

# Report on the management of eYV 8` gVc\_^ V\_eAVeç` Jvf ^ :\_df dR\_TV 7f \_U

Third quarter 2010

# Report on the management of the Government Petroleum Insurance Fund

## Third quarter 2010

The purpose of the Government Petroleum Insurance Fund is to provide a reserve for payments to cover losses and liability associated with the State's Direct Financial Interest in petroleum activities (SDFI). The Ministry of Petroleum and Energy owns the fund. Pursuant to the Act relating to the Government Petroleum Insurance Fund, Norges Bank is responsible for the operational management of the fund. In the National Budget for 2011, the government has proposed that the fund be wound up with effect from 31 December 2010 and its assets transferred to the Government Pension Fund Global.

The ministry has defined a strategic benchmark portfolio for the fund consisting of 50 percent euro, 15 percent pounds sterling and 35 percent US dollars. The benchmark index consists of Barclays Global Aggregate treasury indices for the three currencies and a money market deposit to weight the interest rate risk as measured by modified duration in each currency to 4 (see Section 3).

During the year, the currency weights in the actual benchmark portfolio fluctuate with market developments. However, at the beginning of July each year, the actual weights are returned to the strategic currency weights. The table below shows the weights in the fund's actual and strategic benchmark portfolios at the end of the third quarter of 2010.

Government Petroleum Insurance Fund. Benchmark portfolio as at 30 September 2010. Percent

Currency	Strategic benchmark portfolio	Actual benchmark portfolio
Euro	50.0	52.2
Pounds sterling	15.0	14.8
US dollars	35.0	33.0
<b>Total</b>	<b>100</b>	<b>100</b>

## 1 Key figures

The return on the fund in the third quarter of 2010 was 1.7 percent. This was 0.03 percentage point higher than the return on the benchmark portfolio defined by the Ministry of Petroleum and Energy. The market value of the fund at the end of the quarter was 20.5 billion kroner, down from 21.0 billion kroner at the end of the second quarter.

Table 1-1 provides a historical overview of risk and return for the fund, while Chart 1-1 shows movements in the fund's market value.

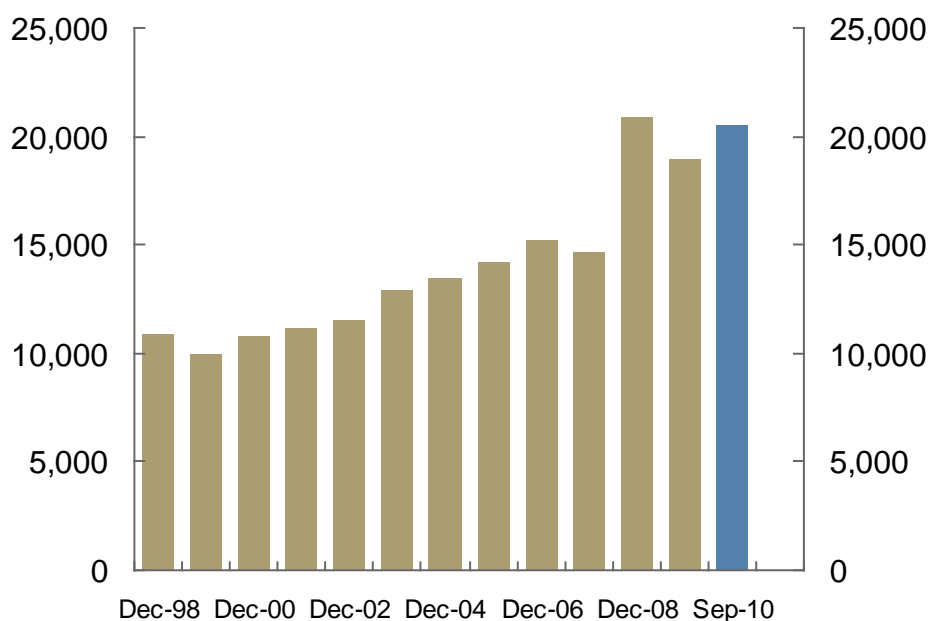
**Table 1-1** Risk and return. Annualised figures as at 30 September 2010

	Past year	Past 2 years	Past 3 years	Past 5 years	Past 7 years	Past 10 years
Actual return (percent)	4.37	5.64	5.73	4.58	4.60	5.24
Benchmark return (percent)	4.12	5.25	5.39	4.34	4.38	5.03
Excess return (percentage points)	0.24	0.38	0.34	0.24	0.22	0.21
Standard deviation (percent) <sup>1)</sup>	2.52	3.23	2.98	2.64	2.48	2.54
Tracking error (percentage points)	0.12	0.20	0.19	0.16	0.14	0.13
Information ratio <sup>2)</sup>	2.07	1.91	1.77	1.43	1.52	1.62

1) The standard deviation is a measure of variations in the return/excess return during a period. Each monthly return/excess return is compared with the mean for the period. The higher the standard deviation, the greater the variations relative to the mean and the higher the risk.

