obligations to Norges Bank. Another form of credit risk is counterparty risk, which arises through derivative and foreign exchange contracts. Settlement risk, which arises in connection with the purchase and sale of securities since not all transactions take place in real time, also gives rise to counterparty risk.

The limits for exposure to a particular bank (exposure limits) include time deposits and foreign exchange trading (spot, forward and swap transactions). Maximum exposure to the most creditworthy banks has been set at NOK 1bn. Uninsured deposits may be made with counterparties with a minimum long-term rating of AA-/AA-/Aa3, respectively,

from at least one of the three major rating agencies: Fitch, Moody's or Standard & Poor's. Transactions are not permitted with a counterparty if any of the three agencies have rated that counterparty lower than A-/A3/A-.

Investments where the counterparty has posted collateral in the form of cash or securities may be undertaken if the counterparty has a long-term rating no lower than A-/A3/A- from at least one of the three agencies Fitch, Moody's or Standard & Poor's.

The tables below show third party agreements, investments and collateral at 31 December 2011 and 2010. Amounts in NOK million.

31 DEC. 2011	Rating S & P	EUR	USD	GBP	Total
<b>Market value third party agreements</b>		<b>1 991</b>	<b>2 949</b>	<b>-</b>	<b>4 940</b>
<b>Collateral</b>					
	AAA	2 876	2	1	2 879
Sovereigns	AA-	16	-	-	16
Supranational bodies		-	2 044	205	2 249
<b>Total collateral</b>		<b>2 892</b>	<b>2 046</b>	<b>206</b>	<b>5 144</b>

31 DEC. 2010	Rating S & P	EUR	USD	GBP	Total
<b>Market value third party agreements</b>		<b>12 288</b>	<b>4 617</b>	<b>-</b>	<b>16 905</b>
<b>Collateral</b>					
	AAA	11 766	-	-	11 766
Sovereigns	AA+	3 048	17	-	3 065
Supranational bodies	AA	170	-	-	170
Total collateral		1	1 696	670	2 367
<b>Sum sikkerhet</b>		<b>14 985</b>	<b>1 713</b>	<b>670</b>	<b>17 368</b>

### 23.3 Liquidity risk

As a central bank, Norges Bank is not exposed to liquidity risk. Note disclosure requirements under IFRS are therefore not relevant.

## Note 24 Government Pension Fund Global (GPF Global)

### Income statement

Amounts in NOK million

	Note	2011	2010
<b>Profit/loss on the portfolio excluding foreign exchange gains/losses</b>			
Interest income from bank deposits		162	377
Interest income, lending associated with reverse repurchase agreements		1 004	350
Net income/expenses and gains/losses from:			
- Equities and units		- 173 099	207 070
- Bonds and other fixed income instruments		92 346	60 316
- Financial derivatives		- 5 693	- 3 552
- Financial assets real estate	10	86	-
- Investment properties	10	- 130	-
Share of the profit/loss on jointly controlled entities, real estate		- 31	-
Interest expense repurchase agreements		- 629	- 574
Other interest expense		- 286	- 105
Other expenses	4	24	- 9
<b>Profit/loss on the portfolio before foreign exchange gains/losses</b>	<b>3</b>	<b>- 86 246</b>	<b>263 873</b>
Foreign exchange gains/losses		49 205	- 8 498
<b>Profit/loss on the portfolio</b>		<b>- 37 041</b>	<b>255 375</b>
Management fee	5	- 2 539	- 2 959
<b>Profit/loss for the period</b>		<b>- 39 580</b>	<b>252 416</b>
<b>Statement of comprehensive income</b>			
Profit/loss for the period		- 39 580	252 416
Translation reserve arising from consolidation of foreign subsidiaries		- 3	-
<b>Total comprehensive income</b>		<b>- 39 583</b>	<b>252 416</b>

## Balance sheet

Amounts in NOK million

	Note	31 Dec. 2011	31 Dec. 2010	31 Dec. 2009
<b>ASSETS</b>				
<b>Financial assets</b>				
Deposits in banks		7 276	6 303	4 644
Lending associated with reverse repurchase agreements	6	79 820	255 501	191 473
Cash collateral paid		-	-	140
Unsettled trades		2 272	4 864	17 572
Equities and units	7	1 806 798	1 733 378	1 496 759
Equities lent	7, 8	137 130	162 483	150 847
Bonds and other fixed income instruments	7	1 324 255	1 038 793	918 500
Bonds lent	7, 8	3 256	215 090	161 990
Financial derivatives	9	2 227	3 068	2 263
Financial assets, real estate	10	4 415	-	-
Jointly controlled entities, real estate	10	2 546	-	-
Other financial assets	11	3 244	1 358	251
<b>Total financial assets</b>		<b>3 373 239</b>	<b>3 420 838</b>	<b>2 944 439</b>
<b>Non-financial assets</b>				
Investment properties	10	4 062	-	-
Other non-financial assets		6	-	-
<b>Total non-financial assets</b>		<b>4 068</b>	<b>-</b>	<b>-</b>
<b>TOTAL ASSETS</b>	<b>12, 13, 14</b>	<b>3 377 307</b>	<b>3 420 838</b>	<b>2 944 439</b>
<b>LIABILITIES AND OWNER'S CAPITAL</b>				
<b>Financial liabilities</b>				
Short-term borrowing		11	2 939	6 238
Borrowing associated with repurchase agreements	6	19 280	132 992	109 536
Cash collateral	8,9	36 926	172 309	154 676
Unsettled trades		3 310	20 358	11 925
Short-sale bonds	7	-	809	10 278
Financial derivatives	9	5 957	9 372	8 118
Other financial liabilities	11	251	4 639	3 625
Management fee payable		2 539	2 959	3 228
<b>Total financial liabilities</b>	<b>12, 13, 14</b>	<b>68 274</b>	<b>346 377</b>	<b>307 624</b>
<b>Owner's capital</b>		<b>3 309 033</b>	<b>3 074 461</b>	<b>2 636 815</b>
<b>Total liabilities and owner's capital</b>		<b>3 377 307</b>	<b>3 420 838</b>	<b>2 944 439</b>

## Statement of cash flows

Amounts in NOK million

	2011	2010
<b>Operating activities</b>		
Interest received on deposits in banks	179	377
Net cash flow in connection with reverse repurchase agreements	170 095	- 57 392
Net cash flows arising from purchase and sale of equities and units	- 239 987	- 70 201
Net cash flows arising from purchase and sale of bonds and other fixed income instruments	- 21 094	- 180 835
Payments made to acquire financial assets real estate	- 4 270	-
Payments made to acquire investment properties	- 4 301	-
Payments made to acquire jointly controlled entities, real estate	- 2 620	-
Net cash flows arising from financial derivatives	- 9 147	- 1 433
Dividends received from investments in equities and units	49 208	41 257
Interest received on bonds and other fixed income instruments	48 036	45 752
Income received in connection with equity and bond lending	2 230	1 676
Income received from investments in financial assets real estate	130	-
Income received from investments in investment properties	60	-
Interest paid on short-term borrowing from banks	- 21	- 209
Net cash flows related to repurchase agreements	- 114 347	23 742
Cash collateral received/paid related to securities lending, derivatives and reverse repurchase agreements and other non-financial assets	- 135 382	17 773
Cash flow related to other financial assets, and other financial liabilities and other non-financial assets	- 5 587	1 112
Payment of other expenses	- 248	- 29
Management fee paid to Norges Bank	- 2 959	- 3 228
<b>Net cash outflow from operating activities</b>	<b>- 270 025</b>	<b>- 181 640</b>
<b>Financial activities</b>		
Inflow from the Norwegian government	274 155	185 230
<b>Net cash inflow from financing activities</b>	<b>274 155</b>	<b>185 230</b>
<b>Net change in cash and cash equivalents</b>		
Cash and cash equivalents at 1 January	3 363	- 1 594
Net cash payments in the period	4 130	3 590
Foreign exchange gains/losses on cash and cash equivalents	- 228	1 367
<b>Cash and cash equivalents at 31 December</b>	<b>7 265</b>	<b>3 363</b>
Cash and cash equivalents comprise:		
Deposits in banks	7 276	6 303
Short-term borrowing	- 11	- 2 939
<b>Total cash and cash equivalents at 31 December</b>	<b>7 265</b>	<b>3 363</b>

## Statement of changes in owner's capital

Amounts in NOK million

	Inflows from owner	Retained earnings	Translation reserve foreign subsidiaries	Deposits in krone account*
1 January 2010	2 319 481	317 334	.	2 636 815
Total comprehensive income	.	252 416	.	252 416
Inflows during the period	185 230	.	.	185 230
<b>31 December 2010</b>	<b>2 504 711</b>	<b>569 750</b>	.	<b>3 074 461</b>
1 January 2011	2 504 711	569 750	.	3 074 461
Total comprehensive income	.	- 39 580	- 3	- 39 583
Inflows during the period	274 155	.	.	274 155
<b>31 December 2011</b>	<b>2 778 866</b>	<b>530 170</b>	<b>- 3</b>	<b>3 309 033</b>

\* Due to different accounting frameworks, owner's capital for the Government Pension Fund Global (GPF) according to Norges Bank's financial statements will each year deviate slightly from the equity capital of the GPF in the central government accounts. This is due to the transfers to the GPF through the year being based on estimates of income in the GPF. Actual recognised income (net accrual) in the central government accounts will not be known until after year end. In the central government accounts the difference between the net accrual and the transfers is shown as receivables/payables between the GPF and the Treasury. In cases of too high transfers to the GPF, the Treasury has a receivable from the GPF, and the GPF correspondingly has lower equity capital in the central government accounts than as shown in Norges Bank's financial statements. On the other hand, in cases of too low transfers to the GPF compared with the recognised income, the GPF has a receivable from the Treasury, and correspondingly higher equity capital for the GPF is shown in the central government accounts than in the Norges Bank financial statements. See the central government accounts Chapter 3 for further information.

### GPF Note 1

The accounting policies for the financial reporting of the investment portfolio of the Government Pension Fund Global appear in Note 1 Transition to International Financial Reporting Standards (IFRS) and accounting policies.

### GPF Note 2

Significant estimates and critical accounting judgements for the financial reporting of the investment portfolio of the Government Pension Fund Global appear in Note 2 Significant estimates and critical accounting judgements.

### GPF Note 3 Profit/loss on the portfolio before foreign exchange gains/losses

Amounts in NOK million

	Interest income/ expense	Dividends	Net income/ expense	Realised gains/ losses	Unrealised gains/ losses	Total
Interest income from bank deposits	162	.	.	.	.	162
Interest income, lending associated with reverse repurchase agreements	1 004	.	.	.	.	1 004
Net income/expenses and gains/losses from:						
- Equities and units*	.	49 793	1 869	27 067	-251 827	-173 099
- Bonds and other fixed income instruments*	48 691	.	349	4 600	38 706	92 346
- Financial derivatives	-1 407	.	.	-6 358	2 072	-5 693
- Financial assets real estate	.	.	-52	.	138	86
- Investment properties	.	.	60	.	-190	-130
Share of the profit/loss on jointly controlled entities, real estate	.	-	.	-	-31	-31
Interest expense from repurchase agreements	-629	.	.	.	.	-629
Other interest expense	-286	.	.	.	.	-286
Other expenses	.	.	24	.	.	24
<b>Profit/loss on the portfolio before foreign exchange gains/losses</b>	<b>47 534</b>	<b>49 793</b>	<b>2 250</b>	<b>25 309</b>	<b>-211 132</b>	<b>-86 246</b>

\* Net income/expense equities and units and bonds and other fixed income instruments is from security lending activities

Amounts in NOK million

	Interest income/ expense	Dividends	Net income/ expense	Realised gains/ losses	Unrealised gains/ losses	Total
Interest income from bank deposits	377	.	.	.	.	377
Interest income, lending associated with reverse repurchase agreements	350	.	.	.	.	350
Net income/expenses and gains/losses from:						
- Equities and units*	.	42 775	1 446	30 494	132 355	207 070
- Bonds and other fixed income instruments*	47 077	.	274	5 273	7 692	60 316
- Financial derivatives	- 2 519	.	.	- 538	- 495	- 3 552
Interest expense from repurchase agreements	- 574	.	.	.	.	- 574
Other interest expenses	- 105	.	.	.	.	- 105
Other expenses	.	.	- 9	.	.	- 9
<b>Profit/loss on the portfolio before foreign exchange gains/losses</b>	<b>44 606</b>	<b>42 775</b>	<b>1 711</b>	<b>35 229</b>	<b>139 552</b>	<b>263 873</b>

\* Net income/expense equities and units and bonds and other fixed income instruments is from security lending activities

## GPFG Note 4 Other expenses

Amounts in NOK million

Table 4.1 Specification other expenses		
	2011	2010
Salaries, employer's National Insurance contributions and other personnel-related costs	2	-
IT, information and decision support systems, outsourced administrative services	2	-
Consulting and legal fees	11	-
Fees related to real estate asset management (external)	6	-
Other expenses, subsidiaries real estate	5	-
<b>Total operating expenses, subsidiaries real estate</b>	<b>26</b>	<b>-</b>
Other expenses, investment portfolio excluding subsidiaries	-50	9
<b>Total other expenses</b>	<b>-24</b>	<b>9</b>

The operating expenses in subsidiaries related to management of real estate investments shown in Table 4.1 in the amount of NOK 26m are not included in operating expenses in Norges Bank that form part of and are covered by the management fee from the Ministry of Finance. See further information in Note 5 Management fee. The real estate asset class includes additional expenses related to property management, which are included in the income statement line Net income/expenses and gains/losses, Investment properties, and in the line Share of profit/loss in jointly con-

trolled entities, real estate. These expenses are incurred by the company that owns the property.

The income of NOK 50m, presented as Other expenses, investment portfolio excluding subsidiaries in Table 4.1, is primarily attributable to the reversal of a provision for capital gains withholding tax on equities in China, based on a reduction of unrealised capital gains during 2011 in this market. The provision was reduced by an amount of NOK 75m.

## GPFG Note 5 Management fee

Amounts in NOK million

Table 5.1 Specification management fee	2011	2010
	Percent	Percent
Salaries, employer's National Insurance contributions and other personnel-related costs	447	389
IT, information and decision support systems	214	223
Custody and settlement costs	406	382
Outsourced IT analysis costs	254	213
Consulting and legal fees	73	116
Base fees external managers	371	452
Other costs	107	81
Allocated common costs Norges Bank	121	115
<b>Management fee excluding performance-based fee</b>	<b>1 993</b>	<b>1 973</b>
Performance-based fees to external managers	546	986
<b>Total management fee</b>	<b>2 539</b>	<b>2 959</b>

Table 5.1 shows costs incurred by Norges Bank that are reimbursed by the Ministry of Finance as the principal for the management of the investment portfolio of the Government Pension Fund Global. Fees to external managers and custody and settlement fees are invoiced directly and paid individually for each of the portfolios managed by NBIM. All other costs included in the basis for calculation of the management fee are costs that are common for the management of both portfolios, and are allocated to the individual portfolio using a cost allocation model based primarily on market values and asset class composition. The management fee is a function of expenses presented in the Norges Bank income statement as Total other operating expenses.

In addition to the operating expenses that are shown above and that are reimbursed through the management fee from the Ministry of Finance, operating and administrative expenses are incurred in the subsidiary companies that

are incorporated as a part of the management of the investment portfolio for the Government Pension Fund Global. These expenses are consolidated into the income statement of the investment portfolio of the Government Pension Fund Global, and are paid using funds received or earned by the investment portfolio. Subsidiaries that are consolidated into the financial reporting for the investment portfolio are not consolidated into the annual financial statements of Norges Bank, pursuant to the accounting regulation for Norges Bank § 2.3, paragraph 4, and these expenses will therefore not be included in Norges Bank's operating expenses. These expenses will through consolidation be shown as expenses in the income statement for the investment portfolio, and are deducted from Profit/loss on the portfolio. In 2011 these expenses amounted to NOK 26m. See also GPFG Note 4 Other expenses.



## GPF Note 6 Repurchase and reverse repurchase agreements

Norges Bank uses the markets for repurchase and reverse repurchase agreements in its financing activities internally and through securities lending programmes (see GPF Note 8 External agency securities lending). At any time the bank will have lent portions of its holdings in bonds through repurchase agreements, against receiving a corresponding amount in cash (repos and sell buy backs). This may be in the form of financing of the asset management (borrowing of cash), or lending of securities with the aim of reinvesting received cash at a higher interest rate and thus creating additional income or returns. In addition, the Bank is a party to reverse repurchase agreements where the counterparty has transferred bonds or equities to the Bank and where the Bank has transferred cash to the counterparty (reverse repo, buy sell backs and triparties). Such contracts are used in connection with placing liquidity and also through agency securities lending as reinvestments of cash collateral received related to lent securities. Rules have been laid down regarding the types of securities eligible as collateral. To be eligible as collateral, bonds shall have a credit rating of at least A or the equivalent from at least one of the rating agencies Fitch, Moody's or Standard & Poor's.

For repurchase agreements, the lent security is not derecognised. Received cash is recognised as Deposits in banks, with a corresponding liability to pay back the cash, recognised as Borrowing associated with repurchase agreements. For reverse repurchase agreements, the security received as collateral is not recognised in the balance sheet, while transferred cash is derecognised from Deposits in banks. A corresponding receivable is recognised as an asset, Lending associated with reverse repurchase agreements.

In addition to collateral related to each transaction, the Bank has established a process for monitoring the net market value of the outstanding contracts by comparing the collateral value against the transaction value per counterparty, where additional collateral in the form of either securities or cash is posted or received if the exposure is above a threshold value. Within the investment portfolio of the Government Pension Fund Global, the Bank had not received or posted such cash collateral at year-end. In the financial statements, posted and received additional collateral in the form of securities is treated in the same manner as other security collateral.

In the second half of 2011, the volume of outstanding repurchase and reverse repurchase agreements was reduced significantly, especially in EUR-denominated securities, as part of a reduction in exposures due to high financial market risk.

Table 6.1 shows total outstanding repurchase and reverse repurchase agreements at year-end 2011, with comparative amounts for 2010, and corresponding securities collateral or lent securities. Transferred and received securities are shown as measured at fair value. In order to show the total exposure for the contracts, unsettled trades have been shown separately and included under received and posted collateral/lent securities. This securities collateral has not yet been transferred and therefore is not included in the lines Bonds posted as collateral or lent and Bonds/Equities received as collateral in Table 6.1, while the corresponding cash amount to be transferred is included in Borrowing associated with repurchase agreements and Lending associated with reverse repurchase agreements.

Amounts in NOK million

Table 6.1 Specification of repurchase and reverse repurchase agreements				
	31 Dec. 2011		31 Dec. 2010	
	Carrying amount	Fair value	Carrying amount	Fair value
<b>Repurchase agreements</b>				
Borrowing associated with repurchase agreements (cash borrowed or received as collateral)	19 280	19 280	132 992	132 992
Bonds posted as collateral or lent (asset)	17 551	17 551	130 198	130 198
Unsettled trades (asset)*	1 410	1 410	205	205
<b>Net overcollateralisation (undercollateralisation) repurchase agreements</b>	<b>319</b>	<b>319</b>	<b>2 589</b>	<b>2 589</b>
<b>Reverse repurchase agreements</b>				
Reverse repurchase agreements outside of securities lending programme	44 393	44 393	101 990	101 990
Reverse repurchase agreements through securities lending programme (reinvestment of cash collateral)	35 427	35 427	153 511	153 511
<b>Lending associated with reverse repurchase agreements (cash lent or placed)</b>	<b>79 820</b>	<b>79 820</b>	<b>255 501</b>	<b>255 501</b>
Bonds received as collateral	-	67 399	-	243 481
Equities received as collateral	-	13 161	-	5 813
<b>Total collateral received reverse repurchase agreements</b>	<b>-</b>	<b>80 560</b>	<b>-</b>	<b>249 294</b>
Unsettled trades (liability)**	1 537	1 537	7 820	7 820
<b>Net overcollateralisation (undercollateralisation) reverse repurchase agreements</b>	<b>-</b>	<b>2 277</b>	<b>-</b>	<b>1 613</b>
<b>Additional collateral repurchase / reverse repurchase agreements</b>				
Posted cash collateral (additional collateral)	-	-	-	-
Posted bond collateral	-	-	505	505
Received bond collateral	-	72	-	384
<b>Total additional collateral</b>	<b>-</b>	<b>72</b>	<b>-</b>	<b>121</b>
<b>Net overcollateralisation (undercollateralisation) repurchase and reverse repurchase agreements</b>	<b>-</b>	<b>2 668</b>	<b>-</b>	<b>4 081</b>

\*Cash not yet received, securities not transferred to counterparty. Repurchase agreement has been recognised.

\*\*Cash not yet transferred, securities not received from counterparty. Reverse repurchase agreement has been recognised.

The table shows that outstanding repurchase agreements were reduced by 86% from year-end 2010 to year-end 2011, while outstanding reverse repurchase agreements were reduced by 69% in the same period. The change was implemented in the second half of the year and was due to high risk in financial markets.

At the same time Table 6.1 shows that the investment portfolio of the Government Pension Fund Global was overcollateralised in the amount of NOK 319m with regard to repurchase agreements at year-end 2011, compared to NOK 2 589m at the end of 2010. This implies that the Bank has a surplus of this amount of received cash over posted collateral/lent securities. Correspondingly, Norges Bank is overcollateralised with regard to reverse repurchase agreements in the amount of NOK 2 277m as at 31 December 2011, since the Bank had an excess of received securities collateral rela-

tive to cash placed in this amount. The corresponding overcollateralisation as at year-end 2010 was NOK 1 613m. Total overcollateralisation across these instrument types, including additional collateral, was NOK 2 668m at 31 December 2011 compared with NOK 4 081m the previous year-end.

Outside of agency securities lending programmes, Norges Bank had lent a net amount of NOK 25bn for the investment portfolio of the Government Pension Fund Global at year-end 2011, compared with net borrowing of NOK 31bn at year-end 2010. This comprises the net effect of cash borrowed of NOK 19 280m and cash lent of NOK 44 393m at year-end 2011 (borrowed cash of NOK 132 992m and lent cash of NOK 101 990m at year-end 2010), and reflects zero leverage at the end of 2011, based on a significant share of cash in the securities portfolios at the end of 2011. See also a further description of leverage in GPF Note 14 Risk.

## GPF Note 7 Equities and units/Bonds and other fixed income instruments

Amounts in NOK million

Table 7.1 Specification of equities and units			
			31 Dec. 2011
	Fair value excluding dividends	Accrued dividends	Fair value including dividends
Equities and units			
Listed equities and units	1 940 789	3 139	1 943 928
<b>Total equities and units</b>	<b>1 940 789</b>	<b>3 139</b>	<b>1 943 928</b>
<i>Of which equities lent</i>			137 130
			31 Dec. 2010
	Fair value excluding dividends	Accrued dividends	Fair value including dividends
Equities and units			
Listed equities and units	1 893 714	2 147	1 895 861
<b>Total equities and units</b>	<b>1 893 714</b>	<b>2 147</b>	<b>1 895 861</b>
<i>Of which equities lent</i>			162 483

Amounts in NOK million

Table 7.2 Specification of bonds and other fixed income instruments				
31 Dec. 2011	Nominal value*	Fair value excluding accrued interest	Accrued interest	Fair value including accrued interest
<i>Government bonds</i>				
Government bonds issued in local currency	554 293	605 600	6 965	612 565
<b>Total government bonds</b>	<b>554 293</b>	<b>605 600</b>	<b>6 965</b>	<b>612 565</b>
<i>Government-related bonds</i>				
Sovereign bonds**	12 592	13 184	279	13 463
Bonds issued by local authorities	26 016	27 855	527	28 382
Bonds issued by supranational bodies	33 629	35 819	505	36 324
Bonds issued by federal agencies	94 454	97 488	1 507	98 995
<b>Total government-related bonds</b>	<b>166 691</b>	<b>174 346</b>	<b>2 818</b>	<b>177 164</b>
<i>Inflation-linked bonds</i>				
Inflation-linked bonds issued by government authorities	83 105	105 175	541	105 716
<b>Total inflation-linked bonds</b>	<b>83 105</b>	<b>105 175</b>	<b>541</b>	<b>105 716</b>
<i>Corporate bonds</i>				
Bonds issued by utilities	19 709	21 781	376	22 157
Bonds issued by financial institutions	85 842	78 589	1 643	80 232
Bonds issued by industrial companies	77 733	84 583	1 369	85 952
Total corporate bonds	183 284	184 953	3 388	188 341
<i>Securitised bonds</i>				
Covered bonds	223 642	219 041	4 761	223 802
Mortgage-backed securities	48 581	11 046	80	11 126
Asset-backed securities	7 061	4 244	8	4 252
Commercial mortgage-backed securities	13 539	4 524	21	4 545
<b>Total securitised bonds</b>	<b>292 823</b>	<b>238 855</b>	<b>4 870</b>	<b>243 725</b>
<b>Total bonds and other fixed income instruments</b>	<b>1 280 196</b>	<b>1 308 929</b>	<b>18 582</b>	<b>1 327 511</b>
<i>Of which bonds lent</i>				3 256
<i>Of which short-sale bonds</i>				-

\* Nominal values have been translated into NOK at the closing rate at the balance sheet date.

\*\* Sovereign bonds were reclassified as government related bonds as from 1 January 2011. Comparative amounts have been restated.

Amounts in NOK million

31 Dec. 2010	Nominal value*	Fair value excluding accrued interest	Accrued interest	Fair value including accrued interest
<i>Government bonds</i>				
Government bonds issued in local currency	485 739	501 175	6 394	507 569
<b>Total government bonds</b>	<b>485 739</b>	<b>501 175</b>	<b>6 394</b>	<b>507 569</b>
<i>Government related bonds</i>				
Sovereign bonds**	12 290	13 162	264	13 426
Bonds issued by local authorities	32 321	33 142	667	33 809
Bonds issued by supranational bodies	25 581	27 565	441	28 006
Bonds issued by federal agencies	83 789	85 615	1 345	86 960
<b>Total government-related bonds</b>	<b>153 981</b>	<b>159 484</b>	<b>2 717</b>	<b>162 201</b>
<i>Inflation-linked bonds</i>				
Inflation-linked bonds issued by government authorities	88 544	102 835	502	103 337
<b>Total inflation-linked bonds</b>	<b>88 544</b>	<b>102 835</b>	<b>502</b>	<b>103 337</b>
<i>Corporate bonds</i>				
Bonds issued by utilities	19 609	21 013	384	21 397
Bonds issued by financial institutions	114 637	108 892	2 060	110 952
Bonds issued by industrial companies	68 332	73 468	1 363	74 831
<b>Total corporate bonds</b>	<b>202 578</b>	<b>203 373</b>	<b>3 807</b>	<b>207 180</b>
<i>Securitised bonds</i>				
Covered bonds	195 974	192 780	4 210	196 990
Mortgage-backed securities	112 611	55 356	246	55 602
Asset-backed securities	18 366	14 117	19	14 136
Commercial mortgage-backed securities	18 807	6 026	33	6 059
<b>Total securitised bonds</b>	<b>345 758</b>	<b>268 279</b>	<b>4 508</b>	<b>272 787</b>
Total bonds and other fixed income instruments	1 276 600	1 235 146	17 928	1 253 074
<i>Of which bonds lent</i>				215 090
<i>Of which short-sale bonds</i>				809

\* Nominal values have been translated into NOK at the closing rate at the balance sheet date.

\*\* Sovereign bonds were reclassified as government-related bonds as from 1 January 2011. Comparative amounts have been restated.

At the end of 2011, holdings of bonds issued by the sovereign states Portugal, Ireland, Italy, Greece and Spain amounted to NOK 57bn. Of this, Portuguese holdings amounted to 1%, Irish 7%, Italian 58%, Greek 3% and Spanish 31%.

Total holdings as at 31 December 2010 issued by these sovereigns amounted to NOK 94bn.

## GPF Note 8 External agency securities lending

Norges Bank has entered into securities lending agreements with external agents, giving these agents the right to lend securities held by Norges Bank to other market participants with borrowing needs. Both equities and bonds are lent. The purpose of the lending activity is to create additional returns for the investment portfolio of the Government Pension Fund Global from its securities holdings. When a security is lent out, the borrower transfers collateral to the agent in the form of cash or securities. The collateral is held on behalf of Norges Bank. Agreements with agents have provisions reducing the Bank's counterparty risk in cases where collateral has been received in the form of cash or government bonds. These provisions ensure the bank will be compensated if the counterparty is unable to return the borrowed securities or if the collateral posted for the loan is insufficient to cover any losses in the event of borrower default. Norges Bank bears this risk itself in cases where collateral has been received in the form of equities. Reinvestments by the agent of cash collateral received take the form of positions in the repo market: reverse repurchase agreements, buy sell backs and triparties (see Note 6 Repurchase and reverse repurchase agreements). At 31 December 2011, all reinvestments were in the form of reverse repurchase agreements. By comparison, similar contracts accounted for 90% of total reinvestments at year-end 2010, the rest being in the form of bonds.

Securities lent are presented on separate lines in the balance sheet. Cash collateral received is recognised in the balance sheet as part of Deposits in banks with a corresponding liability Cash collateral received, since Norges Bank has

the right to dispose of this cash. Collateral received in the form of securities is not recognised in the balance sheet, because these are not reused (rehypothecated), but are left in custody. Reinvestments in the form of reverse repurchase agreements and bonds are recognised in the balance sheet in the same manner as ordinary investments. Due to increased risk in financial markets in the second half of 2011, Norges Bank reduced its lending programme towards year-end. Exposure has been reduced in general, and specifically with regard to securities lending and collateral denominated in euro and collateral in the form of US securitised bonds.

