



NORGES BANK
INVESTMENT MANAGEMENT

2014-2016 STRATEGY

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OUR MISSION IS TO SAFEGUARD
AND BUILD FINANCIAL WEALTH
FOR FUTURE GENERATIONS

INTRODUCTION

Our strategy for 2014–2016 continues the direction set in the previous strategy for 2011–2013 and aligns with our goal to secure a high long-term real return of the fund. We aim to achieve this goal with an acceptable risk, as a responsible investor, and through an efficient organisation. Our ability to invest for the long-term depends on trust in the way that we manage the fund. A transparent management of the fund will help achieve this.

THE STRATEGIC DIRECTION FOR THE NEXT THREE YEARS:

- We will manage the economic and systematic drivers of real return in the fund.
- We will focus on the long-term risks to the purchasing power of the fund.
- We will be a global leader in responsible investment.
- We will develop a winning team of talented employees.
- We will be professional, accountable and transparent in our management.

LONG-TERM REAL RETURN

The fund was established to underpin long-term considerations when phasing petroleum revenues into the Norwegian economy. Our mission is to safeguard and build financial wealth for future generations. Long-term, sound management of the fund helps ensure that both present and future generations can benefit from Norway's petroleum wealth.

We manage the fund on behalf of the Norwegian government with an objective to secure the highest possible real return with an acceptable risk. The fund is not dedicated to finance any specific future liabilities, and the probability of large withdrawals from the fund is limited. This makes the fund truly long-term. The fund is currently one of the largest single-owner funds in the world with assets of more than 5,000 billion kroner.

Key decisions on fund strategy are anchored in the Norwegian Parliament. Our investment mandate is laid down by the Ministry of Finance on the basis of the Parliament's deliberations. The mandate defines the investment universe and the fund's strategic reference index.

The strategic reference index expresses a set of broad market exposures. It is based on widely used and publicly available indices to ensure transparency and tractability. The fund's long-term real return will be determined by developments in the broad markets as outlined in the reference index, and the specific constraints in the investment mandate. The key constraints are an investment universe limited to public investments in fixed-income and equity and private real estate, a set asset allocation and a narrow scope to deviate from the strategic reference index. High demands on public transparency and specific cost restrictions may put additional constraints on our management of the fund.

We advise the Ministry of Finance on fund strategy. Our advice is directly linked to the overall objective for the fund as we manage it, and does not take account of the macroeconomic situation or the overall wealth position of Norway. The overall objective of the fund may over time be better served if a larger share of the fund is invested in assets with income streams that grow in line with the global economy. We will prepare the organisation for a change in this direction.

Our investment strategies are founded on academic insight, empirical evidence and practical experience

from financial markets. We seek to diversify across asset classes, countries, sectors, companies and strategies to reduce risk in the fund. We seek to exploit time-variations in the return and risk properties of different asset types. We conduct in-depth analysis to add value and focus on underlying economic fundamentals.

We seek to capitalise on the fund's unique combination of characteristics. We are a large, global investor with a long investment horizon. The sheer size of the fund presents opportunities, but we also acknowledge that not all strategies are worth pursuing given the size, the objective of the fund, and the restrictions in our investment mandate. We invest globally, are measured in a basket of global currencies, and believe that the fund in principle should be invested as broadly as possible, in all countries and markets. We aim to improve the trade-off between the fund's expected long-term real return and risk, and believe that short-term fluctuations in returns may provide attractive investment opportunities. We receive regular inflows and can increase our investments in risk assets and provide liquidity when other investors' risk capacity or liquidity is constrained.

Our investment strategies are grouped into three broad categories: fund allocation, portfolio management and securities selection, and this will be reflected in how we structure our organisation.



FUND ALLOCATION

We will broaden the fund's exposure to different sources of return, and seek to exploit time-varying investment opportunities.

Fund allocation aims to improve the fund's exposure to broad markets and sources of return, in both the medium and the longer term. We seek to determine, diversify and dynamically manage the different sources of real return and exploit economic and systematic risk premia.

The starting point for our management of the fund is to construct a tailor-made reference portfolio. We will continue to develop and refine alternative weighting schemes to support the long-term objective of the fund. We will strengthen our capacity to undertake economic analysis, and seek to improve diversification across different sources of economic risks. We will further refine the fund's exposure to sources of systematic risk.

