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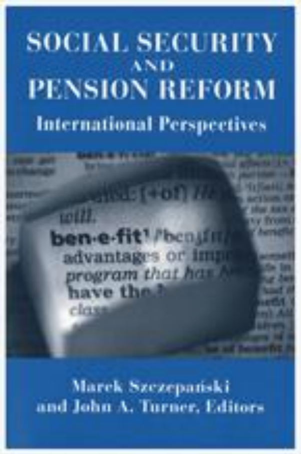

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Because of population aging, many countries have established reserve funds to mitigate the effects of future deficits in their social security programs (Jarrett 2011). According to the OECD, in 2009, 17 of 34 member states had social security reserve funds. They have accumulated a total of $4.554 trillion, of which about $2.540 trillion belonged to the U.S. Social Security Trust Fund (OECD 2011).

The purpose of this chapter is to describe a special reserve fund, the Norwegian Government Pension Fund. Its uniqueness is reflected in both its organizational structure and its principles of accumulation and investment of resources. This fund consists of two parts: Pension Fund-Global and Pension Fund–Norway. In view of a clearly defined commitment to the social security program of the latter, and a general commitment of the former, only the latter is recognized as a reserve fund in the OECD statistics. This chapter, however, mainly focuses on the Global Fund, which is one of the largest investors in the global financial market.

This chapter addresses issues related to the development and the operation of the Norwegian Government Pension Fund Global (GPFG), which the Norwegian government uses to invest funds derived from the extraction of oil. After 15 years of regular fuel revenue receipts and through active investment policy, GPFG became the second-largest pension fund in the world (after Japan) and the first in Europe, with assets of NOK 3.496 trillion ($626 billion, based on $1.00 = 5.58 kroner),

This chapter first provides an overview of Social Security programs in Norway. It then discusses the Norwegian Government Pension Fund, focusing on the Norwegian Pension Fund Global.

ORGANIZATION OF THE SOCIAL SECURITY PROGRAM IN NORWAY

The involvement of the Norwegian government in the organization of social protection of the population began in the late nineteenth century with the establishment of accident insurance for factory workers in 1885. The start of the development of the social security program took place in 1957, and 10 years later an additional mandatory retirement plan depending on the amount of remuneration of labor was implemented. In 1967, social benefits introduced for different groups prior to the Second World War were integrated in a single National Security program (Ambasada Norwegii w Polsce 2010). The current social security program consists of three components (Lovdata 1966, 1998, 2002; Norwegian Labour and Welfare Organisation [NAV] 2012):

1) The National Insurance Scheme, under an act of February 28, 1997;
2) The Family Allowance Scheme, regulated by an act of March 8, 2002;
3) The Scheme for Cash Benefits for Families with Small Children, established by an act of June 26, 1998.

In 2006, the social security reform process began. One of the most important changes was the establishment of a new institution, NAV. This office started its operations on July 1, 2006, and replaced the two previous institutions, Norwegian National Insurance (*Trygdeetaten*) and the Norwegian Labour and Welfare Service (Aetat). NAV's primary objective is to create opportunities for employment, while at the same time protecting the rights to social security benefits (NAV 2007–2009). The organizational structure includes 457 local NAV offices. The first offices were established in the autumn of 2006, while the target number was reached in March 2011.

The social security program is financed by contributions from employees, the self-employed, and employers, and also from government subsidies. The amount of the contribution is determined annually by the Parliament (NAV 2012). In 2012, four rates applied:

1) 7.8 percent of income from employment, paid by workers;

2) 11.0 percent of the income from the self-employed;

3) 14.1 percent of the gross payroll for employers (with no ceiling on earnings);

4) 3.0 percent of other income (e.g. pensions).

The benefits of social security include old-age, survivor's and disability pensions, temporary assistance grants for the chronically ill and those recovering from accidents, care allowances for persons with disabilities, rehabilitation benefits, compensation for accidents at work, benefits for single parents, unemployment, sickness and maternity benefits, medical sickness and maternity allowances, and funeral benefits (NAV 2012).

The right to individual benefits usually depends on the length of membership in the social security program. Most of the benefits, however, are calculated on the base rate, the G value (from *grunnbeløp*), determined annually by the Parliament in May. Since May 1, 2011, this rate amounts to NOK 79,216 (NAV 2011c) ($14,196).

THE PRINCIPLES OF FUNCTIONING AND THE REFORMS OF THE NORWEGIAN SOCIAL SECURITY PROGRAM

Norwegian authorities reformed the social security program, taking effect starting January 1, 2011. The program is currently undergoing a period of transition in which old and new rules operate simultaneously. The most important aspects of the current system and the changes are indicated below.