Norges Bank earns a net income from these securities lending programmes. The net income comprises the pure lending fee, from which costs related to cash collateral received are subtracted, as well as interest income and realised returns from reinvestments. The agent's portion, which is a consideration for carrying out the transactions, is also deducted. Net income from securities lending is presented on the income statement lines Net income/expenses and gains/losses from equities and units and Net income/expenses and gains/losses from bonds and other fixed income instruments. Net income related to equities lending within the investment portfolio of the Government Pension Fund Global amounted to NOK 1 869m in 2011, while the corresponding income from bond lending amounted to NOK 349m in 2011 (see also GPF Note 3 Profit/loss on the portfolio before foreign exchange gains/losses). Corresponding amounts for 2010 were NOK 1 446m and NOK 274m, respectively.

Tables 8.1 and 8.2 present an overview of positions within external agent securities lending programmes at year-end 2011 compared with year-end 2010:

Amounts in NOK million

Table 8.1 Securities lent		
	31 Dec. 2011	
	Carrying amount	Fair value
<i>Securities lent</i>		
Equities lent	137 130	137 130
Bonds lent	3 256	3 256
<b>Total securities lent</b>	<b>140 386</b>	<b>140 386</b>
<i>Collateral received</i>		
Cash collateral received	36 405	36 405
Equities received as collateral	-	102 170
Bonds received as collateral	-	11 337
<b>Total collateral received related to securities lending</b>	<b>36 405</b>	<b>149 912</b>
<b>Net overcollateralisation</b>	<b>-</b>	<b>9 526</b>

Amounts in NOK million

Table 8.1 Securities lent		
	31 Dec. 2010	
	Carrying amount	Fair value
<i>Securities lent</i>		
Equities lent	162 483	162 483
Bonds lent	215 090	215 090
<b>Total securities lent</b>	<b>377 573</b>	<b>377 573</b>
<i>Collateral received</i>		
Cash collateral received	172 309	172 309
Equities received as collateral	-	123 995
Bonds received as collateral	-	98 962
<b>Total collateral received related to securities lending</b>	<b>172 309</b>	<b>395 266</b>
<b>Net overcollateralisation</b>	<b>-</b>	<b>17 693</b>

Amounts in NOK million

Table 8.2 Reinvestment of cash collateral related to securities lending		
	31 Dec. 2011	31 Dec. 2010
	Carrying amount	Fair value
<i>Reinvestment related to securities lending</i>		
Reverse repurchase agreements	35 427	153 511
Asset-backed securities	-	13 541
Other fixed income instruments	-	3 831
Total reinvestment in the form of bonds and other fixed income instruments	-	17 372
<b>Total reinvestment of cash collateral</b>	<b>35 427</b>	<b>170 883</b>
Unrealised loss bonds and other fixed income instruments	-	1 341

## GPGF Note 9 Financial derivatives

Table 9.1 is a specification of financial derivative holdings at market value as at 31 December 2011 and 31 December 2010, classified as assets or liabilities. Table 9.2 shows the nominal values of positions in financial derivatives for pur-

chased (long) and sold (short) positions as exposure. Nominal values are the basis for the calculation of any cash flows and gains/losses for the contracts.

Amounts in NOK million

Table 9.1 Specification of financial derivatives			
			Fair value
			31 Dec. 2011
	Assets	Liabilities	Net
<b>Foreign exchange contracts</b>	<b>1 603</b>	<b>964</b>	<b>639</b>
<b>Listed futures contracts</b>	<b>5</b>	<b>224</b>	<b>- 219</b>
Interest rate swaps	463	4 639	- 4 176
Credit default swaps	2	0	2
Equity swaps	154	130	24
<b>Total swap contracts</b>	<b>619</b>	<b>4 769</b>	<b>- 4 150</b>
<b>Options</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total financial derivatives</b>	<b>2 227</b>	<b>5 957</b>	<b>- 3 730</b>

Amounts in NOK million

			Fair value
			31 Dec. 2010
	Assets	Liabilities	Net
<b>Foreign exchange contracts</b>	<b>402</b>	<b>316</b>	<b>86</b>
<b>Listed futures contracts</b>	<b>43</b>	<b>22</b>	<b>21</b>
Interest rate swaps	1 847	7 300	- 5 453
Credit default swaps	41	749	- 708
Equity swaps	21	77	- 56
<b>Total swap contracts</b>	<b>1 909</b>	<b>8 126</b>	<b>- 6 217</b>
<b>Options</b>	<b>714</b>	<b>908</b>	<b>- 194</b>
<b>Total financial derivatives</b>	<b>3 068</b>	<b>9 372</b>	<b>- 6 304</b>



Amounts in NOK million

Table 9.2 Financial derivatives exposure				
	Exposure			
	31 Dec. 2011		Average 2011	
	Purchased	Sold	Purchased	Sold
<b>Foreign exchange contracts</b>	<b>132 848</b>	<b>-</b>	<b>64 778</b>	<b>-</b>
<b>Listed futures contracts</b>	<b>1</b>	<b>14 682</b>	<b>5 228</b>	<b>9 851</b>
Interest rate swaps	8 163	18 956	20 106	52 806
Credit default swaps	1 645	12	19 373	280
Equity swaps	30	335	25	550
<b>Total swap contracts</b>	<b>9 838</b>	<b>19 303</b>	<b>39 504</b>	<b>53 636</b>
<b>Options</b>	<b>-</b>	<b>-</b>	<b>14 464</b>	<b>11 987</b>
<b>Total financial derivatives</b>	<b>142 687</b>	<b>33 985</b>	<b>123 974</b>	<b>75 474</b>

Amounts in NOK million

	Exposure			
	31 Dec. 2010		Average 2010	
	Purchased	Sold	Purchased	Sold
<b>Foreign exchange contracts</b>	<b>29 849</b>	<b>-</b>	<b>27 468</b>	<b>-</b>
<b>Listed futures contracts</b>	<b>16 791</b>	<b>17 056</b>	<b>20 557</b>	<b>16 267</b>
Interest rate swaps	25 002	74 689	14 035	70 908
Credit default swaps	37 092	2 246	30 926	2 434
Equity swaps	39	128	823	85
<b>Total swap contracts</b>	<b>62 133</b>	<b>77 063</b>	<b>45 784</b>	<b>73 427</b>
<b>Options</b>	<b>33 845</b>	<b>15 217</b>	<b>24 829</b>	<b>15 840</b>
<b>Total financial derivatives</b>	<b>142 618</b>	<b>109 336</b>	<b>118 638</b>	<b>105 534</b>

### Foreign exchange contracts

This item consists of foreign currency exchange contracts with normal settlement for future delivery. Contract exposure is the sum of the nominal value of the contracts at any given point in time.

### Listed futures contracts

Futures contracts are listed contracts to exchange a specified asset (security, index, interest rate or other) at an agreed price, with future delivery, normally settled in cash, and with initial and daily margin settlement of gains and losses. Exposure is the nominal value of the contracts.

### Over-the-counter (OTC) financial derivatives

#### Interest rate swaps

Interest rate swaps generally comprise contracts in which two parties agree to exchange interest payment streams based on different interest rate calculation methods;

typically one party pays a floating rate, and the other pays a fixed rate.

Exposure is the nominal value of the contract, and the direction (purchased/sold) indicates whether Norges Bank receives (has purchased) or pays (has sold) a fixed rate of interest.

#### Credit default swaps

In a credit default swap, the seller receives a periodic premium or lump sum from the purchaser as compensation for assuming the credit risk. The purchaser receives payment from the seller only if the credit protection of the underlying loan is triggered (by a credit event). A credit event might, for example, be a default on the underlying credit or bond. The protection normally expires after the first credit event.

The underlying assets for credit default swaps are corporate bonds, securities issued by sovereign states and corporate bond indices.

Exposure direction (purchased/sold) indicates whether Norges Bank has purchased or sold protection for all or part of the credit risk associated with the various types of underlying assets.

#### Equity swaps

Equity swaps are agreements between two counterparties to exchange cash flows based on changes in the underlying securities. In addition to the periodic cash flow, payments are received in connection with dividends and corporate events.

Exposure corresponds to the nominal value of the contracts. The direction (purchased/sold) indicates whether Norges Bank receives or pays cash upon settlement.

#### Options

The buyer of an option has the right to buy or sell an asset at an agreed price at an agreed time in the future, while the seller has the obligation to buy or sell the asset at the agreed price and time. Options include swaptions, which are agreements which grant the buyer the right to enter into a swap.

Exposure is the nominal value of the contracts. Options written by Norges Bank are reported as sold. Options where Norges Bank has paid a premium are reported as purchased contracts.

Amounts in NOK million

Table 9.3 Collateral related to positions in financial derivatives		
	31 Dec. 2011	31 Dec. 2010
<b>OTC financial derivatives</b>		
Net fair value OTC (carrying amount)	-3 535	-6 269
Cash collateral received related to OTC positions	521	1
<b>Futures contracts and equity swaps</b>		
Fair value futures contracts	-219	21
Fair value equity swaps	24	-56
Deposits with clearing brokers (collateral posted)	433	331
Bonds posted as collateral to clearing brokers	762	620

Norges Bank delivers or receives cash collateral in connection with positions in foreign exchange contracts and OTC financial derivatives (interest rate swaps, credit default swaps and swaptions). Follow-up against collateral thresholds is done per counterparty, and if the net market value of positions held by the counterparty exceed the given threshold limits, the party with the negative position is required to post additional collateral to the other party. At year-end 2011, Norges Bank had received cash collateral from counterparties related to OTC positions in the amount of NOK 521m, an amount significantly higher than the NOK 1m of cash collateral received

at 31 December 2010. The general increase in collateral received is due to various factors including the downgrading of some counterparties during 2011. A downgrade results in a lowering of the threshold for the counterparty, resulting in turn in a requirement for the counterparty to post additional cash collateral. Other factors include market volatility and increased foreign currency trading. Norges Bank has not delivered any cash collateral on negative market value positions at year-end 2011 or year-end 2010 on behalf of the investment portfolio of the Government Pension Fund Global, due to Norges Bank's high creditworthiness.

## GPFG Note 10 Real estate

The real estate asset class in the investment portfolio of the Government Pension Fund Global comprises unlisted investments classified as financial assets, jointly controlled entities and investment properties.

2011 was the first accounting year with investments in this asset class, and at year-end, the investment portfolio of the Government Pension Fund Global has interests in real estate in London and in Paris. A total of NOK 11 009m was invested in financial assets, investment properties and jointly controlled entities during the year. These assets have

a carrying amount of NOK 11 023m as at 31 December 2011. Total net carrying amount for the asset class at 31 December was NOK 11 129m.

Tables 10.1 and 10.2 show profit/loss items for the period and balance sheet items for the asset class, respectively. The tables are followed by descriptions of the investments as classified for financial reporting purposes under IFRS. Tables 10.3 and 10.4 provide an overview of investment properties, those owned directly as well as those owned through jointly controlled entities.

Amounts in NOK million

Table 10.1 Income statement items – real estate asset class		
	2011	2010
<i>Profit/loss on the real estate asset class excluding foreign exchange gains and losses</i>		
Interest income from bank deposits	1	-
Net income/expenses and gains/losses from:		
- Financial assets real estate	86	-
- Investment properties	-130	-
Share of the profit/loss in jointly controlled entities real estate	-31	-
Other interest expenses	-1	-
Other expenses	-4	-22
<b>Profit/loss on the real estate asset class before foreign exchange gains/losses</b>	<b>-79</b>	<b>-22</b>

Amounts in NOK million

Table 10.2 Balance sheet items – real estate asset class		
	31 Dec. 2011	31 Dec. 2010
<b>ASSETS</b>		
<b>Financial assets</b>		
Deposits in banks	138	1
Financial assets real estate	4 415	-
Jointly controlled entities, real estate	2 546	-
Other financial assets	14	-
<b>Total financial assets, real estate asset class</b>	<b>7 113</b>	<b>1</b>
<b>Non-financial assets</b>		
Investment properties	4 062	-
Other non-financial assets	6	-
<b>Total non-financial assets</b>	<b>4 068</b>	<b>-</b>
<b>TOTAL ASSETS</b>	<b>11 181</b>	<b>1</b>
<b>FINANCIAL LIABILITIES</b>		
Other financial liabilities	52	22
<b>Total financial liabilities, real estate asset class</b>	<b>52</b>	<b>22</b>
Net assets, real estate asset class	11 129	- 21

### Financial assets real estate

The first real estate investment in the investment portfolio of the Government Pension Fund Global was completed on 1 April 2011 and entitles the portfolio to a 25% share in the net operating income (NOI) generated by properties that are located in and around Regent Street in London. This portfolio of properties is managed by The Crown Estate. Two additional investments were made in the third quarter of 2011. The total purchase price, including additional investments, of investments made in 2011 was NOK 4 270m, of which NOK 182 comprised transaction costs.

The investment is accounted for as a financial asset under IAS 39 Financial Instruments: Recognition and Measurement. The investment is measured at fair value and presented as Financial assets real estate in the balance sheet. As at 31 December 2011, the fair value of the investment was measured at NOK 4 415m.

Earned income and fair value changes as well as transaction costs to complete the investment are shown in the income statement as Net income/expenses and gains/losses from financial assets real estate. Net operating income amounted to NOK 130m, transaction costs, NOK 182m, and fair value changes NOK 138m, adding up to the total amount on the income statement line Net income/expenses and gains/losses from financial assets real estate for 2011 of NOK 86m.

For additional information, see GPFG Note 13 Fair value measurement.

### Investment properties

Norges Bank has acquired 50% of seven properties in and around Paris for the investment portfolio of the Government Pension Fund Global. All properties are jointly controlled and

managed by Norges Bank and AXA Group and are regarded as being jointly controlled assets under IAS 31 Interests in Joint Ventures. The properties are accounted for as investment property at fair value under IAS 40 Investment Property. A total of NOK 4 301m was invested in investment properties during the year. At year-end 2011, the carrying amount was NOK 4 062m. AXA Group is the manager of all the properties.

For additional information see Note 2 Significant estimates and critical accounting judgements and GPFG Note 13 Fair value measurement.

### Jointly controlled entities

Norges Bank has acquired 50% of three French companies (société civile immobilière) for the investment portfolio of the Government Pension Fund Global, each of which owns properties in and around Paris. All companies are jointly controlled and managed by Norges Bank and AXA Group and are regarded as being jointly controlled entities under IAS 31. These investments are accounted for using the equity method in the consolidated financial statements for the investment portfolio. The properties are accounted for in the underlying entities as investment property at fair value under IAS 40.

A total of NOK 2 620m was invested in jointly controlled entities during the year. At year-end 2011, the carrying amount was NOK 2 546m. AXA Group is the manager of these properties.

For an overview of jointly controlled entities see GPFG Note 15 Subsidiaries and jointly controlled entities. For additional information, see also Note 2 Significant estimates and critical accounting judgements and GPFG Note 13 Fair value measurement.

Amounts in NOK million

Table 10.3 Specification of net income/expenses and gains/losses from investment properties and share of the profit/ loss in jointly controlled entities, real estate

	2011	
	Investment properties*	Jointly controlled entities real estate**
Gross rental income	74	53
Direct property expenses	-14	-
Net rental income	60	53
Fair value changes	-190	-71
<b>Net income/expenses and gains/losses from investment properties</b>	<b>-130</b>	
Other income/expenses in jointly controlled entities, real estate		-13
<b>Share of profit/loss in jointly controlled entities, real estate</b>		<b>-31</b>

\*Income and expenses from directly held investment properties.

\*\*Share of income and expenses in jointly controlled entities.

External valuations have been obtained of all the properties as at 31 December 2011 that differ somewhat from the purchase price. As there are no observed factors indicating that the value of the properties has changed materially since the transaction date, it is the assessment of management that the consideration paid in the recent transaction is the best

estimate of fair value as at 31 December 2011. Recognised fair value changes correspond to transactions costs attributed to the individual property.

The portfolio primarily comprises office properties in central Paris. The portfolio has a well diversified tenant structure, with over 50 leases.

Amounts in NOK million

Table 10.4 Investment properties directly held and held in jointly controlled entities

	Investment properties*	Jointly controlled entities real estate**
Investment properties at 31 Dec. 2010	-	-
Additions (new investments)	4 300	2 617
Capital expenditure	1	-
Disposals	-	-
Fair value changes	- 190	- 71
Net exchange differences from translation into NOK	- 49	- 43
<b>Investment properties at 31 Dec. 2011</b>	<b>4 062</b>	<b>2 503</b>
Share of other assets (net) in jointly controlled entities		43
<b>Jointly controlled entities, real estate</b>		<b>2 546</b>

\* Investment properties directly held.

\*\* Share of investment properties and other assets (net) in jointly controlled entities.

Table 10.4 shows the investment portfolio's share of investment properties and net other assets in jointly controlled entities.

Total assets and liabilities in jointly controlled entities as at 31 December 2011 are shown in Table 10.5:

Amounts in NOK million

Table 10.5 Jointly controlled entities, total assets and liabilities*		
	31 Dec. 2011	31 Dec. 2010
Current assets	170	-
Investment properties	5 006	-
Current liabilities	84	-
Equity capital	5 092	-

\* One hundred percent of the carrying amounts of the jointly controlled entities, prepared in accordance with IFRS.

## GPFG Note 11 Other financial assets / Other financial liabilities

Specification of other financial assets and other financial liabilities is shown in Tables 11.1 and 11.2.

Amounts in NOK million

Table 11.1 Other financial assets		
	31 Dec. 2011	31 Dec. 2010
Withholding tax	744	1 239
Accrued income from external agency securities lending	106	119
Receivables from other portfolios under common management*	2 371	-
Other receivables, subsidiaries real estate	23	-
<b>Other financial assets</b>	<b>3 244</b>	<b>1 358</b>

\* Receivables from other portfolios under common management comprise the net value of deposits and repurchase and reverse repurchase agreements vis-à-vis other portfolios managed by Norges Bank. These related party transactions have been conducted under the arm's length principle

Amounts in NOK million

Table 11.2 Other financial liabilities		
	31 Dec. 2011	31 Dec. 2010
Tax due on foreign equities gains	-	88
Other liabilities abroad	199	229
Other liabilities, subsidiaries real estate	52	-
Liabilities to other portfolios under common management*	-	4 322
<b>Other financial liabilities</b>	<b>251</b>	<b>4 639</b>

\* Liabilities to other portfolios under common management comprise the net value of deposits and repurchase and reverse repurchase agreements vis-à-vis other portfolios managed by Norges Bank. These related party transactions have been conducted under the arm's length principle.

## GPFG Note 12 Currency distribution

Amounts in NOK million

Table 12.1 Currency distribution of the balance sheet as at 31 December 2011 and 31 December 2010								
								31 Dec. 2011
	USD	CAD	EUR	GBP	CHF	JPY	Other	Total
Deposits in banks	1 866	85	270	94	755	78	4 128	7 276
Lending associated with reverse repurchase agreements	51 096	5 353	5 938	7 820	-	3 497	6 116	79 820
Unsettled trades	539	-	24	3	-	880	826	2 272
Equities and units	592 945	49 222	432 975	279 278	117 154	83 784	251 440	1 806 798
Equities lent	38 030	834	1 175	20 292	2 532	25 949	48 318	137 130
Bonds and other fixed income instruments	463 286	27 845	560 223	151 410	4 249	67 444	49 798	1 324 255
Bonds lent	3 256	-	-	-	-	-	-	3 256
Financial derivatives	2 372	-39	694	242	-13	20	-1 049	2 227
Financial assets, real estate	-	-	-	4 415	-	-	-	4 415
Jointly controlled entities, real estate	-	-	2 546	-	-	-	-	2 546
Other financial assets	161	272	2 949	-334	68	87	41	3 244
<b>Total financial assets</b>	<b>1 153 551</b>	<b>83 572</b>	<b>1 006 794</b>	<b>463 220</b>	<b>124 745</b>	<b>181 739</b>	<b>359 618</b>	<b>3 373 239</b>
Investment properties	-	-	4 062	-	-	-	-	4 062
Other non-financial assets	-	-	6	-	-	-	-	6
<b>Total assets</b>	<b>1 153 551</b>	<b>83 572</b>	<b>1 010 862</b>	<b>463 220</b>	<b>124 745</b>	<b>181 739</b>	<b>359 618</b>	<b>3 377 307</b>
Short-term borrowing	-14	0	0	25	0	0	0	11
Borrowing associated with repurchase agreements	10 888	-	105	-	-	2 452	5 835	19 280
Cash collateral	36 405	-	521	-	-	-	-	36 926
Unsettled trades	223	4	17	10	7	876	2 173	3 310
Financial derivatives	595	60	1 365	3 461	5	186	285	5 957
Other financial liabilities	198	-	41	12	-	-	-	251
Management fee payable	-	-	-	-	-	-	2 539	2 539
<b>Total financial liabilities</b>	<b>48 295</b>	<b>64</b>	<b>2 049</b>	<b>3 508</b>	<b>12</b>	<b>3 514</b>	<b>10 832</b>	<b>68 274</b>

Amounts in NOK million

31 Dec. 2010

	USD	CAD	EUR	GBP	CHF	JPY	Other	Total
Deposits in banks	422	41	681	170	- 11	50	4 950	6 303
Lending associated with reverse repurchase agreements	67 503	277	168 506	7 365	-	7 231	4 619	255 501
Unsettled trades	1 487	33	2 523	31	60	288	442	4 864
Equities and units	592 971	53 984	394 203	236 938	98 658	84 194	272 430	1 733 378
Equities lent	25 418	917	38 477	22 662	6 115	21 370	47 524	162 483
Bonds and other fixed income instruments	357 578	24 941	459 350	113 462	5 125	55 429	22 908	1 038 793
Bonds lent	57 586	2 085	116 823	30 340	45	-	8 211	215 090
Financial derivatives	- 7 660	- 32	- 1 061	- 2 312	- 2	- 162	14 297	3 068
Other financial assets	122	-	291	12	932	-	1	1 358
<b>Total financial assets</b>	<b>1 095 427</b>	<b>82 246</b>	<b>1 179 793</b>	<b>408 668</b>	<b>110 922</b>	<b>168 400</b>	<b>375 382</b>	<b>3 420 838</b>
Short-term borrowing	2	-	-	-	1 706	359	872	2 939
Borrowing associated with repurchase agreements	34 392	462	66 482	19 521	-	7 831	4 304	132 992
Cash collateral	54 398	-	116 713	1 198	-	-	-	172 309
Unsettled trades	11 374	479	7 383	198	36	270	618	20 358
Short-sale bonds	809	-	-	-	-	-	-	809
Financial derivatives	201	63	3 877	2 540	- 192	7 508	- 4 625	9 372
Other financial liabilities	207	- 48	1 547	2 571	- 50	358	54	4 639
Management fee payable	-	-	-	-	-	-	2 959	2 959
<b>Total financial liabilities</b>	<b>101 383</b>	<b>956</b>	<b>196 002</b>	<b>26 028</b>	<b>1 500</b>	<b>16 326</b>	<b>4 182</b>	<b>346 377</b>



## **GPFG Note 13 Fair value measurement**

### **Control environment**

The control environment for fair value measurement of financial instruments and investment property is organised around a formalised and documented valuation policy and guidelines which are supported by work and control procedures. The policy document lays down valuation policies and sets reporting requirements for the NBIM valuation committee.

The valuation committee, which comprises the NBIM leader group, meets every quarter prior to the publication of the financial reporting. The committee reviews the documentation, discusses major pricing issues and approves the valuation.

The valuation environment has been established in accordance with best market practices for valuation. This is implemented in practice through daily valuation of all holdings, except for real estate investments, where valuations are performed on a quarterly basis. These processes are scalable with regard to market changes and are based on internal and external data solutions.

Generally, all holdings and investments are valued by external, independent valuation specialists. Valuation providers have been chosen on the basis of thorough analyses performed by the internal unit in NBIM responsible for the valuation. Valuation providers are followed up on an ongoing basis through regular discussions, controls and price challenges for individual securities. For a large portion of holdings, prices from independent price providers are based on observable market prices. For holdings that are insufficiently liquid for valuation to be based on observable prices, widely accepted models are used. Here observable inputs are used to the degree possible, but in some cases, owing to illiquid markets, non-observable inputs are used.

The valuation process is subject on a daily basis to numerous controls by NBIM's valuation department as well as by the external fund accountant. Controls are based on defined thresholds and sensitivities, which are monitored and adjusted in accordance with prevailing market conditions. At each month-end for financial instruments and at the end of each quarter for real estate investments, more extensive controls are performed to ensure fair value measurement. In this connection, particular attention is paid to illiquid financial instruments and real estate investments, i.e. investments deemed to pose valuation challenges. Illiquid instruments are identified with the help of sector and currency classifications, price differences between different external price providers, degree of coverage of the instru-

ment by external price vendors, credit rating indicators, bid/ask spreads, and activity in the market.

A valuation memo and report are prepared at each quarter-end documenting the results of the controls performed and the most important sources of uncertainties in the valuations.

### **Valuation techniques**

#### ***Equities and units, bonds and other fixed income instruments, and financial derivatives***

NBIM has defined hierarchies for price sources used for valuation. Holdings that are included in the benchmark portfolio are normally priced in accordance with the index providers' prices, while the remaining holdings of equities and bonds are priced almost exclusively through the use reputable independent external price providers' prices. In NBIM, analyses are done as part of the extended controls at month end in which prices provided by the hierarchy are compared with alternative price sources. Adjustments are made when alternative prices are considered to be more representative of fair value.

In the price hierarchy, equities are valued almost exclusively on the basis of official closing prices from stock exchanges or last traded exchange prices, and are thus observable market prices. Sixty-six percent of the holdings in bonds are also valued using observable market prices. Over 85% of the investments for the Government Pension Fund Global as at year-end 2011 comprised holdings traded in active markets and are therefore associated with low valuation risk (Level 1).

Portions of the bond portfolio and most interest rate derivatives are valued by price providers using models because the instruments are not traded in active markets. Observable market data are used in the models as much as possible. The models are generally a combination of market standard and proprietary models but based on standard valuation principles. Model types vary according to the asset class or sub-class under review. For bonds these will include credit spreads based on observable prices for comparable instruments, non-adjusted and option-adjusted discounted cash flow models for bonds containing embedded options, and models with discount margins for floating-rate bonds. In the OTC derivative market, option pricing models as well as implicit yield curves and credit spreads are mainly used.

Data used in the different valuation models, observable as well as unobservable, include the following elements:

- Bond prices – prices based on price quotes and relevant market activity.
- Credit spreads - obtained from the credit derivative market as well as trades of more liquid bonds.
- Yield curves – often the foundation of the valuation model obtained from various fixed income markets.
- Foreign exchange rates - obtained from exchanges and trading markets for use in the valuation of spot, forward and futures contracts.
- Equity prices – obtained from exchanges or standard data sources.
- Prepayment rates – early repayment of principal. Estimates based on both historical and expected levels can have a material effect on the valuation of individual types of bonds, obtained from various market sources.
- Default and recovery estimates – assumptions regarding expected default and loss given default are important inputs in the models that price structured instruments. Data sources are the same as for prepayment rates.
- Structuring and cash flow details per tranche – analysis of structured bonds produces estimated cash flows which are an essential input for such instruments. Data sources are the same as for prepayment rates.
- Volatility – the extent to which the price of a security fluctuates is a key input in the valuation of options. Data sources are the same as for prepayment rates.
- Correlation - the extent to which changes in one variable are interdependent with changes in another variable. Data sources are the same as for prepayment rates.
- Counterparty risk – prices are based on an assumption of risk-free counterparties. This is a reasonable assumption, owing to the existence of netting agreements and the use of collateral.

### ***Real estate investments***

Investments in the real estate asset class consist of financial assets real estate, investment property and jointly controlled entities, see GPF Note 10 Real estate for further information. For all these investments fair value is the relevant measurement basis, for the financial asset where the ownership interest relates to an income stream, and at the property level where the bank has an ownership interest in investment property, either directly or through jointly controlled entities. At each reporting date real estate investments are adjusted to reflect their fair values as estimated by external independent valuation specialists using the discounted cash flow method or the yield method, unless it is deemed that the purchase price is a better estimate of fair value.

The real estate portfolio valuations are by nature predisposed to significant forward-looking judgements, key assumptions and estimates respective of the individual property type, location, expected future cash flows (such as lettings, tenants' profiles, future revenue streams, and the property's overall repair and condition) as well as applicable discount rates. Such estimates generally reflect recent market transactions of comparable properties having similar location, nature and quality characteristics. In addition, and as applicable, development risks (such as future construction costs and letting risks) are considered when determining the fair value of properties under construction or development. These assumptions are market standard and in accordance with international valuation standards. As a result, the valuations reflect best local market estimates at the valuation date and are sensitive to fluctuations to key assumptions. Events of assumptions not being achieved may have a material effect on the value of the property portfolio.

The discounted cash flow method involves the projection of a series of periodic cash flows either to an operating property or a development property, or from a portfolio of properties as is the case for the interest in an income stream. To this projected cash flow series, an appropriate risk adjusted market discount rate is applied to establish an indication of the present value of the income stream associated with the property. The calculated periodic cash flow is typically estimated as gross rental income, less vacancy, collection losses, direct and indirect operating expenses and other obligations to arrive at the net operating income. A series of periodic net operating incomes, along with an estimate of the terminal value (calculated using a consistent valuation approach as described here) are discounted to present value. The terminal value is the capitalised present value estimate of the net cash flow at disposition that is

anticipated at the end of the projection period. The aggregate of these net present values equals the market value of the property or the financial asset.

The yield method converts anticipated future cash flow benefits in the form of rental income into present value. This approach requires careful estimation of future benefits and the application of investor yield or return requirements. Properties valued using this method capitalise net rental income on the basis of an initial yield, generally referred to as the 'net initial yield' approach, adjusted for factors not included in net rental income, for example vacancy, lease incentives, and refurbishment.