In the reference portfolio we choose securities, instruments and markets from a wider opportunity set than used in the strategic reference index, to capture a greater share of the global market portfolio. New frontier markets will be added to our equity investments, and the scope of our fixed-income investments will be widened to include additional currencies.

Investment opportunities change over time. Additional markets become investable, new investment opportunities emerge, and the price of risk varies. The fund's overall exposure to different markets and sources of risk and return has to be managed dynamically. Investing with a truly long-term horizon enables us to exploit time-varying investment opportunities. We will deepen our insight and build expertise to further develop our dynamic allocation framework across assets, countries, currencies and risk premia.

■ Fund allocation aims to improve the fund's exposure to broad markets and sources of return.

We will further develop our funding structure of absolute return strategies. These strategies will be expanded in size and scope from the investment today in environmental portfolios, frontier markets, and listed real estate and infrastructure. The macro driven real return portfolios will be expanded.


We aim to build a global, but concentrated, real estate portfolio. Our strategy is to focus our investments in a limited number of large global cities, where we invest in core retail and office properties. Our US investments will be concentrated in New York, Washington D.C, Boston and San Francisco. In Europe, investments outside London and Paris will be selectively extended. In the course of the strategy period we will also consider investment opportunities in global cities outside Europe and the US. We will continue to capture globalisation through investments in global distribution networks. We expect to invest one percent of the fund each of the next three years in the private real estate markets.

PORTFOLIO MANAGEMENT

We will expose the fund to broad markets and risk factors, emphasise low-cost implementation, and use our asset base to provide liquidity to the market.

In recent years there have been a number of changes to the investment strategy, such as increased investments in less liquid markets, management of systematic risks, a tailor-made reference portfolio and a more dynamic allocation. These changes have made index replication a less suitable strategy.

We will implement the targeted market exposure, balancing transaction cost, risk, and return considerations. We will expand our investments in new market segments, and look for relative value opportunities.

 We will implement the targeted market exposure, balancing transaction cost, risk and return considerations.

We maintain a strong focus on minimising trading costs as low costs over time will have a large impact on returns. We expect inflow to the fund to remain considerable, and a key part of our assignment is to invest this capital efficiently. Investments in additional currencies and development of currency allocation strategies will also require that we expand our foreign exchange trading capabilities.

Liquidity-providing strategies can generate returns in less liquid segments of the market such as credit, smaller companies and emerging markets. We will aim for integration between portfolio managers and traders.

Efficient use of our holdings through securities lending is an integrated part of our management. We will expand our lending activities in size and scope. The infrastructure needed to lend securities in new markets and segments will be developed.

Our real estate investments to date have primarily been implemented through joint venture agreements. We will prepare the organisation for management of fully owned properties and a more active role in the development of our properties. Larger ownership stakes in listed real estate companies and public-to-private transactions will be considered.

SECURITIES SELECTION

We will continue to build specialist expertise and conduct comprehensive and thorough analysis of company fundamentals to identify investment opportunities, understand underlying risks, and be an active owner.

While we achieve diversification at the fund level by investing in a broad range of markets and segments, our securities selection strategies are concentrated on markets and sectors where we believe the potential to add value to be the greatest.

Fundamental analysis forms the basis for our securities selection. We aim to increase the scope and depth of both equity and credit analysis. We will double the number of companies under deep analysis to 1,000. We will expand the sources of information, and increase the forecasting horizon and scope. Increased credit research capacity should enable us to explore investment opportunities in new segments of the credit markets, and combining our efforts in equity and credit research will ensure coverage of the companies' full capital structure.

Securities selection is done by specialist portfolio managers who run portfolios with a limited number of holdings within fairly narrow segments. We will increase the number of specialist sector portfolio managers to 50. Concentrated portfolios are encouraged, to allow for high conviction, long-term investment focus, and thorough in-house fundamental research. Two third of our larger investments will be in European companies.