The Norwegian retirement system consists of three components referred to as pillars. The first pillar is the basic pension received from the social security program (*Folketrygden*). The amount of the benefit depends on the amount of income, the duration of membership in the program and the contribution period, marital status, and whether the spouse receives benefits from Folketrygden. The retirement pension from this part of the system consists of the basic pension (*grunnpensjon*), the supplementary pension (*tillegspensjon*) and/or the extra allowance (*særtillegg*) and the care allowance for pensioners with dependent children and/or a spouse (NAV 2012).

The basic pension is granted to persons with at least three years of membership in the program between the ages of 16 and 66. The amount of the basic pension benefit is determined by the length of the insurance period and is independent of both the amount of income earned during the activity period and the contributions paid into the system during the activity period. A full basic pension is received by members of *Folketrygden* after a minimum of 40 years. If the membership period is shorter, the amount of benefits is reduced accordingly (NAV 2011a). A full basic old-age pension is 100 percent of the base G rate (NOK 79,216 since May 1, 2011) (NAV 2011c).

The supplementary pension (*tilleggspensjon*) was introduced in 1967 with the purpose of maintaining a standard of living after retirement close to the level of the work period (NAV 2012). The amount of the benefit is strictly dependent on income, measured by the average number of pension points, and the qualifying years of contributions. In order to obtain supplementary pension rights, the insured needs to exceed the G rate of the pensionable salary for a period of at least three years, with the G rate being the income threshold above which the pension points are counted. The part of income that exceeds the G rate is divided by this rate. Thus, workers earning twice the G rate receive one pension point. This rule applies to pension points calculated on the basis of pensionable salary not exceeding 6G. For income between 6G and 12G, only one-third is taken into account to calculate the number of pension points. Income exceeding 12G is not taken into account. The average final pension points for determining the supplementary pension is calculated as the average of the 20 best years in terms of pension points (NAV 2012).

The extra allowance (*særtillegg*) is granted to pensioners not entitled to a supplementary pension or if the supplementary pension is less than the *særtillegg*. The right to the basic pension is necessary to obtain the extra allowance. The amount of the allowance is decided by Parliament as a percentage of the basic G in two rates, normal, amounting to 94 percent of G and reduced, which is 74 percent of G (NAV 2010).

The age for receipt of social security benefits in Norway is 67 for both men and women. Workers are allowed to continue work after benefit receipt until age 68 with full pension entitlement. At age 68, however, until age 70, if the annual income of the retired person exceeds twice the rate of G, the pension amount above this level is reduced by 40 percent (NAV 2011a).

The pension reform implemented on January 1, 2011, introduces changes in the retirement age, the principles of calculation and payment of benefits and the possibility of combining an old-age pension with further work. The new, flexible, retirement program is primarily aimed at providing the insured with the following (NAV 2012):

- The ability to receive a retirement pension after age 62, if the insured has acquired adequate pension rights. Everyone is still entitled to receive benefits at age 67.
- The selection of the "retirement standard"—the insured worker decides whether to receive the full old age benefit from their pension account, or a partial benefit: 20 percent, 40 percent, 50 percent, 60 percent, or 80 percent.
- The right to change the "level of retirement" once a year.
- The possibility of combining the entitlements and labor income without reducing the received pension benefit.

In addition, those born after 1962 acquire pension rights according to the following new rules (NAV 2012):

- The amount of the old-age pension depends on all the years in which the income accounting for pension points was obtained, until age 75. Based on the new rules, the contributions of the insured create a pension fund, and the amount of the benefit depends on the accumulated capital value. According to the existing rules, the amount of pension was calculated on the basis of the 20 best years of work and allowed full pension after 40 years of participation in the program.
- The funds accumulated in the pension fund (a notional account, rather than an invested account) are indexed annually by the wages growth indicator for those before retirement, and by that indicator decreased by 0.75 percent for persons receiving a benefit;
- The pension fund grows by 18.1 percent of the insured income in excess of the equivalent of 7.1 G.

Persons born between 1943 and 1953 acquire pension rights and receive benefits in accordance with the existing terms and conditions. Persons born between 1954 and 1962 acquire the rights based in part on new and old rules.

The changes introduced in the Norwegian social security program guarantee a greater freedom as to when, and to what extent, the insured person starts drawing a pension. The changes also allow a person to work and receive an unreduced pension, which helps to increase future benefits by raising retirement savings. Despite the right to receive a pension at age 62, the new rules for calculating entitlements encourage prolonged years of work. The flexibility of pension savings withdrawal also applies to persons born between 1943 and 1953, to whom the regulations from before the reform apply.

