



## COMPANIES MUST SUCCEED OVER THE LONG-TERM

Our owner has set a clear objective: to deliver the highest possible returns over time. We achieve this through active management and active, responsible ownership.

The investment mandate for the Government Pension Fund Norway states that Folketrygdfondet is to deliver the highest possible returns over time. For the purposes of our day-to-day investment activities, we have translated this into two sub-goals:

- To achieve a better return than the market in general (excess return compared to benchmark indices).
- To support long-term value creation in companies and in the market.

These goals form the foundation of our investment philosophy. We engage in active management to achieve the goal of excess returns, while the goal of promoting corporate value creation is achieved through active, responsible ownership and the development of best practices and well-functioning markets. We find that the two goals are interdependent. Being an active owner makes us a better manager.

Our long-term returns depend on our portfolio companies' ability to deliver strong results over the long term, and on efficient and well-functioning markets. This is why we take an integrated approach to responsible investment. This involves conducting systematic follow-up of material opportunities and challenges linked to environmental, social and governance (ESG) issues, and being an engaged owner that helps maximise companies' potential. This approach also benefits other shareholders and creditors. In our ownership capacity, we engage with the individual portfolio companies irrespective of any over- or under-weighting relative to our benchmark index. This facilitates a higher long-term return for the Government Pension Fund Norway, in line with our mandate.

### How we organise our responsible investment activities

Folketrygdfondet's board has adopted responsible investment principles (please see [ftf.no](http://ftf.no), English pages) which explain how we exercise our role as owner and creditor and integrate environmental and social considerations into our management of the Government Pension Fund Norway. Responsibility for implementing the principles across the portfolio lies with Folketrygdfondet's CEO. In Folketrygdfondets eierskapsutøvelse (Folketrygdfondet's exercise of ownership rights – please see [ftf.no](http://ftf.no), English pages), the administration describes how we operationalise the principles in Folketrygdfondet's investment activities. Operational implementation has been delegated to the Chief Investment Officer Equities and the Chief Investment Officer Fixed Income. The equities department also has a dedicated ESG staff member. Folketrygdfondet's portfolio managers are responsible for covering material topics, including climate risk, in their investment analyses and company dialogues. This occurs in practice through close cooperation within each department, in line with Folketrygdfondet's team-based management model. ESG is integrated into the investment process through the following measures, among others:

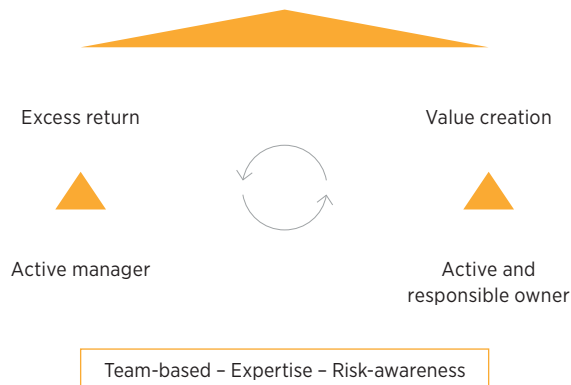
- Responsible investment is a permanent agenda item at the front office morning meetings.
- Material sustainability topics are incorporated into company dialogues.
- Responsible investment is integrated into investment decisions in the form of input to portfolio meetings and company analyses.
- Responsible investment is a fixed item in the approval process for new equity investments in Norway.
- The equity and fixed income departments have an annual plan for responsible investment training, which prescribes one measure per quarter.
- Responsible investment is included in regular reports to the investment committee and the board of directors.

**Folketrygdfondet's ownership role**

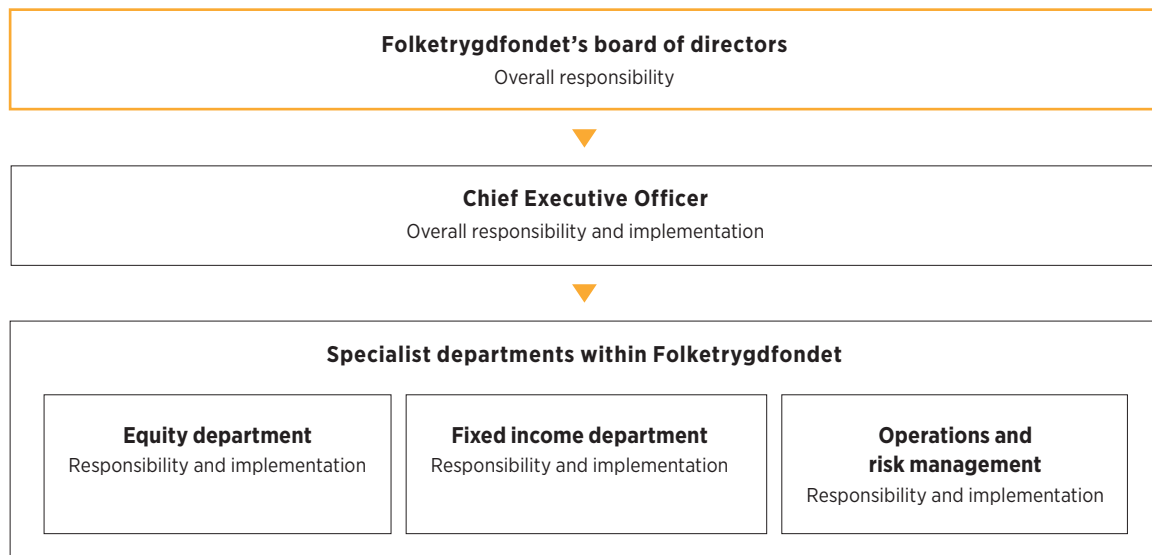
- Dialogue
- General meetings
- Nomination committees and governing bodies
- Good practice development
- The fixed-income portfolio

**OUR INVESTMENT PHILOSOPHY SUMMARISED**

**HIGHEST POSSIBLE RETURNS OVER TIME**



**ORGANISATION**



RESPONSIBLE INVESTMENT INSTRUMENTS

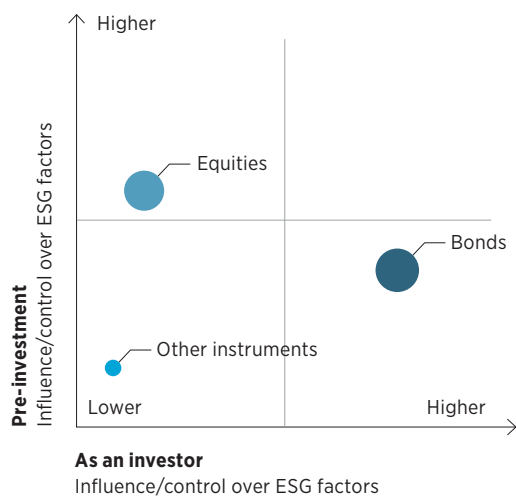
	ESG integrated into management	Exclusion	Dialogue with companies	Voting at general meetings/ bondholder meetings	Promote well-functioning markets
Norwegian equities	●	—	●	●	●
Nordic equities	●	●	●	●	●
Norwegian bonds (corporate)	●	—	●	●	●
Nordic bonds (corporate)	●	●	●	●	●
Government bonds	—	—	N/A	N/A	—
Other instruments	N/A	●	N/A	N/A	●

Folketrygdfondet shall not invest in companies excluded pursuant to the guidelines on observation and exclusion from the Government Pension Fund Global. An overview of exclusions is available on [ftf.no](#). No companies were excluded or re-included during the period.

Illustration 9

WE TAILOR OUR RESPONSIBLE INVESTMENT APPROACH TO OUR DIFFERENT FINANCIAL INSTRUMENTS

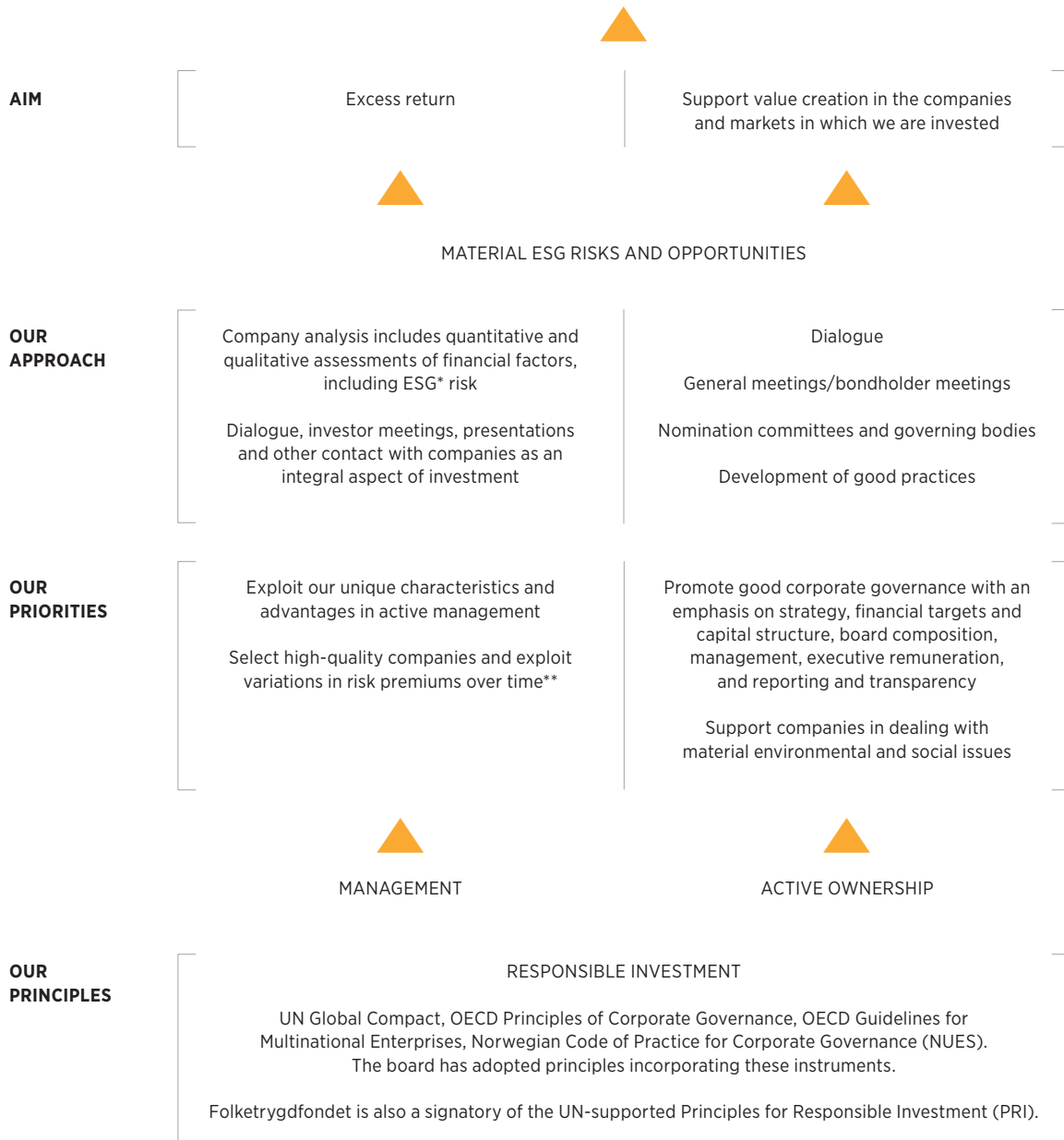
The size of the circle indicates the relative size of the instrument.



**OUR RESPONSIBLE INVESTMENT APPROACH**

OVERARCHING AIM DEFINED IN THE MANDATE FROM THE MINISTRY OF FINANCE:

**HIGHEST POSSIBLE RETURNS OVER TIME**



**Explanation of terms**

\* ESG: Environmental, social and governance issues.

\*\* Exploit variations in risk premiums over time: exploiting the opportunities offered by variations in risk in the market over time.

Buying securities when prices reflect excessively high risk and selling when prices reflect excessively low risk.

**We tailor our responsible investment activities to our various portfolios**

The investment mandate and our unique characteristics as an asset manager guide Folketrygdfondet's selection of measures to promote responsible investment.