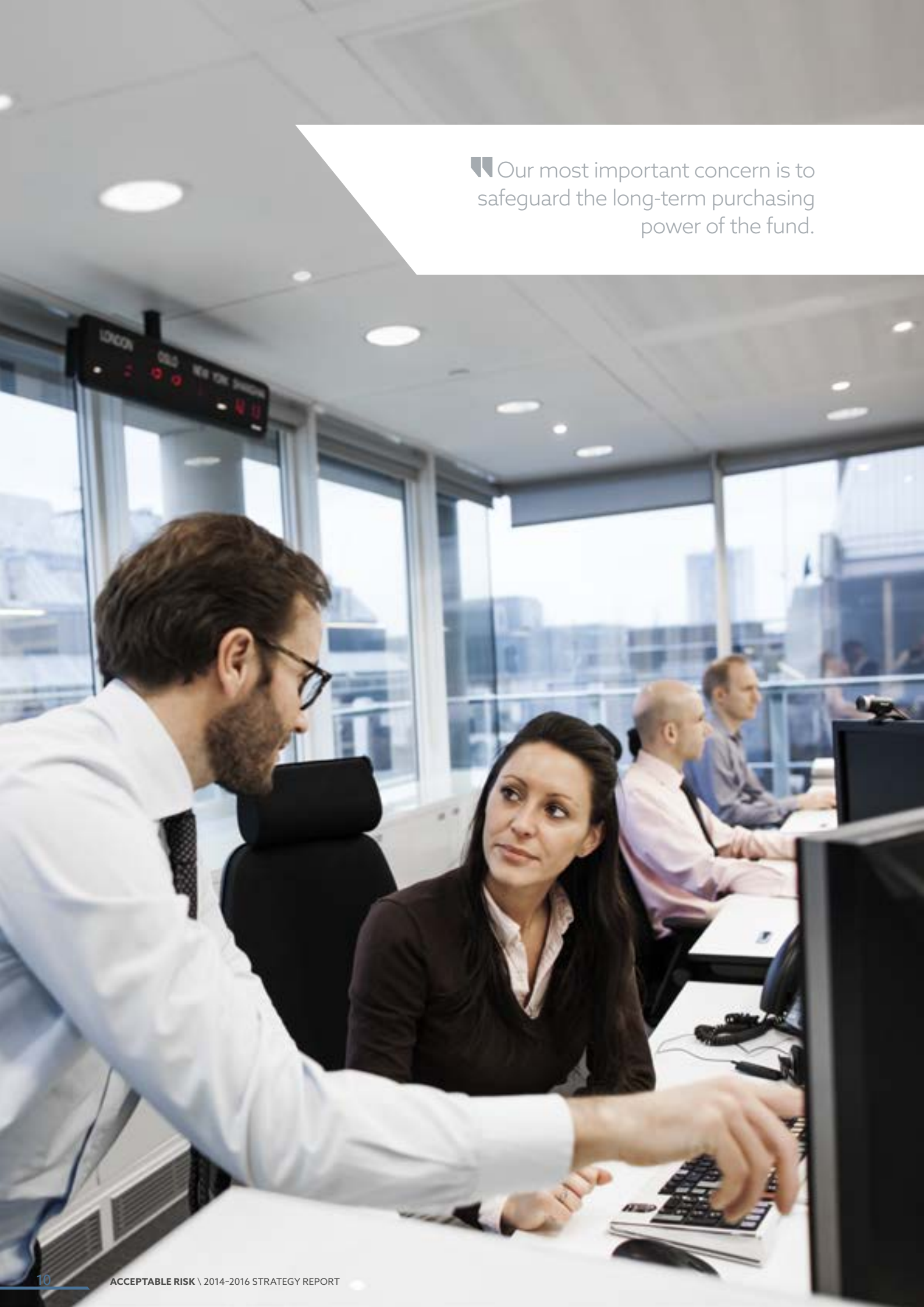
The fund's long-term horizon lends itself to a strategy where we serve as an anchor investor. The fund is in a good position to provide capital in special situations such as in relation to initial public offerings, secondary offerings and capital restructurings. We will use these opportunities to

build larger ownership stakes in selected companies. We expect the number of significant holdings, with more than five percent ownership, to increase to 100 by 2016. We will further develop our absolute return portfolios in environmental, real estate, and infrastructure investments. We will establish cross asset portfolios in selected sectors.