The effects of the implemented reforms were evident right when the new regulations were enforced. In January 2011, 13,600 persons under age 67 took the advantage of the possible pension savings withdrawal. In total, in the first quarter of 2011, 17,834 people aged 62–66 opted to receive benefits, of whom 83.5 percent were male (NAV 2011b). About 60 percent of this group remained in the labor market using the possibility of joining work with drawing pension benefits (NAV 2011e). In the first quarter of 2011, NAV paid pensions to 685,226 people, an increase of about 32,000 compared to the first quarter of 2010. In total, the participation of pensioners in the Norwegian community at that time was 13.88 percent (NAV 2011d).

In addition to the social security program, the second pillar, consisting of employee pension plans (*Obligatorisk Tjenestepensjon* [OTP]), was introduced in 2006 as a part of the retirement system reform. The Norwegian OTP is mandatory for both employees and employers. The third pillar covers all additional, optional forms of benefits offered by private pension funds and other financial institutions. The scope of its organizational system, however, is not specified by the legislature.

THE ORIGINS AND DEVELOPMENT OF THE NORWEGIAN GOVERNMENT PENSION FUND

The Norwegian Government Pension Fund has been operating in its present form since January 1, 2006. Its origins, however, date back to the 1960s. It consists of two separate funds: the Government Pension Fund Global (GPFG), which is the successor of the Government Petroleum Fund, and the Government Pension Fund Norway (GPFN), derived from the Social Insurance Fund. The Norwegian Government Pension Fund is owned by the Norwegian Government and the Ministry of Finance.

The current administration of GPFG and GPFN has been entrusted to two institutions, a special unit operating in the National Bank of Norway called Norges Bank Investment Management (NBIM) and Folketrygdfondet (Norwegian Ministry of Finance 2012). Each of these funds was created at a different time and, although together forming the Norwegian Pension Fund, are independent of each other, governed by separate legislation and adopting different strategies.

The GPFN was established in 1967 under the Social Security Act as the Social Insurance Fund (Lovdata 1966). As mentioned above, in 2006 it was converted into GPFN, managed by *Folketrygdfondet*, an independent entity, under an act of June 29, 2007, fully owned by the state (Lovdata 2007). The aim of GPFN is to accumulate and grow savings in the social security program for the purpose of payment of future pension benefits. The initial capital of the GPFN derived from the surplus generated in the social security program since its establishment in 1967 until the late 1970s. Currently, the proceeds to the fund are profits from its investment activities. The total net gains (net of management costs) increase the GPFN assets and no transfers to the state budget or payments of current benefits occur (Norwegian Ministry of Finance 2012). The value of assets held in the fund at the end of 2011 stood at NOK 129.4 billion ($23.19 billion), of which NOK 78.3 billion ($14.0 billion) is in equity securities, and NOK 51.1 billion ($9.2 billion) is in financial assets with fixed income (SSB 2012b). The investment portfolio of the fund shares included 48 Norwegian companies (with a total value of NOK 60.4 billion) and 90 companies in other Nordic countries (with a value of NOK 17.9 billion). Among the debt securities, almost

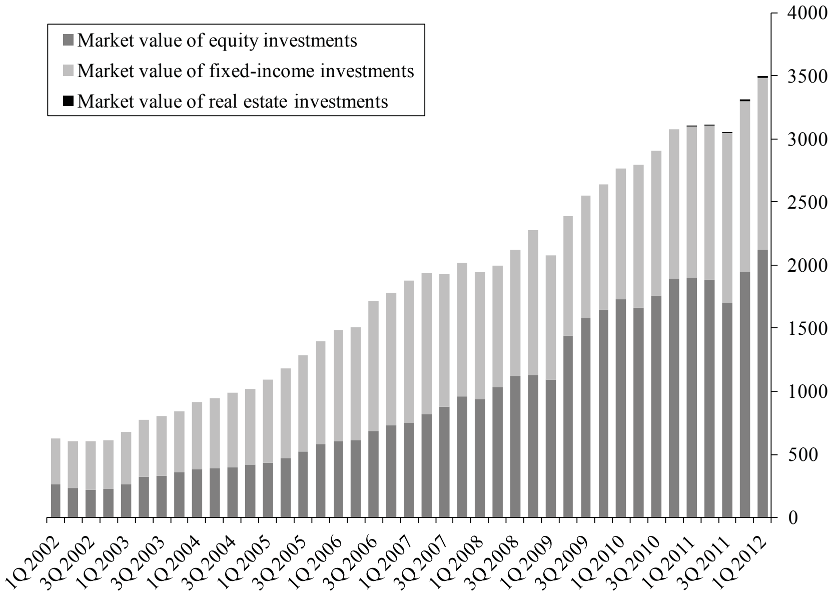
70 percent were corporate bonds of Norwegian companies (worth NOK 35.5 billion); the fund also held government bonds worth NOK 6 billion and foreign debt securities worth NOK 9.6 billion (SSB 2012c). In contrast to the GPFG, the GPFN investment activity is limited to the Norwegian market and the regulated markets of Nordic countries (Finland, Denmark, and Sweden, with the exception of Iceland). GPFG, founded more than 30 years later than the GPFN, is the focus of the remainder of the chapter.