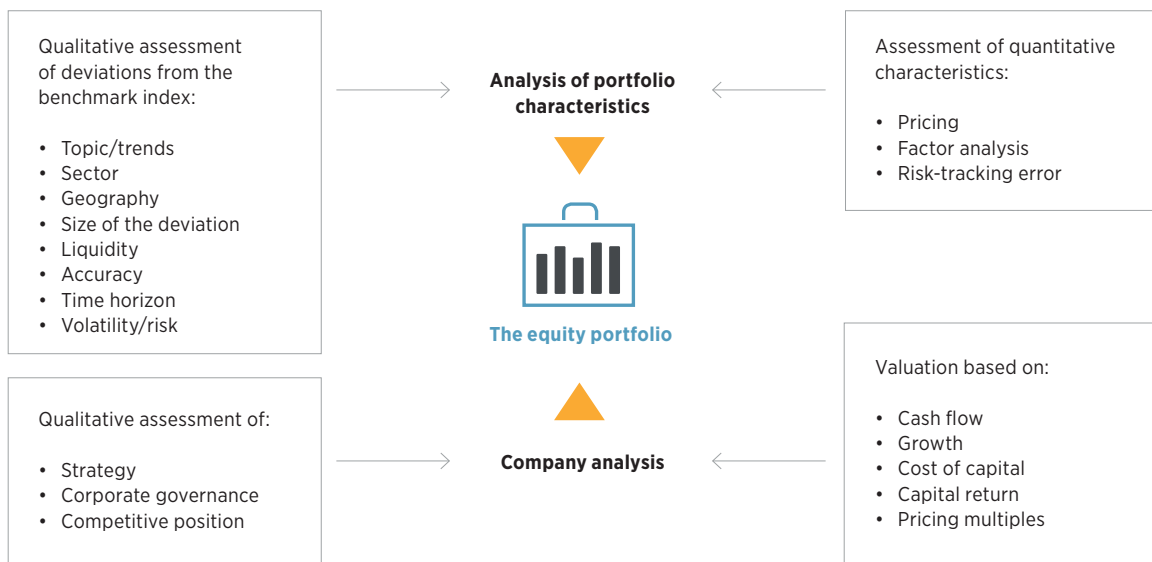
We adapt our efforts and the tools we use to our different financial instruments and portfolios. This is necessary to ensure that our responsible investment efforts serve the overarching aim of achieving the highest possible returns over time. In this assessment, we look to factors such as our influence over ESG issues pre- and post-investment. We prioritise contributing to well-functioning, legitimate, and efficient markets for all our financial instruments and portfolios. This includes supporting the development of strong national responsible investment standards.

For fixed income instruments, we have the greatest influence before we invest, since bondholders do not have ownership rights. We therefore focus on robust pre-investment ESG analysis to identify issues that may affect creditworthiness. For our equity investments, we have the greatest opportunity to influence ESG factors once invested, through our ownership

rights. This makes active ownership a priority for the equity portfolio. Other tools are used in connection with liquidity investments and currency hedging. Due to the low anticipated impact of ESG factors and short investment horizon, these areas are not a priority in our responsible investment efforts, with the exception of procedures for recalling loaned-out shares prior to general meetings. In this context, we concentrate on promoting well-functioning and efficient markets.

The adaptation of responsible investment activities to Folketrygdfondet's distinctive characteristics is discussed further in the strategic plan for management of the Government Pension Fund Norway, which emphasises Folketrygdfondet's long investment horizon as a primary argument in favour of our integrated approach to responsible investment. ESG issues are examined in our assessments of potential high-quality investment targets, and to shed light on possible downside risk linked to failure to address ESG issues. The in-depth company knowledge Folketrygdfondet has gained from several decades of active management give it a broader perspective on individual companies' ESG efforts, and allows us to be a demanding owner.

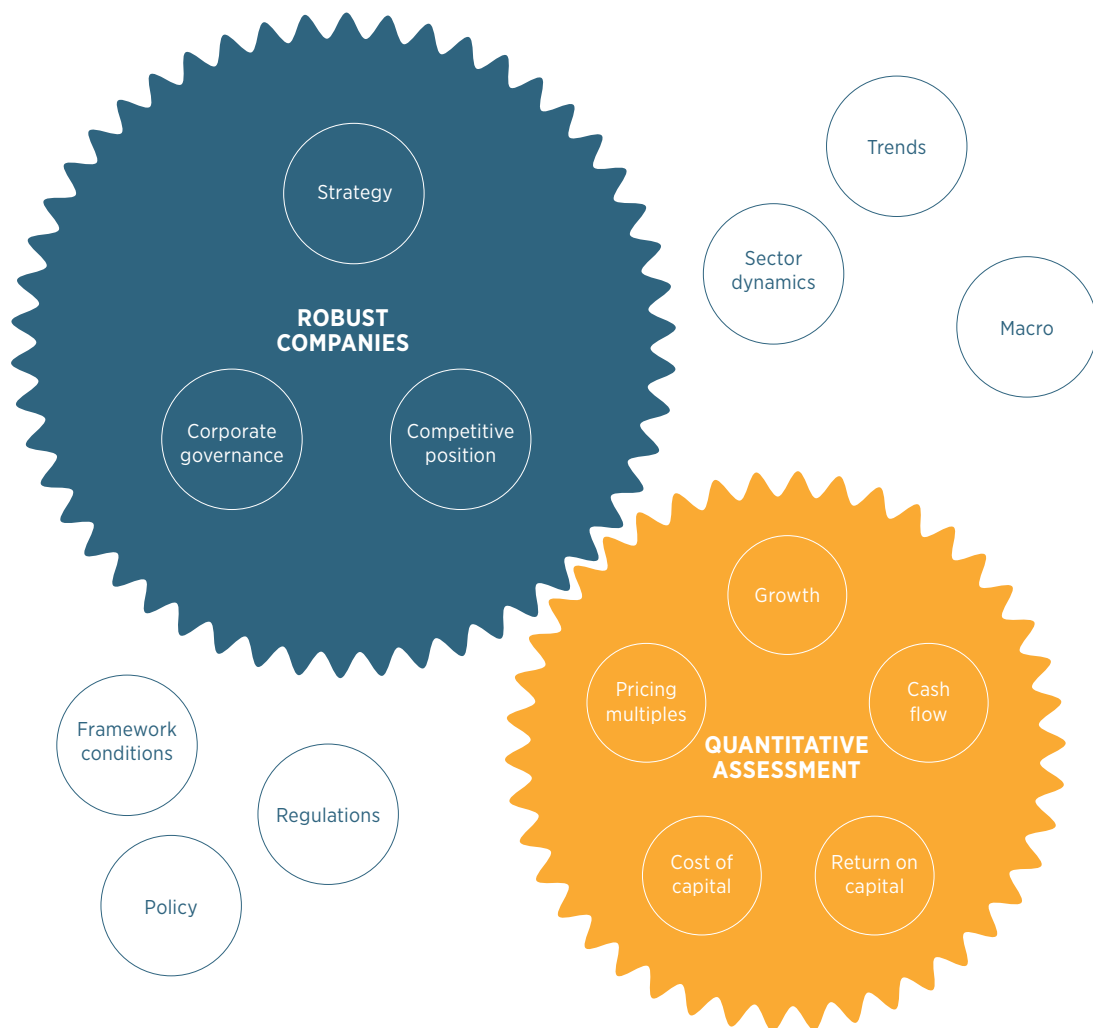
**OUR APPROACH TO ACTIVE MANAGEMENT**



**Folketrygdfondet's ownership role**

- Dialogue
- General meetings
- Nomination committees and governing bodies
- Good practice development
- The fixed-income portfolio

**OUR COMPANY ANALYSIS SUMMARISED**



**Robust companies**

As an active manager, we both select investment targets and over- and under-weight companies compared to the benchmark index. Our investment decisions reflect financial analysis, ongoing contact with relevant companies, and ESG analyses. Our priority is to check whether companies have robust procedures in place for identifying, dealing with, and reporting on material issues. The Oslo Stock Exchange's guidance on corporate social responsibility reporting contains an example of such a process. Folketrygdfondet has developed expectation documents that also contain relevant information for this work.

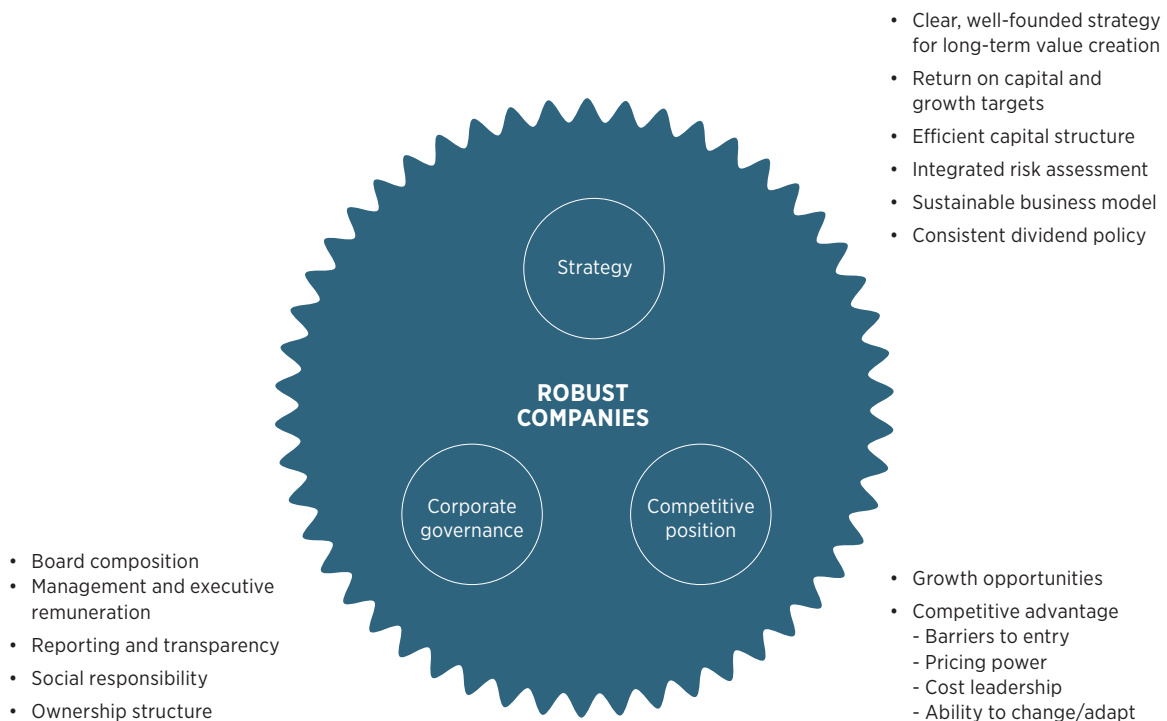
Our aim is to beat the market over the long term, i.e. to generate excess returns by exploiting our unique characteristics and advantages as an asset manager. To implement our mandate, we focus our investments in companies that are long-term value generators. Our

long-term returns are dependent on strong, consistent performance by the companies in which we invest, and on efficient and well-functioning markets.

**Qualitative assessment is crucial**

In our experience, the most successful companies over time are characterised by effective corporate governance, a strong competitive position, and well-considered strategies. In practice, such companies have capable boards and managers as well as a clear, well-founded strategy for long-term value creation. They take a long-term view of resources and risk, as well as deal with threats and exploit opportunities related to sustainable development. We invest time and resources in qualitatively assessing factors related to strategy, corporate governance and competitive position. These assessments provide a starting point for our quantitative analysis of companies.

**KEY TOPICS IN OUR QUALITATIVE ANALYSIS:**





## NORDIC OWNER WITH A PRIMARY FOCUS ON THE OSLO STOCK EXCHANGE

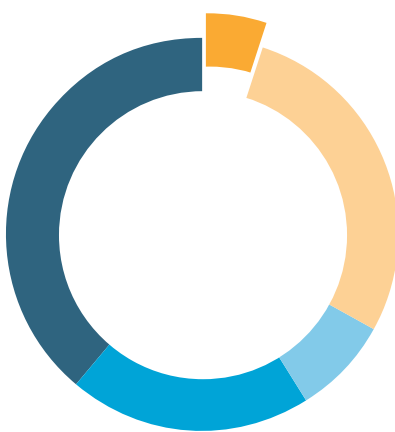
Folketrygdfondet is one of the largest financial investors on the Oslo Stock Exchange, as a top-three shareholder in 41 listed companies. Folketrygdfondet has far smaller shareholdings on the other Nordic exchanges.

The Government Pension Fund Norway follows clear guidelines laid down in the mandate from the Ministry of Finance. The fund capital is invested in securities listed on regulated exchanges in Norway, Denmark, Finland and Sweden. The investment distribution is 85% in Norway and 15% in the other Nordic countries. The investment mandate specifies that the highest permitted shareholding in any Norwegian company is 15 percent, and five percent for

companies from the other Nordic countries.

It is important for companies to maintain contact with their largest shareholders, both on an ongoing basis and in connection with strategically important developments such as acquisitions and changes in capital structure. We are highly aware of our responsibility in this regard, and thus prioritise investing time and resources in ownership dialogues.