### Valuation uncertainty

All equities, bonds, financial derivatives and real estate investments have been allocated to categories reflecting

assessed valuation uncertainty. Level 1 comprises investments that are valued on the basis of observable prices in active markets and are considered to have very limited valuation risk. Investments allocated to Level 2 are valued using models with observable market data. These holdings have some pricing uncertainty. Holdings allocated to category 3 are priced using models with considerable use of unobservable inputs, which implies substantial uncertainty regarding the establishment of fair value. These investments, too, are valued by external professional price providers who are regarded as giving the best estimate of fair value and where the total valuation from different pricing providers varies only to a limited extent.

Table 13.1 groups the investments into categories of assessed pricing uncertainty as at 31 December 2011 and 2010.

Amounts in NOK million

	Level 1		Level 2		Level 3		Total	
	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
<b>Equities</b>	<b>1 942 777</b>	<b>1 894 319</b>	<b>995</b>	<b>1 454</b>	<b>156</b>	<b>88</b>	<b>1 943 928</b>	<b>1 895 861</b>
<b>Total bonds</b>	<b>876 381</b>	<b>726 521</b>	<b>438 838</b>	<b>501 291</b>	<b>12 292</b>	<b>25 262</b>	<b>1 327 511</b>	<b>1 253 074</b>
Government bonds	600 790	491 061	11 775	16 508	-	-	612 565	507 569
Government-related bonds*	98 370	77 769	78 148	84 168	646	264	177 164	162 201
Inflation-linked bonds	98 431	75 182	7 285	28 155	-	-	105 716	103 337
Corporate bonds	3 513	1 389	184 543	204 077	285	1 714	188 341	207 180
Securitised bonds	75 277	81 120	157 087	168 383	11 361	23 284	243 725	272 787
<b>Total financial derivatives</b>	<b>- 219</b>	<b>21</b>	<b>- 3 511</b>	<b>- 6 325</b>	<b>-</b>	<b>-</b>	<b>- 3 730</b>	<b>- 6 304</b>
Assets	5	43	2 222	3 025	-	-	2 227	3 068
Liabilities	- 224	- 22	- 5 733	- 9 350	-	-	- 5 957	- 9 372
<b>Total real estate</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>11 023</b>	<b>-</b>	<b>11 023</b>	<b>-</b>
Financial assets real estate	-	-	-	-	4 415	-	4 415	-
Jointly controlled entities, real estate	-	-	-	-	2 546	-	2 546	-
Investment properties	-	-	-	-	4 062	-	4 062	-
<b>Total</b>	<b>2 818 939</b>	<b>2 620 861</b>	<b>436 322</b>	<b>496 420</b>	<b>23 471</b>	<b>25 350</b>	<b>3 278 732</b>	<b>3 142 631</b>

\* Sovereign bonds are included in government-related bonds as from 1 January 2011. Comparative amounts for 2010 have been restated.

The table above comprises the balance sheet lines Equities and units, Equities lent, Bonds and other fixed income instruments, Bonds lent, Short-sale bonds, Financial derivatives (asset and liability), Financial assets real estate, Jointly con-

trolled entities, real estate and Investment properties. Other balance sheet items are thus not included.

Almost all of the equity holdings are classified as Level 1. Equities classified as Level 2 mainly comprise relatively illiquid holdings, which are priced on the basis of similar more liquid shares issued by the same company. Equities classified as Level 3 comprise a small number of holdings, the valuation of which is particularly uncertain due to a lack of market activity, and equities whose trading has been suspended.

Valuation of bonds is more uncertain and complex than valuation of equities. NBIM carries out analyses for each reporting date to identify the extent to which there have been transactions and price transparency with related market liquidity for different types of bonds as well as for a number of individual securities. Most government bonds and inflation-linked bonds have been allocated to Level 1, and pricing is thus primarily based on observable market prices. Bonds issued by European sovereigns with a high extent of unresolved debt issues are allocated to Level 2, while the more liquid European securities continue to be assessed as belonging to Level 1, with a single bond classified as Level 3. Extensive analyses of pricing and liquidity

have been done for this segment. Government-related bonds are allocated to Levels 1, 2 and 3 on the basis of variation in the degree of trading and price transparency in the markets. Most corporate bonds belong to Level 2, though with some exceptions to both Levels 1 and 3. Covered bonds are mostly categorised in the observable Levels 1 and 2 on the basis of a relatively high degree of liquidity and price transparency in the markets. Other securitised bonds are allocated to Levels 2 and 3 on the basis of varied and in part limited price transparency. Thus, a substantial portion of securitised bonds are still allocated to Level 3 owing to limited activity in the market for these instruments, and the use of unobservable inputs in pricing as well as complex models.

All real estate investments have been allocated to Level 3, as key assumptions, estimates and judgements factor prominently in property valuation models.

#### Movements of Level 3 holdings

Table 13.2 shows a reconciliation of changes in balance sheet amounts for all Level 3 holdings in 2011 and 2010.

Amounts in NOK million

	1 Jan. 2011	Net gains/ losses	Purchases	Sales	Settled	Transferred from Level 1 or 2	Transferred to Level 1 or 2	Foreign exchange gains/ losse	31 Dec. 2011
<b>Equities and units</b>	<b>88</b>	<b>5</b>	<b>43</b>	<b>- 18</b>	<b>- 71</b>	<b>110</b>	<b>- 11</b>	<b>10</b>	<b>156</b>
<b>Bonds</b>	<b>25 262</b>	<b>- 751</b>	<b>690</b>	<b>- 11 265</b>	<b>- 2 786</b>	<b>2 173</b>	<b>- 794</b>	<b>- 237</b>	<b>12 292</b>
<b>Total real estate</b>	<b>-</b>	<b>- 83</b>	<b>11 009</b>	<b>-</b>	<b>.</b>	<b>.</b>	<b>.</b>	<b>97</b>	<b>11 023</b>
Financial assets real estate*	-	138	4 088	-	.	.	.	189	4 415
Jointly controlled entities, real estate**	-	- 31	2 620	-	.	.	.	- 43	2 546
Investment properties*	-	- 190	4 301	-	.	.	.	- 49	4 062
<b>Total</b>	<b>25 350</b>	<b>- 829</b>	<b>11 742</b>	<b>- 11 283</b>	<b>- 2 857</b>	<b>2 283</b>	<b>- 805</b>	<b>- 130</b>	<b>23 471</b>

\* Net gains/losses from financial assets real estate and investment properties are fair value changes recognised during the reporting period. For Financial assets real estate, Purchases does not include transaction costs, because this investment has been classified under the fair value option, and Net gains/losses does not include expensed transaction costs.

\*\* Net gains/losses from Jointly controlled entities, real estate include Share of the profit/loss from jointly controlled entities, real estate. Fair value changes from investment properties owned by jointly controlled entities are thus included in net gains/losses.

Amounts in NOK million

	1 Jan. 2010	Net gains/ losses	Purchases	Sales	Settled	Transferred from Level 1 or 2	Transferred to Level 1 or 2	Foreign exchange gains/ losse	31 Dec. 2010
<b>Equities</b>	<b>5</b>	<b>- 35</b>	<b>0</b>	<b>- 11</b>	<b>- 1</b>	<b>89</b>	<b>- 2</b>	<b>43</b>	<b>88</b>
<b>Bonds</b>	<b>33 518</b>	<b>4 974</b>	<b>611</b>	<b>- 7 400</b>	<b>- 4 844</b>	<b>4 984</b>	<b>- 6 892</b>	<b>311</b>	<b>25 262</b>
<b>Total</b>	<b>33 523</b>	<b>4 939</b>	<b>611</b>	<b>- 7 411</b>	<b>- 4 845</b>	<b>5 073</b>	<b>- 6 894</b>	<b>354</b>	<b>25 350</b>

Holdings allocated to Level 3 in the valuation hierarchy were reduced by NOK 1 879m to NOK 23 471m during 2011. A substantial decline in Level 3 bond holdings of NOK 12 969m was almost counterbalanced by the addition of NOK 11 023m

in real estate investments. Sales were the primary reason for the reduction in bonds, and US securitised bonds not guaranteed by federal agencies accounted for most of these sales.

### Sensitivity for Level 3 holdings

Amounts in NOK million

Table 13.3 Additional specification of Level 3 and sensitivities						
	Sensitivities 31 Dec. 2011			Sensitivities 31 Dec. 2010		
	Specification Level 3 at 31 Dec. 2011	Unfavour- able changes	Favourable changes	Specification Level 3 at 31 Dec. 2010	Unfavour- able changes	Favourable changes
<b>Equities and units</b>	<b>156</b>	<b>- 42</b>	<b>30</b>	<b>88</b>	<b>- 21</b>	<b>14</b>
<b>Total bonds</b>	<b>12 292</b>	<b>- 1 482</b>	<b>1 334</b>	<b>25 262</b>	<b>- 3 130</b>	<b>2 238</b>
Government-related bonds	646	- 65	39	264	- 21	49
Sovereign bonds	50	- 4	2	-	-	-
Bonds issued by local governments	500	- 48	32	64	- 6	5
Bonds issued by federal agencies	96	- 13	5	200	- 15	44
Corporate bonds	285	- 27	25	1 714	- 204	159
Bonds issued by financial institutions	265	- 26	23	1 651	- 196	153
Bonds issued by industrial companies	20	- 1	2	63	- 8	6
Securitised bonds	11 361	- 1 390	1 270	23 284	- 2 906	2 030
Covered bonds	121	- 9	6	-	-	-
Mortgage-backed securities (MBS)	9 970	- 1 191	1 027	18 941	- 2 417	1 615
Asset-backed securities (ABS)	1 087	- 159	210	3 878	- 424	371
Commercial mortgage-backed securities (CMBS)	183	- 31	27	465	- 65	44
<b>Total real estate</b>	<b>11 023</b>	<b>- 620</b>	<b>659</b>	<b>-</b>	<b>-</b>	<b>-</b>
Financial assets real estate	4 415	- 278	288	-	-	-
Jointly controlled entities, real estate	2 546	- 132	143	-	-	-
Investment properties	4 062	- 210	228	-	-	-
<b>Total</b>	<b>23 471</b>	<b>- 2 144</b>	<b>2 023</b>	<b>25 350</b>	<b>- 3 151</b>	<b>2 252</b>

NBIM's analyses indicate that valuation risk was reduced during 2011. The total exposure regarded as being particularly uncertain in relation to valuation was lower by only NOK 1 879m during 2011, to a year-end exposure of NOK 23 471m. However, the composition of holdings transitioned during the year towards more holdings with a lesser degree of perceived valuation risk. While US securitised bonds have an average perceived valuation uncertainty of around 12%, real estate holdings acquired in 2011 are viewed as having approximately 6% average valuation uncertainty. This is the major reason for the reduction of approximately NOK 1 007m in downside valuation risk to NOK 2 144m as of year-end 2011. The overall calculated sensitivity to favourable model input changes was slightly lower at NOK 2 022m. It should be noted that the total valuation risk present in the Level 3 holdings is expected to be less than this as the valuation of all holdings will not move in the same direction with the change of a single unobservable input parameter. For example, faster mortgage prepayments will have a positive impact on the valuation of some of the bonds held while having a negative result on other bond values, thereby representing partly offsetting effects to the total valuation.

The technique used to calculate the sensitivity of bond values is based on the availability of independent price sources and begins with the highest and lowest available price for a specific bond. Where a higher or lower price was not available, a standard sensitivity parameter was used. The level of the resulting valuation change is based on the bond type and the availability, reliability and variation of prices.

US mortgage-backed securities' sensitivity to changes to unobservable inputs contributed more than half of the overall valuation uncertainty of NOK 1 191m unfavourable and NOK 1 027m favourable. Around half of the total MBS exposure of NOK 9 970m at year-end 2011 stemmed from agency-backed interest-only collateralised mortgage obligations, where the most important unobservable parameter implicitly changed was prepayment speed assumptions. The remaining Level 3 MBS exposures comprised bonds not guaranteed by federal agencies. The key parameters changed in this case are various collateral performance related parameters, including expected severities, delinquencies and prepayment speed assumptions, in addition to the estimated yield spread applied to the expected cash flows of the bond in question.

Real estate investment valuations are particularly sensitive to changes in the rate of return (discount rate) and assumptions impacting future revenues. Under an unfavourable scenario, changing the rate of return by +0.20 percentage point on a relative basis, and future market rents by -2.0% on an absolute basis, all else being equal, is expected to change the value of the real estate portfolio by about 5.6% or NOK 620m. Under a favourable scenario, changing the rate of return by -0.20 percentage point on a relative basis, and future market rents by +2.0% on an absolute basis, all else being equal, is expected to change the value of the real estate portfolio by about 6% or NOK 659m.

## GPFG Note 14 Risk

### Government Pension Fund Global investment mandate

See Note 1 for a description of the framework for the management of the Government Pension Fund Global. Pursuant to the regulations of the mandate for management issued by the Ministry of Finance, Norges Bank shall manage the krone deposit in its own name by investing the funds in a portfolio of equities, fixed income securities and real estate, defined as the investment portfolio.

The Bank shall seek to obtain the highest possible return after expenses measured in the currency basket of the benchmark portfolio. The Ministry's strategic benchmark portfolio is divided into asset classes and regions, with rule-based adjustments for certain fixed income sectors and exclusion of selected companies from the investment universe. The investment portfolio may not invest in securities issued by Norwegian entities or issued in Norwegian kroner. These securities are also excluded from the benchmark portfolio. Positions in financial derivatives are part of the relevant asset classes, but are shown separately in the income statement and balance sheet for the investment portfolio of the Government Pension Fund Global.

### Norges Bank's governance structure

The Executive Board of Norges Bank has delegated the responsibility for the management of the Government Pension Fund Global to the Chief Executive Officer (CEO) of Norges Bank Investment Management (NBIM), which is an organisational unit within Norges Bank.

The CEO of NBIM is authorised by a job description and an investment mandate. The Executive Board has issued principles for risk management at NBIM, which include operational and investment risk management, principles for ownership management, principles for organisation and management of NBIM, and principles for compensation to NBIM employees. NBIM must adhere to internationally recognised standards in the areas of valuation, performance measurement and management, measurement and control of risk. Reporting to the Executive Board is done monthly, and more extensively quarterly. The Governor of Norges Bank and the Executive Board are notified without delay in the event of particular events or significant matters.

### NBIM's governance structure

Within NBIM, investment responsibilities are further delegated through investment mandates. Responsibility for processes and personnel is delegated through job descriptions, while process requirements are detailed in policies and guidelines. The composition of the NBIM leader group and the delegation of authority shall ensure segregation of duties between investment management, securities trading, operations, risk management and compliance.

The market risk committee, the credit and counterparty risk committee, and the investment universe committee complement the delegation of responsibility by advising on investment risk management, as well as on the instrument universe.

Internal risk reporting requirements are issued by the CEO through job descriptions to personnel in the risk area. The CEO receives daily, weekly and monthly reporting. The CEO is notified without delay of particular events or serious breaches of the investment mandate.

### NBIM's framework for investment risk

In the investment mandate for the Government Pension Fund Global given to Norges Bank, there are a number of guidelines and restrictions for the combined equity and bond asset class, as well as for the individual asset classes.

Real estate investments are covered in the investment mandate by separate regulations. These regulations provide Norges Bank with a framework for establishing an asset class with diversified exposure to global real estate markets.

Segregation of roles and responsibilities is a cornerstone of process design at NBIM. Processes such as the management of investment mandates, portfolio hierarchy and counterparties are delegated to the chief risk officer (CRO). Changes or additions to existing investment mandates in NBIM, the portfolio hierarchy or new counterparties require approval by the CRO, or a person the CRO has authorised.

The Executive Board's principles for risk management are detailed further in NBIM through policies and guidelines. Responsibility for an effective organisation and process related to risk management is delegated to the CRO to ensure a robust risk management process within NBIM.

***Risk management at NBIM is defined as:***

- Management of market risk
- Management of credit risk
- Management of counterparty risk
- Management of operational risk

The first three items listed are defined by NBIM as investment risk. In NBIM, the investment area has responsibility for managing the portfolio and individual mandate risk, while the risk management area independently measures, manages and reports investment risk across the portfolio, asset classes and other levels within the portfolio that reflect the investment process.

***Investment risk – market risk***

NBIM defines market risk as the risk of a loss or a change in the market value of the portfolio or in parts of the portfolio as a result of changes in financial market variables. This includes movements in credit spreads. Market risk is measured by NBIM along the following dimensions: absolute and relative exposure as compared to the benchmark, volatility and correlation risk, systematic factor risk and liquidity risk. Market risk is actively taken to generate investment returns in line with the objectives of the investment mandates.

***Investment risk – credit risk***

NBIM defines credit risk as the risk of loss due to an issuer being unable to meet its payment obligations. Within credit risk, NBIM measures risk as single issuer credit risk where the probability of default and loss given default are taken into account, and portfolio credit risk where credit risk takes into account the correlation in credit losses between the instruments and the issuers. Credit risk is actively taken to generate investment returns in line with the investment mandates' objectives.

***Investment risk – counterparty risk***

NBIM defines counterparty risk as the risk of loss related to the possible bankruptcy of a counterparty or other similar event leading to counterparty default. Counterparty risk can be divided into credit risk associated with the bankruptcy of a counterparty, settlement risk and custodian risk. Counterparty risk is controlled and mitigated to the greatest extent possible, given the investment strategy.

***Risk management process***

NBIM uses several measurements, processes and systems to monitor and control investment risk. Robust and widely accepted risk management systems and processes are complemented by internally developed measurements and processes.

**Market risk**

Norges Bank measures risk in both absolute terms for the actual portfolio and the relative market risk for investments in the Government Pension Fund Global.

Continuous monitoring, measurement and assessment of market risk are performed along multiple risk dimensions, employing a number of methodologies and approaches. Combining different and complementary risk measures provides a better insight into the risk profile of the holdings in the Government Pension Fund Global.

***Asset class by region***

The portfolio is invested across several asset classes and regions as shown in Table 14.1.



Table 14.1 Allocation by asset class and region						
	Market value* in percent by region		Market value* in percent by asset class		Assets minus liabilities before management fee	
	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Equities						
Americas and Africa	35.9	36.1				
Europe	49.7	48.2				
Asia and Oceania	14.4	15.7				
<b>Total equities</b>			<b>58.7</b>	<b>61.5</b>	<b>1 944 721</b>	<b>1 891 250</b>
Bonds						
Americas and Africa	37.7	35.2				
Europe	56.1	59.2				
Asia and Oceania	6.2	5.6				
<b>Bonds total</b>			<b>41.0</b>	<b>38.5</b>	<b>1 355 722</b>	<b>1 186 170</b>
Real estate						
Europe	100	-				
<b>Total real estate</b>			<b>0.3</b>	<b>-</b>	<b>11 129</b>	<b>-</b>

\* As from 1 January 2011, the calculation of market value in the table above has been changed to include all positions in the portfolio, and not only equity and bond holdings. Comparative amounts for 2010 have been restated.

### Concentration risk

The holdings of the Government Pension Fund Global include substantial investments in government-issued bonds. It is also normal for private companies to issue both bonds and equities.

Table 14.2 shows the largest holdings in bonds issued by governments, including government bonds issued in local currency, sovereign bonds and inflation-linked bonds issued in local currency:

Amounts in NOK million

Table 14.2 Largest holdings within the segment government bonds		
	Market value 31 Dec. 2011	Market value 31 Dec. 2010
US	249 072	164 627
UK	109 813	98 581
France	79 790	73 609
Japan	67 036	58 461
Germany	51 294	54 991
Italy	32 914	52 345
Netherlands	20 218	25 361
Spain	17 975	14 229
Austria	15 561	12 940
Belgium	14 813	11 224

Table 14.3 shows the portfolio's largest holdings of non-government issuers across both bonds and equities. Covered

bonds issued by financial institutions are included in the bonds column.

Amounts in NOK million

Table 14.3 Largest total positions excluding sovereigns, for both bonds and equities				
31 Dec. 2011	Sector	Bonds	Equities	Total
Royal Dutch Shell PLC	Oil & Gas	0	30 983	30 983
Nestle SA	Consumer Goods	0	25 346	25 346
European Investment Bank	Government-related	24 099	0	24 099
Kreditanstalt fuer Wiederaufbau	Government-related	22 703	0	22 703
HSBC Holdings PLC	Financials	948	19 583	20 530
Vodafone Group PLC	Telecommunication	1 338	18 858	20 196
Novartis AG	Health Care	0	19 281	19 281
Nationwide Building Society	Financials	17 618	0	17 618
BP PLC	Oil & Gas	0	17 277	17 277
Exxon Mobil Corp	Oil & Gas	0	16 901	16 901
31 Dec. 2010	Sector	Bonds	Equities	Total
HSBC Holdings PLC	Financials	2 780	21 152	23 932
Fannie Mae	Government-related	22 828	-	22 588
European Investment Bank	Government-related	22 273	-	22 273
Royal Dutch Shell PLC	Oil & Gas	-	21 403	21 403
Nestle SA	Consumer Goods	-	21 285	21 285
Bank of Scotland PLC	Financials	17 996	-	17 996
Kreditanstalt fuer Wiederaufbau	Government-related	17 108	-	17 108
Vodafone Group PLC	Telecommunication	1 346	15 215	16 561
BP PLC	Oil & Gas	499	15 939	16 438
Banco Santander SA	Financials	5 854	8 794	14 648

Table 14.4 shows the allocation of the real estate portfolio by country, sector, the development share and the vacancy ratio.

Table 14.4 Allocations, real estate portfolio		
Percent	31 Dec. 2011	31 Dec. 2010
<b>Country</b>		
- UK	40.0	-
- France	60.0	-
<b>Sector</b>		
- Office	63.2	-
- Retail	35.4	-
- Residential	0.4	-
- Industrial	0.0	-
- Other real estate	1.0	-
<b>Development</b>	0.9	-
<b>Vacancy</b>	8.1	-

#### Volatility and correlation risk

Norges Bank uses risk modelling to quantify the risk of value change associated with all or parts of a portfolio. These are standard risk measurement techniques based on statistical measures such as standard deviation, which take into account correlations between different instruments in the portfolio. This risk measurement technique provides an estimate of expected change or fluctuation in the portfolio's value on the basis of markets conditions over the past three years. Expected volatility can be expressed in terms of the portfolio's absolute risk or relative risk. The long-term model uses equally weighted weekly return data over the last three years and a parametric calculation methodology. The long-term model is tailored to the long-term investment horizon of the Government Pension Fund Global. The same

models are used for both portfolio risk and tracking error. In addition to the long-term risk model, NBIM uses a responsive risk model. The model uses daily return data where newer data are given a greater weight than older data. The responsive model captures the market dynamics of recent periods to a greater extent, with the result that changes in modelled risk are best explained by short-term fluctuations.

Real estate investments are not included in the volatility calculations. This is consistent with the investment mandate issued by the Ministry of Finance and the Executive Board of Norges Bank in addition to internal guidelines for investment and risk management.

Tables 14.5 and 14.6 present risk both in terms of both the portfolio's absolute risk and the relative risk.

Table 14.5 Portfolio risk in terms of expected volatility, in percent								
Long-term model	31 Dec. 2011	Min 2011	Max 2011	Average 2011	Expected volatility, actual portfolio			
					31 Dec. 2010	Min 2010	Max 2010	Average 2010
Portfolio	9.6	9.5	13.4	12.1	13.2	13.1	15.8	13.6
Equities	16.4	16.4	21.2	19.9	21.1	21.0	25.2	21.7
Bonds	10.5	10.5	12.7	12.0	12.3	11.2	13.4	12.2
<b>Responsive model</b>								
Portfolio	10.1	6.7	15.2	9.3	7.2	6.2	9.8	7.7
Equities	17.7	8.8	26.3	14.8	9.7	9.2	15.9	11.9
Bonds	10.6	6.9	14.4	9.9	8.3	6.3	13.9	9.6

Table 14.6 Relative risk, expected relative volatility in basis points

					Expected relative volatility			
	31 Dec. 2011	Min 2011	Max 2011	Average 2011	31 Dec. 2010	Min 2010	Max 2010	Average 2010
<b>Long-term model</b>								
Portfolio	40	33	65	46	54	37	58	48
Equities	53	40	111	64	61	45	71	58
Bonds	45	38	76	51	77	51	90	76
<b>Responsive model</b>								
Portfolio	44	23	57	35	24	24	59	34
Equities	62	29	115	53	29	27	47	38
Bonds	85	21	97	43	32	31	114	55

Risk measured by the long-term risk model declined for the portfolio as a whole and in both asset classes in 2011. For the portfolio as a whole, measured risk at year-end was 9.6%. This means that for the portfolio, annual fluctuations in value of just above NOK 300bn can be expected. Correspondingly, measured risk at year-end 2010 was 13.2%, which implied that at the beginning of 2011 annual fluctuations of around NOK 400bn could be expected. The actual loss on the portfolio for 2011 of NOK 37bn was within this number, with pronounced fluctuations through the year. In line with the decline in equity markets, the proportion of investments in equities has been reduced due to decreases in market values, which has helped to reduce the risk in the investment portfolio. In addition to this effect, however, the decline was also an artefact of the model, which uses three years' historical data and consequently, historical data from the volatile period in 2008 was no longer included in the model at year-end. Despite the fact that 2011 was also characterised by market turbulence, it was less pronounced than in 2008.

The mandate for the Government Pension Fund Global has a limit of 100 basis points expected relative volatility. Risk is measured and compliance with the limit monitored on the basis of the long-term model.

Expected relative volatility based both on the long-term model and the responsive model were within the limit in 2011. At the end of the fourth quarter of 2011, expected relative volatility for the portfolio according to the responsive model was somewhat higher than at the beginning of the year.

Fluctuations in equity and bond markets increased in 2011, driven by uncertainty regarding European sovereign debt, increased expectations of an economic downturn in

the US and persistent funding challenges for European banks in particular. The unrest reached a peak in the third quarter. Towards year-end 2011, unemployment in the US fell, and economic growth picked up, so that underlying economic developments appear stronger. In December, the European Central Bank implemented measures to support banks, which also reduced market stress.

#### **Strengths and weaknesses**

The strength of these types of risk models is that one can estimate the risk of a portfolio across different asset classes, markets, currencies, securities and derivatives and express the risk through one single figure which takes into account the correlation between different asset classes, securities and risk factors.

Model-based risk estimates are based on historical relationships and may have good forecasting capabilities in markets without significant changes in volatility. In periods with significant changes in volatility and correlation, estimates will be less reliable. Calculated volatility gives a point estimate of risk, and provides little information about the total risk profile and any tail risk. Annualisation means assuming that volatility and portfolio composition are constant over time. To compensate for these weaknesses, NBIM uses complementary models, methods and various stress tests. In addition, analyses are performed of concentration risk and realised return.

#### **Back-testing of models**

Back-testing of the models is performed to validate the model's ability to estimate risk. One of the methods used is to compare the predicted risk estimated by the models to the actual risk observed in the portfolio's actual return.

The table below summarises the total number of observations where actual loss exceeds the expected risk, the expected frequency and the ratio between them. Only downside risk has been taken into account. The closer the observed/ expected ratio is to 1, the better the model has

estimated risk. Three different confidence intervals are considered. A ratio above one indicates that the risk has been underestimated.

Table 14.7: Comparison between portfolio's expected loss frequency and actual loss frequency

Risk measure	Period	Expected	Observed	Observed/Expected
Standard deviation	2 years	83	75	0.90
Value-at-Risk 95%	2 years	26	26	1.00
Value-at-Risk 99%	2 years	5	9	1.73

Table 14.8: Comparison between expected and actual loss frequency on relative return

Risk measure	Period	Expected	Observed	Observed/Expected
Standard deviation	2 years	83	66	0.79
Value-at-Risk 95%	2 years	26	18	0.69
Value-at-Risk 99%	2 years	5	6	1.15

### Credit risk

Credit risk is the risk of losses from issuers of fixed income instruments defaulting on their payment obligations. Fixed income instruments in the portfolio's benchmark portfolio are all rated as investment grade by one of the major credit

rating agencies. Investments in bonds are made on the basis of internal assessments of expected return and the investment's risk profile and how it complements the portfolio.

Amounts in NOK million

Table 14.9 Bond portfolio by credit rating

31 Dec. 2011	AAA	AA	A	BBB	Higher risk	Total
Government bonds	495 162	79 563	28 235	6 248	3 357	612 565
Government-related bonds	110 336	39 658	12 868	11 352	2 950	177 164
Inflation-linked bonds	77 634	21 011	6 857	-	214	105 716
Corporate bonds	283	25 219	94 555	65 667	2 617	188 341
Securitised bonds	183 963	35 719	12 476	6 672	4 895	243 725
<b>Total bonds and other fixed income instruments</b>	<b>867 378</b>	<b>201 170</b>	<b>154 991</b>	<b>89 939</b>	<b>14 033</b>	<b>1 327 511</b>
31 Dec. 2010	AAA	AA	A	BBB	Higher risk	Total
Government bonds	389 135	108 100	3 254	2 903	4 177	507 569
Government-related bonds	98 950	39 655	11 145	11 779	671	162 201
Inflation-linked bonds	58 558	44 260	-	-	519	103 337
Corporate bonds	4 139	45 576	82 693	69 837	4 935	207 180
Securitised bonds	207 742	40 997	3 549	1 880	18 619	272 787
<b>Total bonds and other fixed income instruments</b>	<b>758 524</b>	<b>278 588</b>	<b>100 641</b>	<b>86 399</b>	<b>28 921</b>	<b>1 253 074</b>

Credit risk in the bond market rose during the year, particularly as a consequence of the debt situation in Europe. Among evidence for this were the higher credit spreads observed on European treasury and corporate bond issues. In addition several sovereigns and companies were downgraded by the rating agencies. New bond investments in 2011 were primarily highly rated bonds, which overshadowed the effect of the downgrades. The composition of the bond portfolio saw an increase in the proportion of sovereign bonds

and a reduction in corporate and securitised bonds. The composition by credit rating was characterised by a change in the allocation among the three best rating categories, whereby the share of AA instruments was reduced and that of AAA and A increased accordingly. At year-end 2011, defaulted bonds had a total market value of NOK 1.5bn, or 0.1% of the bond portfolio; the nominal amount of defaulted bonds was NOK 9.3bn, down from NOK 13.3bn at year-end 2010. Defaulted bonds are grouped with "Higher risk" in the table above.