The basis for its establishment was an act in June 1990 that created the Government Petroleum Fund (the Oil Fund) (Lovdata 1990). Through this fund, the Norwegian government accumulated and invested the excess funds from the extraction of crude oil discovered at the end of 1969. Until the establishment of the Oil Fund, the revenues from extractive industries were used for about 20 years for current public expenditure and national debt redemption. In the 1970s, however, it was evident that the revenues from the petroleum sector are indefinite as they relate to nonrenewable resources. To avoid overheating the Norwegian economy and in view of the long-term use of oil wealth, the Norwegian authorities decided to direct one-third of the net income of the state generated by the oil production to a special fund. The first transfer of funds, however, took place only in 1996; the fund received approximately NOK 2 billion in 1996 (Norwegian Ministry of Finance 2012).

After 15 years of regular fuel revenue receipts and through an active investment policy, GPFG became the second-largest pension fund in the world (after Japan) and the largest in Europe. The fund is also the largest shareholder in the European capital market with about 1.8 percent of shares listed on stock exchanges in Europe and one of the largest investors in the world, with approximately 1 percent share in the global capital market (Towers Watson 2011). The value of assets held in GPFG at the end of the first quarter of 2012 amounted to NOK 3,496 trillion ($627 billion). Figure 6.1 shows the market value of the fund on a quarterly basis from 1998 to 2012.

As mentioned above, the predecessor of today's GPFG was the Oil Fund, transformed into GPFG in 2006. From that time, its purpose is not only to support the government in the long-term, sustainable use of revenues from the petroleum sector, but also to multiply these means in order to finance future pension payments in the public social security

Figure 6.1 Government Pension Fund Global Market Value, 2002–2012 (quarterly data in NOK billions)



SOURCE: NBIM, Government Pension Fund Global first quarter 2012, Oslo (2012b, p. 2).

system (OECD 2011). The fund, however, is an instrument for general saving with undefined future liabilities to the social security program or any other social or economic area. It is not an instrument of Norwegian foreign policy, and is not used for the purpose of achieving political or strategic objectives. The functioning of the GPFG (*Statens pensjons-fond – Utland*) is based on three basic principles (Ambasada Norwegii w Polsce 2012):

1) Annual revenues of the fund are derived from the Norwegian state oil production, financial operations associated with the extraction and profits generated by the fund.
2) The transfer of funds to the budget may not exceed an amount equal to the expected rate of return on investment, set at 4 percent per year. With this principle, the government can only

withdraw the profits earned by GPFG without diminishing its capital. In addition, short-term fluctuations in oil and gas prices do not impact the fiscal policy.

3) The fund's assets are invested exclusively outside Norway. This is to ensure the diversification of investments and the reduction of the adverse impact of fluctuations in oil prices on the domestic economy.

Due to the lack of clearly defined social security pension liabilities of the pension fund, as well as the lack of the connections between the fund and the social security program (GPFG revenues are independent of the contributions of the insured), it is not a typical social security reserve fund established in some countries, such as the United States, with the aim of securing future pension payments. As emphasized by the Norwegian authorities, the idea of the GPFG is a long-term, rational management of resources from the oil deposits to benefit both today's and future generations of the residents of Norway (Norwegian Ministry of Finance 2012). According to the forecasts of the Ministry of Finance, in 2020 the market value of the fund will amount to NOK 6.285 trillion ($1.126 trillion) (Norwegian Ministry of Finance 2011). Assuming that at that time Norway will be inhabited by about 5.5 million people (SSB 2012a), the amount per person will exceed NOK 1.1 million ($197,000). At the end of 2011, the fund's value per capita amounted to about NOK 670,000 ($120,000).