### OWNERSHIP ON THE OSLO STOCK EXCHANGE



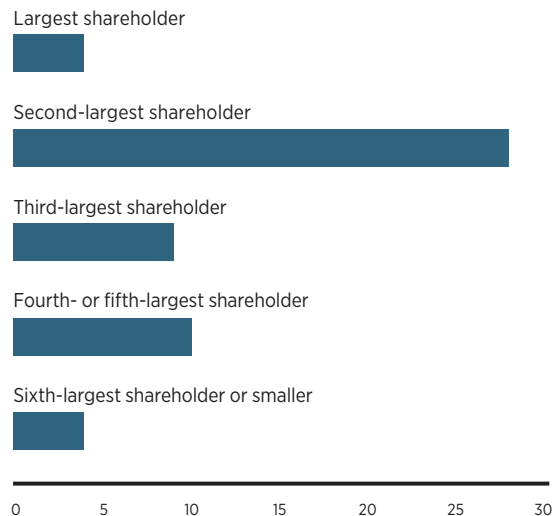
Folketrygdfondet	5.12%
Central and local government	28.09%
Norwegian financial owners	7.92%
Other Norwegian owners	20.00%
Foreign investors	38.87%

**Sources:** Oslo Stock Exchange monthly statistics and Folketrygdfondet as at 31 December 2018

Figure 21

### FOLKETRYGDFONDET'S OWNERSHIP INTERESTS ON THE OSLO STOCK EXCHANGE

Number of companies in which Folketrygdfondet is among the largest shareholders.



**Sources:** Company websites, VPS and stock exchange notices. When a nominee account is specified as one of the largest shareholders, Folketrygdfondet estimates its placement. Owners with shared ownership interests are grouped together when Folketrygdfondet has information indicating this is correct.

Figure 22

**FOLKETRYGDFONDET'S OWNERSHIP INTERESTS ON THE OSLO STOCK EXCHANGE**

Companies in which Folketrygdfondet owned more than five percent of equity or was among the three largest shareholders as of 31 December 2018.

Company name	FTF's shareholding	FTF's shareholder ranking
Nordic Semiconductor	14.44 %	1
Norwegian Property	13.48 %	2
Veidekke	11.56 %	2
TGS-NOPEC Geophysical Company	11.21 %	1
Storebrand	11.04 %	1
Borr Drilling	10.54 %	2
Petroleum Geo-Services	9.88 %	1
Atea	9.83 %	2
MOWI	8.99 %	2
Subsea 7	8.71 %	2
Bakkafrost	8.61 %	3
Norwegian Finans Holding	8.47 %	2
Schibsted	8.28 %	2
Nordic Nanovector	8.00 %	2
Tomra Systems	7.93 %	2
Orkla	7.69 %	2
SpareBank 1 SR-Bank	7.40 %	2
AF Gruppen	7.25 %	4
Scatec Solar	7.19 %	4
Aker Solutions	7.18 %	2
Norsk Hydro	6.88 %	2
Kongsberg Gruppen	6.66 %	2
Yara International	6.48 %	2
SalMar	6.13 %	2
Entra	6.10 %	2
DNB	6.06 %	3
Norwegian Air Shuttle	6.04 %	2
REC Silicon	5.92 %	2
Lerøy Seafood Group	5.32 %	2
Golden Ocean Group	5.13 %	2
Telenor	5.10 %	2
EVERY	5.09 %	3
Wilh. Wilhelmsen Holding	4.94 %	3
Gjensidige Forsikring	4.54 %	2
Aker	4.53 %	2
Grieg Seafood	4.17 %	3
Aker BP	4.13 %	3
Olav Thon Eiendomsselskap	3.76 %	3
Equinor	3.48 %	2
Europris	2.88 %	2
Stolt-Nielsen	2.54 %	2
Wallenius Wilhelmsen	2.46 %	3
Austevoll Seafood	2.42 %	3

**Sources:** Company websites, VPS and stock exchange notices.

When a nominee account is specified as one of the largest shareholders, Folketrygdfondet estimates its placement. Owners with shared ownership interests are grouped together when Folketrygdfondet has information indicating this is correct.

### FOLKETRYGDFONDET'S SHAREHOLDINGS IN INDIVIDUAL COMPANIES

The size of each bar reflects Folketrygdfondet's shareholding in that company as at 31 December 2018.

■ Oslo Stock Exchange ■ Nasdaq Copenhagen ■ Nasdaq Stockholm ■ Nasdaq Helsinki

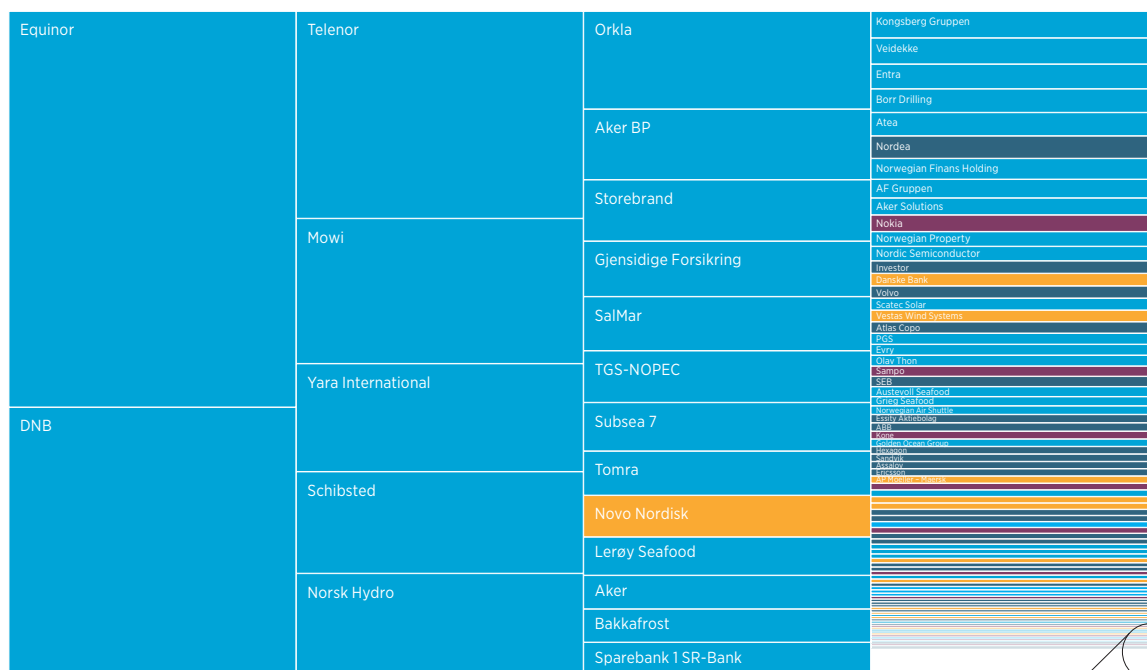


Figure 23

### FOLKETRYGDFONDET'S LARGEST NORDIC INVESTMENTS

Company name	FTF's shareholding	Exchange
Net Entertainment	0.89 %	Nasdaq Stockholm
Bravida Holding	0.86 %	Nasdaq Stockholm
Intrum Justitia	0.77 %	Nasdaq Stockholm
Elekta	0.67 %	Nasdaq Stockholm
Skanska	0.48 %	Nasdaq Stockholm
Vestas Wind Systems	0.46 %	Nasdaq København
SimCorp	0.44 %	Nasdaq København
Danske Bank	0.44 %	Nasdaq København
Arjo	0.42 %	Nasdaq Stockholm
Stora Enso	0.39 %	Nasdaq Helsinki
Lundin Petroleum	0.39 %	Nasdaq Stockholm
Nordea	0.39 %	Nasdaq Stockholm
Epiroc	0.34 %	Nasdaq Stockholm
Pandora	0.34 %	Nasdaq København
Getinge	0.33 %	Nasdaq Stockholm
BillerudKorsnäs	0.32 %	Nasdaq Stockholm
Nokia	0.31 %	Nasdaq Helsinki
Essity	0.30 %	Nasdaq Stockholm
ISS	0.30 %	Nasdaq København
Skandinaviska Enskilda Banken	0.29 %	Nasdaq Stockholm

## OUR PROCEDURES

Meetings with board chairs and management are the most common tool Folketrygdfondet uses in its active ownership. Other important arenas include general meetings, corporate assemblies and nomination committees.

Folketrygdfondet aims to be a demanding, reliable, and responsible owner.

### Arenas

Active, constructive dialogue with portfolio companies is consistent with Folketrygdfondet's role as a large, long-term investor. Through meetings and other contact with the board chair and management, companies get to know us and we get to know them. The primary aim in most of our dialogues is to learn more about the companies.

It is important for us to know the companies, so that we can make sound investment decisions, assess capital requirements, and identify areas in which we can exert influence.

We devote considerable time and resources to active ownership, and always seek to ensure that the portfolio companies are aware of our expectations. We communicate the importance of addressing ownership issues and other material ESG topics in our

broader active ownership efforts, but also in specific cases in which the companies do not appear to be acting in line with our expectations. We address material risks in various ways, including through direct meetings with companies, joint initiatives with other investors and voting at general meetings.

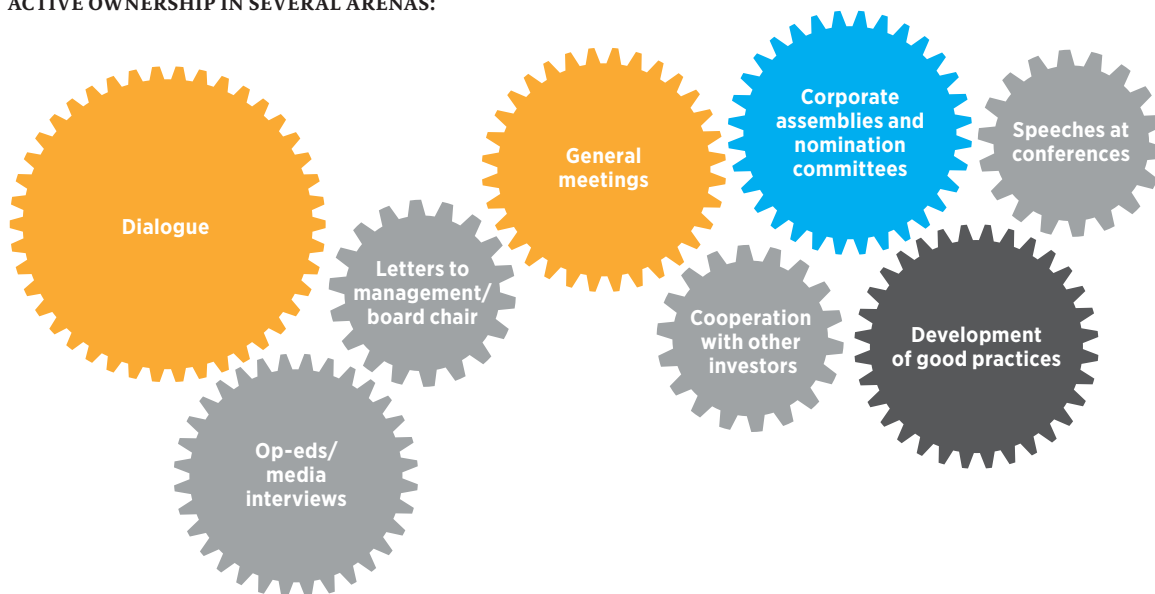
### Topics

We have defined five key ownership issues with which we engage and express our views:

- strategy, capital structure, and financial targets
- board composition
- executive remuneration
- good corporate governance
- reporting and transparency

To make the dialogue as productive as possible for both parties, we have drafted a number of guidance documents on key topics. Please see [ftf.no](http://ftf.no), English pages.

### ACTIVE OWNERSHIP IN SEVERAL ARENAS:



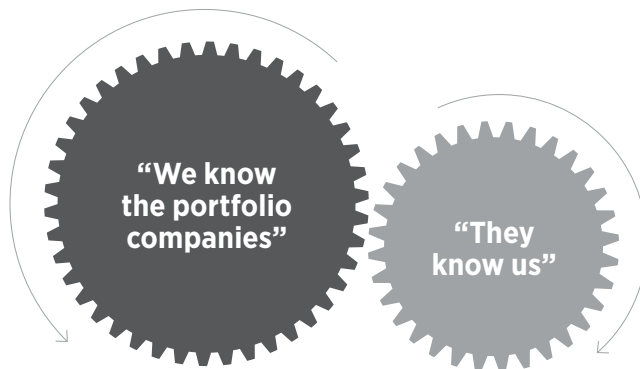
**The portfolios**

Our active ownership in Danish, Finnish and Swedish companies follows the same principles as in Norwegian companies. However, Folketrygdfondet's shareholdings in the other Nordic markets are smaller and spread among a larger number of companies, and we adapt our active ownership activities accordingly. Further, the role of bondholder differs from the role of shareholder, not least because only shareholders have ownership rights. Relations between bondholder and issuer are governed by the loan agreement, and there is limited dialogue with the issuer unless an undesirable event such as default occurs. Our bondholder engagement is therefore different from our shareholder engagement.