Table 14.10: Bond portfolio by credit rating and currency in percent

31 Dec. 2011	AAA	AA	A	BBB	Higher risk	Total
EUR	26.1	7.2	6.3	2.3	0.5	42.4
USD	24.7	2.0	4.1	3.6	0.5	34.9
GBP	9.5	0.4	1.0	0.6	0.0	11.4
JPY	0.0	5.1	0.0	0.0	0.0	5.1
CAD	1.4	0.5	0.1	0.1	0.0	2.1
Other currencies	3.6	0.0	0.2	0.2	0.1	4.1
<b>Total</b>	<b>65.3</b>	<b>15.2</b>	<b>11.7</b>	<b>6.8</b>	<b>1.1</b>	<b>100.0</b>

31 Dec. 2010	AAA	AA	A	BBB	Higher risk	Total
EUR	26.0	14.1	3.3	2.1	0.5	46.0
USD	21.3	2.5	3.6	4.0	1.7	33.1
GBP	9.2	0.6	1.0	0.6	0.0	11.4
JPY	0.0	4.4	0.0	0.0	0.0	4.4
CAD	1.4	0.6	0.1	0.1	0.0	2.2
Other currencies	2.8	0.0	0.0	0.1	0.0	2.9
<b>Total</b>	<b>60.7</b>	<b>22.2</b>	<b>8.0</b>	<b>6.9</b>	<b>2.3</b>	<b>100.0</b>

During the course of 2011, the use of credit derivatives was reduced considerably (see GPF Note 9 Financial derivatives).

In addition to the credit rating based approach, credit risk management at Norges Bank is complemented by additional credit risk measures. These model-based approaches complement the credit rating method and are used to monitor credit risk independently of the credit rating. These methods are comparable to the volatility and correlation risk model in the manner in which credit risk is quantified into one number and are a function of observable credit spreads and equity prices as well as the volatility and correlations between them.

### Counterparty risk

Norges Bank is exposed to risk vis-à-vis counterparties in the international settlement and custody systems where trades are settled. Additionally, counterparties are necessary to ensure efficient cash management, effective trading and hedging of market and/or credit risk. Repurchase and reverse repurchase agreements and securities lending via external agents also give rise to counterparty risk.

Norges Bank reduces counterparty risk by using several counterparties and by setting strict credit rating requirements. Concentration is also reduced by setting exposure limits for individual counterparties. Rating requirements for

counterparties with unsecured bank deposits are higher than in situations when collateral is posted. Netting agreements are used to further mitigate counterparty exposure when trading in OTC derivatives and foreign exchange contracts. Additional mitigation of counterparty risk is ensured through collateral requirements for counterparty net positions with positive market value.

The methods used to calculate counterparty risk are in accordance with recommendations by the UK Financial Services Authority. Two methods are used: for OTC derivatives, time deposits, bank deposits, and foreign exchange contracts, a counterparty risk model in which exposures are repriced under different assumptions to take into account possible future market movements is used, thus estimating potential future exposure. Netting agreements and collateral are taken into account in determining net exposure. For

repurchase agreements, securities lending transactions executed via external agents and securities posted as collateral for futures trades, a method is used that adds a premium to the market value that reflects the position's volatility. These positions are also adjusted for netting and actual received and posted collateral when determining net exposure. Table 14.11 is a breakdown of exposure by type of activity/instrument regarded as having counterparty risk. In addition to figures from the internal risk model, the counterparty risk in accordance with the balance sheet, adjusted for recognised and unrecognised collateral, is shown.

Securities lending through external agents was reduced during the second half of 2011 (see GPFG Note 8 External agency securities lending). Activity in repurchase agreements was also reduced in the fourth quarter, thus reducing total counterparty risk, particularly in terms of gross exposure.

Amounts in NOK million

31 Dec. 2011	Carrying amount adjusted for collateral	Gross exposure	Effect of netting	Collateral and guarantees	Net exposure
Time deposits and unsecured bank deposits	7 276	7 691	-	-	7 691
OTC derivatives including foreign exchange contracts	-3 511	5 355	1 601	2 009	1 745
Repurchase and reverse repurchase agreements*	-2 668	1 040	181	-	858
Securities lending transactions**	-9 526	18 097	-	7 624	10 742
Bonds posted as collateral for futures trades	762	772	-	-	772
<b>Total</b>		<b>32 955</b>	<b>1 783</b>	<b>9 633</b>	<b>21 538</b>

\* The column Carrying amount adjusted for collateral takes into account all positions in the repurchase market, including reinvestments of cash collateral. The internal measurement and monitoring of counterparty risk for these types of instruments do not include these reinvestments.

\*\* The column Carrying amount adjusted for collateral includes securities lent and collateral received and is adjusted for unrealised losses connected to reinvestments in the form of bonds.

Amounts in NOK million

31 Dec. 2010	Carrying amount adjusted for collateral	Gross exposure	Effect of netting	Collateral and guarantees	Net exposure
Time deposits and unsecured bank deposits	6 075	5 989	-	-	5 989
OTC derivatives including foreign exchange contracts	-6 098	8 523	5 462	1 581	1 480
Repurchase and reverse repurchase agreements*	-4 081	5 756	579	-	5 177
Securities lending transactions**	-16 352	30 965	-	17 597	13 368
Bonds posted as collateral for futures trades	620	638	-	-	638
<b>Total</b>		<b>51 871</b>	<b>6 041</b>	<b>19 178</b>	<b>26 652</b>

\* The column Carrying amount adjusted for collateral takes into account all positions in the repurchase market, including reinvestments of cash collateral. The internal measurement and monitoring of counterparty risk for these types of instruments do not include these reinvestments.

\*\* The column Carrying amount adjusted for collateral includes securities lent and collateral received and is adjusted for unrealised losses connected to reinvestments in the form of bonds.

The line OTC derivatives including foreign exchange contracts in the table comprises the net market value of foreign exchange contracts (NOK 639m) and swaps (NOK -4 150m). See also Note 9 Financial derivatives. Counterparty risk for derivative positions is followed up on a net basis at Norges Bank.

Norges Bank counterparties have a credit rating from an independent credit rating agency. Only in instances when the counterparty risk is considered very low can an internal credit evaluation be used as the basis for counterparty approval. Credit ratings of the bank's counterparties are monitored and complemented by alternative credit risk indicators. Table 14.12 shows Norges Bank's counterparties classified according to credit rating.

	Norges Banks counterparties (excl. brokers)		Brokers	
	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
AAA	3	3	3	3
AA	50	55	43	57
A	39	23	43	36
BBB	4	-	14	21
BB	-	-	2	6
B	-	-	12	3
<b>Total</b>	<b>96</b>	<b>81</b>	<b>117</b>	<b>126</b>

### Leverage

Leverage is used primarily to ensure effective management of the investments, and not with the aim of increasing the economic exposure to risky assets. The use of leverage is regulated both in the investment management mandate issued by the Ministry of Finance to Norges Bank and in the investment mandate issued by the Executive Board of Norges Bank to NBIM. Leverage is the difference between

net exposure and market value. Net exposure is determined by including securities in the calculation at market value and the derivatives by the underlying exposure. When exposure is greater than market value, the portfolio is leveraged.

At the beginning of 2011, the portfolio had leverage of 2.2%. During 2011, the holding of cash increased, and at year-end 2011 the portfolio had no leverage.

Percent	31 Dec. 2011	2011 Q3	2011 Q2	2011 Q1	31 Dec. 2010
Leverage	0.0 %	0.0 %	0.0 %	1.8 %	2.2 %

### Sale of securities Norges Bank does not own

Sale of securities not owned by Norges Bank (short sales) can only be done if the Bank has established borrowing agreements to cover a negative position. Such transactions

are very rarely undertaken, and at year-end 2011, no securities had been sold in this manner.



## GPF Note 15 Subsidiaries and jointly controlled entities

Norges Bank's ownership interests within the investment portfolio of the Government Pension Fund Global in all material subsidiaries and jointly controlled entities are shown in Table 15.1.

Company	Office Location	Ownership and voting rights in percent
NBIM S.a.r.l	Luxembourg	100
NBIM Louis SPPICAV	Paris	100
NBIM Louis SAS	Paris	100
Matignon 16 SCI*	Paris	50
Champs Elysées Rond-Point SCI*	Paris	50
PB 12 SCI*	Paris	50
Burlington Number 1 (General Partner) Limited	London	100
Burlington Number 1 Partners LP	London	100

\* Jointly controlled entities

# Independent auditor's report

To the Supervisory Council of Norges Bank

## Report on the financial statements

We have audited the accompanying financial statements of Norges Bank, which comprise the statement of financial position as at December 31, 2011, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information. The consolidated financial reporting for the investment portfolio of the Government Pension Fund Global is included in Norges Bank's financial statements and disclosed in Note 24.

### *The Executive Board's and the Governor's responsibility for the financial statements*

The Executive Board and the Governor are responsible for the preparation and fair presentation of these financial statements in accordance with Accounting Act and the Regulation concerning annual financial reporting for Norges Bank. The regulation requires Norges Bank's financial statements to be prepared in accordance with International Financial Reporting Standards as endorsed by the EU (IFRS), but sets certain specific presentation requirements for the investment portfolio of the Government Pension Fund Global, including investments in subsidiaries being part of the investment portfolio. The Executive Board and the Governor are also responsible for such internal control as necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with laws, regulations and auditing standards and practices generally accepted in Norway, including International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance that the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the financial statements have been prepared in accordance with the law and regulations and give a true and fair view of the financial position of Norges Bank as at December 31, 2011, and of its financial performance and its cash flows for the year then ended in accordance with the Accounting Act and the Regulation concerning annual financial reporting for Norges Bank. The regulation requires Norges Bank's financial statements to be prepared in accordance with International Financial Reporting Standards as endorsed by the EU (IFRS), but sets certain specific presentation requirements for the investment portfolio of the Government Pension Fund Global, and subsidiaries that exclusively constitute investments as part of the management of the investment portfolio.

## Report on other legal and regulatory requirements

### *Opinion on the Executive Board's report and the allocation of the total comprehensive income*

Based on our audit of the financial statements as described above, it is our opinion that the information presented in the Executive Board's report concerning the financial statements and the proposal for the allocation of the total comprehensive income complies with the law and regulations and that the information is consistent with the financial statements.

### *Opinion on registration and documentation*

Based on our audit of the financial statements as described above and control procedures we have considered necessary in accordance with the International Standard on Assurance Engagements (ISAE) 3000, «Assurance Engagements Other than Audits or Reviews of Historical Financial Information», it is our opinion that management has fulfilled its duty to produce a proper and clearly set out registration and documentation of the company's accounting information in accordance with the law and bookkeeping standards and practices generally accepted in Norway.

Oslo, 29 February 2012

**Deloitte AS**

Aase Aa. Lundgaard  
State Authorised Public Accountant (Norway)

# Resolution of the Supervisory Council on the financial statements for 2011

In accordance with the current guidelines for the allocation and distribution of Norges Bank's profit, the Supervisory Council adopted the following decision at its meeting on 15 March 2012:

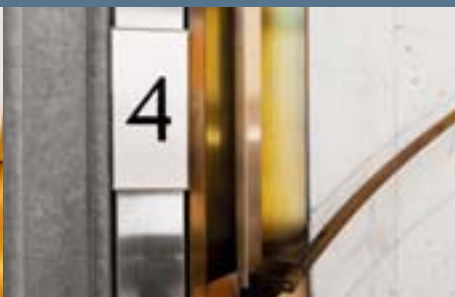
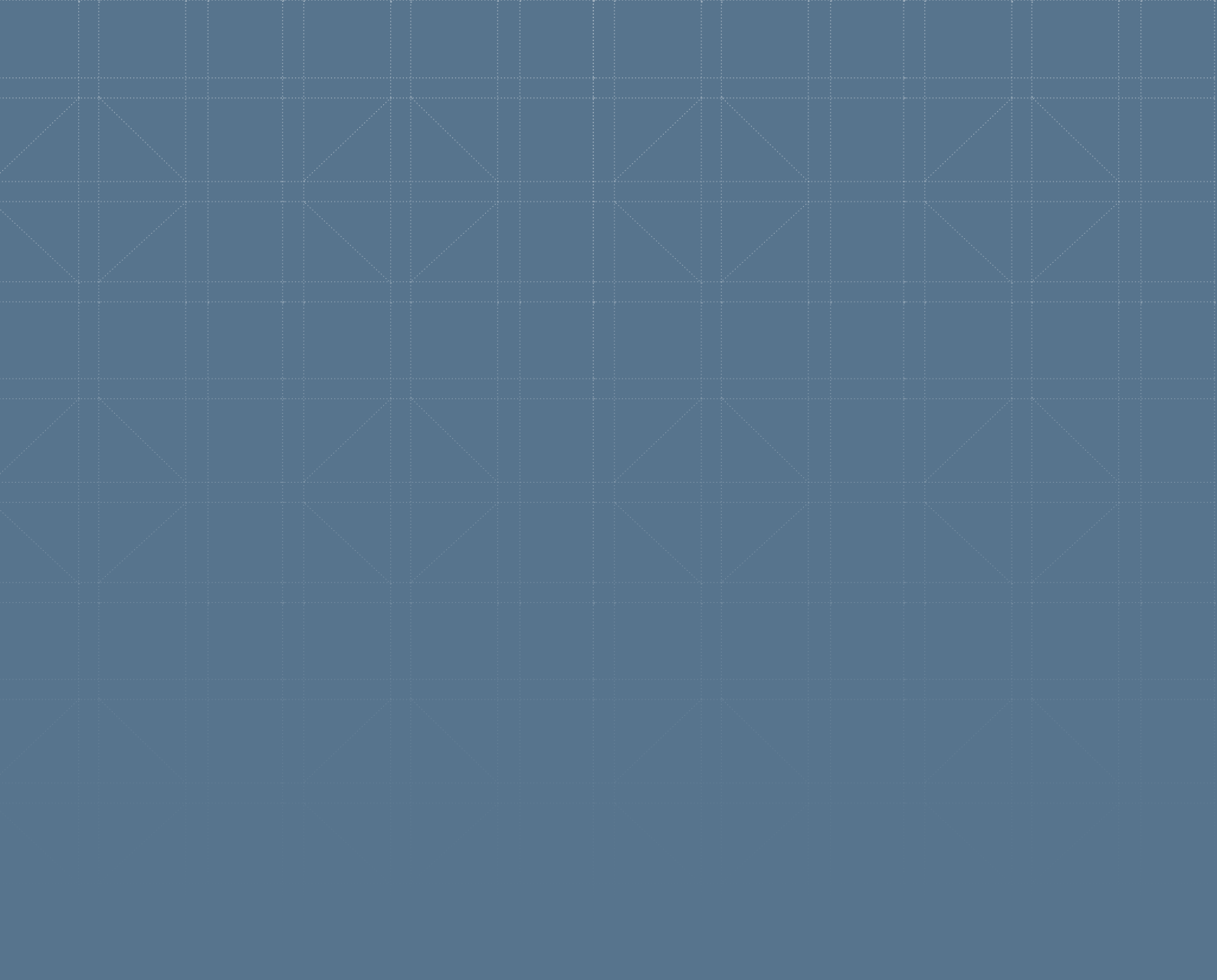
- The Supervisory Council takes note of the Annual Report of the Executive Board for 2011.
- The Supervisory Council takes note of the auditor's report for Norges Bank for 2011.
- The Supervisory Council adopts Norges Bank's financial statements for 2011 with the following transfers and allocations:
  - In connection with the introduction of IFRS, the sum of NOK 205m is to be transferred from "Other capital" to the Adjustment Fund.
  - In accordance with the guidelines, the profit after other allocations of NOK 8 376m is to be transferred to the Adjustment Fund.
  - There is no capital in the Transfer Fund and no transfers will therefore be made to the Treasury.

## The Supervisory Council's statement on the minutes of the meetings of the Executive Board and its supervision of the Bank in 2011

Under the Norges Bank Act, the Supervisory Council submits a separate report to the Storting concerning the minutes of the meetings of the Executive Board and its supervision of the Bank. The report for 2011 was adopted

by the Supervisory Council on 15 March 2012 and will be published and made available on the Bank's website upon submission to the Storting.







Norges Bank's activities **2011**

## CHAPTER 1:

# Responsibilities and organisation

### Promoting economic stability in Norway

The aim of Norges Bank is to promote economic stability in Norway. Norges Bank shall promote price stability by means of monetary policy, promote financial stability, contribute to robust and efficient payment systems and manage the Government Pension Fund Global (GPF) and the Bank's foreign exchange reserves.

The Bank's activities are regulated by the Act of 24 May 1985 relating to Norges Bank and the Monetary System etc (the Norges Bank Act). The Act states that Norges Bank shall be an executive and advisory body for monetary, credit and foreign exchange policy. The Bank shall issue banknotes and coins, promote an efficient payment system domestically as well as vis-à-vis other countries, and monitor developments in the money, credit and foreign exchange markets. The Act authorises the Bank to implement measures customarily or ordinarily taken by a central bank.

The Government has defined an inflation target for monetary policy in a regulation issued pursuant to the Norges Bank Act.

Norges Bank's responsibilities with respect to the management of the Government Pension Fund Global are regulated by the Act relating to the Government Pension Fund Global and a management mandate laid down by the Ministry of Finance.

### Organisation of activities

The highest decision-making bodies of Norges Bank are the Executive Board and the Supervisory Council. The Executive Board oversees the executive and advisory activities of the Bank, while the Supervisory Council supervises the Bank's operations and ensures that the rules governing the Bank's activities are observed. The Executive Board consists of seven members, all appointed by the government, with the Governor as chair and the Deputy Governor as deputy chair. For a more detailed description of the Executive Board's work, see Part I, Annual Report of the Executive Board

Norges Bank's Supervisory Council comprises 15 members appointed by the Storting. By means of its activities and reports, the Council shall provide assurance to the Storting that Norges Bank, including the management of the Government Pension Fund Global, operates in a prudent and appropriate manner and in compliance with legislation and other standards. A secretariat has been established by the Supervisory Council, the Office of the Supervisory Council, which performs oversight and control tasks, administers the agreement with the external auditor and performs secretariat tasks for the Supervisory Council. It also functions as a liaison between the Office of the Auditor General, the external auditor and the Bank, especially with regard to the GPF. The Office of the Supervisory Council is professionally and administratively independent of the Bank. The Supervisory Council submits its report to the Storting.



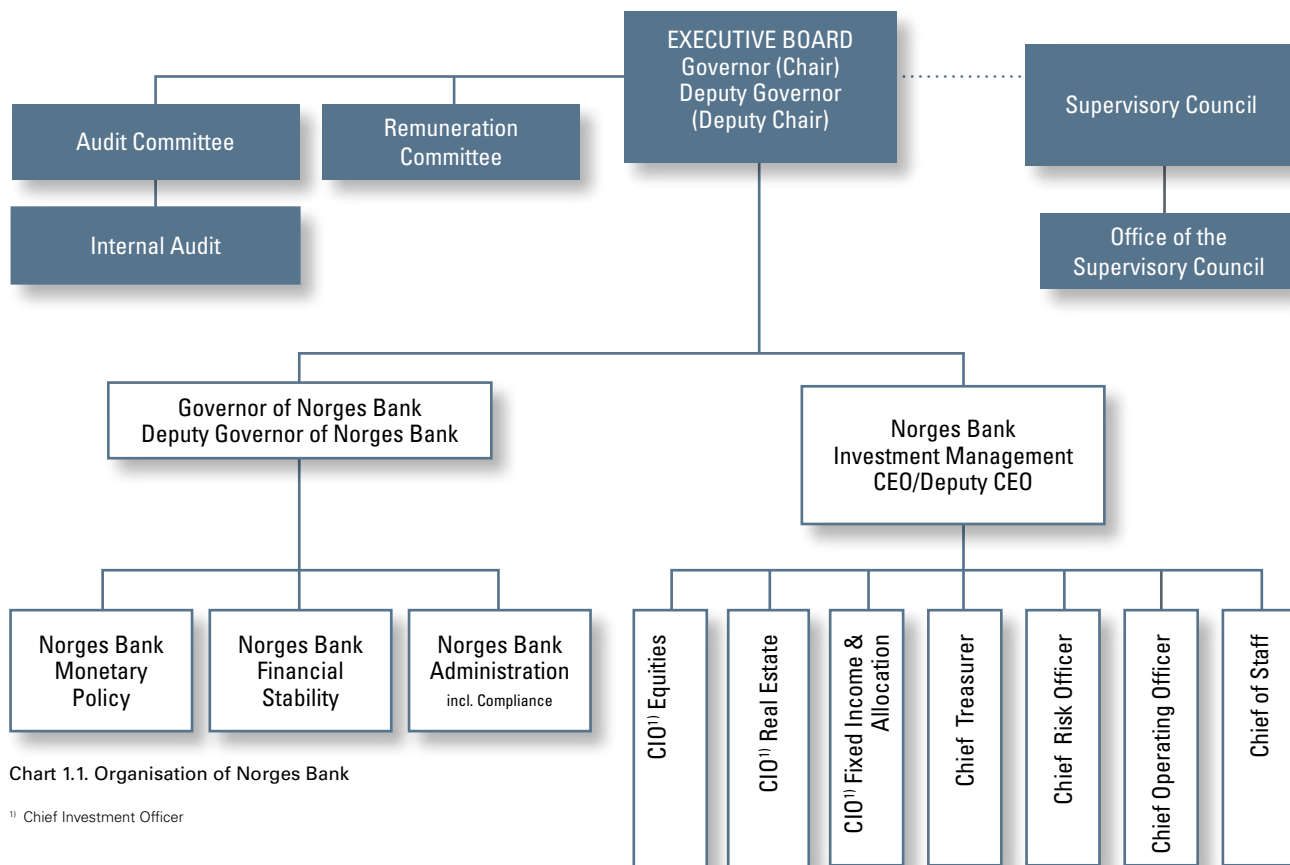


Chart 1.1. Organisation of Norges Bank

<sup>1)</sup> Chief Investment Officer

The Executive Board has delegated a large share of the day-to-day operations of the Bank to the governor, who has further delegated these to the operational areas. Pursuant to Section 5, final paragraph, of the Norges Bank Act, “[t]he Governor is in charge of the Bank’s administration and the implementation of the decisions”.

Organisation of the Bank’s operations is based on clearly defined core activities.

Central banking operations comprise the core areas Norges Bank Monetary Policy (NBMP) and Norges Bank Financial Stability (NBFS). In addition, Norges Bank Administration (NBA) provides staff and support functions.

In the case of Norges Bank Investment Management (NBIM), decision-making authority has been delegated by the Executive Board to the position of chief executive officer. NBIM manages the GPFG and most of Norway’s foreign exchange reserves. NBIM has some support functions of its own, but also receives support from NBA. For more information on the management and organisation of NBIM, see the *Government Pension Fund Global Annual Report*.

Three-year strategic plans are drawn up describing Norges Bank’s current status, challenges and priorities. The strategy, in addition to statutory requirements, provides the framework for the Bank’s activities. Within the annual frameworks allocated for FTEs and budgets and established shared processes, the individual operational areas are allowed considerable freedom with respect to personnel management and budget disposal.

Norges Bank’s governance documents define responsibilities and roles and set the framework for various activities. Governance documents are adopted at different levels, with a varying degree of detail, and may apply to all or parts of the Bank’s operations. The governance documents are viewed in the context of the framework laid down in the Norges Bank Act, the Executive Board’s rules of order, the central bank’s planning and follow-up processes and decisions made by the Board and by management.

# Monetary policy

## Sovereign debt crisis in Europe

*Although underlying inflation was below target in 2011, the decline had come to a halt (see Chart 2.1). Growth in the economy picked up, and capacity utilisation rose to a normal level. However, growth prospects at home and abroad weakened through summer and autumn as a result of increased financial market turbulence, primarily in Europe. Both the consideration of bringing consumer price inflation up to 2.5% and the consideration of stabilising developments in output and employment suggested that the key policy rate should be kept low in 2011.*

The beginning of 2011 was characterised by turbulence related to high levels of sovereign debt in a number of countries. Activity had picked up abroad, but the need to shore up weak government finances appeared to be exerting a drag on growth. Activity in Norway had increased as projected, and growth appeared to have gained a foothold in early 2011. Underlying inflation had fallen in the wake of the financial crisis and was around 1.5% at the beginning of the year.

## Pick-up in growth, but prospects uncertain

The moderate recovery in the global economy continued into 2011. Growth was vigorous in a number of emerging economies, and higher prices for energy and commodities led to rising inflation in many countries. Political unrest in North Africa also contributed to a rise in oil prices. Strong growth in Germany helped to sustain activity in the euro area as a whole, but there was uncertainty related to public finances in Ireland and several southern European countries.

Higher oil prices and favourable prospects for the Norwegian economy contributed to a stronger krone exchange rate at the beginning of the year, although some of the appreciation was expected to be reversed when the situation in the oil market normalised. The strong krone and the low rise in prices for imported consumer goods had a dampening effect on inflation in the first quarter, and there were prospects that inflation would remain low in the following quarters. At the same time, enterprises in Norges Bank's regional network reported that growth had gained a foothold.

In the March *Monetary Policy Report* (1/11), emphasis was placed on the one hand on low inflation and the strong krone, which suggested that the key policy rate should be kept low. On the other hand, accelerating growth at home and abroad, with interest rate expectations rising somewhat abroad, suggested that the key policy rate should be raised more rapidly than projected in October 2010. The interest rate forecast was revised up, and the key policy rate was projected to be increased by 0.75 percentage point through the year (see Chart 2.1).

## The mandate for monetary policy in Norway

Monetary policy in Norway is conducted by Norges Bank. The Bank's activities are regulated by the Norges Bank Act of 1985. Pursuant to Sections 19 and 20 of the Act, Norges Bank sets the interest rates on banks' deposits and loans in the central bank.

The mandate for monetary policy was laid down by the government in 2001. Section 1 of the Regulation on Monetary Policy states:

*"Monetary policy shall be aimed at stability in the Norwegian krone's national and international value, contributing to stable expectations concerning exchange rate developments. At the same time, monetary policy shall underpin fiscal policy by contributing to stable developments in output and employment.*

*Norges Bank is responsible for the implementation of monetary policy.*

*Norges Bank's implementation of monetary policy shall, in accordance with the first paragraph, be oriented towards low and stable inflation. The operational target of monetary policy shall be annual consumer price inflation of approximately 2.5 per cent over time.*

*In general, the direct effects on consumer prices resulting from changes in interest rates, taxes, excise duties and extraordinary temporary disturbances shall not be taken into account."*

*The monetary policy instrument is the key policy rate, which is the interest rates on banks' normal overnight deposits in Norges Bank. The key policy rate has an impact on the shortest money market rates, and the level of longer-term market rates depends on expectations regarding the future path of the key policy rate.*

*Market rates have an impact on the krone exchange rate, securities prices, house prices, credit demand and investment. Norges Bank's key policy rate can also influence expectations with regard to future inflation and economic developments. The interest rate operates through all these channels to influence overall demand and output as well as prices and wages.*

*Decisions concerning interest rates and other important changes are normally taken at the Executive Board's announced monetary policy meetings. Three times a year, publication of the Monetary Policy Report coincides with the key rate decision. In the Report, Norges Bank analyses the current economic situation and provides forecasts for economic developments and for the key rate. On the basis of the analysis in the report, the Executive Board adopts the monetary policy strategy in the form of an interval for the key rate for the period up to the next Monetary Policy Report.*

## Flexible inflation targeting

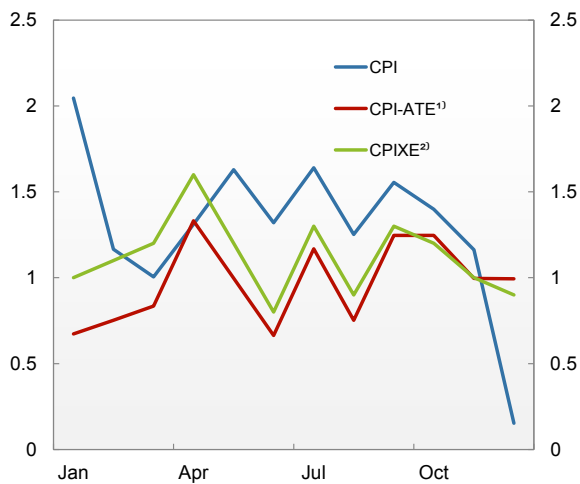
Norges Bank operates a flexible inflation targeting regime, so that interest rate setting gives weight to smoothing fluctuations both in inflation and in output and employment. Flexible inflation targeting builds a bridge between the long-term objective of monetary policy, which is to keep inflation low and anchor inflation expectations, and the objective of smoothing developments in output.

Expectations regarding future interest rates play an important role for developments in output, employment, income and inflation. Through its interest rate forecasts, Norges Bank influences the interest rate expectations of market participants, enterprises and households.

The interest rate forecast is an expression of Norges Bank's overall judgement and assessment. The interest rate cannot always satisfy all the criteria simultaneously and imbalances must be weighed against each other in interest rate setting.

Forecasts of the key policy rate and other economic variables are based on incomplete information concerning the economic situation and the functioning of the economy. Should developments in the economy differ from assumptions or should the central bank change its view of the functioning of the economy, developments in the interest rate and other variables may deviate from the forecasts. The Monetary Policy Report contains an account of any changes in the interest rate forecast and the factors underlying the change. The evaluations in the reports issued through the year are summarised in the Annual Report.