With more than 8,000 companies in the fund, we are mindful that we cannot cover all companies in depth. External managers may facilitate a move into new markets and segments, within both fixed-income and equity, supporting our overall strategy of a truly global, diversified portfolio. We use external equity managers for the majority of our emerging markets investments and for all our investments in frontier markets. External managers will also be used to complement our internal efforts in specific strategies such as investments in smaller companies and environmental mandates. The share of the fund managed by external managers will be targeted at 5 percent as the fund's investments in emerging markets rise, and we expect 100 external mandates by 2016.

■ Fundamental analysis forms the basis for our securities selection.

In our real estate portfolio, we continue to prioritise large equity investments in high quality assets. Investment opportunities in real estate are evaluated based on in-depth analysis of the assets' expected net cash flow after tax and costs. Our real estate investments will require in-depth knowledge and a local presence, and we will strengthen our market research. Due diligence covers market, financial, legal, tax, operational, technical, insurance and environmental considerations, and will be strengthened as we invest in fully owned properties.



“Our most important concern is to safeguard the long-term purchasing power of the fund.”

ACCEPTABLE RISK

We will assess long-term risks to the purchasing power of the fund through an increased focus on future income streams from our investments, and will take a risk-based approach to safeguard our investments.

The fund's objective determines the way we evaluate and manage risk. Our most important concern is to safeguard the long-term purchasing power of the fund. We will expand our capability to assess long-term risks, expected income streams and extreme market conditions. Different dimensions of market risk, such as equity, credit, currency and macro risk are important, but not the only dimensions of risk, our global portfolio is exposed to. To secure an acceptable level of risk in our management of the fund, operational, legal and ownership risk are an integrated part of our risk assessment.

We will enhance our capacity to evaluate changes in market dynamics and economic variables that have the potential to erode the long-term purchasing power of the fund. The fund's long-term real return will be sensitive to persistent shifts in macroeconomic variables and industry structures.

The fund's investments in bonds, equities and real estate generate income in the form of coupons, dividends and rents. We will focus on the risk to the underlying value of our investments and the robustness of the expected stream of future cash flows. We will develop models to increase our understanding of the dynamics of these income streams and how they respond to changes in economic variables. This risk analysis will utilise our analytical insights from security selection. Cash-flow-based analysis will be supplemented with analysis of diversification properties, and risk measures less sensitive to short-term movements in market prices.

The tail risk in extreme financial environments and periods of high economic uncertainty will be given special attention. We will combine the insight we gain from our risk models, the historical and implied pricing structures, with qualitative judgement assessing the likelihood of extreme movements in asset prices.

The reference portfolio has become an important tool in the management of the fund. We will assess the risk-return characteristics of the reference portfolio and how it impacts the overall risk-return profile of the fund. Particular attention will be given to the combined exposure to various risk factors and the relationship between them as these risks tend not to be normally distributed, and standard metrics for risk-adjusting expected returns are less well-suited. We will ensure a robust and scalable platform for the reference portfolio.

We safeguard our investments, and prioritise issues that have the greatest impact on the fund, integrating operational, legal and ownership risk considerations into daily operations. We monitor our daily performance and incidents systematically to avoid unwanted events, learn from mistakes and identify potential risks. We will further strengthen and expand our internal control function to support efficient supervisory oversight.

Strong regulatory, investment and internal compliance are essential to fulfil our management assignment. Regulatory compliance will be strengthened in parallel with investments in new jurisdictions, in less mature markets, and implementation of new structures. We will strengthen our capacity to analyse and monitor the financial infrastructure, market regulation and tax regimes to pursue our interests and meet regulatory requirements. Fraud prevention, detection measures, and conduct of business will be given increased attention in our internal compliance.

RESPONSIBLE INVESTMENT

We will be a global leader in responsible investment, contribute to international standards and principles, integrate ownership issues in the investments process and strengthen the risk monitoring of the portfolio.

The long-term return depends on sustainable development in economic, environmental and social terms. Responsible investment and active ownership are important priorities in our management of the fund. We aim to be at the forefront of global efforts toward responsible investment. We engage in active ownership to enhance returns and to manage our global and diversified portfolio within an acceptable level of risk.

We will contribute to the development of international standards and principles relevant to the fund's interests. UN Global Compact, the OECD Principles for Corporate Governance, and the OECD Guidelines for Multinational Enterprises are the starting point for the development of standards on corporate governance and responsible business conduct.