**Active ownership challenges**

We devote considerable time and resources to active ownership, and always seek to ensure that the portfolio companies are aware of our expectations. We communicate the importance of addressing ownership issues and other material ESG topics in our broader active ownership efforts, but also in specific cases in which the companies do not appear to be acting in line with our expectations. Companies increasingly understand our financial motivation for focusing on ownership issues and the handling of material sustainability concerns, and the companies often have a mature approach to these topics. Nonetheless, it sometimes takes time for companies to operate in accordance with our expectations, in part because such cases are often complex and entail dilemmas and trade-offs.

**OUR ACTIVE OWNERSHIP OBJECTIVES:**



Objective	1. "We know the portfolio companies"	2. "They know us"
<b>How</b>	Know the companies	Influence the companies
<b>Purpose</b>	Increase our understanding of the companies	Improve the companies' awareness of and compliance with our principles and expectations
<b>Arena</b>	Dialogue	General meetings, dialogue, nomination committees, promote good practice
<b>Indicator</b>	Excess return	Support value creation in the companies in which we invest

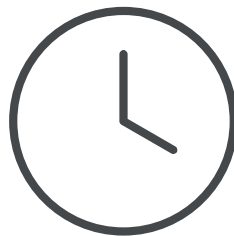
ACTIVE OWNERSHIP CHALLENGES:

Complexity



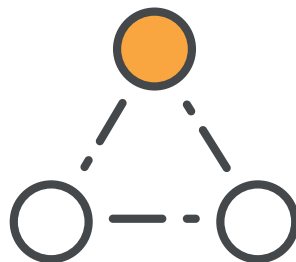
ESG-related issues are seldom clear-cut.

Long-term perspective



Change processes often take time, as does finding solutions that match Folketrygdfondet's expectations.

Distribution of roles and responsibilities



We emphasise dialogue and expect companies to initiate change processes.

We focus on preserving the appropriate distinction between the role of the board and that of the shareholders acting through the general meeting.

## COMPANY DIALOGUE

We monitor ESG issues of material importance to the portfolio companies, which can impact us financially.

Folketrygdfondet is a large, long-term investor, and active and constructive dialogue with our portfolio companies is one of our most important activities as an owner. We aim to be available to the companies, and expect the companies to be available to us. Meetings and other contact with board chairs and management allow the companies get to know us, and vice versa. This is discussed further in *Folketrygdfondets eierskapsutøvelse* (Folketrygdfondet's exercise of ownership rights), which describes Folketrygdfondet's approach to company dialogue.

Our dialogue priorities are determined by company analyses and assessments of portfolio characteristics. In accordance with the investment mandate, we have been communicating clear expectations as to the handling of ownership, environmental and social issues for several years. To make our dialogue with companies as effective as possible, we have developed guidance documents on:

- strategy, capital structure and financial targets
- anti-corruption
- executive remuneration schemes
- climate issues
- human rights
- workers' rights
- environmental issues

We monitor material risks in various ways, including through direct meetings with the portfolio companies, joint initiatives with other investors, and surveys. Folketrygdfondet generally conducts company dialogues alone. Nevertheless, we do cooperate with other investors when this is a more effective way to help raise market standards and/or when doing so will save the company time by enabling it to communicate with several major shareholders simultaneously.

Our dialogue with managers and boards of directors also includes material opportunities and challenges linked to corporate governance and environmental and social conditions. Twice a year, Folketrygdfondet reviews the Norwegian equities

portfolio to identify which companies it needs to contact in the half-year ahead, and what topics to raise.

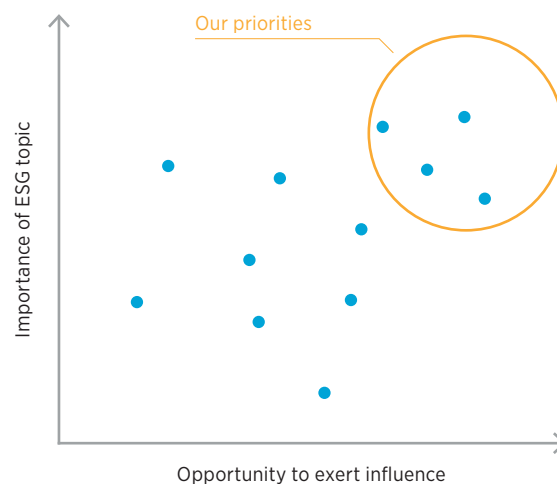
Prior to all meetings with Norwegian companies, Folketrygdfondet reviews the meeting agenda to ensure the inclusion of relevant governance, environmental and social issues. In other words, meetings with board chairs may cover not only financial targets and capital structure, but also the rights of workers in the supply chain. Where a more in-depth sustainability dialogue is needed, we schedule a meeting with relevant specialists at the company. In our experience, this model communicates that Folketrygdfondet takes an integrated view of sustainability, and that sustainability is an integral part of our investment philosophy.

In our analysis of portfolio characteristics, we concentrate on identifying topics that are material for multiple companies or to the markets in which we are invested. In this context, we evaluate potential topics from two perspectives:

- materiality of the ESG topic
- our opportunity to exert influence

Topics that score highly on both factors are prioritised in our responsible investment efforts.

### HOW WE SELECT SUSTAINABILITY TOPICS



The analysis of portfolio characteristics is updated annually, as well as in the event of significant changes. Accordingly, different topics remain a priority for different lengths of time.

**What do we hope to achieve?**

In Folketrygdfondet’s experience, it is difficult to measure the effect of our active ownership over time separately from our investment results. This is both because corporate change processes are often complex and prolonged, and because Folketrygdfondet’s role as an owner is integrated into our investment philosophy.

By focusing on ESG, we seek to promote well-functioning markets and sustainable development in the markets in which we invest. Questions related to corporate governance and social and environmental matters are seldom clear-cut, and it can take time to reach solutions in line with our expectations. Folketrygdfondet’s aim is to ensure that companies initiate and take responsibility for change processes. In our experience, many investors communicate

similar messages, making it difficult to isolate the contribution made by Folketrygdfondet’s active ownership. Nevertheless, Folketrygdfondet has noted increasing understanding of our financial motivation for focusing on governance issues and the handling of material ESG risks among companies, which often take a mature approach to such matters.

A further objective is to help companies overcome material ESG challenges and thereby secure the best possible foundation for long-term value creation. Both active management and active ownership presuppose thorough knowledge of the portfolio companies. In our experience, there is a strong correlation between active management and active ownership. Our aim is to know the companies, and for them to know us. Dialogue with management and boards of directors gives us a basis for understanding performance, strategies, the competitive situation and growth opportunities – all key factors in good investment decisions. Moreover, our dialogues give us the opportunity to be a demanding owner and communicate our expectations to the

Value creation dynamic	For Folketrygdfondet	For companies
<b>COMMUNICATION</b> Exchanging information	Signalling and defining ESG expectations	Clarifying Folketrygdfondet’s expectations
	Seeking detailed and accurate corporate information	Putting challenges in context and eliminating misconceptions
<b>LEARNING</b> Producing and diffusing knowledge	Contextualising investment decisions	Gathering feedback, benchmarking and gap spotting
	Identifying and diffusing industry best practice	Developing knowledge of ESG issues
<b>ORGANISATIONAL DEVELOPMENT</b> Integrating ESG into strategies and operations	Improving ESG integration within Folketrygdfondet	Ensuring that the company’s resource use and priorities are as required to deliver on investor expectations
	Building a long-term relationship with the company based on trust	Building trust among the company’s long-term investors

Table adapted from *PRI Guide to Active Ownership* (2018); Gond (2017).



**Dialogue**

General meetings  
 Nomination committees and governing bodies  
 Good practice development  
 The fixed-income portfolio

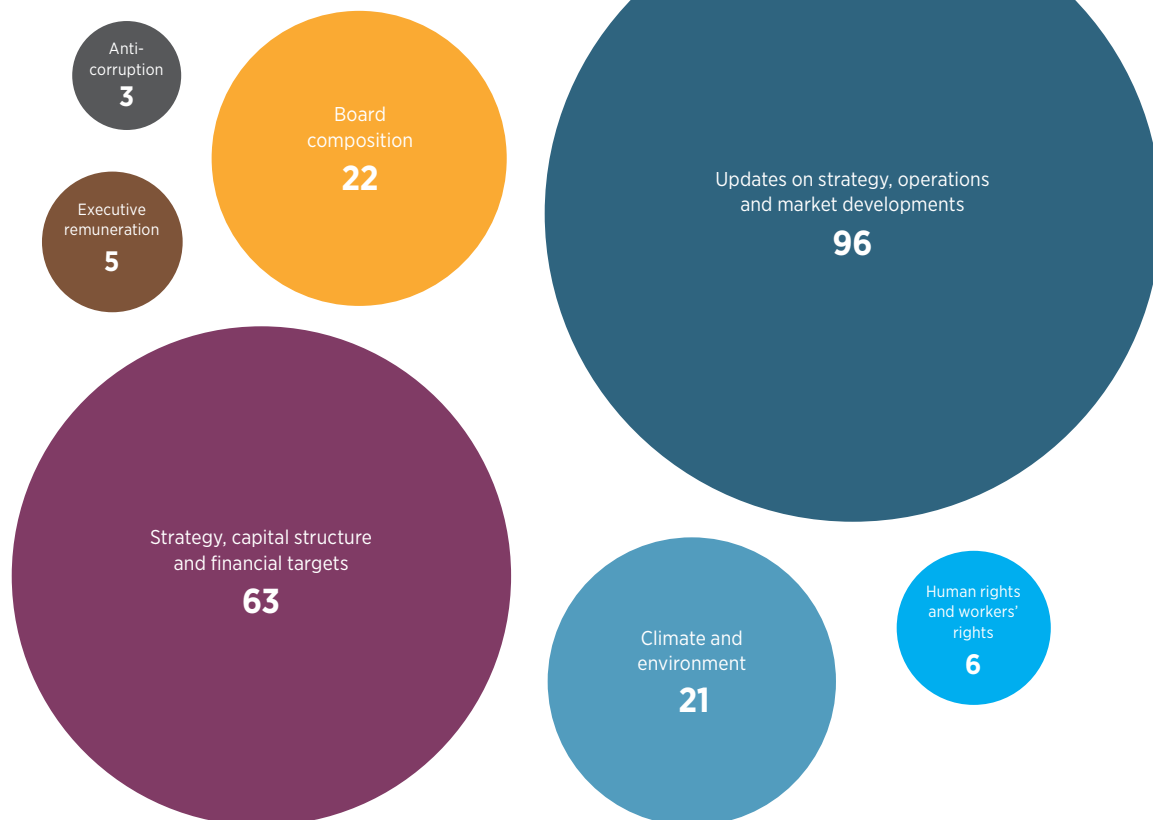
companies. By doing so, we can contribute to positive developments and returns over time. Our active management therefore makes us a better owner, and our active ownership makes us a better active manager.

In 2018, Folketrygdfondet held 143 dialogue meetings with a total of 53 companies listed on the Oslo Stock Exchange. At the portfolio level, we prioritised

two active ownership topics in particular: strategy, capital structure and financial targets, and implementation of the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). This is discussed further in the individual dialogue sections below.

**143 DIALOGUES**

Seven potential topics per dialogue  
 Number of times each topic has been raised:



## STRATEGY, CAPITAL STRUCTURE AND FINANCIAL TARGETS

Well-founded strategic priorities are a prerequisite for efficient capital utilisation and profitability over time. That is why we expect the portfolio companies to adopt long-term financial targets and communicate these clearly to the market. We also see this as important for long-term value creation.

Research<sup>1</sup> and our own experience indicate that companies that have long-term financial targets and communicate these clearly achieve stronger profitability and value creation than companies without clear targets and a long-term perspective.

The Norwegian business sector faces substantial challenges and necessary restructuring. We consider companies' clear communication of their strategies and long-term financial targets to be extremely important. Such communication can help ensure the company operates efficiently and allocates capital to the most profitable projects.