Chart 2.1 Consumer prices. 12-month change. Percent. 2011

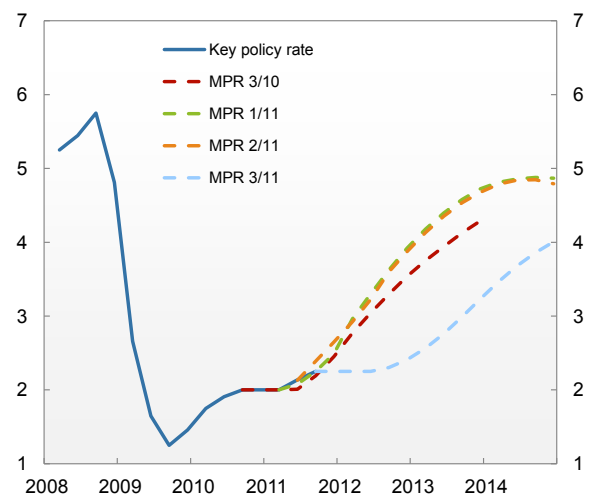


<sup>1)</sup> CPI adjusted for tax changes and excluding energy products.

<sup>2)</sup> CPI adjusted for tax changes and excluding temporary changes in energy prices.

Sources: Statistics Norway and Norges Bank

Chart 2.2 Key policy rate in baseline scenario MPR 3/10, MPR 1/11, MPR 2/11 and MPR 3/11. Percentage points. 2008 Q1 – 2014 Q4.



Source: Norges Bank

## Two-speed developments

The global economy continued to grow through spring, but developments diverged across countries and regions. Growth remained robust in emerging Asian economies and activity in the US economy also appeared to be picking up. There was a strong recovery in some northern European countries and both the European Central Bank and Sveriges Riksbank raised key rates in April. In Ireland, Portugal and Greece, developments were more uncertain and government bond yields continued to rise. In April, Portugal had to request financial assistance from the European Union and the International Monetary Fund (IMF).

At the time of the monetary policy meeting in May, capacity utilisation was close to a normal level and the labour market had tightened. At the same time, the krone exchange rate was strong and inflation low, although there were prospects that both capacity utilisation in the economy and inflation would rise. The objective of stabilising activity and inflation further ahead suggested an increase in the interest rate. The key policy rate was raised to 2.25% in line with the baseline scenario in the *March Report (1/11)*.

The global economy appeared to be growing at a solid pace in the period to summer, with high growth in Asia and South America. A division arose between European economies, with prospects for weak growth or decline in Ireland and southern Europe. In the US and the UK, fiscal tightening dampened growth prospects.

At the time of the June monetary policy meeting, capacity utilisation in Norway had risen to a more normal level, wage growth was picking up and unemployment was lower than expected. Underlying inflation was estimated to be between 1.25% and 1.5% in May. It was assumed that rising wage growth and declining competition in retail trade, combined with higher international commodity prices, would gradually feed through to inflation in Norway.

At the same time, global growth prospects were assessed as more uncertain. The difference between the Norwegian and the global economy entailed a risk that the krone could appreciate, leading to even lower inflation. There was therefore reason to take a gradualist approach in interest rate setting. The possibility that a low interest rate could generate imbalances in the real economy somewhat further ahead was also taken into consideration. The interest rate was kept unchanged at the June monetary policy meeting and the interest rate forecast in the *June Report (2/11)* was generally in line with the gradual increase projected in March (see Chart 2.2). The forecast implied that a further increase in the interest rate after summer was highly probable.

## Increased turbulence and weakened growth prospects

The prospects for growth in the global economy weakened considerably through summer. Two-speed developments continued, but late autumn brought signs that growth was also slowing in emerging economies. Various measures were implemented to dampen rising turbulence in financial markets. The euro area countries agreed on a new loan agreement for Greece, on the same terms as for Ireland and Portugal. The European Central Bank (ECB) reintroduced loans with 6-month maturities and gradually extended the loan maturities to 12 months. The ECB also resumed buying government bonds, making substantial purchases through autumn. In spite of the various measures, financial markets were characterised by rising turbulence, with large movements in equity, bond and foreign exchange markets. Yields on government bonds issued by debt-laden European countries rose, gradually spreading to major economies like Spain and Italy. The probability that the debt crisis in the euro area would worsen and lead to substantial and lasting effects on economic developments was assessed as higher than before summer.

Counterparty risk among European banks increased, money market premiums rose and bank funding became more costly. Expectations regarding key rates abroad fell markedly. At the August monetary policy meeting, the key policy rate was kept unchanged and was thus slightly below the path in the baseline scenario in the *June Report (2/11)*.

In September, the Federal Reserve signalled that it would keep the key rate near zero until mid-2013. The Swiss National Bank set a minimum exchange rate between the euro and the Swiss franc (CHF) in September, leading to wide fluctuations in the krone exchange rate, although the krone moved on the whole approximately as projected in the *June Report (2/11)*.

Developments in the Norwegian economy appeared to be somewhat weaker than expected in September. There was at the same time high activity in the housing market and house prices continued to rise. Inflation was low and underlying inflation, as measured by the CPIXE, was 1.2% in the third quarter. At the August and September monetary policy meetings, emphasis was given to the effect of the turbulence abroad on the outlook for the Norwegian economy. In view of low inflation, weaker prospects for output and employment, higher money market premiums and very low interest rates abroad, the key policy rate was kept unchanged at both meetings. The Executive Board stated that the level of uncertainty with regard to interest rate developments ahead was unusually high.

### Debt crisis affected the Norwegian economy

The premise of the monetary policy analysis in June changed fundamentally in the period to the October monetary policy meeting when a new analysis was presented. Growth among some trading partners was clearly lower than projected in June, and growth prospects had weakened considerably. The sovereign debt crisis persisted and financial markets were affected by the increased risk of a renewed downturn in the global economy. Government bond yields in countries with weak public finances rose further, particularly for Greece. Financial market turbulence led to higher risk premiums in money markets, both in Norway and abroad. There was a marked shift in announced monetary policy among Norway's trading partners, from normalisation to further easing. The European Central Bank lowered its key rate through the second half of 2011 and increased its euro lending to banks.

The rise in consumer prices was weaker than had been projected in June, pulled down by the low rise in prices for domestically produced goods and services (see Chart 2.1). The rise in prices for imported consumer goods was, however, higher than projected as a result of the increase in international commodity prices. Growth in the Norwegian economy remained robust, but the enterprises in Norges Bank's regional network expected somewhat lower growth ahead. The increased risk of a renewed downturn in the global economy, lower external interest rates, higher risk premiums in the Norwegian money market and lower domestic inflation suggested that interest rate increases should be deferred. The forecast for the key policy rate was revised down in the October *Report* (3/11). It was also stated that an interest rate reduction was an alternative if economic unrest abroad intensified further.

Through the last months of the year, economic unrest abroad heightened further, and the risk of a renewed downturn increased, particularly in Europe. Government bond yields in some European countries continued to rise. Overall, yields on Italian, Spanish, Portuguese and Irish government bonds were higher in December than at the time of the October *Report* (3/11), and the unrest spread to government bond yields in other European countries.

As a result of the debt crisis in the euro area, market funding became more difficult to obtain and more costly for European banks.

Market funding also became more costly and less accessible for Norwegian banks. Norwegian banks raised their corporate lending rates, while residential mortgage lending rates showed little change. Money market rates were higher in December than assumed in October. Money market premiums were expected to remain high ahead.

Capacity utilisation in the Norwegian economy remained close to a normal level, but growth prospects weakened. The enterprises in Norges Bank's regional network expected lower output growth into 2012 than projected in October. The enterprises also reported a moderate rise in prices and expectations of a lower rise ahead. In December, underlying inflation was estimated to be between 1% and 1.5%. On the other hand, building activity was still high and growth in petroleum investment and oil-related industries was strong. Higher premiums, low inflation and weakened growth prospects suggested that the interest rate should be lowered in December. Developments ahead were uncertain and an interest rate reduction was considered necessary to mitigate the effects of a particularly adverse outcome on the economy. The Executive Board decided to reduce the key policy rate by 0.5 percentage point in order to guard against an economic setback and even lower inflation.

**Table 1** Interest rate decisions in 2011

Monetary policy meeting	Change in percentage points	Key policy rate after meeting
January	0	2.0
March	0	2.0
May	0.25	2.25
June	0	2.25
August	0	2.25
September	0	2.25
October	0	2.25
December	-0.5	1.75

## Changes in the interest rate forecast through 2011

The interest rate path published in the October 2010 Monetary Policy Report (3/10) implied that the key policy rate would be kept unchanged through the first half of the year and then be raised to around 2.5% towards the end of the year. The forecast was revised up in spring and the key policy rate was raised to 2.25% in May. The economic unrest abroad intensified through summer and autumn and started to affect the prospects for the Norwegian economy. At the October monetary policy meeting, the interest rate increase was deferred further ahead. Chart 2.3 shows the changes in the forecast for the key policy rate from 27 October 2010 to 19 October 2011. The bars in the chart provide a technical illustration of how the various factors affect the changes in the forecast over the year as a whole.

Compared with prospects at the beginning of the year, the key policy rate was raised slightly more rapidly through the first half of the year, while the interest rate level in the second half of the year was lower than expected. The forecast for the years ahead was revised down by about 1 percentage point. The downward revision was related to various effects of weaker prospects abroad.

Key rate expectations abroad appeared to pick up at the beginning of 2011, but fell through the year as countries applied expansionary monetary policy to mitigate the impact of the sovereign debt crisis and increased financial market turbulence. In isolation, a higher interest rate differential would have led to a stronger krone and lower inflation. Prospects for lower central bank key rates abroad therefore indicated that the interest rate would also be lower in Norway (green bars). Higher prices for oil and a favourable outlook for the Norwegian economy contributed to a stronger krone exchange rate in 2011 in addition to the effect of the change in the interest rate differential. The strong krone also pushed down the forecast for the key policy rate (red bars).

In addition, financial market turbulence drove up money market risk premiums and led to higher-than-projected money market rates. The increase in premiums pulled down on the forecast for the key policy rate (light blue bars), particularly the forecasts towards the end of the year. The direct effect on demand of weaker growth prospects abroad also had an impact on the outlook for the Norwegian economy. This also pushed down the forecast for the key policy rate (orange bars).

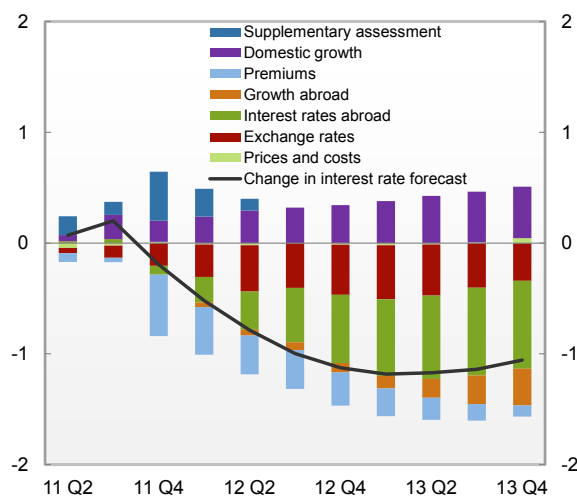
Overall, developments pointed towards a lower key policy rate in the short term. It was judged that there was little purpose in reducing the key policy rate by such a small margin for such a short time. In view of the objective of avoiding abrupt and unex-

pected changes in the key policy rate in the course of the year, the interest rate path was kept unchanged in the short term in March and October even though the model-based forecasts in isolation suggested a slight, temporary reduction in the key policy rate. This supplementary assessment is shown by the dark blue bars.

Growth in the Norwegian economy was having the opposite effect. Overall, capacity utilisation pushed up the interest rate forecast (purple bars). Prices for imported consumer goods rose more than projected through the year, while domestic inflation rose less than expected. Viewing the year as a whole, prices developed approximately as projected and did not contribute to substantial changes in the interest rate path.

Towards the end of the year, growth prospects for the Norwegian economy were revised down compared with the forecast for October. The key policy rate was reduced and Norges Bank stated in December that a lower key policy rate was more closely in line with the low interest rate alternative, as illustrated in the October Report (3/11).

Chart 2.3 Change in the forecast for the key policy rate from Monetary Policy Report 3/10 to Monetary Policy Report 3/11. Percentage points. 2011 Q2 – 2013 Q4.



Source: Norges Bank

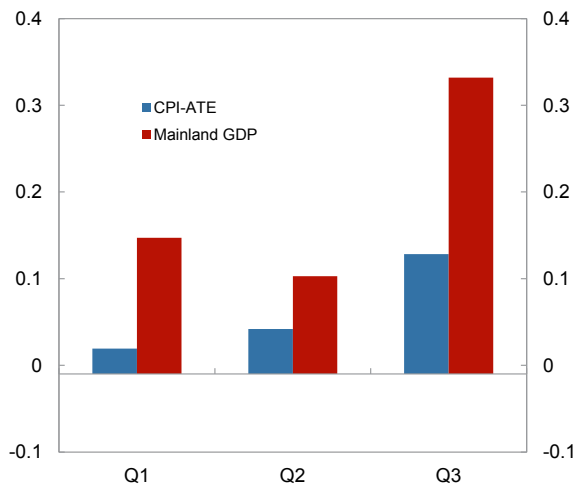
## Accuracy of macroeconomic projections in the short term

In its Monetary Policy Report, Norges Bank publishes projections for the CPI-ATE and mainland GDP. Since 2009, the short-term projections for CPI-ATE inflation and mainland GDP have on average been somewhat higher than actual developments (see Chart 2.4).

The final short-term projections are based on Norges Bank's system for averaging short-term models (SAM) and other information about and assessments of economic developments. To assess whether the additional information has been utilised effectively,

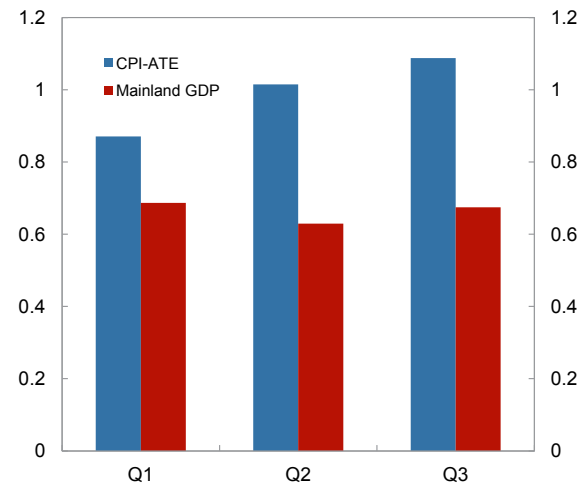
the final projections are compared with the technical projections provided by SAM (see Chart 2.5). Since 2009 the final projections for mainland GDP growth have been more accurate than the SAM projections. The difference is mainly because banks' forecasts were able to capture prospects for weaker growth during the financial crisis fairly quickly. The final projections for the CPI-ATE and the projections provided by SAM have shown a fairly similar level of accuracy.

**Chart 2.4** Average projection error. Four-quarter change. Percentage points. MPR 1/09 – MPR 3/11



Source: Norges Bank

**Chart 2.5** Average absolute projection error in Norges Bank's projections compared with projection error in SAM<sup>1)</sup> MPR 1/09 – MPR 3/11



<sup>1)</sup> Value below 1 indicates that Norges Bank's final projections were more accurate than the projections from SAM.

Source: Norges Bank

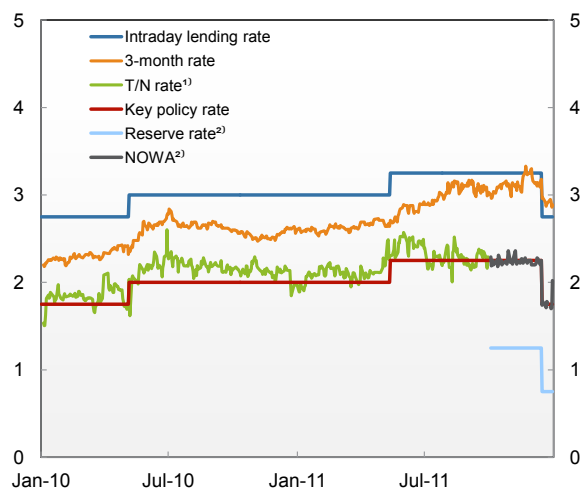


## A new liquidity management system put into operation

A new liquidity management system was put into operation on 3 October 2011. The aim was to curb demand for central bank reserves and to promote lending in the interbank money market. Under the new system, banks receive interest at the key rate only on a defined volume of bank deposits in Norges Bank – a quota. Deposits in excess of this quota bear interest at the reserve rate, which is 1 percentage point lower than the key rate. The new system has resulted in a better distribution of interbank liquidity and a substantial reduction in outstanding central bank reserves.

In its conduct of monetary policy, Norges Bank steers the level of bank reserves, i.e. bank deposits at the central bank, to ensure that the level of short-term money market rates is close to the key rate as set by the Executive Board. To achieve this, reserves are supplied to or drained from the banking system by the central bank through different forms of market operations. Chart 2.6 shows developments in Norges Bank's interest rates, the overnight rate (see fact box on NOWA), and three-month money market rates.

**Chart 2.6** Norges Bank's interest rates and short money market rates (money market rate 1 day ahead and 3 months ahead). Nominal rates. Percent. 1 January 2010 – 31 December 2011



<sup>1)</sup> Estimated by Norges Bank  
<sup>2)</sup> From 3 October 2011

Sources: Thomson Reuters and Norges Bank

The aim of Norges Bank's liquidity management is to ensure that total reserves in the banking system remain stable around a certain level. In order to steer reserves towards the desired level, Norges Bank prepares forecasts of structural liquidity in the banking system. Structural liquidity refers to the total reserves banks hold on account at Norges Bank before the supply or withdrawal of reserves through liquidity policy instruments. Structural liquidity is influenced by current ingoing and outgoing payments over the government's account in Norges Bank, government borrowing transactions, Norges Bank's transactions in the foreign exchange and government securities markets and changes in the volume of notes and coins in circulation. When structural liquidity is lower than the desired level for banks' reserves, Norges Bank provides loans to banks. When structural liquidity is high, Norges Bank offers to accept banks' surplus liquidity as fixed-rate deposits.

In line with the Executive Board's decision of December 2010, Norges Bank introduced a new system for the management of bank reserves in 2011.

Previously, all bank deposits at Norges Bank received interest at the key rate. The key rate formed a floor for very short-term money market rates, as banks will not normally set a lending rate that is lower than the rate they receive from the central bank. The redistribution of liquidity in the interbank market did not function efficiently as the cost to a bank of holding onto the reserves was relatively low. The result was undesirable growth in demand for central bank reserves.

As from 3 October 2011, banks receive interest at the key rate only on a defined volume of bank deposits in Norges Bank. Deposits in excess of this quota bear interest at a lower rate - the reserve rate. In the new system, a bank will not normally wish to hold deposits in the central bank in excess of the quota. If a bank has reserves in excess of its quota, the bank will seek to deposit these reserves with another bank overnight at a better rate than Norges Bank's reserve rate. A bank in need of reserves will thereby be able to obtain these reserves more easily in the interbank market without having to bid up the price to an excessive level. Thus the new system contributes to a more effective redistribution of reserves among banks. In addition, the quota restricts the volume of reserves bearing interest at the key rate, thereby curbing the demand for reserves. This has counteracted an upward trend in bank demand for central bank reserves.

In implementing the new system, Norges Bank seeks to maintain bank reserves in the banking system at an average NOK 35bn with a target range of  $\pm 5$ bn around this level. Banks' quotas total NOK 45bn. Thus, surplus liquidity

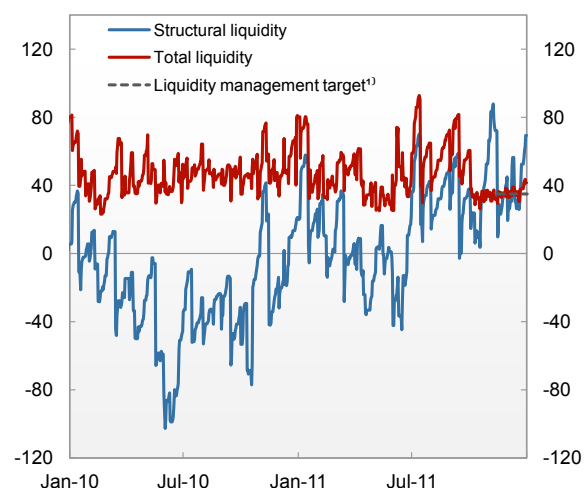
in the banking system is still substantial while the target range allows for fluctuations in the level of bank reserves. When bank reserves rise towards the top end of the target range, Norges Bank offers banks F-deposits. Similarly, when reserves fall towards the lower end of the target range, banks are offered F-loans. F-loans and F-deposits are fixed-rate loans and deposits with specified maturities extended to banks established in Norway. The interest rate is usually determined by multi-price auction.<sup>1</sup> Maturities vary from one day to several weeks and depend on the liquidity situation. F-loans are only provided against collateral in the form of approved securities.

The total quota for bank reserves is set at NOK 45bn. Each quota is calculated based on a bank's total assets. The banks have been divided into three groups with all the banks in a group assigned the same quota, with the exception of settlement banks, which are assigned an additional amount in their quota. The quotas will be reviewed twice a year.

### Banks' krone liquidity and Norges Bank's market operations in 2011

In 2011, structural liquidity averaged NOK 20bn (see Chart 2.7). Up to 3 October, Norges Bank supplied krone liquidity through ordinary F-loans so that total liquidity in the banking system averaged NOK 50bn. After the new liquidity system came into operation, F-deposits must also be used to drain liquidity in order to keep total reserves at the desired level. In the period following the introduction of the new system, liquidity in the banking system averaged NOK 35bn, exactly in line with Norges Bank's target for bank reserves in the new liquidity management system. A total of 20 F-loan auctions and 30 F-deposit auctions were held (as from 3 October) in 2011.

**Chart 2.7** Structural liquidity and surplus liquidity in the market. In billions of NOK. 1 January 2010 – 31 December 2011



<sup>1</sup> From 3 October 2011

Source: Norges Bank

### Swap arrangement

A swap arrangement was established in 2008 to ensure banks' access to longer-term funding, under which banks could obtain Treasury bills from the government in exchange for covered bonds (OMF). The arrangement had a total utilisation of NOK 230bn. No auctions have been held under the swap arrangement since 2009.

Under the swap arrangement, swap agreements were initially valid for up to three years. In March 2009, the term of the agreements was extended to up to five years. Under the agreements, loans cannot be redeemed before the final maturity date. In a submission to the Ministry of Finance dated 29 September 2010, Norges Bank recommended an offer of early termination of agreements for the banks taking part in the swap arrangement. The Ministry of Finance decided to follow this advice and offer early termination of swap agreements, and Norges Bank published a calendar for early termination of swap agreements in 2011. NOK 38bn was utilised for this purpose in 2011. The balance of remaining funds in the swap arrangement at end-2011 was about NOK 153bn.

<sup>1</sup> In a multi-price auction, also referred to as an American auction or an ordinary auction, banks submit bids for a desired amount and interest rate. Norges Bank decides the aggregate amount of the allotment. The banks' interest rate bids are ranked in descending order and the allotment is distributed until the aggregate amount is reached. The banks awarded an amount in the distribution pay the interest rate they bid.

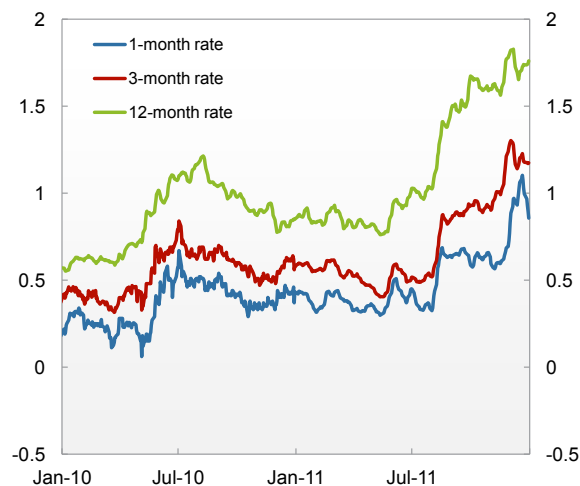
## Money market premiums

Money market premiums<sup>2</sup> fell in the first half of 2011 after being driven up during the first period of turbulence around the debt crisis in the euro area in summer 2010. When renewed turbulence arose in summer 2011 and intensified further through autumn, premiums in the Norwegian money market rose. At the end of 2011, the premium on three-month money market rates was above 1 percentage point. This was higher than in other countries. Chart 2.8 shows developments in premiums on 1-, 3- and 12-month money market rates.

The rise in money market premiums coincided with a deterioration in the funding situation for European banks. Activity in the bank bond market was considerably lower in the second half of 2011. This also influences the costs facing Norwegian banks seeking market funding.

Finance Norway (FNO, the trade organisation for banks, insurance companies and other financial institutions in Norway) has in collaboration with banks drawn up rules for the calculation and publication of the NIBOR rate<sup>3</sup>, partly after an initiative taken by Norges Bank. The purpose of the rules is to ensure a more transparent structure for the calculation of NIBOR, which is an important benchmark rate in the money market and for bank lending rates. The rules include a definition of the benchmark rate and how it should be understood in relation to other countries' benchmark rates. Criteria for banks' admission to the NIBOR panel are also included.

**Chart 2.8** Spread between money market rates and expected key policy rate. Percentage points. 5-day moving average. 1 January 2010 – 31 December 2011



Sources: Thomson Reuters and Norges Bank

<sup>2</sup> Money market rates minus expected key rate over the same horizon

<sup>3</sup> NIBOR is an abbreviation for *Norwegian InterBank Offered Rate*.

## NOWA – Norwegian Overnight Weighted Average

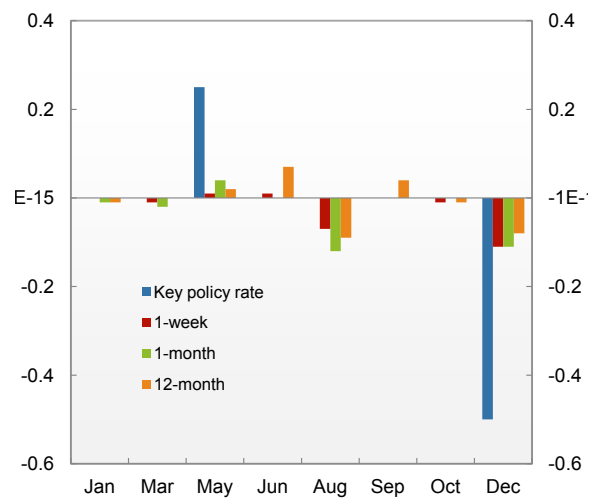
At the same time as the new liquidity system was put into operation, Norges Bank began quoting the NOWA rate. NOWA is a weighted average of interest rates charged on completed unsecured overnight loan transactions between Norwegian banks. Previously, interest rates on actual transactions in the Norwegian market were not recorded. The rules for calculating NOWA were laid down by Finance Norway (FNO), while Norges Bank is responsible for calculating and quoting NOWA on behalf of FNO. In the period since 3 October, NOWA has on average been one basis point lower than the current key policy rate. The volume of transactions has averaged just below NOK 8bn per day.

## Minor fluctuations in the money market

Norges Bank's communication of monetary policy primarily aims to stabilise inflation expectations by providing an account of and explaining interest rate setting. The aim of publishing the Bank's interest rate forecasts and monetary policy strategy is to make it easier for others to anticipate and evaluate monetary policy. When market participants understand the central bank's response pattern, market rates can react with a stabilising effect to new information on economic developments.

Changes in money market rates after monetary policy meetings are an indicator of whether the decision is anticipated by money market participants. Large changes may indicate that the decision was unexpected. In the five-year period from 2007 to 2011, the average change in the 1-week rate after a monetary policy meeting was 5 basis points (0.04 percentage point). The 1-month and 12-month rate changed on average by 6 and 5 basis points respectively. In 2011, the average change in the 1-week rate was 3 basis points. The average change in the 1-month and 12-month rate was 4 basis points. Changes lower than the historical average may indicate that the interest rate decision was largely expected by market participants. The key policy rate was raised by 0.25 percentage point in May. The increase in May was expected by the market and thus resulted in only minor changes in money market rates. The largest changes in money market rates came after the monetary policy meetings in August and December. The announcement of an unchanged key policy rate in August contributed to a fall in the 1-week rate of 7 basis points, while the 1-month and 12-month rate fell by 12 and 9 basis points respectively (see Chart 2.9). When the key policy rate was reduced by 0.5 percentage point in December, the 1-week and 1-month rate fell by 11 basis points, while the 12-month rate fell by 8 basis points. This indicates that the interest rate decrease was largely expected by market participants. There were otherwise only minor changes in short-term money market rates. This may indicate that market participants have interpreted developments in both the Norwegian and the global economy in the same way as Norges Bank.

