The Report on Energy Stocks in the Government Pension Fund Global

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Recipient: Norges Bank

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On 12 June, the Storting deliberated Meld. St. 14 (2018-2019), *Energy Stocks in the Government Pension Fund Global*. The report proposed omitting equity investments in companies classified as exploration and production companies from the benchmark index and the investment universe for the Government Pension Fund Global (GPFG) in order to reduce overall oil price risk in the Norwegian economy. It was proposed, at the same time, to ask Norges Bank to review its efforts relating to climate risk in the Fund. The Storting endorsed these proposals, cf. Innst. 339 S (2018-2019).

Exploration and production companies

In the report, the Ministry of Finance noted that the remaining petroleum resources primarily take the form of future tax revenues from oil companies' operations on the Norwegian continental shelf and revenues from the state's direct financial interest in oil and gas fields. Net profit taxation and field interests imply that the state's revenues will, as a general rule, follow the profitability of upstream activities. Not investing the GPFG in exploration and production companies may serve to reduce the overall risk associated with this type of activities in the Norwegian economy.

In assessing which companies to omit from the GPFG, the Ministry of Finance referred, in the report, to the classification made by the Fund's equity index provider, FTSE Russell, of individual companies into various subsectors. By applying the index provider's classification of companies as belonging to subsector «0533 Exploration and Production», the Fund's investment universe can be defined to omit exploration and production companies on an ongoing basis, including upon corporate events, IPOs and changes in companies' activities over time. It was noted, at the same time, that such classifications are based on an element of discretionary assessment on the part of the index provider. This includes, *inter alia*, assessments as to what constitutes the main activity of companies, but also assessments as to the number of subsectors companies shall be classified into and thereby how narrowly defined these subsectors shall be.

The Ministry of Finance noted in the report that FTSE Russell is planning certain changes to its company classification with effect from 1 July 2019, including a more fine-meshed division of the companies currently assigned to subsector «0533 Exploration and Production». The most recently available information from FTSE Russell suggests that this subsector will be abolished with effect from 1 July 2019, although it will predominantly be continued as the subsector «60101010 Oil: Crude Producers».[1] However, some of the companies in the current subsector «0533 Exploration and Production» will from that same date, according to the information from FTSE Russell, instead be classified as belonging to the new subsector «60101020 Oil Refining and Marketing».

In the report, the Ministry of Finance stated that it will, in consultation with Norges Bank, establish rules for the phaseout of exploration and production companies from the GPFG's benchmark index and investment universe. Norges Bank is therefore requested to assess which subsectors will, based on FTSE Russell's changes with effect from 1 July 2019, encompass exploration and production companies in the current subsector «0533 Exploration and Production», as well as a time schedule for the phaseout of the equity investments in exploration and production companies from the Fund's strategic benchmark index and investment universe. The Ministry will, based on the Bank's assessments, revert to Norges Bank with proposals for specific amendments to the provisions in the management mandate for the GPFG and a plan for the phaseout of exploration and production companies from the Fund's strategic benchmark index and investment universe.

It is requested that Norges Bank's assessments be submitted to the Ministry of Finance by 13 September 2019.

Climate risk

The objective for the investments in the GPFG is to achieve the highest possible return, given an acceptable level of risk. The Fund shall be managed responsibly within the overarching financial objective. As part of its risk management of the investments in the Fund, Norges Bank shall seek to capture relevant risk factors. The Ministry of Finance has in the management mandate for the GPFG stipulated, *inter alia*, limits on, and requirements for the management, measurement and control of, various types of risk, and has also required responsible investment to form an integral part of the management of the Fund.

Climate risk is one of several financial risk factors which need to be addressed in the management of the GPFG. The Climate Risk Commission (NOU 2018: 17, *Climate Risk and the Norwegian Economy*) notes that climate risk arises as the result of uncertainty, since we do not have full knowledge of the various implications of climate change, climate policy and climate-related technological development. It was noted in the report on energy stocks in the GPFG that climate risk may have an impact on several of the companies in which the GPFG is invested.