Well-functioning financial markets are essential to the objective of the fund. Sound regulations and consistent enforcement are prerequisites for well-functioning markets. We will contribute to the development of such rules and regulations through direct interaction with regulators and other stakeholders.

“ We engage in active ownership to enhance returns and to manage our global and diversified portfolio within an acceptable level of risk.

In order to achieve results, our ownership activities need to be consistent and predictable. We will further develop our set of principles for responsible investment. These principles will lean on internationally recognised standards. In key areas we will formulate position papers and expectation documents to positively influence market practices. We will support academic research on the relationship between long-term financial returns and environmental, social and governance issues.

As a long-term shareholder with a global portfolio, we work to ensure sound corporate governance and board accountability. Our ownership efforts will continue to be principles-based, and priority will be given to areas of material risk. As a minority shareholder, we work to ensure equal treatment of shareholders and strengthen shareholder rights to protect the value of our



investments. Our priorities need to be recognised by co-investors and other minority shareholders. We will expand our global network with peers and other international institutions. We will focus more on emerging and frontier markets as these may entail particular ownership challenges.

Voting is our primary means to exercise ownership rights. Our goal is to vote at all company general meetings in line with our voting principles. The number of companies where we assess the issues in detail will increase. We will make our voting intentions public before the annual shareholder meetings to increase transparency, and encourage initiatives to strengthen the vote execution chain.

Direct company interaction will concentrate on large holdings by value or ownership share. Our responsible investment work is integrated into the investment process, and relevant information for our 1,000 largest holdings will be readily available to all our portfolio managers. Environmental, social and governance issues will be raised as agenda items at company meetings.

The number of large ownership positions in the portfolio will increase. An increased board interaction will ensue for our 100 largest holdings, and in special situations. We will expand our involvement in the board nomination process in companies where we have material holdings. Where applicable, we will do this through membership of nomination committees, and in other instances through direct dialogue with the chairman of the board. We will use our Corporate Governance Advisory Board to support our work on board nomination and governance issues.

We manage our global and diversified portfolio within an acceptable level of risk. We will continue to monitor the portfolio and analyse relevant and material risk factors at country, sector and company level. We analyse common risk factors

across sectors independently of geographical location. Companies are analysed on their adherence to international principles and sector-specific standards.

We will strengthen the risk monitoring of our holdings, and develop our criteria for investability. There may be countries, sectors and companies we choose not to invest in due to sustainability issues. There may also be situations where we decide to divest after other initiatives have failed. We will be prepared for a new role in relation to the exclusion of companies breaching a minimum standard of ethical conduct.

Environmental considerations are an integrated part of our real estate investment activities. We work to improve water and energy efficiency as well as waste management at the properties we invest in.

We will continue our work on children's rights, water management, climate change, well-functioning markets, equal treatment of shareholders, and board accountability. New areas of focus may be added towards the end of the strategy period. We will give priority to industry specific initiatives where we see challenges which may impact our long term return.

Environmental related mandates in equity and bonds are set to increase in size and scope. The investments will increase to 50 billion kroner and be diversified across renewable energy, energy efficiency, water and waste management, and pollution control. The mandates will be managed by both internal and external managers and we will strengthen our environmental investment team. We will report on these mandates as a dedicated allocation and outline risk and return separately.

EFFICIENT ORGANISATION

We will improve the organisation through talent development, recruitment to our investment areas at our international offices, and enhanced support solutions for investment decisions.

Our core values, excellence, innovation, integrity, and team spirit underpin our culture and how we operate. A high level of expertise and efficiency is expressed through excellence and innovation. A culture characterised by respect, trust and collaboration is represented by integrity and team spirit.

“Our employees are our most valuable assets.

We are a knowledge-based organisation and operate in a global, highly competitive and constantly evolving market. Our employees are our most valuable assets. A key objective ahead is to develop talented employees, through tailored development and training. We will reward a global mindset, and an eagerness to perform. We will evaluate our employees based on their performance, and encourage our employees to compete as a winning team.

Growth in assets under management and new types of investments will require additional resources and new skills. We will build the organisation from a diverse talent base. We hire for potential, and will recruit both young talents and more experienced specialists. We will increase the number of women at all levels in the organisation.