2) The information ratio (IR) is a measure of risk-adjusted return. It is calculated as the ratio of excess return to the actual relative market risk (as measured by tracking error) to which the portfolio has been exposed. The IR indicates how much excess return has been achieved per unit of risk.

**Chart 1-1** Market value. In millions of kroner



## 2 Market value and return

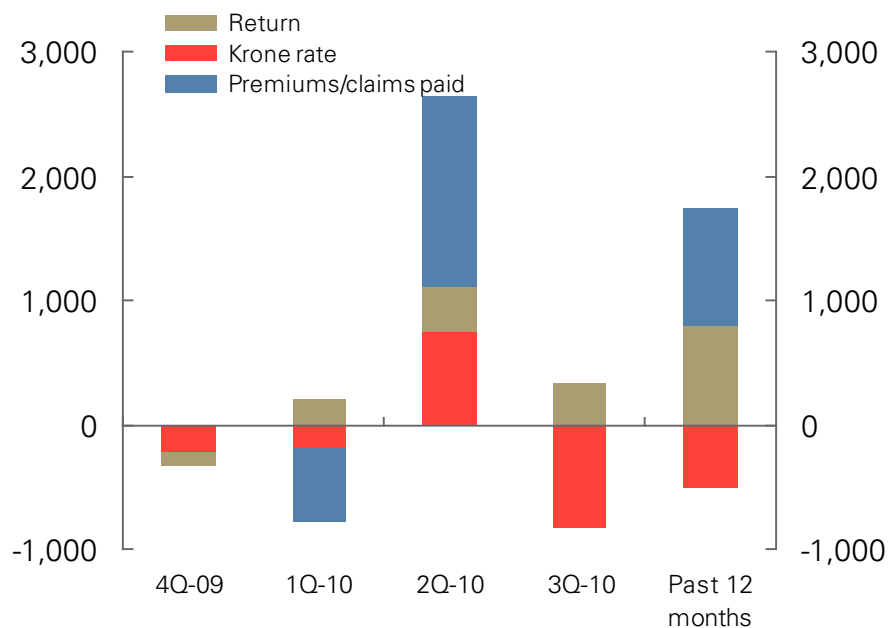
The fund's market value fell by 0.5 billion kroner during the third quarter. A positive return on investment measured in international currency increased the fund's market value by 0.3 billion kroner, while a stronger krone against the currencies in which the fund is invested decreased its value by 0.8 billion kroner.

**Table 2-1** Market value. Millions of kroner

Currency	31.12.2009	31.03.2010	30.06.2010	30.09.2010
Euro	9 672	9 222	10 556	10 710
Pounds sterling	2 751	2 587	3 133	3 044
US dollars	6 538	6 576	7 342	6 772
<b>Total market value</b>	<b>18 962</b>	<b>18 385</b>	<b>21 031</b>	<b>20 525</b>

Chart 2-1 shows developments in the fund's market value over the past 12 months, while Table 2-1 presents the composition of the fund by investment currency.