THE INVESTMENT STRATEGY OF THE GOVERNMENT PENSION FUND GLOBAL

GPFG is a unique investor considering not only its large asset value, but also its lack of necessity of achieving short-term investment objectives. Its investment policies are designed to take into account the specific characteristics of the fund and the specificity of the markets in which the assets are invested. For this reason, the Ministry of Finance and the National Bank of Norway carry out a continuous review of the fund's investment strategy to develop it in the best direction to increase funds accumulated in the fund and to achieve the desired rate of return at a moderate level of risk. It is the basic principle to be respected by NBIM, the entity responsible for managing the assets of GPFG (Norwegian Ministry of Finance 2010). The real average annual rate of return of the fund for the period 1997–2011 was 2.7 percent and therefore below the 4 percent estimated by the Ministry of Finance. The annual performance of the GPFG is characterized by extremes, from a loss of −23.3 percent to profits of 25.6 percent (Norwegian Ministry of Finance 2012). The Norwegian Government points out, however, that GPFG is based on a long-term investment objective, and the loss-making assets in the investment portfolio have a great potential for growth in the future.

GPFG investment policy has evolved with the growth of its assets (Table 6.1). The first transfers from the state budget to the fund (then *Statens petroleumsfond*) were invested exclusively in government bonds, in accordance with the investment policy of the Norwegian Central Bank. In 1998, NBIM was established—the body responsible for the management of the investment policy of the fund in accordance with the guidelines of the Ministry of Finance. In that year, it was decided to include stocks in the investment portfolio on the condition that they not exceed 40 percent of the fund (Norwegian Ministry of Finance 2012). Nine years later, this limit was raised to 60 percent, and in the subsequent year the Ministry decided to permit real estate investments limited to 5 percent of the portfolio (Norwegian Ministry of Finance 2010).

The diversification of the GPFG portfolio pertains to different categories of investments, as well as geographical dispersion. For the purpose of the investment policy of the fund, the following three regions were determined: Europe, America/Africa, and Asia/Oceania, with the investment limits within each of these regions defined separately for investments in equity and debt securities. So far, they were established, respectively, as 50 percent, 35 percent, and 15 percent for equities, and 60 percent, 35 percent, and 5 percent for investments in fixed income securities (NBIM 2012a). This indicates that more than half of the GPFG assets were located in securities and real estate in Europe. The current financial crisis not only shook the capital markets, but also revealed a number of anomalies and problems in the public finances of certain European countries. The changes observed in global finance in 2008–2010 contributed to the GPFG management decision to change

Table 6.1 Stages of Development of the Government Pension Fund Global Investment Policy

Year	Events
1969	The discovery of oil in the North Sea—extraction since 1971.
1990	The decision of the Norwegian Parliament to set up the Government Petroleum Fund for long-term management of revenues from oil sales.
1996	The first transfer of funds to the Fund in the amount of approximately NOK 2 billion.
1997	The decision of the Ministry of Finance to start investing in equity funds—the fund previously invested only in government bonds.
1998	January 1—the NBIM commencement—NBIM manages the fund on behalf of the Ministry of Finance. The change in the structure of the investment portfolio of the fund—40 percent of the portfolio conversed from debt to equity instruments.
2000	Five emerging markets added to benchmark index.
2002	Corporate bonds included in debt instruments benchmark index.
2004	The establishment of ethical guidelines for the fund's investment plan.
2006	Name changed to: Government Pension Fund Global.
2007	The decision of the Ministry of Finance to increase the limit of investment in equities from 40 percent to 60 percent and the inclusion of small and medium-sized enterprises to the portfolio.
2008	The decision to start investing in real estate to a maximum of 5 percent of the fund's assets. The inclusion of all emerging markets in benchmark index.
2009	Evaluation of ethical guidelines. The share of stocks in the portfolio of the fund has reached the limit of 60 percent in June. The fund reached a record rate of return, 25.6 percent.
2010	Rules for investing in real estate adopted.
2011	The first investments in real estate (located in London and Paris).
2012	A new benchmark for investments in debt instruments. New rules of geographic diversification of investments in equity.

SOURCE: Author's study based on Norwegian Ministry of Finance (2012, pp. 13–39).

the geographical spread of the fund investments by reducing the share of European investment in the fund and increasing its commitment to emerging markets. The category of emerging markets includes 23 countries, among others: Argentina, Chile, Brazil, Mexico, Poland, the Czech Republic, Russia, and Hungary (NBIM 2012a). The new rules of geographical diversification were introduced progressively since 2012, and this process is expected to take about six years.

In addition to the investment guidelines of the Ministry of Finance, the fund management is obliged to comply with the rules developed by the Council of Ethics. The council, operating since 2004, is preparing recommendations for the Ministry of Finance on exclusion from GPFG portfolio of companies operating in the production of weapons, destroying the environment, disrespecting ethical standards, and violating human rights. By the end of 2011, based on council recommendations, a total of 55 companies were excluded, among others: British American Tobacco Plc., Philip Morris International Inc., and Japan Tobacco Inc. (the tobacco industry); Wal-Mart Stores, Inc. (human rights violations); Alliant Techsystems Inc., General Dynamics Corp., and Hanwha Corp. (cluster weapons); and Singapore Technologies Engineering Ltd. (landmines) (Council on Ethics 2012).