Chart 2.9 Change in key policy rate and effect on money market rates following monetary policy meetings in 2011. Percentage points

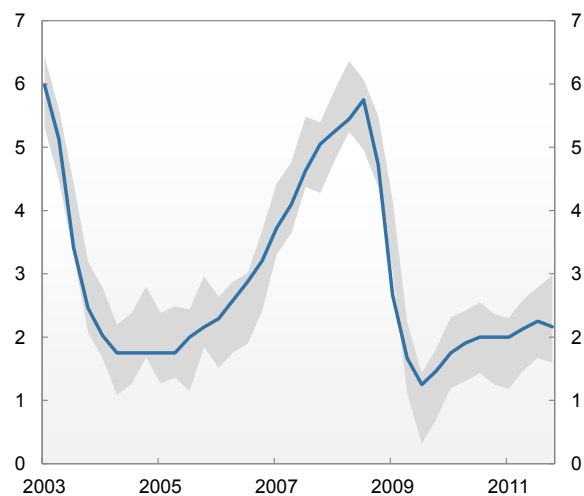


Source: Norges Bank

## Historical response pattern

Market participants will attempt to form an idea of how the central bank responds to new information and how the key policy rate is set as a result of developments in economic variables. Norges Bank has estimated an interest rate rule that seeks to explain historical interest rate changes on the basis of changes in a few macroeconomic variables. The rule includes inflation developments, wage growth, mainland GDP and central bank key rates abroad. The interest rate in the previous period is also taken into account. Such an estimated reaction function does not of course capture all the elements that are given weight and can only provide an indication. From autumn 2008 to summer 2009, Norges Bank reduced the key policy rate more rapidly than indicated by the historical response pattern (see Chart 2.10). Since summer 2009, Norges Bank has raised the key policy rate four times, in line with the historical response pattern. In December 2011, Norges Bank lowered the key policy rate, partly as a result of increased risk premiums in the money market. Premiums are not included in the historical response pattern and the interest rate is therefore in the lower part of the average pattern of interest rate setting at end-2011 (shown in the chart by the shaded area).

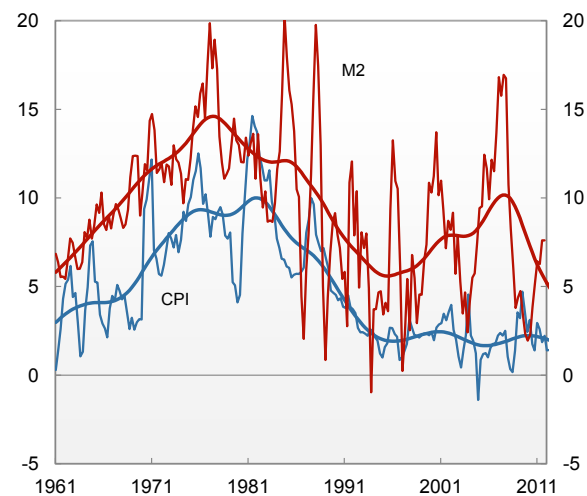
**Chart 2.10** Key policy rate and interest rate developments following from Norges Bank's average pattern of interest rate setting<sup>1)</sup>. Percent. 2003 Q1 – 2011 Q4



<sup>1)</sup> Interest rate developments are explained by inflation developments, growth in mainland GDP, wage growth and key rates among trading partners. See *Staff Memo 3/08* for further discussion

Source: Norges Bank

**Chart 2.11** Consumer prices (CPI) and money supply (M2) Estimated trend rise<sup>1)</sup>. Four-quarter change. Percent 1961 Q1 – 2011 Q4



<sup>1)</sup> Trend estimated using an HP-filter. See *Staff Memo 2005/2* for further discussion

Sources: Statistics Norway and Norges Bank

## Monetary growth and inflation

Historically, there has been a relationship between inflation and growth in the money supply (M2)<sup>4</sup> (see Chart 2.11). There is a tendency for stronger monetary growth to accompany higher inflation and vice versa. Trend monetary growth may serve as a rough cross-check of inflation projections generated by other models.

The ten years up to 2008 saw an increase in trend monetary growth despite large annual fluctuations. Strong growth in the Norwegian economy and high credit growth drove monetary growth up to a particularly high level in the period from 2006 to 2008. At the same time, consumer price inflation was low as a result of favourable supply-side conditions in the Norwegian and international economy. Inflation picked up and exceeded the inflation target in 2008. Since then,

monetary growth has fallen quickly, but picked up again in 2011. The downward trend continued towards the end of 2011. Trend inflation has been relatively stable.

<sup>4</sup> The money supply (M2) consists of banknotes and coins, redeemable bank deposits, certificates of deposit and units in money market funds owned by the money-holding sector (households, non-financial enterprises, municipal administration and financial enterprises other than state lending institutions, banks and money market funds).

## Inflation is low and stable

*Inflation stabilised in the early 1990s after falling from a high level in the previous decade. Viewed over time, inflation has been low and stable and remained somewhat below, but fairly close to, 2.5%.*

In accordance with Norges Bank's mandate for monetary policy, the operational target of monetary policy is an annual rise in the consumer price index (CPI) of close to 2.5% over time. CPI inflation over a short period does not provide an adequate basis for assessing whether monetary policy objectives have been achieved over time. Chart 2.12 shows the 10-year moving average for annual CPI inflation.

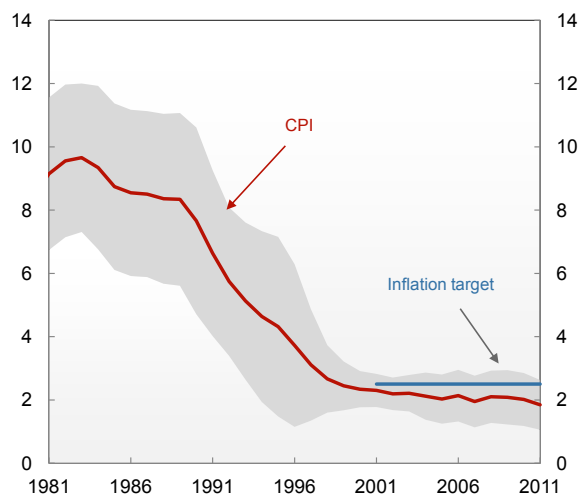
Over the past ten years, average annual CPI inflation has been 1.8%. The deviation from the inflation target of 2.5% is the result of a number of favourable supply-side shocks to the economy earlier in the decade, including strong growth in productivity, an ample supply of labour from other

countries and lower price rises for imported goods. This is reflected in strong growth in the Norwegian economy coupled with a period of lower-than-expected inflation.

Under a flexible inflation targeting regime, monetary policy also gives weight to stabilising developments in output and employment. Chart 2.13 shows the movements in the output gap since 1980. The output gap shows the difference between the actual level and the estimated normal level of mainland GDP. Thus measured, fluctuations in the economy have, on average, been somewhat less pronounced over the past ten years than around 1990. The impact on output in autumn 2008 and spring 2009 was nevertheless more pronounced than it had been for several years.

The band around average inflation in Chart 2.12 shows inflation variability. Over a longer time horizon, inflation variability has decreased. Variability in the output gap, shown in Chart 2.13, appears to have been diminishing since the end of the 1990s.

**Chart 2.12** Inflation. 10-year moving average<sup>1)</sup> and variation<sup>2)</sup> in CPI. Percent. 1981 – 2011

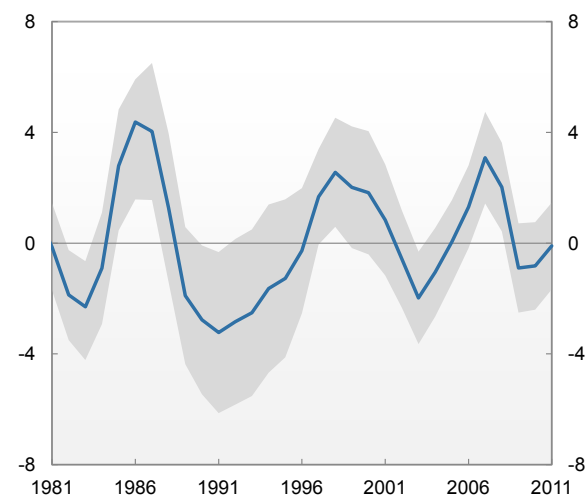


<sup>1)</sup> The moving average is calculated 10 years back

<sup>2)</sup> The band around the CPI is the variation in the CPI adjusted for tax changes and excluding energy products in the average period, measured by  $\pm$  one standard deviation

Sources: Statistics Norway and Norges Bank

**Chart 2.13** Output gap estimates<sup>1)</sup>. Level and variation<sup>2)</sup>. Percent. 1981 – 2011



<sup>1)</sup> The output gap measures the difference between actual and estimated potential GDP for mainland Norway

<sup>2)</sup> The band shows the variation in the output gap measured by  $\pm$  one standard deviation. The standard deviation is calculated over a 10-year period

Source: Norges Bank

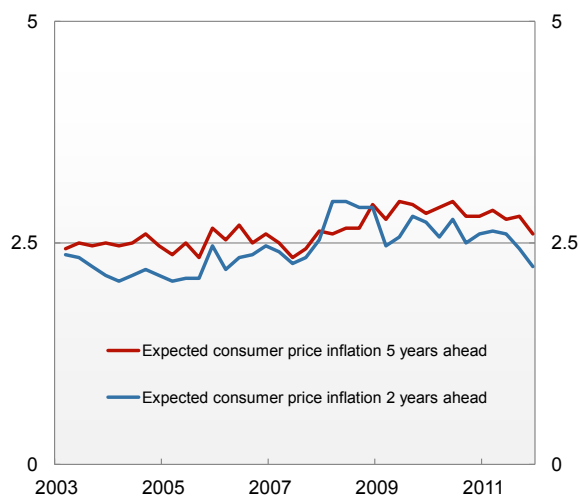
## Confidence in the inflation target

Confidence in achieving the inflation target is a precondition for the stabilising effect of monetary policy on developments in output and employment. Inflation will not be at target at all times, but if there is confidence in monetary policy, expected inflation will be close to the inflation target over time, which in itself contributes to stabilising inflation.

Perduco has been commissioned by Norges Bank to carry out quarterly surveys of inflation expectations. According to these surveys, inflation expectations in 2011 Q4 were fairly close to 2.5% (see Chart 2.14). Expected consumer price inflation two years ahead is below the target of 2.5% and above the target five years ahead. Consensus Forecasts Inc. compares different institutions' forecasts of consumer price inflation in Norway. Both five years and ten years ahead, consumer price inflation is expected to be approximately 2.5%.

An indicator of price expectations among financial market participants is provided by the yield curve in fixed income markets. Long-term forward rates may under certain conditions provide an indication of expected inflation. Chart 2.15 shows the long-term forward rate differential between Norway and the euro area. Owing to a higher inflation target in Norway, this differential will normally be in the area of 0.5-1 percentage point, depending on risk premiums in the fixed income market. This differential was generally close to 1 percentage point in 2011. The differential was slightly lower in the first half of the year, but edged up in the second half, partly as a result of expectations of very low interest rates abroad. A wider spread can be an indication that price expectations in Norway are higher than implied by the inflation target. Overall, the indicators suggest that there is confidence that inflation over time will be close to 2.5%.

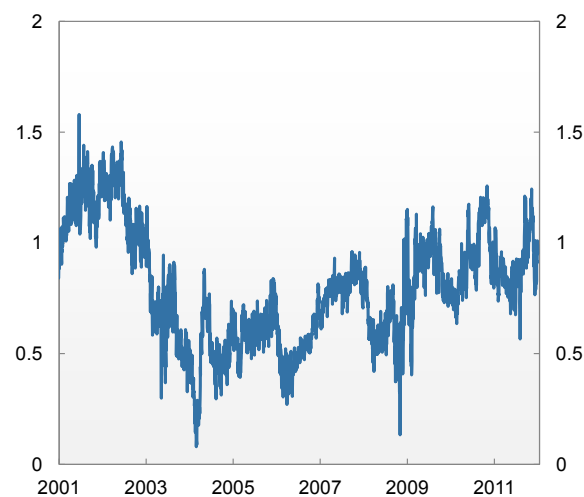
**Chart 2.14** Expected consumer price inflation 2 and 5 years ahead.<sup>1)</sup> Percent. 2003 Q1 – 2011 Q4



<sup>1)</sup> Average of expectations of employer/employee organisations and economists (financial sector and academia)

Source: Perduco AS

**Chart 2.15** Long-term forward rate differential between Norway and the euro area. Percentage points. 1 December 2001 – 31 December 2011



Sources: Thomson Reuters and Norges Bank

## CHAPTER 3:

# Financial stability

### Weaker prospects for financial stability

*The year 2011 was marked by heightened turbulence in international financial markets, especially in Europe. Owing to the turbulence in international financial markets and to weaker growth prospects abroad, Norges Bank assessed the financial system as being somewhat more vulnerable at end-2011 than at the beginning of the year.*

Global growth prospects weakened through the year as a result of the sovereign debt crisis in several euro area countries. The European banking sector faced growing difficulties during the year because banks were heavily exposed to bonds issued by the most severely affected euro area sovereigns and because of weaker macroeconomic developments. The turbulence spread, exacerbating the situation in money and credit markets.

Norwegian banks were well capitalised and posted solid earnings in 2011. Losses on loans were low and banks had limited exposures to government securities and other debt of the most vulnerable euro area countries. But Norwegian banks were also affected by the turbulence abroad, primarily because borrowing in money and credit markets became more expensive and less accessible. Nevertheless, Norwegian banks had better access to wholesale funding than euro area banks, because investors considered Norwegian banks to be more solid and at a lower risk of losses.

Norwegian enterprises are basically solid with good debt-servicing capacity. However, low growth among trading partners will affect Norwegian export firms and reduce their earnings. Banks losses on corporate loans may then increase.

Owing to turbulence in international financial markets and to weaker growth prospects abroad, Norges Bank assessed the financial system as somewhat more vulnerable at end-2011 than at the beginning of the year. Banks' reliance on foreign funding sources is deemed to be a challenge in the short term. At the same time, banks' losses on loans and securities may rise, if developments abroad substantially weaken Norwegian business sector profits. Challenges to the financial system in Norway may also arise further ahead. The household debt burden is high and house prices are rising rapidly. For that reason, many households may be vulnerable when the key policy rate is raised to a more normal level or if the outlook for the real economy deteriorates. These developments would also have an adverse impact on the wider economy and financial sector.

Norges Bank's stress tests of banks' capital adequacy revealed that the increase in capital adequacy ratios since 2009 made the Norwegian banking sector better equipped to withstand a severe global downturn, but that a further increase in capital adequacy ratios would be necessary to maintain lending in bad times.



## Norges Bank's tasks in the area of financial stability

Financial stability is one of Norges Bank's primary objectives and, along with the objective of price stability, shall contribute to economic stability. Norges Bank's tasks with regard to ensuring a stable and robust financial system are provided for in the Norges Bank Act. Section 1 states that the Bank shall issue banknotes and coins, promote an efficient payment system domestically as well as vis-à-vis other countries, and monitor developments in the money, credit and foreign exchange markets. Section 3 states that the Bank shall notify the ministry when, in the opinion of the Bank, there is a need for measures to be taken by others than the Bank in the field of monetary, credit or foreign exchange policy. Four other sections of the Norges Bank Act are also relevant: Section 13 grants Norges Bank the sole right to issue Norwegian banknotes and coins. Pursuant to Section 17, Norges Bank carries out banking services for the government. Section 19 empowers Norges Bank to lend to and make deposits in commercial and savings banks, while under Section 20 Norges Bank accepts deposits from banks. This entails a special re-

sponsibility for ensuring that the banking sector functions as intended. The Act relating to Payment Systems charges Norges Bank with the responsibility for authorising clearing and settlement systems for banks and for supervising these systems.

Norges Bank monitors the financial system as a whole, and twice a year sends a submission to the Ministry of Finance containing assessments of the outlook for financial stability and advice on measures that may counteract the build-up of systemic risk. The Bank provides an account of the analyses on which these assessments are based in its Financial Stability reports. These reports are published at the same time as the submissions to the ministry are sent.

Norges Bank manages the liquidity in the banking sector on a daily basis by lending to banks and accepting deposits. This gives Norges Bank a special responsibility for monitoring liquidity risk in the banking system. As lender of last resort, Norges Bank has a key role in dealing with crises in the financial system.

## How Norges Bank analyses financial stability

Experience, especially from the financial crisis in 2008, shows that financial crises have substantial adverse impacts on the real economy. For the first time in generations, global GDP declined in 2009.

When a financial institution takes substantial risk, the wider financial system may be affected. An individual institution may have insufficient incentive to limit risks when other participants in the economy are affected by the risk the institution assumes. Thus, risks that appear to be isolated to individual financial institutions can develop into risks to the entire financial system, known as systemic risks.

To uncover a possible build-up of systemic risk in the financial sector, Norges Bank analyses vulnerabilities within the system and sources of risk outside the financial system.

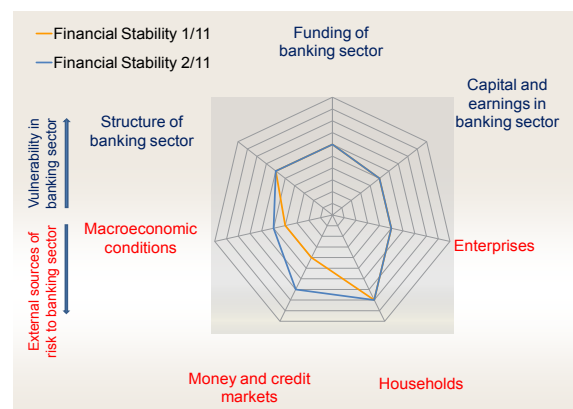
Assessments of the financial strength of banks are essential elements of analyses of vulnerabilities within the system. Norges Bank monitors developments in banks' Tier 1 capital ratios and performs stress testing. Analyses are also performed of the consequences of the structure of the banking sector for the resiliency of the financial system. All this provides a basis for recommendations for measures to improve bank solvency. Norges Bank also monitors bank funding and proposes measures aimed at enhancing the resilience of bank balance sheets to liquidity shocks. Monitoring requires data on banks' asset-liability management, banks' funding instruments, investment portfolios and the markets for these instruments and securities. The data are gathered from bank statistics, external data providers, contact with banks and other sources. In addition, Norges Bank conducts its own liquidity survey where the largest banks report their perceptions of the funding situation. Owing to the turbulent market situation, the surveys were expanded in both scope and frequency in 2011.

The work to assess the state of the Norwegian financial system also involves monitoring sources of risk outside the system. Norges Bank therefore analyses factors such as property price de-

velopments and the debt-servicing capacity of enterprises and households. In this connection, Norges Bank also conducts surveys of banks to obtain qualitative information on the demand for, supply of and terms for new loans. The general state of the macro-economy is also analysed. Another possible source of risk to banks is money and credit market conditions outside Norway. This may be crucial for how much banks can borrow in international markets and the cost of foreign funding.

Assessments of these sources of vulnerability may be summarised as in Chart 3.1.

**Chart 3.1** Vulnerabilities in the Norwegian banking sector and external sources of risk to the banking sector <sup>1)</sup>



<sup>1)</sup> A value of 0, i.e. origo, denotes the lowest level of risk or vulnerability. A value of 10 denotes the highest level of risk or vulnerability

Source: Norges Bank

As the chart shows, macroeconomic conditions, especially money and credit conditions abroad, deteriorated through 2011.

## Norges Bank's recommendations for measures

### Banks need robust funding and additional capital

In July 2011, the European Commission announced a draft directive for regulating bank capital adequacy and liquidity, Capital Requirements Directive (CRD) IV. Under the EEA Agreement, CRD IV will also apply to Norwegian banks once it has been passed by the Council and the European Parliament. The Commission's draft directive generally follows Basel Committee proposals from December 2010. In *Financial Stability 1/11* and *2/11*, Norges Bank stated its view that the regulatory changes were a step in the right direction and will make the financial system more robust. Norges Bank has recommended incorporating the new capital adequacy requirements into Norwegian law as quickly as is practicable. In the view of Norges Bank, a robust and integrated set of rules can serve as a stamp of quality for banks in turbulent times.

Unlike the Basel Committee, which is proposing minimum standards for how strictly countries can regulate their banks, the European Commission seeks to harmonise capital regulations in all EU/EEA member states. Thus, an EU member state will not be able to set stricter standards for its banks than the authorities in other EU states. Instead, several EU countries, including the UK, Spain and Sweden, have argued that the directive should set minimum requirements for individual states' capital regulations. In Norges Bank's view, Norwegian authorities should advocate greater national leeway in financial sector regulation.

In autumn 2011 the European Banking Authority (EBA) announced that all large European banks will have to achieve a minimum Core Tier 1 capital ratio of 9% from 1 July 2012. The requirement may result in higher minimum capital requirements in the market. In *Financial Stability 2/11*, Norges Bank therefore called on the largest Norwegian banks to raise their Core Tier 1 ratios. To facilitate stable credit standards, it would be preferable if this were mainly achieved through earnings retention. Finanstilsynet (Financial Supervisory Authority of Norway) has supported the EBA measures and announced that it would follow up the requirements in Norway.

Banks continue to have substantial short-term funding. Moreover, they will need new long-term funding to replace funding under the liquidity-provision schemes from 2008-2009, which will gradually be phased out. In *Financial Stability 2/11*, Norges Bank stated that until the two new quantitative liquidity requirements are introduced in 2015 and 2018,

Norwegian banks will have to increase their liquidity coverage and increase the long-term portion of their wholesale funding. Ready access to reliable and relevant information on banks' solvency and funding structure can dampen uncertainty in the financial system. The new liquidity standards proposed by the Basel Committee and European Commission will require banks to disclose more information about their funding structure. In *Financial Stability 1/11* and *2/11*, Norges Bank stated its view that Norwegian banks should already now be directed to disclose more detailed information on their funding structure.

Developments in the housing market and household debt may be a source of turbulence in the Norwegian economy in the longer term. On several occasions, Norges Bank has pointed to challenges related to low weights on residential mortgage loans for banks using the internal ratings-based (IRB) approach for risk-weighting balance sheet items. Norges Bank has also recommended lower limits for such risk weights. In this area, the Ministry of Finance announced in the National Budget for 2012 that it would consider raising capital requirements for residential mortgage loans within the framework of international regulations, including the risk models banks use.

In connection with the implementation of Basel II rules, a provisional requirement was included for banks' regulatory capital not to fall below 80% of Basel I capital requirements, even for IRB banks. The rule mandating this floor was originally to expire at the end of 2011, but is to be reintroduced from 2013 when CRD IV is to take effect. Norges Bank thus supported the recommendation of the Ministry of Finance for the 80% floor to apply in 2012 as well.

In November 2011, the Financial Stability Board (FSB), composed of G20 countries and international organisations, including the IMF, OECD, EU and BIS, proposed higher Core Tier 1 capital requirements for global systemically important banks: between 1 and 2.5 percentage points higher, depending on the bank's importance to the financial system. This requirement, which comes on top of the Basel III standards, is to be implemented gradually between 2016 and 2019 (see Box 3.3). Among the banks operating in Norway, it is expected that Nordea will be considered a global systemically important bank. The Swedish authorities have already proposed higher capital requirements for the four largest Swedish banks from 2013. The Norwegian authorities should consider similar requirements for the largest Norwegian banks.

## Macroprudential regulation

Like the Basel Committee's proposal, the European Commission's draft capital and liquidity directive (CRD IV) also contains a countercyclical capital requirement. A countercyclical buffer will be required in periods of especially high credit growth or other developments entailing higher systemic risk, in accordance with further regulations issued by the authorities. In a comment on the Financial Crisis Commission's report (NOU 2011:1), Norges Bank emphasised that the supervision and regulation of systemic risk, known as macroprudential regulation, should be given more weight ahead.

The Bank has been part of a working group with the Ministry of Finance and Finanstilsynet to explore possible ways of organising work to determine countercyclical buffers and other macroprudential measures in Norway. The working group presented a report in January 2012.

## Dealing with troubled banks

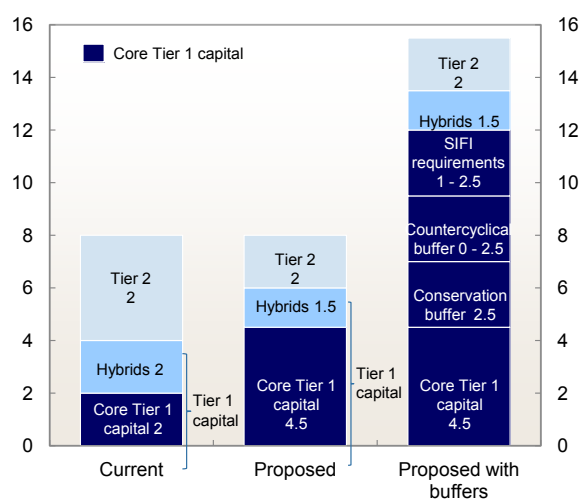
The international turbulence illustrates the importance of sound and credible plans for managing banking crises. Because of the absence of such plans during the financial crisis, a substantial share of banks' losses ended up on government balance sheets, contributing in some countries to the sovereign debt crisis. Passing on losses in this way may furthermore encourage increased financial sector risk-taking, making new crises more likely. The Norwegian crisis resolution system should also be improved. Norges Bank has argued for granting the authorities expanded powers to split up a bank to maintain essential public services performed by the bank without the use of public funds. For example, in its comments on the Financial Crisis Commission report (NOU 2011:1), Norges Bank stated that it should be possible to convert portions of a bank's debt to equity if a bank encounters severe problems. Norges Bank has also advanced that view together with Finanstilsynet in comments on the forthcoming EU directive on crisis resolution. In their comments, Norges Bank and Finanstilsynet supported attempts to harmonise bank resolution rules in EU member states. At the same time, Norges Bank and Finanstilsynet emphasised the benefits of national instruments and rules in addition to the common European framework.

An important part of a crisis resolution regime is that credible plans for both recapitalisation and the orderly resolution of a troubled bank are in place. EU countries such as the UK and Spain have already begun to draw up such plans. Nordea is to complete its plans in the course of 2012 in order to meet the requirements recently agreed on by the G20 countries. The current state of the European banking sector

## Capital requirements

All buffers are to be equity capital of the same quality as Core Tier 1 capital. If a bank does not meet the conservation buffer requirements, there will be restrictions on the amount of dividend that may be paid to owners. The countercyclical buffer will be set at greater than zero and up to 2.5% in periods of sharp growth in bank lending. In periods of a weaker economy, the buffer will be set at zero. SIFI requirements apply to systemically important financial institutions.

Chart 3.2 Current and proposed minimum capital requirements and new capital buffer requirements. As a percentage of risk-weighted assets



Source: Norges Bank

may delay the EU's work on a new crisis resolution system. In the view of Norges Bank, there is no reason to wait for possible EU rules before starting work on plans for the largest banks in Norway.

## Payment systems have functioned effectively

*The Norwegian payment system functioned effectively in 2011. Stable payment system operations are highly important to financial stability. All payments between banks and between customers of different banks are cleared and settled in these interbank systems.*

### Norges Bank's responsibility and role in monitoring the Norwegian payment system

Norges Bank ensures secure and efficient settlement of interbank payments in banks' accounts at Norges Bank and supplies society with banknotes and coins in a manner that promotes an efficient payment system. Norges Bank also monitors the Norwegian payment system with a view to promoting a robust and efficient payment system, thereby contributing to financial stability.

While this work is primarily aimed at minimising risk in the interbank clearing and settlement system, Norges Bank also monitors important trends in the payment system as a whole. Norges Bank's oversight of authorised interbank systems relies on reporting requirements and supervisory meetings. Oversight and monitoring of interbank systems follow international recommendations, primarily from the BIS Committee on Payment and Settlement Systems (CPSS). Two interbank systems are licensed under the Payment Systems Act: the Norwegian Interbank Clearing System (NICS) and the private settlement bank DNB Bank ASA. The private settlement bank Sparebank1 SMN is exempt from the licensing requirement.

Clearings from NICS are settled in Norges Bank for banks with settlement at the central bank. Once settlement has been carried out at Norges Bank, DNB Bank ASA and Sparebank 1 SMN perform settlement with their participant banks.

There were few cases of disruptions in the two licensed interbank systems in 2011.

In the *Annual Report on Payment Systems*, Norges Bank discusses developments in interbank systems and retail payment systems. In the most recent *Report*, Norges Bank pointed out that the financial crisis revealed the importance of robust clearing and settlement systems for the ability of financial markets and financial institutions to function in periods of stress. It is Norges Bank's view that Norwegian clearing and settlement systems compare well internationally. In the *Report*, Norges Bank also provides an account of its work to monitor and supervise financial infrastructure.

With regard to retail payment systems, Norges Bank focuses on how to enhance the efficiency of payments and accounting in the business and government sectors by better utilisation of electronic data interchange. Norges Bank also emphasises that banks should bolster their cost coverage for cash services by raising fees and operating more efficiently. This approach is preferable to reducing the availability of cash to customers.

### Stable operation of Norges Bank's settlement system

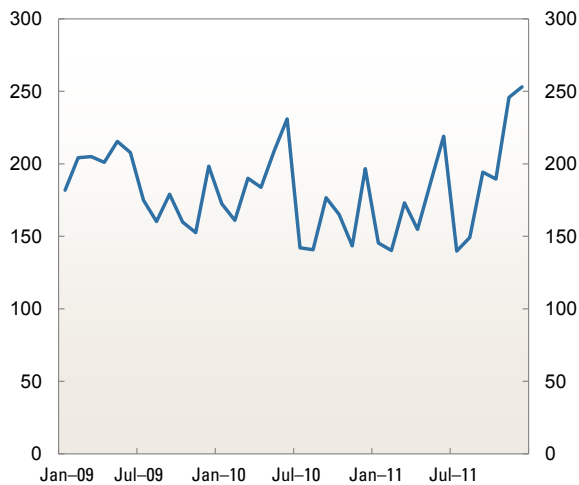
Norges Bank is the system's settlement bank for interbank payments in Norway. This function is associated with Norges Bank's responsibility pursuant to the Norges Bank Act to promote an efficient payment system domestically and vis-à-vis other countries and with banks' accounts with and access to loans from Norges Bank. Because the central bank is the issuer of money, deposits in the central bank are without credit or liquidity risk to banks. Therefore, the interest rate on central bank money provides the basis for interest rate formation in the economy as a whole.