### What do we hope to achieve?

Our objective is maximum value creation both within the portfolio companies and in the market generally. Accordingly, we want companies to communicate clear targets for their return on capital, growth, and capital structure, to detail their tax policies and risk assessments, and to provide well-reasoned explanations for their strategic priorities. We assume that companies have a long-term strategy and a sustainable business model based on robust risk assessments, including climate risk. The strategy should include a clear, consistent dividend policy. Clear communication of a company's dividend policy is a prerequisite for predictability.

<sup>1</sup> Barton, Manyika, Williamson: *Finally, Evidence That Managing for the Long Term Pays Off*, HBR (2017)

There are several dividend policy models. What is critical is that each company selects the model that best matches the company's current operational phase and sector. An efficient capital structure is important to maximise long-term value creation. We expect that cash flow, after the deduction of growth and maintenance investments, will be distributed to shareholders. Dividends can be regarded as a residual. Any gaps between the long-term capital structure goal and actual capital structure should be explained. Insofar as possible, a dividend policy should specify the prioritised dividend form: cash or other dividend forms such as share buybacks/capital reductions.

From our perspective as an asset manager, this focus on communication is also about obtaining reliable data from companies. We want to have the best possible insight into the assessments, criteria, and objectives that underpin the companies' strategies for long-term competitiveness, growth and profitability.

### What are we doing?

We revised and updated our guide detailing our expectations regarding board-level work on strategy, capital structure and financial targets at the end of 2017 (please see [ftf.no](http://ftf.no), English pages). The most important changes in our expectations relate to the communication of dividend policy, tax policy and long-term strategy. The guide is available on [ftf.no](http://ftf.no).

We seek to promote more efficient allocation of capital by companies and markets, and to contribute to long-term value creation. Neither we nor other investors can take over the responsibilities and role of the board of directors. However, we can ask the right questions and expect satisfactory answers.

### Developments in 2018

In 2018, Folketrygdfondet used its updated expectation document in its dialogues with the managers and/or board chairs of various companies. Our aim was both to communicate our expectations and to obtain feedback from the companies.

The companies responded positively to the expectation document. In our experience, the document provides a good starting point for discussion of companies' long-term strategies, objectives and priorities for value creation over time. However, we have also noted that changing communication habits linked to strategy takes time. Companies with a long time horizon are more successful. This is why companies' communication of long-term strategy will remain an important topic in our ongoing dialogues with the portfolio companies.

## CLIMATE AND ENVIRONMENT

Implementation of the TCFD recommendations was a priority in Folketrygdfondet's responsible management work in 2018.

Climate risk is a material consideration for several of our portfolio companies. The significance of different climate risks for individual companies varies, depending on factors such as core activities.

### **What are we doing?**

Climate has been an important topic in Folketrygdfondet's management of the Government Pension Fund Norway for several years. We have developed a guide (please see [ftf.no](http://ftf.no), English pages) that sets out our expectations as to the portfolio companies' efforts to address climate challenges and their reporting on risks and opportunities, targets and results.

In 2018, Folketrygdfondet focused on the implications of the recommendations made by the Task Force on Climate-related Financial Disclosures (TCFD) working group for climate risk in the Government Pension Fund Norway. This work will continue for the foreseeable future. Folketrygdfondet's approach is to integrate the recommendations through gradual changes based on the structure and distinctive characteristics of our mandate.

The purpose of the TCFD recommendations is to facilitate financially relevant climate-related reporting. The requested information can be divided into two main categories: 1) how companies affect the environment through greenhouse gas emissions; and 2) the extent to which companies' business models and strategies are exposed to climate risk.

Folketrygdfondet supports the intention behind the recommendations, and considers it positive and important that the recommendations cover both how companies are affected by climate change and how companies affect the climate. As a large, universal shareholder in Norwegian and Nordic companies, Folketrygdfondet needs such information to make sound investment decisions and to understand how climate risk may affect the markets in which Folketrygdfondet invests.

Our focus is on ensuring that the portfolio companies understand the environmental impact of their activities in the form of greenhouse gas emissions, and the extent to which their business models and strategies are exposed to climate risk. The companies must consider what analyses and measures are required in order to identify and address climate risk.

The recommendations cover four areas: governance, strategy, risk management and targets, and metrics. The recommendations are intended to be relevant to companies in different sectors, countries and regions. In addition, special recommendations are included for specific sectors and industries.

### **What do we hope to achieve?**

Our priority is to ensure that the portfolio companies understand the impact of their activities on the climate through greenhouse gas emissions, and the extent to which their business models and strategies are exposed to climate risk. The companies must consider what analyses and measures are required in order to identify and address climate risk.

Folketrygdfondet requires sound, reliable information for use in company analysis. We therefore welcome

**CORE ELEMENTS OF THE TCFD FRAMEWORK**



**Governance**

The organisation’s governance around climate-related risks and opportunities.

**Strategy**

The actual and potential impacts of climate-related risks and opportunities on the organisation’s businesses, strategy, and financial planning.

**Risk management**

The processes used by the organisation to identify, assess, and manage climate-related risks.

**Metrics and targets**

The metrics and targets used to assess and manage relevant climate-related risks and opportunities.

Illustration 20

reporting by companies on their emissions, and how they handle significant climate-related commercial opportunities and risks.

Such reports may cover greenhouse gas emissions, absolute and relative targets for emissions reductions, and overviews of problems and investments required to adapt to expected climate-related changes, including future legislation, customer demands and physical climate change.

**Developments in 2018**

*Governance*

In 2018, Folketrygdfondet’s board decided to update the responsible investment principles (please see [ftf.no](http://ftf.no), English pages). In line with the TCFD recommendations, it was clarified that, “The Government Pension Fund Norway shall continuously assess and manage material sustainability-related risk, both threats and opportunities.” In addition, the administration updated the document Folketrygdfondets eierskaps-

utøvelse (Folketrygdfondet’s exercise of ownership rights – please see [ftf.no](http://ftf.no), English pages), expanding on Folketrygdfondet’s efforts to address systemic sustainability risk, including climate risk.

*Strategy and risk management*

Folketrygdfondet’s mandate provides the starting point for the assessment of portfolio risk, including climate risk. As a long-term, active investor, Folketrygdfondet measures excess return relative to its benchmark index. The benchmark index is composed of equities (60 percent) and bonds (40 percent), and is split between Norwegian investments (85 percent) and other Nordic investments (15 percent).

As an active manager, Folketrygdfondet has the opportunity to adapt portfolio weightings in response to changes in the financial risk profile. Our strategy for achieving excess returns is further explained in Folketrygdfondet’s strategic plan (please see [ftf.no](http://ftf.no), English pages), which identifies political develop-

ments, structural trends, sector dynamics and other material changes in framework conditions as some of the assessment factors included in our analyses. Our investment decisions are underpinned by broad-based information-gathering, analyses and contact with companies, including ESG analysis.

Folketrygdfondet's ability to generate excess returns in the short, medium and long-term is dependent on reliable assessments of market risk, including climate-related risk. Such assessments are therefore an integral part of our investment responsibilities. At the same time, it is vital for our long-term returns that the portfolio companies deliver robust long-term results.

To improve our understanding of how climate affects our investment activities, we have prepared an annual emissions analysis for the equities portfolio since 2013. The emissions analysis improves our understanding of the financial risk associated with altered emissions prices, and gives us greater insight into the portfolio companies' readiness to manage climate-related risk, as emissions reporting is a prerequisite for doing so. Information access and quality are particular challenges in this regard. When companies do not report their emissions, we use estimates. Even when companies do report their emissions, difficulties arise with regard to a lack of standardisation and quality assurance. This is why Folketrygdfondet has prioritised better and more comprehensive climate reporting in its active ownership activities for several years.

Although an emissions analysis improves our understanding of climate-related issues, it also has significant limitations. For example, the analysis tells us nothing about how the companies in the portfolio are positioned with regard to legislative changes or the transition to a low-emission economy (transition risk). Further, it says little about how the portfolio will be impacted by physical climate change and resulting consequences (extreme weather, drought, floods and changes in raw material supply). The TCFD has addressed this complexity by recommending supplementation of emissions analyses with several additional tools,

such as scenario analyses.

Different scenarios for climate policy and atmospheric heating produce very different estimates of transition risk and physical risk. Accordingly, developing a robust methodology for climate-related scenario analysis is a prerequisite in order for such information to be useful and relevant for investors and companies. The TCFD recommendations recognise that the development and use of climate-related scenario analysis is at an early stage, and calls for further methodological development. Thus far, we have not attempted to quantify the effect of different climate scenarios on the portfolio, having concluded that the scenario analysis models developed to date are insufficiently mature. This will be a priority in our climate risk-related work going forward. Official Norwegian Report (NOU) 2018:17 – Climate risk and the Norwegian economy – is an important contribution in this regard.

To effect a meaningful expansion of their climate-risk analyses, investors generally require better information access, quality and standardisation. Key questions in this regard are whether aggregated company information accurately represents investors' climate risk and whether 'top-down' analyses of investor climate risk should be developed.

Taking Folketrygdfondet's distinctive characteristics into account, it appears most sensible to start with a 'bottom-up' assessment of climate risk in the portfolio. This is why, in 2018, we collaborated with several other Norwegian investors to engage in active ownership with companies in industries identified by the TCFD as particularly exposed to climate-related risk. Further, climate risk was incorporated into Folketrygdfondet's ongoing dialogue with portfolio company management. The insights gained through this dialogue are used to further evaluate the portfolio under different climate scenarios.

#### *Metrics and targets*

We have conducted emissions analyses of the Norwegian equity portfolio since 2013. The analysis for 2018

measures greenhouse gas emissions for the equity portfolio as a whole (weighted to reflect our ownership percentages), and makes a comparison with our benchmark index. Due to the weaknesses of the emissions analysis, it is used only as an indicator of climate risk, not as a metric by which the portfolio is managed. Folketrygdfondet does not assess climate risk separately from investment performance.

Folketrygdfondet's CO<sub>2</sub>e analysis\* is based on our equity portfolio as at 31 December 2018. The figures are calculated using Bloomberg's analysis tool for measuring the carbon footprint of securities portfolios.

For the first time this year, Folketrygdfondet reports the proportion (rather than the absolute number) of companies in the portfolio and the benchmark index, respectively, that report their CO<sub>2</sub> emissions. We use the targets in the TCFD recommendations. In other words, the targets include the portfolio's CO<sub>2</sub> intensity, adjusted for both our share of each company's market value (equity method) and each company's relative size within the portfolio (weighted average CO<sub>2</sub> intensity).

\* CO<sub>2</sub>e stands for CO<sub>2</sub> equivalent, and compares the emissions of different greenhouse gases relative to one unit of CO<sub>2</sub>. It is calculated by multiplying the emissions of a given greenhouse gas by the gas's 100-year global warming potential. Source: SSB.

The analysis incorporates 2017 data on direct emissions (Scope 1) and indirect emissions from energy (Scope 2). Emissions estimates are used for companies that do not report emissions directly or to the CDP.

#### We use the following indicators in our emissions reporting related to equities:

1. The portfolio's absolute CO<sub>2</sub> emissions. The figure is based on the total emissions of the portfolio companies, adjusted to reflect our ownership percentages (tonnes of CO<sub>2</sub>e).
2. The portfolio's CO<sub>2</sub> efficiency. The figure is based on the portfolio companies' emissions compared to our investment (tonnes of CO<sub>2</sub>e/NOK million invested).
3. The weighted average of the portfolio's CO<sub>2</sub> intensity. The figure is based on the portfolio companies' total CO<sub>2</sub> emissions compared to sales (tonnes of CO<sub>2</sub>e/NOK million in sales), adjusted to reflect the value of the shareholding in each company compared to the portfolio value.
4. The portfolio's CO<sub>2</sub> intensity. The figure is based on the portfolio companies' total CO<sub>2</sub> emissions compared to sales (tonnes of CO<sub>2</sub>e/NOK million in sales), adjusted to reflect our share of the companies' market value.

#### CO<sub>2</sub> ANALYSIS FOR THE EQUITY PORTFOLIO AS AT 31 DECEMBER 2018

	Portfolio	Benchmark index	Difference
Percentage of companies that report their greenhouse gas emissions	80.76	77.80	-
TCFD Total CO <sub>2</sub> emissions (tonnes of CO <sub>2</sub> e)	2,571,012	161,735,488	-
TCFD Total CO <sub>2</sub> emissions per NOK million invested (tonnes)	18.23	19.58	-1.34
TCFD Weighted average CO <sub>2</sub> intensity (weighted average tonnes/NOK million)	23.92	25.36	-1.44
TCFD CO <sub>2</sub> intensity (tonnes/NOK million in sales)	28.09	29.61	-1.51

## Climate risk in the portfolio

**Joint active ownership related to climate risk**

To identify risks and opportunities in the portfolio, Folketrygdfondet participated in a joint investor dialogue with several of the largest Norwegian companies in the portfolio, covering several of the industries specifically referred to in TCFD's supplemental guidance.