THE INVESTMENT PORTFOLIO OF THE GOVERNMENT PENSION FUND GLOBAL IN 2011

In 2011, GPFG assets increased by approximately NOK 234 billion, and at the end of this period, their value amounted to NOK 3.312 trillion. As a result of persisting high oil prices on the world markets, the government receipts transferred to the fund were the highest since 2008 and amounted to NOK 271 billion (SSB 2012b). Table 6.2 presents the basic information on the investment portfolio and the financial performance of GPFG between 2006 and 2011 (since the transformation of the Oil Fund into the Pension Fund).

In 2011, the value of the fund's assets was almost two times higher than in 2006. This value is dependent on transfers from the state budget, rates of return on investments, and changes due to fluctuations in the Norwegian krone (all GPFG investments are made outside Nor-

Table 6.2 Government Pension Fund Global Market Value, Annual Results, and Cash Flows from the State Budget, 2006–2011 (NOK billion)

	2011	2010	2009	2008	2007	2006
Equity instruments	1,945	1,891	1,644	1,129	958	726
Fixed-income instruments	1,356	1,186	996	1,146	1,061	1,058
Real estate investments	11	0	0	0	0	0
Transfer of funds from the budget	271	182	169	384	314	288
Generated profit/loss	−86	264	613	−633	504	124
Change due to fluctuations in krone	49	−8	−418	506	−154	−28
Total net change	234	437	365	257	235	384
Total GPFG value	3,312	3,077	2,640	2,275	2,019	1,784

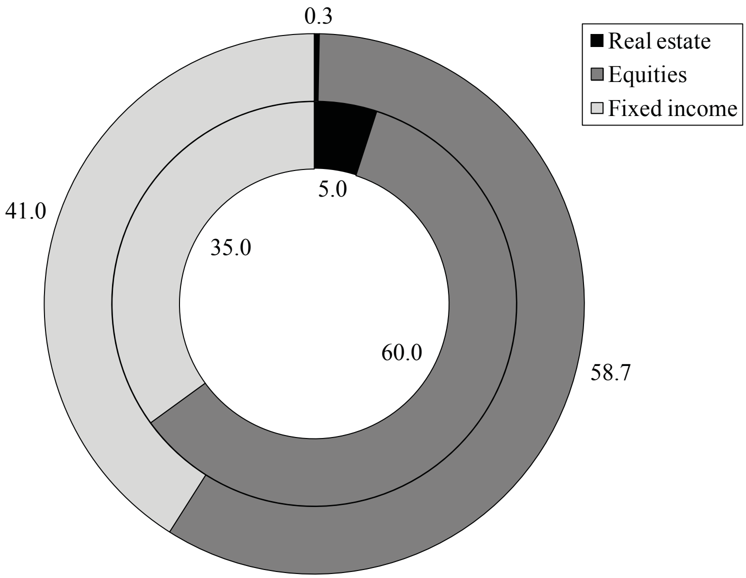
SOURCE: Author's study based on NBIM, *Government Pension Fund Global Annual Report 2006, 2007, 2008, 2009, 2010, 2011.*

way). In the analysed period, the worst result from investing activities was achieved in 2008—the rate of return was −23.3 percent (in international currency) and it was the weakest result since the establishment of the fund.[1] The loss of NOK 633 billion, however, was compensated by record transfers from the state budget (NOK 384 billion) and the weakening of the Norwegian krone against the currencies in which the fund invests (NBIM 2009). At the end of 2011 the loss amounted to NOK 86 billion. With funds from the state budget and the depreciation of NOK the assets increased eventually by NOK 234 billion, but this was the lowest figure since 2005.[2] A negative rate of return in 2011 (−2.5 percent in international currency) was the consequence of negative results from investments in equity; the declines in stock markets in Asia, the United States and Europe generated the loss of −8.8 percent. The rising prices of debt instruments, however, resulted in a 7 percent return on investment in this type of GPFG securities. Comparing these figures with their reference indexes (the FTSE Global for shares, the index prepared by Barclays Capital for bonds) shows that the rate of return on investment in shares is 0.48 percentage points lower than its benchmark, while in the case of bonds, the result is 0.52 percentage points higher (NBIM 2012a).