All banks in Norway can have accounts with Norges Bank. At end-2011, 129 banks had accounts at Norges Bank, as opposed to 134 in 2010. Of these, 21 banks settled their payments on a daily basis in Norges Bank's settlement system (NBO), either in the form of individual payments or net settlement. The other banks mainly used their account for payments, primarily associated with loans from and deposits with Norges Bank. The CLS Bank (Continuous Linked Settlement) has an account that is used for daily settlement of the NOK part of foreign exchange trades within the international system for settlement of such trades. Oslo Clearing ASA is a central counterparty in trades in financial instruments and has an account with NBO for daily settlement of interbank positions. Three central banks and the Bank for International Settlements (BIS) also have accounts with NBO.

In 2011, an average of NOK 183bn per day was settled in Norges Bank's settlement system, compared with NOK 176bn in 2010. At end-2011, banks had sight deposits and reserves on deposit totalling NOK 41.5bn. A new solution for settling central government payments through the banks' joint clearing system NICS went into operation in November. This solution reduces settlement risk. Chart 3.3 shows the turnover in Norges Bank's settlement system in recent years.

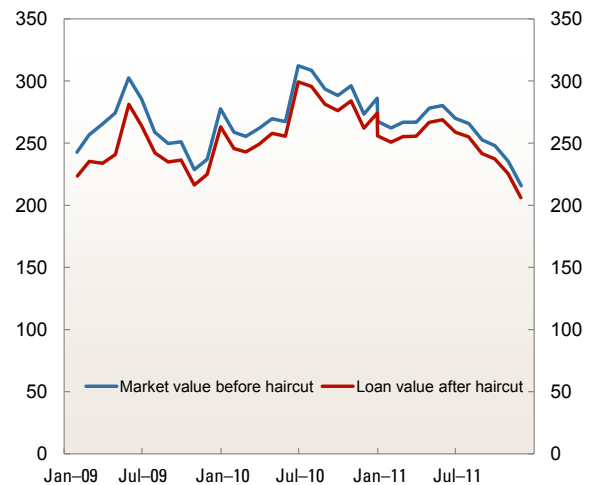
Norges Bank has contracted with EDB ErgoGroup ASA for provision of ICT operating services for the settlement system. There were no serious interruptions in the settlement system's technical operations in 2011.

Chart 3.3 Norges Bank's settlement system



Source: Norges Bank

Chart 3.4 Banks' collateral for loans from Norges Bank



Source: Norges Bank

Banks pay for the settlement services provided by Norges Bank, and prices are set so that revenue covers the relevant costs for providing these services. For 2011, prices were set to cover NOK 53m in costs.

Along with the central banks of Denmark, Iceland and Sweden, Norges Bank participates in a Nordic forum for exchanging experiences concerning settlement systems and solutions for banks' collateral for loans from central banks.

### Collateral for loans from Norges Bank

Norges Bank extends loans to banks against collateral in the form of securities. Such loans help to increase the efficiency of the implementation of monetary policy and payment settlements. In order to be used as collateral, securities must satisfy a number of requirements. Borrowing facilities and collateral requirements are stated in the regulations and guidelines issued by Norges Bank.

At end-2011, banks had a total stock of securities as collateral for loans from Norges Bank of NOK 206bn, after haircuts, compared with NOK 274bn in 2010. In addition, banks' fixed-rate deposits (F-deposits), which can also be used as collateral, totalled NOK 51bn. The number of securities approved as collateral at Norges Bank was 820 at end-2011. Chart 3.4 shows banks' collateral for loans from Norges Bank in recent years.

In October, Norges Bank circulated for comment a proposal to raise haircut rates when calculating loan values. The proposal is to come into force on 15 February 2012 at the same time as other rule changes approved in 2010.

The central banks of Denmark, Sweden and Norway allow banks to pledge deposits in one central bank as collateral for loans in one of the other central banks. This arrangement, called the Scandinavian Cash Pool (SCP), may only be used for intraday liquidity. Thus, the five banks that participate in the arrangement are better able to manage their liquidity across national borders. Approximately NOK 3bn was on average borrowed from Norges Bank through the SCP in 2011. Banks only occasionally used deposits with Norges Bank as collateral for loans in another Scandinavian central bank.

### Centralised securities settlement in Europe

The European Central Bank (ECB) is developing centralised securities settlement for the euro and other currencies known as TARGET2-Securities (T2S). The purpose of T2S is to simplify cross-border securities settlement in Europe. The system is currently scheduled to go live in 2015-2016. The Eurosystem has invited central banks outside the euro area to take part in negotiations on conditions for participation in T2S. Along with the central banks of Denmark, Iceland, Poland, Sweden, Switzerland and the UK, Norway has been taking part in the negotiations, which began in 2010. In 2011, the central banks of Poland, Switzerland and the UK withdrew from the negotiations.

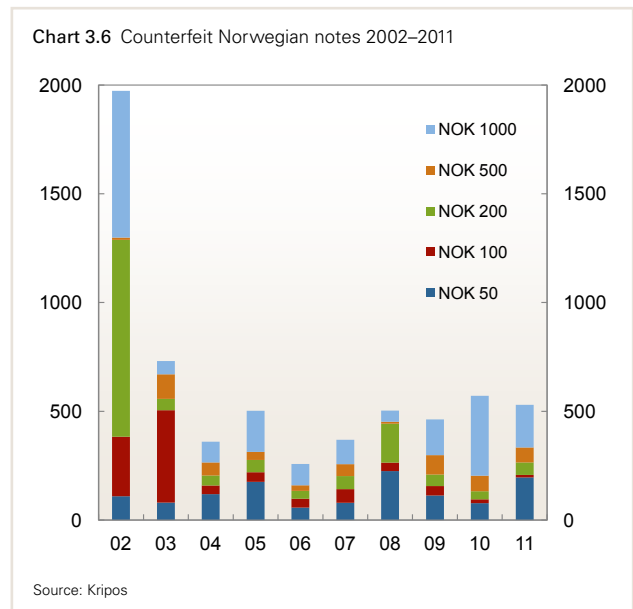
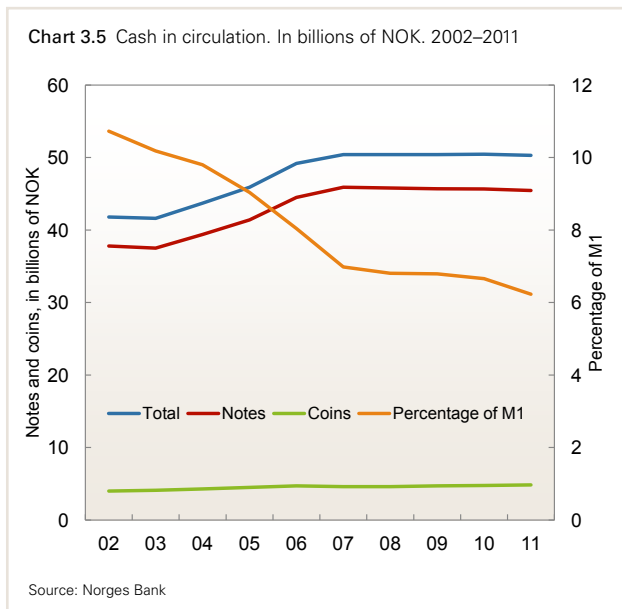
To coordinate the views of participants in Norway, a national user group has been established, with the participation of banks, investment firms, the Norwegian Central Securities Depository (VPS), Finance Norway (FNO) and the Norwegian Securities Dealers Association, while Finanstilsynet has observer status. Norges Bank chairs the user group. The matter of Norwegian participation in T2S was the subject of a consultation among financial market participants. Norges Bank's conditions for concluding an agreement with the ECB on T2S are that Norwegian market participants wish to join and that the agreement protects Norges Bank's interests. A decision on Norwegian participation in T2S will be made when the agreement is finalised.

### Account management for the government

Norges Bank performs tasks relating to the management of the central government's liquid assets and debt in NOK. The legal basis for these responsibilities is provided for in the Norges Bank Act and they are regulated by means of agreements between Norges Bank and the Ministry of Finance. A primary function is to amass government liquidity each day in the government's sight deposit account with Norges Bank. At end-2011, approximately 400 government agencies had a total of approximately 1 040 accounts with Norges Bank. The sum of the amounts in these accounts constitutes the balance of the government's sight deposit account. The government receives interest on these funds. In addition, the Ministry of Finance also sets internal interest rates for certain government-owned funds and deposits. The government represented by the Ministry of Finance pays an annual fee to cover the costs of the banking services that Norges Bank performs for the government.

Norges Bank has contracted with EDB ErgoGroup ASA to provide ICT services for the account system. Account management services for the government at Norges Bank were also stable in 2011.

Actual payment services for the government are performed by banks by agreement with the Norwegian Government Agency for Financial Management (DFØ). DFØ has agreements for payment and account services with DNB Bank ASA, Nordea Bank Norge ASA and SpareBank 1 Alliansen. Norges Bank has agreements with these banks on how the government's funds shall be transferred between banks and Norges Bank each day.



## Notes and coins

### Cash circulation remains stable

The yearly average value of notes and coins in circulation increased in the period from 2003 to 2007. In recent years, circulation has remained stable, amounting in 2011 to just below NOK 50.4bn (see Chart 3.5). The value of notes and coins in circulation as a share of the value of means of payment used by the public (M1) continues to decrease.

The value of notes in circulation averaged NOK 45.5bn in 2011, i.e. a decline of NOK 0.2bn from the previous year. The value of coins in circulation averaged NOK 4.9bn in 2011, an increase of NOK 0.1bn from 2010.

### Low seizure of counterfeit Norwegian banknotes

The number of counterfeit banknotes seized in Norway is low. In the period from 2002 to 2004, Norges Bank upgraded the smaller denominations in the banknote series. Following this upgrade, the number of counterfeit Norwegian notes seized has been very low (see Chart 3.6). In 2011, just over 500 notes were seized, corresponding to approximately four counterfeit notes per million notes in circulation. This is very low compared with many other countries. The quality of most counterfeits is very poor, making them easy to spot.

### Organisation of cash distribution

The Norges Bank Act assigns Norges Bank responsibility for issuing notes and coins. This involves ensuring that a sufficient quantity is produced to meet the general public's cash requirements and to ensure its availability. Norges Bank supplies banks with cash, and banks are responsible for further distribution to the general public. The central bank is also responsible for maintaining the quality of notes and coins in circulation through the withdrawal and destruction of worn and damaged notes and coins.

The objective of Norges Bank's cash handling activities is to promote the efficiency of cash distribution and of the payment system as a whole. Various measures have been implemented to ensure the optimal division of responsibilities and duties between participants and a clearer distinction between different types of service. Norges Bank plays a more clearly defined role as wholesaler, and banks have taken greater responsibility for interbank distribution of cash. Measures also include an arrangement whereby, on certain conditions, banks receive interest compensation for cash holdings in private depots. At the end of 2011, a total of 13 private depots were established in different parts of Norway. The depots are operated by Norsk Kontantservice AS (NOKAS) and Loomis Norge AS.

The Norges Bank Act assigns Norges Bank the sole right to issue banknotes and coins. Norges Bank must therefore function as debtor for these means of payment. Although production, destruction and distribution may be performed by others, Norges Bank must ensure that these operations are carried out in accordance with the requirements that it imposes.

Norges Bank has outsourced a number of operations in the area of cash handling (see Chart 3.7). Notes and coins are produced by external suppliers. Processing services associated with central bank responsibilities (destruction, etc.) and services associated with the management of central bank depots (Bergen, Oslo, Stavanger, Tromsø and Trondheim) are performed by NOKAS. Beginning on 1 January 2012, Norges Bank is responsible for central bank depot operations in Oslo.

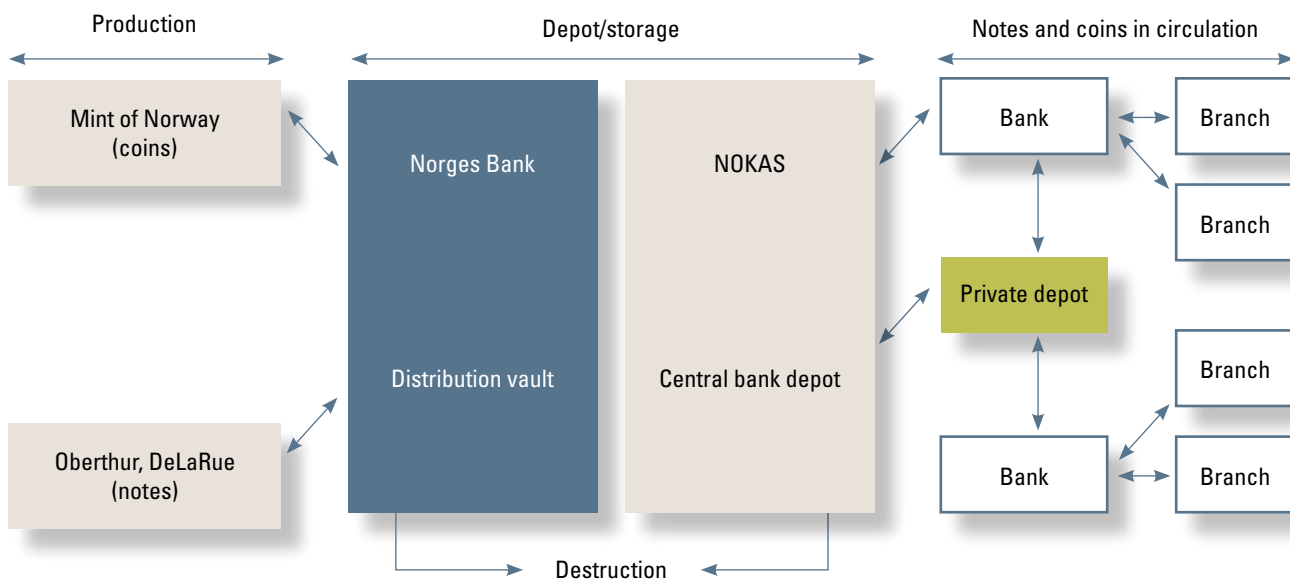


Chart 3.7 The note and coin lifecycle



### Withdrawal of the 50-øre coin

In March 2011, Norges Bank decided that the 50-øre coin shall no longer be legal tender from 1 May 2012. The reason for the decision is that this denomination no longer circulates as an ordinary coin used for payment. While it is used in shops to give change, re-use of these coins by customers appears to be very limited. Thus, Norges Bank has been producing a large number of 50-øre coins every year, even though there are more than enough of these coins to start with.

### Commemorative coin issues

Norges Bank issues jubilee and commemorative coins in gold and silver, pursuant to Section 16 of the Norges Bank Act, and special edition circulation coins, pursuant to Section 13 of the Norges Bank Act, which is the general legal basis for issuing coins.

Section 16 of the Norges Bank Act confers upon the King-in-Council the power to approve issuance of gold and silver coins. Since 1994, this authority has been delegated to Norges Bank. On 27 May 2011, the King-in-Council conferred authorisation to approve such coin issues to the Ministry of Finance.

### Commemorative coins in 2011

In 2011, Norges Bank issued two commemorative coins in silver and a 10-krone special edition circulation coin.

The two commemorative coins in silver were issued on 8 January 2011 to mark the central role of sports in Norway. One coin commemorated the 150th anniversary of the Norwegian Olympic and Paralympic Committee and Confederation of Sports (NIF), while the other marked the FIS Nordic World Ski Championships in Oslo. The silver coins have a nominal value of NOK 200, and each coin was limited to an issue of 40 000 coins. These silver coins are still available for purchase, individually or in sets.

Six artists were invited to participate in a competition for the design of the coins' reverse. The winning designs were by Ina Viktoria Kristiansen of Uniform Strategisk. The portrait of H.M. King Harald V on the obverse of both coins was created by Ingrid Austlid Rise, designer at Det Norske Myntverket (Mint of Norway).

2011 was the bicentenary of the founding of Norway's first university. To mark the event, Norges Bank issued a special edition 10-krone circulation coin. In connection with the decision, it was emphasised that the occasion was not geographically limited to Oslo but commemorated the beginnings of higher education and science and scholarship in Norway in a broad sense. The coin was put into circulation on 3 May. Norges Bank collaborated with UIO:200, an anniversary planning body established by the University of Oslo to commemorate the bicentenary in 2011.

A competition was held for the design of the coin's reverse. The winning design is by Enzi Finger and features a Greek Ionic column, a classic – as well as classical – university symbol. The obverse of the coin features the portrait of H.M. King Harald V, created by the designer Ingrid Austlid Rise.



## CHAPTER 4:

# Investment management

At the end of 2011, Norges Bank managed assets amounting to a total of NOK 3 575bn in international capital markets. The assets primarily comprised the Government Pension Fund Global (GPF), which is managed on behalf of the Ministry of Finance. The Bank also manages its own international reserves. Performance reports are published on Norges Bank's website.

### Foreign exchange reserves and claims on the IMF

Norges Bank's international reserves comprise foreign exchange reserves and claims on the International Monetary Fund (IMF). Excluding borrowing in foreign exchange, the market value of foreign exchange reserves came to NOK 262bn at end-2011.

Foreign exchange reserves are to be used for transactions in the foreign exchange market in support of monetary policy or financial stability. In addition, foreign exchange reserves are used to meet Norway's international obligations.

Norges Bank's Executive Board issues guidelines for the management of foreign exchange reserves and has delegated responsibility to the Governor of Norges Bank for issuing supplementary rules in certain areas. Reserves are divided into a money market portfolio and a long-term portfolio. In addition, capital is accumulated in a petroleum buffer portfolio for transferring foreign exchange to the GPF.

The money market portfolio and the petroleum buffer portfolio consist only of fixed income investments, while the long-term portfolio has a 40% strategic allocation to equities and a 60% allocation to fixed income instruments. The main strategy for both the long-term portfolio and the money market portfolio is defined by means of benchmark indices. These are constructed portfolios with a given country or currency distribution and with specific securities or fixed income indices in various submarkets or currencies. The benchmark index provides the basis for managing and monitoring risk exposure and for evaluating the actual return Norges Bank achieves in its reserve management.

The long-term portfolio accounts for the largest portion of foreign exchange reserves and amounted to NOK 224bn at end-2011. The objective of the management of the long-term portfolio is a high long-term return, but it should also be possible to use the portfolio in support of monetary policy or financial stability if deemed necessary.

The return on the long-term portfolio was 2.71% in 2011, measured in terms of the benchmark portfolio's currency basket. In NOK terms, the return was 5.01%. The difference reflects the depreciation of NOK in relation to the benchmark portfolio's currency basket.

Over the past 10 years, the annual nominal return has been 4.87%, measured in terms of the benchmark portfolio's currency basket. Net of management costs and adjusted for inflation, the annual return came to 2.67%. In 2011, the long-term portfolio outperformed the benchmark index by 0.15 percentage point.

The extent to which the actual portfolio may deviate from the benchmark portfolio is subject to a limit. Investment management is to be organised so that the expected tracking error (relative volatility) does not exceed 1 percentage point. Expected tracking error is an overall risk measure and is measured based on a model using historical market fluctuations. In 2011, average expected tracking error was measured at 0.54 percentage point.

In connection with the revision of the investment mandate, the maximum ownership limit in a single company was increased from 5% to 10% in line with that applying to the GPF. Ownership interest refers to investments in equity instruments that allow the owner or a proxy to exercise voting rights in a company. The same applies to agreements entitling the holder to achieve such an ownership position. Norges Bank's investments are financial and not strategic. The Executive Board has issued common guidelines for the exercise of ownership rights for foreign exchange reserves and the GPF. Norges Bank's annual report on the GPF includes an extensive account of the Bank's exercise of ownership rights.

The money market portfolio is the most liquid portion of foreign exchange reserves and, together with the long-

term investment portfolio, is to be invested so that it can be used for monetary policy purposes or to promote financial stability. In addition, the money market portfolio is used to meet Norges Bank's international obligations, including transactions involving the IMF and loans to individual countries. The portfolio is invested so that it can within one trading day be used for transactions in the foreign exchange market without having to realise any sizeable losses. The portfolio consists of short-term money market instruments, primarily secured loans to approved international banks and Treasury bills with a maturity of up to one year.

In 2010, the Executive Board decided that the size of the money market portfolio is to be between the equivalent of SDR (Special Drawings Rights) 2bn and SDR 3bn. At the same time, it was decided that the portfolio may be placed in government securities with a residual maturity of up to one year. The Executive Board decided that the currency composition of the benchmark index is to be 50% in USD and 50% in EUR. It is to be composed of overnight money market indices and Treasury bill indices.

Against the background of financial market developments through summer 2011, a USD amount equivalent to SDR 1.5bn (NOK 12.9bn) was transferred from the long-term investment portfolio to the money market portfolio with effect from end-August. From the same date, the currency composition of the benchmark index is to be 75% in USD and 25% in EUR.

The deviation between the actual portfolio and the benchmark portfolio is subject to a limit. The currency weights may deviate by +/- 5 percentage points from the benchmark index. The limit for relative volatility (expected tracking error) is set at 1.0 percentage point and the Bank uses a model based on historical market fluctuations. Relative volatility is estimated at an average 0.11% in 2011.

At end-2011, the money market portfolio stood at NOK 34.8bn (SDR 3.8bn), an increase of NOK 10.6bn (SDR 1.1bn) from end-2010. In 2011, the portfolio returned 0.48%, measured in local currency, while the benchmark index returned 0.44%. The low return figures must be seen in connection with the strict requirements regarding liquidity and preparedness that apply to the portfolio.

Gross revenues from the State's Direct Financial Interest in the petroleum sector (SDFI) are transferred to Norges Bank and placed in the petroleum buffer portfolio. Norges Bank also purchases foreign currency directly in the market in periods in order to cover the amount that is to be allocated to the GPFG.

The petroleum buffer portfolio is invested exclusively in money market instruments. At the end of 2011, the market value of the petroleum buffer portfolio was NOK 6bn. Funds are transferred from the petroleum buffer portfolio to the GPFG each month, with the exception of December, when transfers are normally not made. This means that at year-end the portfolio is usually larger than the average value at the end of the other months (after transfers). In 2011, the buffer portfolio returned 2.25% in NOK terms. A benchmark index has not been established for the petroleum buffer portfolio.

Claims on the IMF consist of SDRs, the reserve position and Norway's bilateral loans to the IMF. Norges Bank has been allocated SDR 1 563m from the IMF. Norges Bank has concluded an agreement with the IMF providing for voluntary purchase and sale of SDRs, bringing the actual holding of SDRs to between SDR 782m and SDR 2 345m. At end-2011, SDR holdings came to SDR 1 523m, or NOK 13 995m. Norges Bank has entered into an agreement that provides the IMF with the right to draw up to SDR 3bn to finance the IMF's general loan schemes. After the IMF expanded the New Arrangements to Borrow (NAB) in March 2011, the IMF's drawings under the bilateral loan scheme are transferred to NAB. The Ministry of Finance has entered into an agreement for the provision of loans up to SDR 300m to the IMF for use in its loan scheme for low-income countries. At end-2011, the IMF had drawn a total of SDR 524m under these schemes.

## The Government Pension Fund Global

Norges Bank is responsible for the operational management of the GPFG on behalf of the Ministry of Finance. At end-2011, the market value of the GPFG was NOK 3 312bn before deduction of Norges Bank's management fee. In 2011, the Ministry of Finance transferred a total of NOK 271bn to the GPFG.

Investment management is conducted pursuant to the regulation "Mandate for the management of the Government Pension Fund Global". The Ministry of Finance has established a strategic benchmark index consisting of a 60% allocation to equities and 40% to fixed income instruments. The benchmark index consists of equity indices for 46 countries and fixed income indices in 11 currencies. The benchmark index reflects the Ministry's investment strategy for the GPFG and is an important basis for managing the risk associated with the operational management of the GPFG and for evaluating Norges Bank's management performance. The Ministry of Finance has set limits for how far the actual portfolio may deviate from the benchmark portfolio.

In 2011, the Fund posted a negative return of 2.54%, measured by the benchmark portfolio's currency basket, which is a measure of return that gives the best indication of the GPFG's international purchasing power. In NOK terms, the return on the GPFG was a negative 1.39%. Measured in international currency, the return on the equity portfolio was a negative 8.84%, while the fixed income portfolio returned 7.03%.

In 2011, the return was 0.13 percentage point lower than the return on the benchmark index. The equity portfolio underperformed the benchmark index by 0.48 percentage point, while the fixed income portfolio outperformed the index by 0.52 percentage point.

Since 1998, the annual nominal return has been 4.48%, measured in international currency. Net of management costs and adjusted for inflation, the annual return has been 2.42%.

For a more detailed presentation of investment management in 2011, see the *Government Pension Fund Global Annual Report 2011*.

## CHAPTER 5:

# International cooperation

Norges Bank participates in international cooperation through several channels, such as the Bank's active participation in financing schemes and agreements with the IMF and its shares in the Bank for International Settlements (BIS). The Bank has extensive contact with central banks in other countries and international organisations.

## Loans and support in connection with the international financial crisis

### Increased quotas and loan agreements with the International Monetary Fund (IMF)

In connection with the financial crisis in 2008-2009, a series of measures were introduced to strengthen the lending capacity of the IMF. The financial resources of the IMF were increased through bilateral loans to the IMF from member countries, an enlargement of the multilateral New Arrangements to Borrow (NAB) and the decision to increase member countries' IMF quotas.

With the consent of the Ministry of Finance, a loan agreement between Norges Bank and the IMF was signed on 26 June 2009. The agreement authorised the IMF to draw up to SDR 3bn to fund its general lending facilities.

The enlarged NAB took effect on 11 March 2011. Norway contributed SDR 3.9bn (about NOK 35.5bn<sup>5</sup>) of the total amount of SDR 370.0bn. The Ministry of Finance is party to the agreement with IMF for the NAB arrangement, while Norges Bank administers Norway's participation and provides foreign exchange reserves in accordance with Section 25 of the Norges Bank Act.

Norges Bank's bilateral loan to the IMF was to be transferred to the enlarged NAB upon activation. As a transitional arrangement, Norges Bank has in consultation with the Ministry of Finance decided to maintain the bilateral loan arrangement with the IMF. The IMF may draw on the bilat-

eral loans from Norges Bank to finance lending that was approved before the new NAB was activated in March 2011. The IMF repays these drawings the same day by borrowing from the NAB facility with Norway. Hence, in practice the IMF no longer uses the bilateral loan from Norges Bank. At 31 December 2011, the IMF had thus borrowed a total of SDR 403.6m from Norway under the NAB.

On 15 December 2010, the IMF's Board of Governors decided to revise the quota system, entailing a doubling of the quotas to SDR 476.8bn (about NOK 4371.5bn). The Storting (Norwegian parliament) approved an increase in Norway's IMF quota on 17 November 2011. The quota for Norway will increase from SDR 1883.7m (NOK 17.3bn) to SDR 3754.7m (NOK 34.4m) when a sufficient number of countries have ratified the agreement for it to be activated.

On 21 December 2011, Minister of Finance Sigbjørn Johnsen sent a letter to the IMF offering to provide up to SDR 6bn to the IMF through a bilateral loan agreement, subject to the approval of the Storting. The loan offer is part of the international work aimed at strengthening the lending capacity of the IMF, partly in response to the debt crisis in some euro area countries. The loan is to be used for the IMF's general lending arrangements and will not be earmarked for a specific country or region. A loan agreement has yet to be signed as the IMF has not yet adopted a resolution to increase its loans.

In June 2010, the Ministry of Finance concluded an agreement with the IMF to provide up to SDR 300m in loan resources to the IMF's low-income country (LIC) facilities. In a letter dated 15 July 2010, the Ministry of Finance requested pursuant to Section 25 of the Norges Bank Act that Norges Bank meet Norway's commitments under the agreement by providing funds through transfers of foreign exchange reserves. Thus, Norges Bank is responsible for the practical implementation and follow-up of the agreement. At 31 December 2011, the IMF had drawn SDR 120m under the agreement.

<sup>5</sup> According to the exchange rate between SDR and NOK as at 15 Desember 2011 (9.168340).

## Loan agreement with Seðlabanki Íslands

On 19 November 2008, the IMF authorised a loan to Iceland of USD 2bn under a two-year stand-by arrangement. In addition, loan agreements between Iceland and the other Nordic countries were signed on 1 July 2009. The Ministry of Finance approved a loan from Norges Bank to the Icelandic central bank and provided a government guarantee for the loan in its letter of 22 June 2009. The Icelandic government has guaranteed repayment of the loan to Norges Bank. Seðlabanki Íslands had drawn the entire loan of EUR 480m as of 31 December 2011.

## Regular contact and cooperation with other central banks and international organisations

Norges Bank has shares in the Bank for International Settlements (BIS), whose task is to foster cooperation between central banks. The BIS provides banking services to central banks and is also a research body and discussion forum for its member banks. The governor of Norges Bank regularly attends meetings of the BIS.

Pursuant to section 25 of the Norges Bank Act, Norges Bank shall administer Norway's financial rights and fulfil the corresponding obligations ensuing from membership of the International Monetary Fund (IMF). Norges Bank has been commissioned by the Ministry of Finance to be responsible for day-to-day IMF work in Norway.

The highest decision-making body of the IMF is the Board of Governors. In 2011 Norway was represented by the Governor of Norges Bank, Øystein Olsen, and the Secretary General of the Ministry of Finance, Svein Gjedrem, was his alternate. The Board normally meets once a year at the Annual Meeting of the IMF. Apart from this meeting, voting by the Board of Governors takes place by ballot. An Executive Board consisting of 24 executive directors is responsible for day-to-day business. The five Nordic and three Baltic countries comprise a single constituency with a joint representative on the Board. The office of board member is rotated among the Nordic countries. Denmark holds this position in the period 2010–2012.