The first round of dialogue covered the following industries:

- the energy sector (both energy production and offshore/oil service)
- materials, and
- consumer staples

Dialogue meetings will continue in 2019.

The purpose of the meetings is to discuss with the companies and several of their largest investors how they can identify and manage climate risk, and to communicate our expectations in this area. In our experience, such dialogue helps raise awareness and enables companies and investors to learn from one another. This gives investors like Folketrygdfondet greater insight into the opportunities and challenges the companies face.

<b>Index: follow-up of TCFD recommendations</b>	<b>Folketrygdfondet's response</b>
<b>Governance</b>	
a) Describe the board's oversight of climate-related risks and opportunities	Mandate for the management of the Government Pension Fund Norway, chapter 2 Ownership report, page 64 ("How we organise our responsible investment activities")
b) Describe management's role in assessing and managing climate-related risks and opportunities	Principles for responsible investment <i>Folketrygdfondets eierskapsutøvelse</i> (Folketrygdfondet's exercise of ownership rights) Ownership report, page 64 ("How we organise our responsible investment activities")
<b>Strategy</b>	
a) Describe the climate-related risk and opportunities the organisation has identified over the short, medium and long term	Ownership report, pages 82-83 ("Strategy and risk management")
b) Describe the impact of climate-related risks and opportunities on the organisation's businesses, strategy, and financial planning	Ownership report, pages 82-83 ("Strategy and risk management") Strategic plan, pages 9-12
c) Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario	Ownership report, pages 82-83 ("Strategy and risk management")
<b>Risk management</b>	
a) Describe the organisation's processes for identifying and assessing climate-related risks	Ownership report, pages 82-83, 85 ("Strategy and risk management") Strategic plan, pages 9-12
b) Describe the organisation's processes for managing climate-related risks	Ownership report, pages 82-83 ("Strategy and risk management")
c) Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management	Ownership report, pages 82-83 ("Strategy and risk management")
<b>Metrics and targets</b>	
a) Disclose the metrics used by the organisation to assess climate-related risks and opportunities in line with its strategy and risk management process	Ownership report, pages 83-84 ("Metrics and targets")
b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks	Ownership report, page 84 ("Metrics and targets")
c) Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets	Ownership report, pages 83-84 ("Metrics and targets")

## ANTI-CORRUPTION

Corruption undermines value growth in society and harms the operations of involved companies. At the individual level, the financial consequences of corruption may involve exclusion from markets, lost contracts, fines and prolonged legal proceedings.

As a financial investor, Folketrygdfondet therefore considers it vital that companies take anti-corruption efforts seriously. The portfolio companies are expected to combat all forms of corruption, including blackmail and bribery.

### **What do we hope to achieve?**

In its capacity as an investor, Folketrygdfondet applies the clear requirement that the companies in which it invests may not be involved in corruption.

### **What are we doing?**

The portfolio companies bear independent responsibility for protecting their operations, assets and reputations against corrupt practices. Companies must identify, address and report on material challenges. To clarify our expectations of the companies, we have prepared an expectation document on anti-corruption (please see [ftf.no](http://ftf.no), English pages). We address corruption risk in our dialogue with the boards and management teams of the portfolio companies where relevant.

### **Developments in 2018**

In 2018, we conducted precautionary anti-corruption dialogue with three portfolio companies. The aim was to understand their strategies for preventing, detecting and mitigating corruption risk. In our experience, a thorough understanding of a company's risk profile is crucial for setting anti-corruption priorities. The tone at the top and corporate culture are also decisive. That is why we have included the tone at the top and culture-building as topics in our anti-corruption dia-

logues. Our aim is to understand management efforts to integrate anti-corruption into corporate culture, and the challenges that arise in this context.

## HUMAN RIGHTS AND WORKERS' RIGHTS

We expect the portfolio companies to respect human rights and workers' rights. The appropriate measures depend on where in the supply chain risk arises.

Violations of human rights and workers' rights have a negative impact on economic growth, promote social inequality, and foster political and civil unrest. For companies, the impacts may entail operational disruption due to delays, reduced productivity and lower quality. Companies may also suffer a reputational loss.

### **What do we hope to achieve?**

We expect portfolio companies to avoid and prevent involvement in breaches of human and workers' rights by adopting a careful approach and conducting necessary analyses to survey their risk exposure. We expect the companies to operate in accordance with the OECD Guidelines for Multinational Enterprises.

### **What are we doing?**

Responsibility for ensuring that fundamental human and workers' rights are respected throughout the organisation, and that respect for such rights is integrated into the corporate culture, rests with the portfolio company boards and management teams. This includes assessing whether the business is at risk of involvement in human rights or workers' rights violations and where in the supply chain any such risks arise.

To clarify our expectations of the companies, we have prepared two guides, on human rights and workers' rights, respectively. We discuss risks associated with human rights and workers' rights in our dialogue with company boards and managers where relevant.



**Developments in 2018**

In 2018, we conducted precautionary dialogues concerning human and workers' rights with six portfolio companies. In these dialogues, we concentrated on matters such as the companies' efforts to ensure employee safety, new EU data protection rules, and companies' efforts to address issues related to responsible shipbreaking. We have a particular focus on understanding the systems and processes companies adopt to manage these risks.

Traditionally, the risk of contributing to violations of human rights and workers' rights has been particu-

larly relevant for companies with operations or supply chains in countries impacted by poverty, weak public institutions and/or undemocratic political governance. However, rapid technological developments are increasing the risk of human rights violations in other types of businesses. This makes human rights relevant to an increasing number of portfolio companies. For example, the risk of involvement in breaches of privacy has become more prominent in our portfolio, and is something we are addressing in our dialogue with companies.

**COMPANY DIALOGUES BY TOPIC IN 2018**

<b>Portfolio</b>	<b>Number of companies</b>	<b>Number of dialogue meetings</b>
Financial targets and capital structure	37	63
Climate and environment	14	21
Anti-corruption	3	3
Human rights and workers' rights	6	6

## WE ARE AVAILABLE TO THE PORTFOLIO COMPANIES

Our aim is to be a constructive and responsible owner. We ask challenging questions about important issues, but are also available to the companies.

In some cases, Folketrygdfondet asks a company for an update, feedback, clarification or action on a specific matter or in connection with a particular topic that we consider highly important for the company. At the same time, companies have their own priority topics and issues. We know that being a large shareholder entails certain responsibilities, and we prioritise being available to the companies in which we have invested.

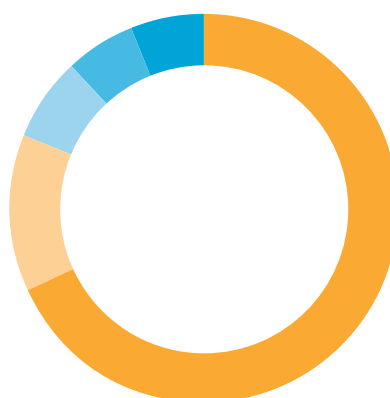
Folketrygdfondet held 143 dialogue meetings last year, discussing key ownership issues with some 53 companies.

This dialogue with board chairs and managers enables us to understand a company's strategy, operations, growth opportunities and risk profile, and thereby makes us a better active manager, not least because we can evaluate the portfolio companies' capital needs and strategic priorities.

Our meetings with companies often take place at a high level. We prioritise this form of working in relation to our equity investments, and devote considerable time and resources to direct company contact. In our ownership capacity, we use such meetings to discuss both specific incidents in a company and key ownership questions, including capital structure and financial targets. When it is helpful to have subject matter experts present, for example when discussing specific environmental or social issues, both Folketrygdfondet and the company ensure the participation of staff with the appropriate expertise.

We apply the same active ownership principles to our Norwegian and Nordic equity investments.

### OVERVIEW OF OUR DIALOGUE PARTNERS



Management	69 %
Nomination committee	13 %
Styreleder	7 %
Board	6 %
IR/others	6 %

However, we distinguish between active ownership within and outside Norway. One reason for doing so is that we generally have smaller ownership interests in Nordic companies.

## WE PROTECT SHAREHOLDER INTERESTS

General meetings are a key arena for Folketrygdfondet's active ownership. In 2018, we voted against proposals put forward by the boards of seven Norwegian companies because we determined that shareholder interests were set aside.

Voting at the general meetings of all the portfolio companies is a central aspect of Folketrygdfondet's active ownership. Whenever possible, we try to attend the general meetings of portfolio companies listed on the Oslo Stock Exchange in person.

### What is the purpose?

All active ownership has the overarching purpose of supporting maximum value creation over time. In the vast majority of cases, we vote for board proposals at general meetings because we find them to be well founded and consistent with company strategy.

In some instances, however, we see that a board proposal challenges shareholder interests and recognised good corporate governance principles. Folketrygdfondet considers it important to be a strong representative of minority shareholders in Norwegian-listed companies. Equal treatment of all shareholders is of fundamental importance. Along with other minority shareholders, we have a clear interest in compliance with the rules and protection of the interests of all shareholders.

From a longer-term perspective, good corporate governance is also about preserving confidence in the integrity of the Norwegian stock market.

### What do we achieve?

Over time, shareholders including Folketrygdfondet have successfully presented their views on the design and scope of executive remuneration schemes and board authorisations. Controversial pay and authorisation proposals were more common before, but are now

the exception.

In general, we have seen an improvement in recent years in the dialogue between company boards and shareholders. This has improved the boards' ability to consider shareholder views before proposals are put forward, thereby reducing the number of surprises and confrontations at general meetings.

Our procedures for

### General meetings

- Folketrygdfondet votes at the general meetings of portfolio companies.
- Wherever practicable, we aim to participate in person in the general meetings of companies listed on the Oslo Stock Exchange.
- If we vote by proxy, we always issue voting instructions.
- Prior to a general meeting, we conduct a thorough review of the agenda and vote in accordance with our principles, guidelines and assessments.
- Folketrygdfondet recalls all loaned-out shares in a given company prior to its general meeting.
- Our starting point is that we want to vote in favour of the board's proposals. If we disagree with a board proposal, we seek to explain our position before the general meeting.
- If we vote against a board proposal, we normally publish a voting statement on our website after the general meeting.
- Our aim is to help secure broad agreement on the general meeting agenda, and we consider pre-general meeting dialogue with the company a positive measure in this regard.

Nomination committee independence

**Folketrygdfondet put forward a shareholder proposal for reasons of principle at the general meeting of Norwegian Air Shuttle**

At the general meeting of Norwegian Air Shuttle ASA on 8 May 2018, the board of directors sought to amend the articles of association to make the board chair a permanent member of the nomination committee. Folketrygdfondet voted against the proposal, and put forward an alternative, which provided that the committee's members should be elected by the general meeting for a two-year term. Although our proposal was not adopted, it did secure the support of KLP and DNB.

In our view, members of nomination committees must be independent of individual board members. The independence of the nomination committee is crucial in enabling

shareholders to have the necessary confidence in nomination committee proceedings and recommendations. A clear division of roles and responsibilities between the board of directors and the nomination committee is fundamental to the committee's work. In principle, we want to vote for board proposals at general meetings. In this case, however, the shareholders were asked to approve an amendment to the articles of association that was inconsistent with our fundamental view on nomination committee independence. Folketrygdfondet informed the company of its voting intentions in advance, and continued its dialogue with the company on the topic after the general meeting.