Based on these figures, the changes to the investment policy of GPFG can be observed in the structure of the investment portfolio, i.e., a gradual increase in the share of stocks. As a result, starting from 2009, the shares occupy a dominant position in the structure of the investment. At the end of 2011, GPFG held shares of a market value of about NOK 1.945 trillion (an increase of NOK 54 billion compared to 2010), which accounted for 58.7 percent of total assets, slightly below the permissible limit of 60 percent of the investment in such instruments (see Figure 6.2). At the same time, 41 percent of the GPFG assets were invested in the fixed income securities, significantly exceeding the 35 percent limit adopted for the strategic investment portfolio. The market value of debt instruments has increased over 2011 by NOK 170 billion to the level of NOK 1.356 billion (NBIM 2012a).

In 2011, the GPFG investment portfolio included the first real estate investment. In April 2011, the management of the fund finalized

Figure 6.2 Strategic and Actual Structure of the Government Pension Fund Global Investment Portfolio, 2011 (%)



SOURCE: Author's study based on NBIM (2012a, p, 14).

the purchase of a 25 percent stake in the Crown Estate's Regent Street in London, with a value of NOK 4.2 billion (approximately GBP 452 million). Three months later, the fund acquired a 50 percent interest in 7 properties located in Paris and the surrounding area with a total value of NOK 5.5 billion (EUR 702.5 million). By the end of the year, the involvement in real estate had increased by another 2 buildings located in London at the Regent Street and three in Paris. In total, GPFG held shares in 13 buildings (114 premises), primarily office and retail space. The total market value of these investments at the end of 2011 was approximately NOK 11 billion, which accounted for only 0.3 percent of the value of the investment portfolio with an acceptable level of 5 percent. Due to the transaction costs, the return on investment in real estate in 2011 was negative and amounted to −0.79 percent (−4.37 percent in international currencies) (NBIM 2012a).

The Ministry of Finance plans to gradually increase the fund's involvement in the real estate market to reach the 5 percent threshold in 2020. Given the projections on the value of the fund's assets (Norwegian Ministry of Finance 2011), about NOK 250–300 billion of GPFG assets is expected to be invested in the European real estate market in the target year.

At the end of 2011, GPFG held stocks, bonds, and real estate shares registered in 68 countries (Norwegian Ministry of Finance 2011). Table 6.3 shows the capital structure of the GPFG investment portfolio in terms of geographic diversification in 2011. About 50 percent of its shares were listed on the European markets, 35 percent on the markets in the Americas, Africa, and the Middle East, and 15 percent in Asia and Oceania. The rates of return on investments in these regions (measured in international currency) were, respectively, −12.1 percent, −2.4 percent, and 15.5 percent.

Analysing the fund's commitment to national stock markets of individual countries (Table 6.3), the largest share (30.3 percent) of the GPFG investment portfolio was placed in the securities listed on the markets in the United States (2,041 investments with a total value of more than NOK 588.4 billion), followed by the British market (16.3 percent of the GPFG portfolio, 397 investments worth NOK 317.7 billion), France (6.9 percent), Switzerland (6.3 percent), Germany (5.8 percent), and Japan (5.6 percent). The investments in securities of Japanese companies accounted for 40 percent of the total value of shares purchased in the Asia-Pacific (NBIM 2012c). As a result of the earthquake and tsunami that hit Japan in March 2011, their value has decreased by 18.7 percent. More negative returns were received on investments made in the four countries considered to be the largest emerging markets, i.e., India (−34.4 percent), China (−21.8 percent), Russia (−19.5 percent), and Brazil (−10,1 percent) (NBIM 2012a).

At the end of 2011, the fund held securities issued by 8,005 companies, while in the previous year this number was equal to 8,496. According to the investment policy of the Ministry of Finance, the fund is not allowed to exceed 10 percent of the shareholding of one company. In the analysed period, the highest share was recorded in the Irish company Smurfit Kappa Group, in which the fund held 9.6 percent of shares worth NOK 773 million. In total, the participation of the fund exceeded 5 percent in 53 companies (17 companies in 2010). The 10 largest investments in equity securities included companies from Switzerland, the UK and the United States (see Table 6.4) with an oil sector company, Royal Dutch Shell Plc, on the top of the ranking, as GPFG acquired 2.2 percent of its shares worth nearly NOK 31 billion (NBIM 2012a).

The fund's investments in fixed income securities include bonds, inflation-indexed bonds, corporate bonds, securitized debt instruments and bonds issued by public entities such as regional authorities or state-owned enterprises. The GPFG debt investment portfolio in 2011 was dominated by government bonds (46 percent), followed by securitized debt instruments (18 percent) and corporate bonds (14 percent). The fund had a total of 5,215 series of debt securities issued by 1,404 entities, while in the previous year it was a series of 8,659 issued by 1,686 entities. Ninety-four percent of these investments were denominated in Euros, U.S. dollars, British pounds, and Japanese yen (NBIM 2012a).