**Chart 2-1** Change in market value. In millions of kroner



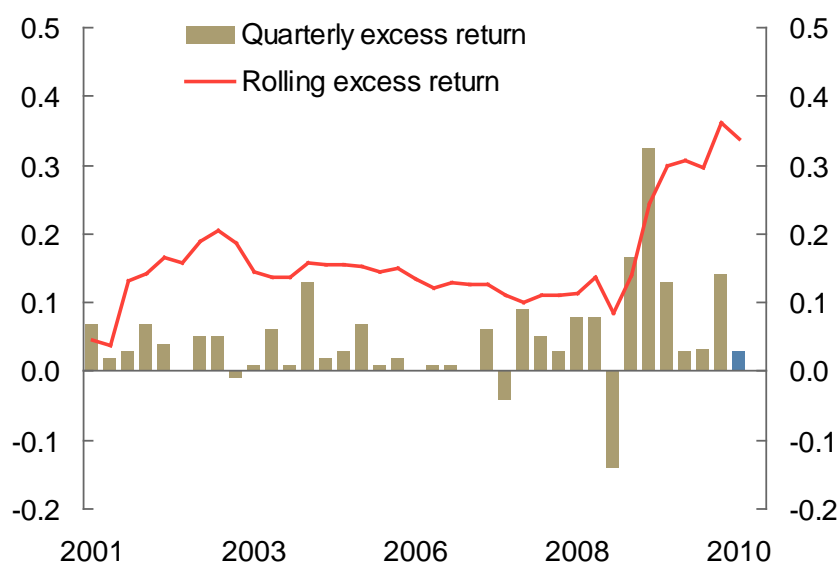
**Table 2-2** Return. Percent

	Actual portfolio	Benchmark portfolio	Excess return
2009	1.15	0.49	0.65
1Q2010	1.22	1.19	0.03
2Q 2010	1.82	1.68	0.14
<b>3Q 2010</b>	<b>1.73</b>	<b>1.70</b>	<b>0.03</b>
<b>Jan-Sep2010</b>	<b>4.85</b>	<b>4.63</b>	<b>0.21</b>

The return on the fund in the third quarter of 2010 was 1.73 percent measured in international currency (i.e. measured in terms of a currency basket corresponding to the composition of the fund's benchmark portfolio). Measured in kroner, the return was -2.41 percent. The difference is due to the appreciation of the krone during the quarter against the currencies included in the benchmark portfolio. The actual return was 0.03 percentage point higher than the benchmark return.

**Chart 2-2** Quarterly return and three-year rolling annualised return. Percent

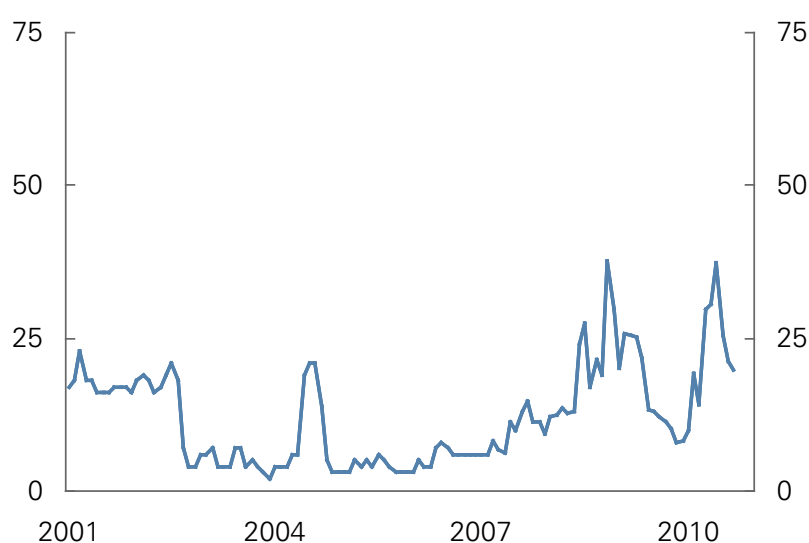
**Chart 2-3** Quarterly excess return and three-year rolling annualised excess return. Percentage points



### 3 Market risk and management guidelines

Market risk in the fund is measured as expected tracking error. This is a statistically-defined measure of risk which says something about the amount of variation we can normally expect in the difference between the return on the benchmark portfolio and the return on the actual portfolio in which the fund is invested. The Ministry of Petroleum and Energy has decided that market risk in the fund must always be less than tracking error of 0.75 percentage point. This means that, under normal market conditions, the annual return on the actual portfolio is expected to deviate from the return on the benchmark portfolio by less than 0.75 percentage point in two out of every three years. Chart 3-1 shows movements in market risk. Expected tracking error was 0.20 percentage point (20 basis points) at the end of the third quarter, up from 0.37 percentage point at the end of the second quarter.

**Chart 3-1** Expected tracking error. Basis points



The Ministry of Petroleum and Energy has also set a limit for interest rate risk in the fund as measured by modified duration. This measure says something about the expected change in the value of the fund following a change in general interest rate levels. The ministry has decided that the fund's modified duration is to be a maximum of 5. Table 3-1 shows the fund's modified duration as at 30 September 2010, while Table 3-2 shows the composition of the bond portfolio by credit rating.