**NORWEGIAN COMPANIES WHERE FOLKETRYGDFONDET VOTED AGAINST BOARD PROPOSALS**

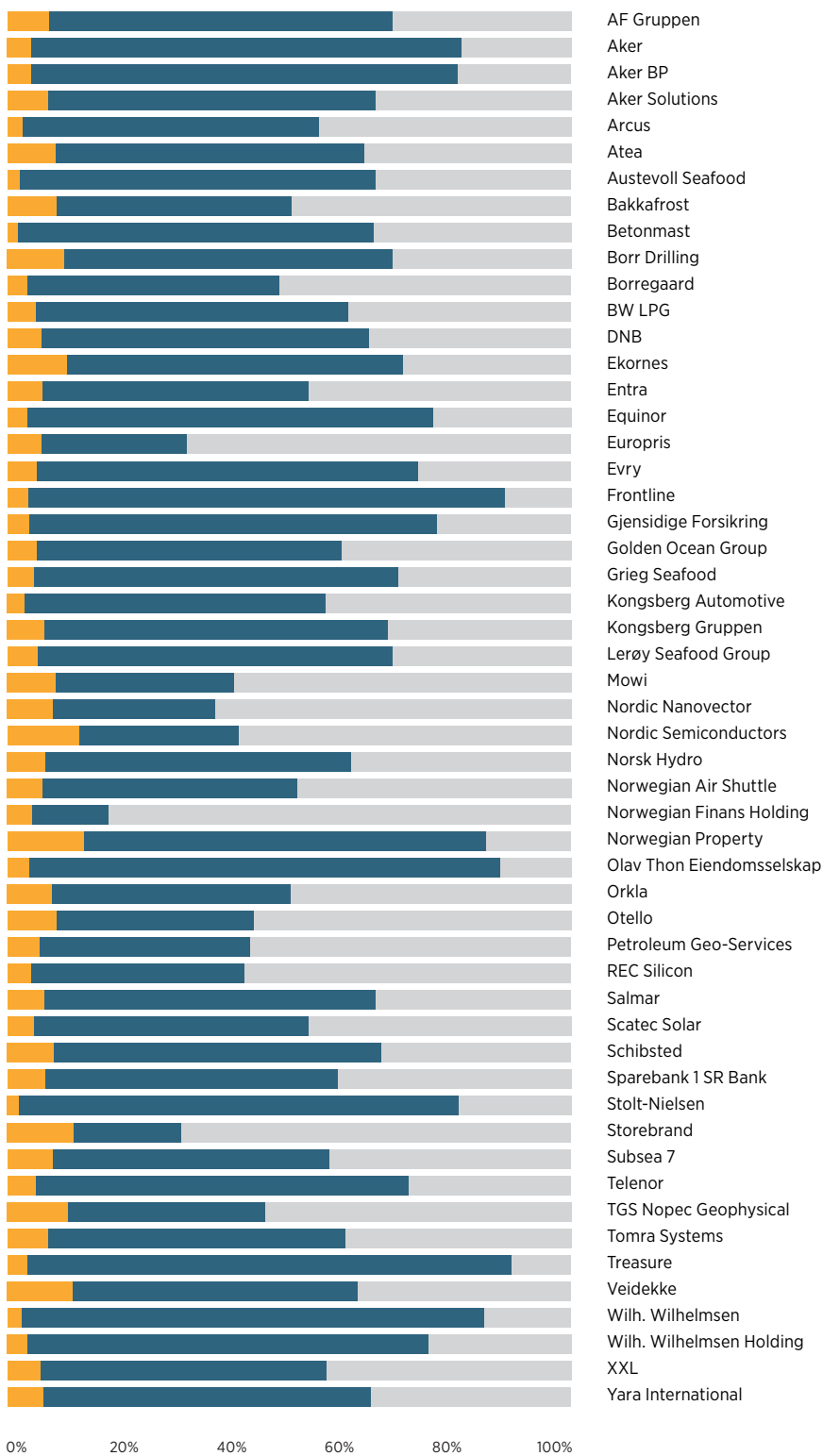
All proposals were adopted despite Folketrygdfondet's vote.

Company	Date	Type of case   Why we voted against	Percentage of votes against	
			Folketrygdfondet	Total
Subsea 7 S.A.	17 April 2018	Board composition <i>Reason:</i> Jean Cahuzac is the CEO of Subsea 7. Section 8 of the Norwegian Code of Practice for Corporate Governance states that the board of directors should not include executive personnel. One of the board's main tasks is the supervision of company management, which includes appointment and dismissal of the CEO. Folketrygdfondet considers that board members can only supervise company management adequately if they are not recruited from among management.	13.9	25.0
Stolt-Nielsen Limited	19 April 2018	Board composition <i>Reason:</i> Niels G. Stolt-Nielsen is the CEO of Stolt-Nielsen Limited. Section 8 of the Norwegian Code of Practice for Corporate Governance states that the board of directors should not include executive personnel. One of the board's main tasks is the supervision of company management, which includes appointment and dismissal of the CEO. Folketrygdfondet considers that board members can only supervise company management adequately if they are not recruited from among management.	2.6	4.5
Scatec Solar ASA	23 April 2018	Executive remuneration, share repurchase authorisation and authorisation to issue shares  <b>Item 8b</b> Statement on salaries and other remuneration for senior employees  <b>Item 13</b> Board authorisation to acquire own shares  <b>Item 14</b> Board authorisation to implement a capital increase  <i>Reason:</i> Folketrygdfondet supports remuneration schemes that are targeted and performance-dependent. Incentive schemes should be linked to personal targets, company targets and targets designed to ensure good long-term value creation for shareholders. Moreover, we expect option schemes and other share-based programmes to be capped and to have a reasonable scope.  Since Scatec Solar's option scheme lacked a cap and could result in the issue of new shares totalling up to 5 percent, Folketrygdfondet considered that the scheme had an excessive scope and could entail an excessive transfer of value from the shareholders to the company's employees.	8.7 8.7 8.7	10.0 8.7 8.7

Company	Date	Type of case   Why we voted against	Percentage of votes against	
			Folketrygdfondet	Total
Norwegian Air Shuttle ASA	8 May 2018	<p>Amendment of articles of association concerning nomination committee <i>Reason:</i> The board proposed amending the second paragraph of Article 8 of the articles of association to make the board chair a permanent member of the nomination committee. Folketrygdfondet is fundamentally opposed to such an arrangement.</p> <p>Folketrygdfondet takes the view that members of nomination committees must be independent of individual board members. The independence of the nomination committee is crucial in enabling shareholders to have the necessary confidence in nomination committee proceedings and recommendations. A clear division of roles and responsibilities between the board of directors and the nomination committee is fundamental to the committee's work. Both the current provision in the articles of association on the composition of the nomination committee and the proposed amendment to the second paragraph of Article 8 breached section 7 of the Norwegian Code of Practice for Corporate Governance.</p>	12.1	26.8
Norwegian Property ASA	19 April 2018	<p>Executive remuneration and authorisation to issue shares</p> <p><b>Item 12C</b></p> <p><i>Reason:</i> Folketrygdfondet wants its portfolio companies to have well-functioning and robust boards of directors. Folketrygdfondet is fundamentally opposed to issuing options to board members, and to board members performing additional tasks for the company beyond their board appointment. This also follows from section 11 of the Norwegian Code of Practice for Corporate Governance. Section 1 of the nomination committee's recommendation stated that one of the proposed board members would be providing advisory services to the company in addition to the board appointment, and that this would be remunerated by means of an option agreement.</p> <p>Under item 12 c, it was proposed that the board be authorised to increase the share capital, including to facilitate the issue of shares in connection with incentive schemes for board members. Since both the issue of options to board members and the conclusion of agreements with board members relating to advisory services are contrary to Folketrygdfondet's fundamental views and the Norwegian Code of Practice for Corporate Governance, Folketrygdfondet voted against the proposal under item 12 c.</p> <p><b>Item 14B</b> Board authorisation to acquire own shares (incentive scheme)</p> <p><i>Reason:</i> The purpose of the board authorisation proposed under item 14 b was identical to the purpose under item 12 c. Please see the voting statement relating to item 12 c.</p>	15.9	16.4
Frontline	21 September 2018	<p>Board composition <i>Reason:</i> Robert Hvide Macleod is the CEO of Frontline Ltd. Section 8 of the Norwegian Code of Practice for Corporate Governance states that the board of directors should not include executive personnel. One of the board's main tasks is the supervision of company management, which includes appointment and dismissal of the CEO. Folketrygdfondet considers that board members can only supervise company management adequately if they are not recruited from among management.</p>	4.1	13.1
Borr Drilling	25 September 2018	<p>Board composition <i>Reason:</i> The board of Borr Drilling Ltd. requested an authorisation from the general meeting granting it power to appoint new board members. Folketrygdfondet is fundamentally of the view that board members should be elected by the shareholders at a general meeting.</p>	14.7	23.8

**ATTENDANCE 2018 – NORWEGIAN COMPANIES**

Ordinary general meetings that Folketrygdfondet attended.



**Folketrygdfondet** attended a total of 53 ordinary general meetings in 2018, as well as 12 extraordinary general meetings.

■ Folketrygdfondet  
■ Other shareholders  
■ Not represented

**The attendance rate** for all ordinary general meetings attended by Folketrygdfondet was 61.2 percent, with a range from 17.8 percent to 89.5 percent.

## VOTED AT 85 NORDIC GENERAL MEETINGS

In 2018, Folketrygdfondet voted at a total of 85 general meetings of companies listed on stock exchanges in Sweden, Denmark and Finland.

In total, we voted against or abstained from voting on 29 proposals put forward by the boards of Swedish, Danish or Finnish companies. Most of the board proposals we voted against in the Nordic portfolio companies related to executive remuneration statements and incentive schemes. We often find that executive remuneration statements contain insufficient information on the scheme in question, that incentive programmes lack individual performance requirements, or that schemes include a strong discretionary element.

We voted against or abstained from voting for individual board members in the case of three Swedish companies. In one instance, the CEO had been proposed as the board chair – a dual appointment that is contrary to Swedish law. Since it was only possible to vote for or against the board as a whole, we decided to abstain from voting for the entire board. In the second instance, we voted against a board member who has been involved in several corruption cases. In the third company, we voted against a board chair who had participated in less than 75 percent of board meetings. We also voted against candidates for the nomination committees of two Swedish companies where the proposals detailing the candidates contravened Swedish law or the Swedish corporate governance recommendation.

We voted against or abstained from voting on auditor fees and/or auditor reappointment in relation to two companies because the fees for non-audit services exceeded the fees for audit services. Auditors are supposed to perform a control function, and their inde-

pendence from the company is put at risk if they provide extensive advisory services in addition to auditing. Compared to previous years, shareholders in companies listed in Sweden submitted far fewer various proposals to general meetings. Many of these proposals concern issues falling outside the shareholders' remit, as defined by the general principles governing the distribution of roles in listed companies. Shareholder proposals are much rarer in the other Nordic countries.

Our procedures for

### General meetings of Nordic companies

- Folketrygdfondet votes by proxy at the general meetings of the Nordic portfolio companies.
- The proxy authorisation always includes voting instructions.
- Prior to all general meetings, we conduct a thorough review of the agenda items, and vote in accordance with our principles, guidelines and assessments.
- Folketrygdfondet recalls loaned-out shares in the relevant company if we intend to vote against an agenda item based on a matter of principle.
- Our starting point is that we want to vote for board proposals. When we vote against a board proposal, we report this in the aggregated country statistics in the Ownership report.
- Our aim is to help ensure that agenda items are broadly supported, and that companies take a positive view of shareholder dialogue prior to general meetings.

## VOTING RELATED TO COMPANIES LISTED IN DENMARK, FINLAND AND SWEDEN IN 2018

	Sweden	Denmark	Finland	Total
<b>Total number of general meetings voted</b>	<b>47</b>	<b>23</b>	<b>15</b>	<b>85</b>
<b>Total number of matters voted</b>	<b>758</b>	<b>329</b>	<b>158</b>	<b>1,245</b>
<b>Board proposals</b>				
• Against	16	9	1	<b>26</b>
• Abstained from voting	3			<b>3</b>
<b>Board proposals where Folkestrygdfondet has voted against/abstained from voting, by topic</b>				
• Executive remuneration statement	9	4		<b>13</b>
• Board/board remuneration		1		<b>1</b>
• Auditor fees/auditor reappointment		1	1	<b>2</b>
• Articles of association	1 (abstained)	3		<b>3</b>
				<b>1 (abstained)</b>
• Authorisation to issue shares/repurchase own shares	3			<b>3</b>
• Nomination committee	2			<b>2</b>
• Against entire board/one board member	2			<b>2</b>
	1 (abstained)			<b>1 (abstained)</b>
<b>Shareholder proposals</b>				
• Against	11			<b>11</b>
• For	1			<b>1</b>
• Abstained				



## MEMBER OF EIGHT NOMINATION COMMITTEES

Folketrygdfondet is represented on eight nomination committees of Norwegian companies. We also participated in three corporate assemblies in 2018.

Folketrygdfondet considers it important to help ensure that the boards of the portfolio companies have strong expertise and the right composition. Folketrygdfondet expects the companies in which it invests to have a nomination committee.

Company boards are becoming more professional, and it is crucial that boards collectively possess the necessary skills. Nomination committees have therefore assumed an increasingly central role in recent years. Folketrygdfondet has helped to drive this development forward, not least through its participation in the Eierforum group of institutional investors and through

the Norwegian Corporate Governance Board (NUES).

Our top priority is to make sure that the portfolio companies have reliable processes in place to elect competent boards. We therefore prioritise participating in nomination committees in some of the companies in which we have invested. However, the number of nomination committees has to be limited due to the time-consuming nature of the work involved.

Folketrygdfondet does not participate in company boards, but was involved in several corporate assemblies in 2018, in addition to the various nomination committees.