We expect the organisation to grow to 600 employees over the strategy period, including 200 in our real estate organisation. The majority of new recruitments will be investment personnel at our international offices, and we expect that more than half of our employees will work at our international offices by 2016.

Our governance model is built on clear delegation, well-defined roles and responsibilities, segregation

of duties and effective systems for control and quality assurance. We will continue our drive to establish common processes and to improve communication, collaboration and information sharing across departments and offices.

The management of our real estate investments requires a different governance structure than public market investments. Each investment may require a tailor-made investment structure. We expect to take a more active role in the development and management of the properties we own, and investing in real estate is resource-intensive. Experience so far suggests that the potential to exploit synergies between our real estate investments and our public market investments is limited. We will organise real estate as a separate entity, and strengthen the investment decision structure.

We aim to continuously improve the organisation's effectiveness and efficiency. We have a strong focus on cost-efficient management and will seek to exploit further economies of scale. Increased investments in private markets, real assets, new geographies and less mature markets will add to costs, but we still target internal operating costs to remain at five basis points.

We will extend our cross asset system during the first half of the strategy period, and enhance our solutions for portfolio management, risk management and trading. We will continue to consolidate and simplify the application portfolio, give priority to information security and strengthen our internal IT development capacity.

Investment management is a highly information-intensive business, and we expect data requirements to increase from portfolio and risk management. The data warehouse solution will be expanded, and assure consistent core data.



We will make data readily available as information to support our decision making, and secure access to information from mobile platforms.

We have insourced the operational processes related to trade confirmation and settlement, income handling, tax handling, corporate actions and valuation. We aim to increase automation and standardisation of these processes to achieve an efficient operational setup. Investments in less mature markets will, however, require competence and capacity to handle manual processes. Flexible and robust support functions will be essential and our global operating model will be enhanced accordingly.

We will still rely on external service providers for services such as global custody services, IT infrastructure, and certain data processing and application management services. These services will remain outsourced throughout the strategy period. The model for core custody will be enhanced to secure a competitive service level and cost structure.



TRANSPARENT MANAGEMENT

We will work to improve the knowledge of the fund, provide clear and comprehensive information and be open on all relevant aspects of our management.

We manage the fund on behalf of current and future generations. We have a fiduciary duty to these and need to be professional and accountable to build trust and legitimacy. We acknowledge that trust and legitimacy are built over time. We work to increase the general knowledge about the fund, our management, and the task we are entrusted with.

We aim to be transparent and open about all aspects of our management, and disclose timely, accurate and relevant information to ensure legitimacy in Norway and internationally. Our ambition is to be open about all relevant matters as long as it does not jeopardise the fund's expected return.

We will be open about how we evaluate markets, but will not provide forecasts on market developments. We explain our financial results in relation to both the current market situation and the overall objective of the fund. We will avoid commenting on how we regard single investments, unless this concerns matters of principle. As a government institution, and part of a central bank, we will refrain from commenting on other countries' fiscal and monetary policy. We will complement our quarterly reports with a monthly update on the fund's investments and returns.

We will extend the series of discussion notes, and use these as an important vehicle to communicate the underpinnings of both our investment strategies and our advice to the Ministry of Finance. The Norwegian Finance Initiative will be our platform to strengthen financial research in areas relevant to the management of the fund.

We will increase the reporting on our work as an active and responsible investor. We share our principles and report on our engagements with regulators and interest groups. We will communicate to companies and other stakeholders that we share a common interest in long-term, sustainable value creation. We will support initiatives to improve corporate transparency, and expect the companies we invest in to disclose relevant information.

■ ■ We work to increase the general knowledge about the fund.

The main information and communication channel will be our website www.nbim.no. We intend to enhance the content of the site during the period to facilitate further information sharing and increase knowledge of our management of the fund. We will aim for clear, comprehensive, and understandable information on all aspect of the fund, available to all at the same time.



SUMMARY

In our management of the fund, we aim to safeguard the international purchasing power of the fund for future generations. We endeavour to do this as prudently, efficiently and transparently as possible. Our assignment comes with great responsibility and is dependent on the trust of key stakeholders to succeed. We will build on the foundations laid during 15 years of managing the fund, and strive for excellence in all aspects of our management assignment.

THE STRATEGIC DIRECTION FOR THE NEXT THREE YEARS:

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- We will be a global leader in responsible investment.
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