The countries in the Nordic-Baltic constituency primarily coordinate their views on important IMF matters through the Nordic-Baltic Monetary and Financial Committee (NBMFC). The Norwegian members are the secretary general of the Ministry of Finance and the deputy governor of Norges Bank. The other countries are represented at a comparable

level. The NBMFC normally meets twice a year. Coordination between the countries is aimed at arriving at a common stance, which the board member representing the group then presents to the IMF Executive Board. Norwegian policy on matters to be brought before the IMF Executive Board is set by the Ministry of Finance on the advice of Norges Bank. The division of responsibility between the Ministry and the Bank is set out in a written joint understanding.

The International Monetary and Financial Committee (IMFC) has a key function as an advisory body to the Executive Board of the IMF. The IMFC meets twice a year. The Committee provides policy guidelines for the activities of the IMF. The IMFC's members are ministers or central bank governors who represent either a country or a constituency composed of several countries. Minister of Finance Sigbjørn Johnsen represented the Nordic-Baltic constituency at the IMFC meeting in April 2011, while the central bank governor of Denmark represented the constituency in September 2011.

An important part of the activities of the IMF involves monitoring economic developments in member countries, with particular emphasis on macroeconomic conditions and financial stability. The main emphasis is on bilateral surveillance through Article IV consultations, which take place annually for most countries. Norway holds such consultations every two years unless special circumstances call for annual consultations. In the intervening years, the IMF conducts a simplified consultation and no written report is submitted to the Board of the IMF. The IMF conducted an Article IV consultation with Norway in 2011. The preliminary conclusions were published on 22 November 2011 and the report was discussed by the Board of the IMF on 27 January 2012.

Norges Bank cooperates extensively with the other Nordic central banks. The annual meeting of Nordic central banks in 2011 was organised by the Danish central bank. Staff from various departments in the central banks meet at regular intervals to discuss issues relating to economic analysis, monetary policy, financial stability, payment systems, legal matters concerning central banks, human resource policy, etc.

Norges Bank also has regular contact with the European Central Bank (ECB) and central banks of non-euro area EU member states. Norges Bank has established an arrangement with the ECB, the Bank of England and certain other central banks, which affords employees the opportunity to work at these institutions for periods of up to 12 months.

As from 1 January 2011, the EU has strengthened surveillance of threats to financial stability through the establishment of new bodies for micro-prudential oversight, the Eu-

European System of Financial Supervisors (ESFS), and for macroprudential surveillance, the European Systemic Risk Board (ESRB). Norway is an observer at the meetings of the ESFS through a representative from Finanstilsynet (Financial Supervisory Authority of Norway) who is the Norwegian observer at meetings of the microprudential oversight committee for the banking sector, the European Banking Authority (EBA). Norges Bank has also participated in meetings. The Bank participates in a working group of the EBA that is working on designing liquidity rules in the European Commission's proposal for a new banking regulation in the EU (CRD IV). The EFTA member states Norway, Iceland and Lichtenstein are negotiating with the European Commission to establish an agreement on participation in the new surveillance structure and adaptation to the decisions of the new EU body.

The Governor of Norges Bank, the Director General of Finanstilsynet and the Secretary General of the Financial Stability Board Regional Consultative Group for Europe participate in the meetings.

Norges Bank participated in a number of meetings where macroprudential supervision and regulation are discussed with other Nordic and Baltic countries. Even though Norway is not represented on the Basel Committee, Norges Bank participates in the work of a sub-committee, the Research Task Force.

In the area of cash, Norges Bank Financial Stability has close contact with the European System of Central Banks and participates in important international events, including the European Banknote Conference and the Central Bank Counterfeit Deterrence Group, as secretary, chair of a committee and member of the Executive Committee.

## Technical assistance to the central banks of Malawi and Zambia

For many years, Norges Bank has provided various kinds of technical assistance to central banks in developing countries. In order to promote more efficient and performance-oriented technical assistance to such central banks, Norges Bank assumed responsibility for the IMF's technical assistance to the Reserve Bank of Malawi in 2006. This work is now nearing completion and in July 2011 a similar agreement on technical assistance was approved for the Bank of Zambia.

Norges Bank's assistance to both countries is formally administered by the IMF, but financed by the Norwegian Ministry of Foreign Affairs. It was agreed early in 2010 to

extend the agreement for Malawi with somewhat reduced scope until the end of 2011, and in 2011 it was agreed that the work would continue into 2012. After that the work will be concluded. Norges Bank has placed up to 2 FTEs annually at the disposal of the Reserve Bank of Malawi, consisting of 1 FTE in the form of a long-term assignment as adviser to the Reserve Bank and up to 1 FTE in the form of short-term assignments. Short-term assignments cover a broad range of central bank tasks. In 2011, a total of eight short-term visits of between one and two weeks each were completed within a broad range of external and internal central bank activities. Two short-term visits are planned in winter 2012 before the work is completed.

The IMF has conducted an evaluation of the technical assistance to the Reserve Bank of Malawi during the period from October 2006 to December 2008. Norges Bank's technical assistance was assessed in general as performance-oriented and successful. A new evaluation in September 2010 reached the same conclusion. The cooperation with the Reserve Bank of Malawi is documented in detail in Norges Bank's *Occasional Papers* No. 40, *Central Bank Modernization*. In October 2009, Director Asbjørn Fidjestøl took over the post of Monetary and Central Bank Operations Adviser. He concluded his work in December 2011.

Norges Bank has also placed 2 FTEs at the disposal of the Bank of Zambia. In 2011, three short-term visits of around two weeks were made. Special adviser Gunnvald Grønvik has been appointed to the post of adviser for the technical assistance programme.

## CHAPTER 6:

# Other functions

### Foreign exchange transactions

In 2011, Norges Bank's commercial foreign exchange transactions mainly comprised foreign exchange purchases to build up the Government Pension Fund Global (GPFG).

The GPFG is built up through transfer of foreign exchange income from the State's Direct Financial Interest in petroleum activities (SDFI) and through Norges Bank's purchases of foreign exchange in the market.

The system for transferring foreign exchange from the SDFI and calculating Norges Bank's foreign exchange purchases was most recently changed in 2004. The Ministry of Finance determines the monthly allocation to the GPFG. Any foreign exchange required by Norges Bank in excess of the transfer from the SDFI is purchased in the foreign exchange market. Daily foreign exchange purchases are then fixed for a month at a time and are announced on the final working day of the previous month. The actual transfers may differ from the estimates. Adjustments are made for any differences when foreign exchange purchases are made in the following month. As a result, Norges Bank's foreign exchange purchases may vary somewhat from month to month.

Capital is not normally transferred to the GPFG in December and foreign exchange is therefore not normally purchased by Norges Bank in this month. Foreign exchange income from the SDFI may nevertheless be transferred to Norges Bank in order to minimise the Government's exchange costs.

Norges Bank purchased NOK 89.7bn in the foreign exchange market in 2011 (see Table 2). Transfers from the SDFI amounted to NOK 173.1bn.

**Table 2:** Norges Bank's daily foreign exchange purchases for the GPFG in 2011

Month	Daily amounts (millions of NOK)	Total per month (millions of NOK)
January	0	0
February	0	0
March	0	0
April	0	0
May	300	6 300
June	400	8 000
July	400	8 400
August	400	9 200
September	500	11 000
October	550	11 550
November	1 600	35 200
December	0	0
2011		89 650



## Government debt 2011

According to an agreement between the Ministry of Finance and Norges Bank, the Bank shall provide services as adviser, facilitator and payment agent in connection with raising and managing domestic government loans. The Ministry of Finance pays for bank-related services provided by Norges Bank to the Ministry in connection with government debt and liquidity management and for variable costs incurred by Norges Bank in its capacity as provider of services to the Ministry of Finance.

The Government's schedule for the issue of short- and long-term securities in 2011 was published in an auction calendar in December 2010. Six auctions of government bonds and eight auctions of short-term government paper (Treasury bills) were held in 2011. Ad hoc auctions were not held. The total volume issued, excluding the Government's own purchases in the primary market, amounted to NOK 20bn in government bonds and NOK 32bn in Treasury bills.

The strategy for long-term government borrowing is based on maintaining a yield curve for government bonds with maturities of up to approximately 10 years. The pattern for government bond borrowing has been to issue a new 11-year bond every second year. No new 11-year bonds were issued in 2011. A bond with a volume outstanding of NOK 46bn matured in May 2011.

According to the issue programme for short government paper, new Treasury bills are issued on IMM dates<sup>6</sup> and mature on the IMM date one year later. The loans are increased through subsequent auctions.

The government paper auctions have been held via the Oslo Børs trading system. The bid-to-cover ratio, which is the volume of bids in relation to the volume allocated in the auction, averaged 2.26 for government bonds and 2.83 for Treasury bills.

By 11 July, Norges Bank had entered into agreements with six primary dealers, who are under the obligation to furnish binding bid and offer prices for agreed minimum

amounts of government bonds and Treasury bills on Oslo Børs. On 11 July a primary dealer withdrew from the government bond agreement. On 1 November, another primary dealer withdrew from the agreement in both government bonds and Treasury bills. In return for furnishing these binding bid and offer prices, the primary dealers may borrow government paper for a limited period. In 2010, lending limits for the shortest bonds were NOK 6bn and between NOK 4bn and 5bn for other bonds. For Treasury bills, the lending limits were NOK 6bn for each loan. In addition, the primary dealers have exclusive rights to participate in auctions of government securities.

Since June 2005, the Government has used interest rate swaps in its domestic debt management. An interest rate swap is an agreement between two parties to exchange future interest payments associated with a given principal. Use of interest rate swaps gives the Government the flexibility to change the average period during which the interest rate on the debt portfolio is fixed without changing its borrowing strategy. The Ministry of Finance has entered into framework agreements with several counterparties. Norges Bank performs the operational functions in connection with entry into interest rate swap agreements on behalf of the Ministry of Finance. The commercial decisions are taken by the Ministry. At end-2011, the average fixed-rate period for government debt was four years. If existing interest rate swaps are taken into account, the fixed-rate period was 1.2 years.

Total government domestic debt securities registered in the Norwegian Central Securities Depository (VPS) at end-2011 amounted to NOK 417bn, calculated at face value. Of this, the volume of Treasury bills used in the swap arrangement amounted to NOK 153bn. Foreign investors hold approximately 49%, while life insurance companies and private pension funds hold approximately 12% of total government debt securities. For government bonds, the proportion of holdings is 71% for foreign investors and 11% for life insurance companies and private pension funds.

<sup>6</sup> International Monetary Market dates: the third Wednesday in March, June, September and December.

## Research in 2011

Research at Norges Bank contributes to the basis for the Bank's decisions. Research at the Bank focuses on monetary policy and financial stability and is anchored in the international and Norwegian research community. Research is to be of a quality that meets the standards required for publication in peer-reviewed international or national journals.

### Publications

In 2011, 13 articles were accepted for publication in peer-reviewed journals. The average for the past three years is 15 articles. The themes cover many areas from property markets, money markets, foreign exchange markets to monetary policy. An overview of approved and published articles is documented on the Bank's website. Current research activity is documented in the Bank's *Working Papers* series and 23 papers were published in this series in 2011, while the average for the past three years is 28 papers. The articles cover a wide range of subjects, such as forecasts, cyclical movements, securities pricing and foreign exchange. Some of the articles are also related to Norges Bank's bicentenary project. In 2011, Norges Bank's *Working Papers* were downloaded 2 511 times from the Internet portal Research Papers in Economics (RePEc).

### Conferences, workshops and seminars

Norges Bank hosted a number of research seminars and conferences in 2011. In June, Norges Bank organised a workshop on the interaction between monetary policy and financial stability, with articles on credit, asset prices and monetary policy transmission mechanisms, DSGE models with an explicit role for financial intermediation, endogenous price bubbles and monetary policy. In August, Norges Bank hosted the *5th Japanese-European Bayesian Econometric and Statistics Meeting*. In September, the Bank organised a workshop on financial intermediation with guest lecturers who spoke on the topics of banks, housing markets and the repo market. Together with the University of Stavanger, the Bank organised the *7th Annual Central Bank Workshop on the Microstructure of Financial Markets*, where researchers and practitioners discussed central themes linked to the formulation, regulation and development of securities markets, with particular focus on market liquidity, algorithmic trading and market structure. The articles presented at these conferences can be downloaded from the Bank's website.

A number of the Bank's research projects have been presented at Norwegian and international conferences and seminars. As part of an international research community, Norges Bank has extensive contact with researchers at universities and other central banks. Norges Bank hosts research seminars with guest lecturers who present their work and take part in seminars and workshops. Norges Bank arranged 57 seminars in 2011 where invited guest lecturers presented their research and took part in meetings and discussions with the Bank's staff.

### Support for economic research

Norges Bank supports economic research in a number of ways. The endowed chair established by Norges Bank at University of Oslo fosters greater awareness about macroeconomics and monetary policy issues. Norges Bank's Economic Research Fund provides financial support for researchers studying abroad or attending international conferences to present their own research work and for research conferences in Norway. In 2011, Norges Bank's Economic Research Fund decided to award Ingvild Almås (Norwegian School of Economics) the prize for best doctoral dissertation *Essays on Economic Inequality*. Almås explores income distribution across countries and to what extent income is distributed fairly.

### Norges Bank's bicentenary project

In connection with Norges Bank's bicentennial in 2016, the Executive Board decided in December 2007 to launch a major research project in two phases, to be published in book form. "Norges Bank's bicentenary project 1816–2016" will be a joint project with contributions from both Norwegian and international research communities. The steering committee comprises the international experts Professor Michael Bordo of Rutgers University, New Jersey, and Professor Marc Flandreau of the Graduate Institute in Geneva, Deputy Governor of Norges Bank Jan F. Qvigstad and Director Øyvind Eitrheim.

The goal is to produce three books dealing with various aspects of Norges Bank's activities over the past 200 years by the beginning of the bicentenary year. The project will also serve to highlight the role of Norges Bank as a public institution from a historical perspective.

The three books have the following working titles:

- *The History of Norges Bank 1816–2016*
- *The Monetary History of Norway 1816–2016*
- *Topics in Central Banking*

The books are also intended to meet the required standards of an internationally recognised academic publisher. The first two books will be published in both Norwegian and English, the third book in English only. In 2010, the Bank appointed Professor Einar Lie, University of Oslo and Professor Jan Tore Klovland, Norwegian School of Economics (in collaboration with Øyvind Eitrheim of Norges Bank), as project coordinators for the first two books.

In 2011, researchers at the Norwegian School of Economics, the University of Oslo and BI Norwegian Business School have conducted research into the history of Norges Bank. In order to enhance this research effort, Norges Bank has also provided funding for a three-year doctoral project on the first three decades of the history of Norges Bank in collaboration with the 1814-project at the University of Oslo.

In 2011, international cooperation was strengthened through an international conference on “The sub-prime crisis and how it changed the past;” at the Graduate Institute in Geneva on 3–4 February. In June, Norges Bank arranged a week-long seminar on economic history for young researchers in collaboration with *inter alia* the University of Venice.

In 2011, a first version of the timeline documenting Norges Bank’s history was published on the Bank’s website. The timeline shows developments in Norges Bank’s organisation and governance structure, means of payment (notes and coins), price stability, financial stability and investment management. A booklet on the work relating to the development of the Norwegian payments system in the period 1945–2010, with particular focus on Norges Bank’s role, was published as Norges Bank’s *Occasional Paper* no. 44. Six research papers were published as Norges Bank *Working Papers* and six master’s theses written in connection with the Bank’s bicentenary project were published in 2011 as Norges Bank *Staff Memos* on the Bank’s website.

## CHAPTER 7:

# The organisation

### Focus on human resources

Norges Bank is a centre of specialist expertise with a high degree of internationalisation and employees from 31 countries. This diversity provides the Bank with a richer working environment, but also places considerable demands on the Bank's ability to organise and adapt to the new realities. A stable low level of sickness absence and structured feedback in the form of annual manager appraisals and working environment surveys support the view of the Bank as an inclusive workplace that successfully integrates employees across nationalities, age and gender.

Norges Bank makes targeted efforts to bolster its reputation as one of Norway's most attractive workplaces. Furthermore, the Bank funds an external post-doctoral scholarship with the aim of attracting intellectual capital and promoting relevant economic research.

Recruitment of new staff aims at ensuring a supply of capable managers and skilled specialists. The Bank's recruitment processes are to be transparent and professional and ensure that the Bank hires the most qualified candidates, regardless of age, gender, religion, ethnic background, dis-

ability or sexual orientation. In addition to meeting the Bank's normal recruitment needs, NBIM's Investment Talent Programme helped to recruit a small group of candidates who will have the opportunity to develop their professional skills over a four-year period.

It is the Bank's aim to achieve greater gender balance. In spring 2011, a joint action plan was drawn up to further strengthen equal opportunity measures at the Bank. The target for the proportion of women is 40% regardless of job category. The number of women in managerial positions is still too low.

A key instrument in retaining staff with critical skills is a competitive pay and incentive system that is actively used to promote and reward good performance. Clear requirements will be imposed through active use of the individual employee's skills, and the Bank will establish conditions to ensure that highly motivated and qualified staff members are given the opportunity for lifelong learning. The Bank aims to facilitate greater rotation and mobility across areas, and build up new expertise by means of high-quality scholarships and study programmes abroad.

### Human resource policy instruments

*Norges Bank's human resource policy objectives involve ensuring that the Bank attracts, develops and retains qualified staff. This level of ambition is dependent on appropriate human resource policy instruments and that these instruments produce the desired results. Pay and incentive systems at Norges Bank should be competitive.*

*Norges Bank has an employee pension fund. Benefits from the pension fund are coordinated with benefits from the National Insurance Scheme. Employees contribute 2% of their gross annual salary to the pension fund. The Bank's insurance programme covers personal insurance, group life insurance, accident and*

*medical insurance, travel insurance and occupational injury insurance. These costs make up 1% of the Bank's total personnel expenses. The Bank has a loan scheme for employees where the interest rate is equal to the norm interest rate<sup>7</sup>.*

*Employees of Norges Bank have access to the Bank's conference and holiday facilities at Venastul, near Lillehammer. Some of the parking places at the head office of the Bank are available for use by employees.*

<sup>7</sup> The norm interest rate laid down by the Ministry of Finance for use in the taxation of loans on favourable terms for employees.

Norges Bank has worked systematically through the year to continuously improve the working environment. Individual health appraisal interviews based on the results of the annual working environment survey have formed the basis for targeted measures. In April the Bank renewed its inclusive workplace agreement (IA-avtalen). The aim of the agreement is to reduce sickness absence, improve workplace modification for employees with functional impairments and raise the real retirement age. The Bank has, in collaboration with employee organisations, drawn up a binding three-year action plan.

The Bank's management development programmes were completed in autumn, resulting in increased focus on the role of manager. The Bank will implement further management measures and new organisational changes in 2012 to continue to attract, develop and retain qualified staff.

## Communications activities

Pursuant to the Norges Bank Act, Norges Bank is obliged to "inform the public of developments in monetary, credit and foreign exchange conditions". In addition, through active communications activities, the Bank seeks to achieve the broadest possible understanding of its conduct of monetary policy, the mechanisms contributing to financial stability and its investment management activities. The Bank places considerable emphasis on responding to growing interest with transparency and predictability.

Norges Bank presents forecasts for the Norwegian economy and for the key policy rate three times a year in the *Monetary Policy Report*. The outlook for financial stability is presented twice a year in the *Financial Stability* report. A report on payment systems is published annually. In addition, the Bank held eight monetary policy meetings in 2011. Three surveys – the lending survey, the regional network report and the survey of inflation expectations – are published four times a year. The Bank also publishes quarterly reports on the Government Pension Fund Global (GPFG).

The public can also subscribe to a text message alert of interest rate decisions and follow news about the Bank on Twitter. The Bank also uses the website Flickr to post and store images from both the present and the past.

In 2011, Norges Bank's timeline was completed and published on the Bank's website. The timeline presents important events in the history of the Bank from 1816 up to the present. Time series for economic variables such as output, inflation and the money supply are also published here.

Norges Bank conducted a total of 14 press conferences in 2011. Of these, eight were related to the Executive Board's monetary policy meetings, two presented the *Financial Stability* reports and four the GPFG quarterly reports. As from 2011, the press conferences in connection with the monetary policy meetings were held at 2 p.m. to coincide with the announcement of the interest rate decision.

The executive management of Norges Bank gave 42 speeches in 2011, of which 11 were published in full text on the Bank's website while the charts used were published for 17 of the speeches. The Bank's executive management is as a rule available for short interviews after speeches.

Norges Bank's website is continuously being developed and, after its redesign in 2008, efforts have been made to enhance user-friendliness. In addition to news reports, the website includes detailed information about the Bank's tasks and electronic versions of publications issued by Norges Bank, excluding NBIM publications. User statistics show an average of 641 000 hits per month in 2011, a decrease from 648 000 per month in 2010. In 2011 Norges Bank developed a new solution for access to the website via mobile devices. In an evaluation of public websites, Norges Bank's website was awarded five out of six stars in 2011.

In addition to the *Annual Report*, online information and the other reports mentioned above, Norges Bank issues the following publications: the journal *Penger og Kreditt* is published semi-annually on the Bank's website, and articles for the English version, *Economic Bulletin*, are added to the annual volume, also published on the website, as they are finalised. Research projects are documented in the *Working Papers* series, of which 23 were issued in 2011. Some of these are later printed as articles in external books and journals. The *Staff Memo* series contains other documentation or reports that form part of the Bank's work on key issues and 22 were published exclusively on the website. Core documents and other important information are translated into English, with simultaneous publication in Norwegian and English in most cases. These include major speeches, press releases, reports, brochures, circulars, monetary policy meeting documents and information to be published on the Bank's website.

## Distribution of costs by main function

Norges Bank distributes costs by main function. The purpose of this is to illustrate total costs for the Bank's various main functions and to increase awareness with regard to cost-effectiveness.

In 2011, costs were distributed among the following main function categories:

- Monetary policy
- Management of the GPFG
- Management of long-term foreign exchange reserves
- Financial stability
- Settlement services
- Purchase, production and distribution of notes and coins
- Other functions <sup>8</sup>

The basis for the cost distribution is operating expenses and operating income in the Bank's internal financial statements, with the addition of depreciation, amortisation and imputed cost of pension benefits <sup>9</sup>. Emphasis has been placed on including expenses and income that provide a picture of the cost of the Bank's ordinary operations. Internal rent has been used instead of depreciation of the building in Oslo as the basis for distribution of costs for the Bank's main building in Oslo. These factors result in deviations from figures for operating expenses and operating income in the annual financial statements.

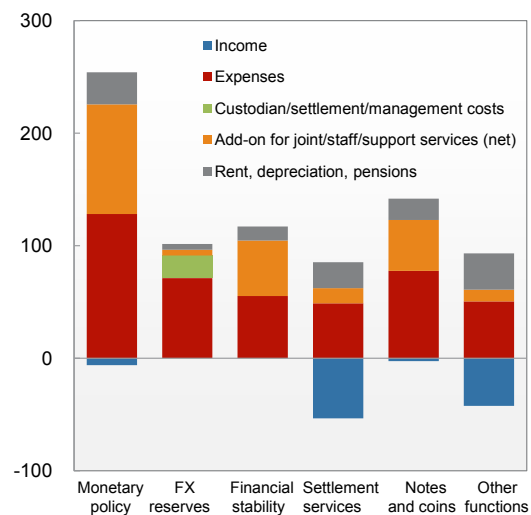
The distribution is based on a cost driver analysis. The distribution keys are set based on judgement, and the results must be viewed accordingly.

Gross costs in 2011 amounted to NOK 3332m and net costs to NOK 688m. The corresponding figures for 2010 were NOK 3800m and NOK 711m. Net use of resources has declined by just over NOK 20m. The reduction is largely the result of a change in accounting policies for cost transfer and activation as from 2011.

Management of the GPFG is by far the most resource-intensive function. Gross costs were NOK 2539m in 2011 and NOK 2962m in 2010. External managers' fees were more than NOK 500 million lower in 2011 than in 2010. Norges Bank's costs related to the management of the GPFG are covered by the Ministry of Finance according to the principle of full cost coverage.

Chart 7.1 shows the distribution of costs excluding the GPFG.

Chart 7.1 Use of resources in 2011 distributed by main function excluding the GPFG (in millions of NOK)



Source: Norges Bank

<sup>8</sup> This includes building operation and services to the government.

<sup>9</sup> Return and interest resulting from the Bank's tasks relating to monetary policy and management of financial wealth are not included.

# Appendix

## Governing bodies, management and organisation

### The Executive Board

**Øystein Olsen**, Chair

Appointed Governor of Norges Bank  
1 January 2011 for a term of up to six years

**Jan F. Qvigstad**, Deputy Chair

Appointed Deputy Governor of Norges Bank  
1 April 2008 for a term of up to six years

**Brit K. Rugland**

Appointed 1 January 2004–31 December 2005  
Reappointed 1 January 2006–31 December 2009  
and 1 January 2010–31 December 2013

**Liselott Kilaas**

Appointed 1 January 2004–31 December 2007  
Reappointed 1 January 2008–31 December 2011  
and 1 January 2012–31 December 2015

**Ida Helliesen**

Appointed 1 January 2010–31 December 2013

**Eirik Wærness**

Appointed 1 January 2010–31 January 2013

**Egil Matsen**

Appointed 1 January 2012–31 December 2015

### Alternates

**Gøril Bjerkan**

Appointed 1 January 2010–31 December 2013

**Espen R. Moen**

Appointed 1 January 2012–31 December 2015

### Employee representatives:

**Jan Erik Martinsen**

Appointed 1 January 2001–31 December 2012

**Petter Nordal** (Alternate)

**Gøril Bjerkehol Havro**

Appointed 1 January 2011–31 December 2012

**Jens Olav Sporastøyl** (Alternate)

### Supervisory Council

**Reidar Sandal**, 2010–2013, Chair

Alternate: **Ola Røtvei**, 2010–2013

**Frank Sve**, 2010–2013, Deputy Chair

Alternate: **Tone T. Johansen**, 2010–2013

**Eva Karin Gråberg**, 2012–2015

Alternate: **Rita Lekang**, 2012–2015

**Runbjørg Bremset Hansen**, 20012–2015

Alternate: **Camilla Bakken Øvald**, 2012–2015

**Tormod Andreassen**, 2012–2015

Alternate: **Beate Bø Nilsen**, 2012–2015

**Morten Lund**, 2012–2015

Alternate: **Torunn Hovde Kaasa**, 2008–2011

**Synnøve Søndergaard**, 2010–2013

Alternate: **Britt Hildeng**, 2010–2013

**Reidar Åsgård**, 2010–2013

Alternate: **Kari-Anne Opsal**, 2010–2013

**Erland Vestli**, 2010–2013

Alternate: **Jan Blomseth**, 2010–2013

**Marianne Lie**, 2010–2013

Alternate: **Lars Gjedebo**, 2010–2013

**Monica Salthella**, 2010–2013

Alternate: **Lars Haakon Søråas**, 2010–2013

**Randi Øverland**, 2012–2015

Alternate: **Anne Grethe Kvernød**, 2012–2015

**Vidar Bjørnstad**, 2012–2015

Alternate: **Hans Kolstad**, 2012–2015

**Tine Sundtoft**, 2012–2015

Alternate: **André Støylen**, 2012–2015

**Ingebrigt S. Sørfonn**, 2012–2015

Alternate: **Solveig Ege Tengesdal**, 2012–2015

### Office of the Supervisory Council

Svenn Erik Forsstrøm, Director

## Executive management

Øystein Olsen, Governor  
Jan F. Qvigstad, Deputy Governor

## Norges Bank Monetary Policy

Jon Nicolaisen, Executive Director  
Amund Holmsen, Deputy Executive Director

### **Department for Market Operations and Analysis**

Kristine Falkgård, Director

### **Economics Department**

Marianne Sturød, Director

### **International Department**

Anne-Berit Christiansen, Director

### **Monetary Policy Department,**

Kjetil Olsen, Director

### **Research Department**

Øystein Røisland, Director

### **Human Resources and**

### **Administration Department**

Ilse Bache, Director

## Norges Bank Financial Stability

Kristin Gulbrandsen, Executive Director  
Birger Vikøren, Deputy Executive Director

### **Cashier's Department**

Trond Eklund, Director

### **Interbank Settlement Department**

Kjetil Watne, Director

### **Liquidity Surveillance Department**

Sindre Weme, Director

### **Regulatory Policy Department**

Arild J. Lund, Director

### **Macroprudential Department**

Ingvild Svendsen, Director

### **Payment Systems Department**

Knut Sandal, Director

### **Research Department**

Farooq Akram, Director

### **Shared Services**

Ragnhild L. Solberg, Director

## Norges Bank Administration

Jannecke Ebbesen, Executive Director

### **Communications Department**

Mette Fossum Beyer, Acting Director  
of Communications

### **Economy Department**

Per Arne Eriksen, Director

### **Facility Services**

Marit Kristine Liverud, Director

### **General Secretariat**

Bjarne Gulbrandsen, Director

### **HR**

Jane K. Haugland, Director

### **IT**

Ola Jan Bjerke, Director

### **Legal Department**

Marius Ryel, Executive Director

### **Security Department**

Arne Haugen, Head of Security

## Internal Audit

Ingunn Valvatne, Head of Internal Audit

## Norges Bank Investment Management

CEO and CIO Allocation Yngve Slyngstad  
Deputy CEO and Chief of Staff Trond Grande

### **Investment, equities**

CIO Equities Petter Johnsen

### **Investment, real estate**

CIO Real Estate Karsten Kallevig

### **Investment, allocation and fixed income**

CIO Allocation Yngve Slyngstad

### **Trading and treasury**

Chief Treasurer Jessica Irschick

### **Operations**

Chief Operating Officer Age Bakker

### **Risk management**

Chief Risk Officer Jan Thomsen

### **Administration and staff**

Chief of Staff Trond Grande