### REPRESENTATIVES ON NOMINATION COMMITTEES AND GOVERNING BODIES

#### Corporate assemblies

Norsk Hydro ASA	Chief Investment Officer Equities Nils Bastiansen	Member
Statoil ASA	Chief Investment Officer Equities Nils Bastiansen	Deputy chair
Telenor ASA	Deputy Managing Director Lars Tronsgaard	Deputy chair

#### Nomination committees

Yara International ASA	Deputy Director Equities Ann Kristin Brautaset	Member
Schibsted ASA	Deputy Director Equities Ann Kristin Brautaset	Member
Storebrand ASA	Deputy Managing Director Lars Tronsgaard	Member
TGS-NOPEC ASA	General Counsel Christina Stray	Member
Veidekke ASA	Portfolio Manager Joakim Gjersøe	Member
Marine Harvest ASA	Chief Investment Officer Equities Nils Bastiansen	Member
Gjensidige Forsikring ASA	Portfolio Manager Joakim Gjersøe	Member
Telenor ASA	Deputy Managing Director Lars Tronsgaard	Member

## PROMOTING WELL-FUNCTIONING MARKETS

Folketrygdfondet participates in external initiatives to develop good practices and standards for commercial activity. We consider this an important instrument for ensuring both well-functioning markets and robust long-term returns.

Folketrygdfondet participates in various forums to exchange information and experience with other investors and to support the development of new regulations and standards. Satisfactory long-term returns can only be achieved in well-functioning markets. Robust standards for commercial activity are a further prerequisite.

Cooperation with other investors is important for the adoption of good practices and commercial standards.

### What are we doing?

We participate in Norwegian and international initiatives, and also cooperate on a case-by-case basis when prudent to protect our financial interests. In 2018, we worked to promote strong standards through the external initiatives in which we are engaged. For example, in the context of the Norwegian Forum for Responsible and Sustainable Investment (Norsif), we chaired a working group focusing on responsible fixed income investment. The working group published a report entitled ESG Integration in Norwegian Fixed Income (see [norsif.org/resurser](http://norsif.org/resurser)), which examines how Norwegian investors deal with the issue.

Another initiative to which Folketrygdfondet contributed is the Norwegian restructuring forum (Norsk restruktureringsforum, see [reforum.no](http://reforum.no)), which has developed a Norwegian recommendation on restructuring processes. The recommendation provides guidance for company boards and managers on the re-establishment of an operational and financial foundation for profitable future operations. A further aim is to establish a mechanism for continued development of the recommendation and knowledge sharing in this area through seminars on relevant topics.

Folketrygdfondet also submitted comments for three public consultations (please see [ftf.no](http://ftf.no), English pages), on relevant topics. These include proposals concerning implementation of the Prospectus Regulation and rules on national prospectuses, implementation

### Contributing to well-functioning markets

#### Revision of the Norwegian Code of Practice for Corporate Governance

**The Norwegian Corporate Governance Board (NUES) issued a revised code of practice in 2018. Folketrygdfondet supports the changes and the board's decision to retain the recommendations on nomination committee independence.**

On 29 May 2018, Folketrygdfondet submitted consultation comments supporting retention of the NUES recommendation that nomination committee members should be independent of the board of directors. The function of the nomination committee is to evaluate whether the board has the right composition and necessary expertise in view of the company's needs. Undesirable conflicts of interest may arise if nomination committee members have to evaluate their own work as board members. The revised code of practice also supports this view.

Folketrygdfondet also proposed revision of the code's provisions on ethics and corporate social responsibility to include a recommendation that the board of directors should evaluate company objectives, strategies and risks on an ongoing basis, including material risks and opportunities related to corporate responsibility. In Folketrygdfondet's view, the revised code of practice represents an improvement, in that companies must now explain how considerations related to the world around them impact company value creation.

of supplementary legislation relating to MiFiD II and MIFIR, and revision of the Norwegian Code of Practice for Corporate Governance.

### What do we hope to achieve in 2018?

In 2018, we will continue to promote robust standards through the external initiatives in which we are actively engaged. We also intend to provide feedback in public consultations and other input where relevant.

## PARTICIPATION IN EXTERNAL INITIATIVES IN 2018

Initiative	Purpose	FTF appointments
Norwegian Institute of Directors	To promote value creation through good corporate governance. Promote the development of best practice standards for board work	<ul style="list-style-type: none"> <li>General Counsel Christina Stray, board member and member of the capital markets technical committee</li> </ul>
Norwegian Society of Financial Analysts	To promote: <ul style="list-style-type: none"> <li>public understanding of the function and importance of the capital markets in the Norwegian economy</li> <li>the provision of high quality financial analysis</li> <li>the efficient functioning of the capital market within appropriate operating parameters</li> <li>high ethical standards in financial analysis, asset management, advisory services and trading in financial instruments</li> </ul>	<ul style="list-style-type: none"> <li>General Counsel Christina Stray, board member and member of the equity committee</li> <li>Deputy Director Equities Ann Kristin Brautaset, member of the committee that awards the Stockman Prize</li> <li>Deputy Managing Director Lars Tronsgaard, member of the portfolio committee</li> <li>Portfolio Manager Hege Kristine Huse, member of the bond committee</li> <li>Senior analyst for responsible investments Annie Bersagel, member of the equity committee, the committee on women in front-end finance, and the AFA/CEFA student Committee</li> </ul>
Norwegian Corporate Governance Board (NUES)	To keep the Norwegian Code of Practice for Corporate Governance updated and to promote the code both in Norway and internationally	<ul style="list-style-type: none"> <li>General Counsel Christina Stray, representative</li> </ul>
Eierforum group of institutional investors	To promote corporate governance best practice in Norway and drive forward further development of best practice. The forum is represented on the Norwegian Corporate Governance Board	<ul style="list-style-type: none"> <li>Chief Investment Officer Equities Nils Bastiansen, member</li> </ul>
Norwegian Forum for Responsible and Sustainable Investment (Norsif)	To promote and contribute to the development of the field of responsible investment in the Norwegian financial industry and among other stakeholders	<ul style="list-style-type: none"> <li>General Counsel Christina Stray, chair of the nomination committee</li> <li>Senior analyst for responsible investments Annie Bersagel, chair of the working group on responsible fixed income investment</li> </ul>
CDP (formerly known as the Carbon Disclosure Project)	To prevent climate change and protect natural resources	<ul style="list-style-type: none"> <li>Senior analyst for responsible investments Annie Bersagel, representative</li> </ul>
The UN-supported Principles for Responsible Investment (PRI)	To promote understanding of the investment and asset management implications of environmental, social and governance (ESG) issues	<ul style="list-style-type: none"> <li>Senior analyst for responsible investments Annie Bersagel, representative</li> </ul>
Norsk restruktureringsforum, the Norwegian restructuring forum	Prepare a recommendation on restructuring processes and establish a mechanism for further development of the recommendation	<ul style="list-style-type: none"> <li>Deputy Managing Director Lars Tronsgaard, member</li> </ul>

## A CHANGING HIGH-YIELD MARKET

The new issue volume of the Nordic high-yield market remained relatively high in 2018, at NOK 115 billion. This was on par with the 2017 volume of NOK 117 billion.

Credit spreads in the international bond markets widened throughout most of 2018, although Nordic credit spreads only followed suit towards the end of the year. Increasingly easy access to debt capital in parts of the credit market in recent years may intensify long-term market volatility, due to increasing credit risk and reduced risk appetite among investors.

Several explanations have been posited for the weakness of the international credit market in 2018, including ongoing and anticipated international fiscal policy restrictions, prolonged and increasing political turbulence, and increasing uncertainty about economic developments.

The prolonged, substantial weakening of loan agreement terms may make bond pricing difficult for investors in the high-yield markets – whether international or in the Nordic region. This provides greater room for companies to increase their commercial and financial risk, and creditors will only be able to accelerate their claims once credit quality has been materially reduced. The result may be a general increase in risk-taking at creditors' expense, and larger losses when bankruptcies occur. This trend may also foster greater market volatility, which in turn will affect both investors and borrowers.

### **Long-term stakeholders should take responsibility**

Folketrygdfondet believes investors, arrangers and issuers have a shared responsibility to safeguard the

Nordic high-yield market to preserve its important role as a source of financing for businesses and an investment option for investors. The Nordic market's efficiency in terms of time and documentation makes it an attractive alternative to European and American issue processes, which are far more complex and costly. The processes of the Nordic high-yield market are thus based on trust to a greater degree, and it is important that all stakeholders are aware of this.

Brokers play a critical role in the bond market. It is absolutely crucial for the market that transactions reaching completion have already been adequately quality assured with respect to correct and satisfactory information. Moreover, arrangers must verify that a given company is suitable for the bond market. Brokers should also take responsibility for ensuring that market norms and standards are maintained in connection with the drafting of loan agreements, and that information on loan terms is readily accessible.

Issuers should understand how the market works and the investors' interests, so that market prices reflect the companies' true financial position, and so that good refinancing opportunities are available when needed.

The willingness of investors to accept offered terms must be based on comprehensive information from both the arranger and the issuer, as well as robust analysis of the company and the loan agreement. Productive ongoing dialogue with issuers helps ensure this.

### Responsible fixed income investment

Folketrygdfondet has sought to ensure appropriate integration of responsible fixed income investment criteria into its activities for a number of years. The measures taken include pre-investment assessments, engagement in marketplace development, and active involvement in the protection of creditor interests.

Our experience and an increasing volume of empirical data indicate that ESG factors are an important driver of value creation in fixed income investment.<sup>1</sup> We expect issuers in the bond market to attach high and increasing importance to ESG risk factors going forward, and to focus on these matters and actively share relevant information.

We place particular emphasis on this aspect of our analysis in connection with investment in corporate bonds carrying high credit risk, i.e. high-yield instruments. This is not least because such companies are more vulnerable in the event of commercial and financial difficulties and have less robust debt-servicing capacity.

<sup>1</sup> In 2018, Folketrygdfondet chaired the Norwegian Forum for Responsible and Sustainable Investment (Norsif)'s Working Group for ESG in Fixed Income, which prepared an overview of relevant academic studies. Norsif Working Group for ESG in Fixed Income, *Norwegian Fixed Income and ESG Integration – Theory and Practice* (September 2018).

### Folketrygdfondet's responsible fixed income investment

#### Three channels

- **The investment process**
  - Assess transaction terms and potential participation
- **The marketplace**
  - Promote a well-functioning marketplace
- **As creditor**
  - Protect creditor rights

### Our expectations of borrowers:

- Provision of adequate information to the market
- Equal treatment of creditors
- Understanding of how the bond market works
- Responsible operations and ESG follow-up

## VOTED AT EIGHT BONDHOLDER MEETINGS

Folketrygdfondet takes a solution-oriented approach to bond loan renegotiations. In 2018, we voted at eight bondholder meetings.

Folketrygdfondet responds to all requests for bondholder meetings, and participates actively in negotiations to find solutions beneficial to both the bondholders and the company in question. We consider such involvement important both to protect the value of the individual bond and for the market in general.

In 2018, Folketrygdfondet voted at eight bondholder meetings. Seven of the matters involved amendment of loan agreements, while one related to restructuring.

In addition to formal bondholder meetings, Folketrygdfondet regularly engages in dialogue with issuers, including through company presentations, roadshows, and one-on-one meetings. In 2018, Folketrygdfondet had 99 meetings with 83 issuers.

We recommend

- adopting a proactive approach to defaults and making early loan-agreement waiver requests in the event of negative developments
- providing thorough information at bondholder meetings on how the company intends to comply with the loan agreement going forward
- making identical offers to all bondholders. It is unacceptable to pay higher fees to bondholders who accept a solution that “favors” the company
- providing comprehensive information to the bond market throughout the loan period, particularly if there are negative developments. Thorough reports, presentations and/or webcasts are recommended
- giving a clear presentation. Reliable information from management and a strong market history will positively impact prices in the secondary market and in connection with any refinancing

### **Responsible investment is enshrined in our mandate**

The investment mandate states that the primary goal of Folketrygdfondet's active ownership is to safeguard the financial interests of the Government Pension Fund Norway.

The mandate also specifies that active ownership shall be based on

- the UN Global Compact
- the OECD Principles of Corporate Governance
- the OECD Guidelines for Multinational Enterprises

Folketrygdfondet's board has adopted responsible investment principles that incorporate these guidelines.

The board also expects Folketrygdfondet to comply with national and international standards such as:

- the UN-supported Principles for Responsible Investment (PRI)
- the Norwegian Code of Practice for Corporate Governance (NUES)

Folketrygdfondet is mandated to contribute actively to the development of robust national standards in the area of responsible investment.