**Table 3-1** Modified duration by currency as at 30 September 2010

Currency	Benchmark portfolio	Actual portfolio
Euro	3.86	3.82
Pounds sterling	3.80	4.02
US dollars	3.85	3.99
<b>Total</b>	<b>3.85</b>	<b>3.91</b>

**Table 3-2** Market value as at 30 September 2010 by credit rating<sup>1)</sup>

Percentage of fixed-income portfolio	Aaa	Aa	A
Government and government-related bonds	79.1	19.3	-
Securitised debt	1.6	-	-
<b>Total bonds and other fixed-income instruments</b>	<b>80.7</b>	<b>19.3</b>	<b>-</b>

<sup>1)</sup> Based on credit ratings from at least one of the following rating agencies: Moody's, Standard & Poor's and Fitch.

Table 3-3 provides an overview of the limits for risk exposure set out in the regulation and guidelines, and shows the portfolio's actual exposure in relation to these limits at the end of each quarter. There was one minor breach of the ministry's guidelines in the third quarter of 2010.

**Table 3-3** Key figures for risk and exposure

Risks	Limits	Actual			
		31.12.2009	31.03.2010	30.06.2010	30.09.2010
Market risk	Tracking error max. 0.75 percentage point	0.08	0.14	0.37	0.20
Interest rate risk	Modified duration max. 5.0	3.83	3.77	3.69	3.91

## 4 Financial reporting

The Government Petroleum Insurance Fund's accounts are kept by Norges Bank, but the fund is not included in the Bank's financial statements.

### Operating expenses

The management agreement between the Ministry of Petroleum and Energy and Norges Bank establishes the principles for Norges Bank's remuneration for managing the Petroleum Insurance Fund. For 2010, a fee of 0.06 percent of the average market value of the fund has been stipulated. A management fee of 8.8 million kroner was accrued in the first nine months of 2010.

### Profit and loss account and balance sheet

**Table 4-1** Government Petroleum Insurance Fund. Profit and loss account

(Figures in thousands of kroner)	Quarter			Year to date	
	3Q2010	3Q2009	30.09.2010	30.09.2009	31.12.2009
<i>Profit/loss on financial assets excl. exchange rate adjustments</i>					
Interest income, lending associated with reverse repurchase agreements	6 636	4 003	14 240	17 901	21 769
Net income/expenses and gains/losses from:					
- securities and deposits	319 245	304 169	881 767	168 408	65 067
- financial derivatives	0	0	0	621	621
Interest expenses, borrowing associated with repurchase agreements	24	-22	-17	-183	-196
Other interest expenses	0	0	0	-58	-62
<b>Profit/loss before exchange rate adjustments</b>	<b>325 905</b>	<b>308 150</b>	<b>895 989</b>	<b>186 689</b>	<b>87 198</b>
Exchange rate adjustments	-833 017	-1 673 398	-272 904	-2 856 725	-3 083 940
<b>Profit/loss</b>	<b>-507 112</b>	<b>-1 365 248</b>	<b>623 085</b>	<b>-2 670 036</b>	<b>-2 996 742</b>
Accrued management fee	-3 139	-3 020	-8 756	-8 936	-12 051
<b>Profit/loss after management fee</b>	<b>-510 251</b>	<b>-1 368 267</b>	<b>614 329</b>	<b>-2 678 973</b>	<b>-3 008 792</b>

**Table 4-2** Government Petroleum Insurance Fund.  
Balance sheet

(Figures in thousands of kroner)

	30.09.2010	30.09.2009	31.12.2009
<b>FINANCIAL ASSETS</b>			
Lending associated with reverse repurchase agreements	6 982 973	7 633 647	8 719 352
Securities and deposits	13 256 944	10 822 256	9 604 303
Bonds lent	338 570	4 570 566	4 854 943
Unsettled trades	134 176	0	0
<b>TOTAL FINANCIAL ASSETS</b>	<b>20 712 663</b>	<b>23 026 469</b>	<b>23 178 599</b>
<b>FINANCIAL LIABILITIES</b>			
Cash collateral received	0	3 679 765	4 071 080
Unsettled trades	187 580	58 177	145 696
Management fee due	8 756	8 936	12 051
<b>TOTAL FINANCIAL LIABILITIES</b>	<b>196 336</b>	<b>3 746 878</b>	<b>4 228 827</b>
<b>NET PORTFOLIO*</b>	<b>20 516 327</b>	<b>19 279 591</b>	<b>20 516 327</b>

\* The difference between market value in Table 2.1 and the net portfolio in the balance sheet is due primarily to differences in the treatment of unsettled transfers to the portfolio, which were not recognised in the balance sheet at the end of the quarter.