CONCLUSION

GPFG is one of the largest investors in the global capital market. A characteristic feature of its investment activity is a long-term approach to investment. The main idea of the fund's management is growing the GPFG assets for future generations. Such an investment objective en-

Table 6.3 GPFG Investments in Equity in the Global Capital Market, 2011

Region/country	Investment value (NOK million)	Number	Region/country	Investment value (NOK million)	Number
Europe	966,343	1,567	Africa	9,564	89
Austria	6,119	28	Egypt	750	31
Belgium	16,505	44	Morocco	33	1
Cyprus	111.6	3	South Africa	8,781	57
Czech Republic	903	4	Asia	244,624	3,481
Denmark	18,300	36	China	27,235	1,016
Faeroe Islands	8.9	1	Hong Kong	26,030	327
Finland	15,688	44	India	10,365	120
France	136,215	162	Indonesia	4,427	15
Georgia	56,646	1	Japan	109,633	1,267
Germany	112,797	140	Kazakhstan	174	3
Greece	2,066	29	Malaysia	5,993	79
Guernsey	280	5	Philippines	1,619	26
Hungary	1,407	6	Singapore	7,243	102
Ireland	4,509	25	South Korea	28,856	92
Italy	34,941	118	Taiwan	19,554	401
Jersey	34.9	1	Thailand	3,495	33
Lithuania	1.6	1	Latin America	41,881	174
Luxembourg	431	3	Brazil	33,308	98
The Netherlands	37,745	56	Cayman Islands	10.5	1
Poland	5,844	48	Chile	3,141	33

Portugal	6,681	23	Colombia	367.7	8
Russia	25,246	69	Mexico	4,754	30
Spain	45,077	75	Panama	10	1
Sweden	48,714	85	Peru	290.1	3
Switzerland	121,811	103	Middle East	4,005	73
Turkey	6,936	57	Bahrain	454	1
Ukraine	152.8	3	Israel	3,342	65
Great Britain	317,758	397	United Arab Emirates	209.1	7
North America	641,671	2,333	Oceania	32,646	288
Bermuda Islands	56	2	Australia	31,830	269
Canada	53,151	290	New Zealand	815.4	19
USA	588,464	2041			

SOURCE: Author’s own study based on NBIM (2012c, pp. 1–46).

Table 6.4 The Largest GPFG Investments in Equity Securities, 20011

Issuing entity	Country	Value of shares held (NOK billion)
Royal Dutch Shell Plc	Great Britain	30.983
Nestlé SA	Switzerland	25.346
HSBC Holdings Plc	Great Britain	19.583
Novartis AG	Switzerland	19.281
Vodafone Group Plc	Great Britain	18.858
BP Plc	Great Britain	17.277
Exxon Mobil Corp	United States	16.901
Roche Holding AG	Switzerland	16.279
Apple Inc	United States	16.027
GlaxoSmithKline Plc	Great Britain	15.775

SOURCE: Author's own study based on NBIM (2012a, p. 43).

ables the fund management to focus on prospective investments with above-average returns in the future instead of achieving short-term results. The current financial crisis and the collapse of the capital markets resulted in impairment of investments for many investors. At the same time, GPFG consistently implemented its investment objective by acquiring low-priced shares with a potential for growth in a long-term perspective. For instance, in the second half of 2011, GPFG allocated NOK 150 billion to the purchase of shares in the European market.

Establishing the Government Petroleum Fund and then converting it into a Pension Fund is a testimony to the rational management of Norwegian wealth. Although GPFG has no clearly defined obligations to the social security program, it is stressed in any document governing the operation that it was founded for the benefit of future generations. It is undoubtedly a financial, as well as social, success.

Notes

1. The GPFG investments in international securities are not converted into kroner in connection with financial reporting and are not hedged against moves in the krone. Changes in the krone exchange rate do not affect the fund's international purchasing power. Consequently, the return is generally measured in international currency, a weighted combination of the currencies in the fund's benchmark indices for equities and bonds. This is known as the fund's currency basket and consisted of 35 currencies at the end of the first quarter of 2012 (NBIM 2012b).
2. In 2011, the Norwegian krone weakened by 1.9 percent against the British pound, 2.7 percent against the U.S. dollar, 8.2 percent against the Japanese yen, and strengthened by 0.7 percent against the euro. The fund held 83 percent of the investments in these currencies.

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