Learning from failing. The origins of the Norwegian oil fund

The Norwegian Government Pension Fund Global is the world’s largest sovereign wealth fund.¹ At present, it has a market value of about NOK 7,100 billion (USD 815 billion), which is around 140 per cent of Norway’s GDP. This is a result not only of high levels of petroleum revenue, but also of a solution whereby government revenue is channelled straight into the fund and invested abroad, with clear rules for how capital can be fed back into the Norwegian economy through annual political decisions on balancing the government budget. And it is only the return on the fund that can be used in this way; the capital invested is not available for consumption and must remain in global capital markets. The principles behind the fund have won international recognition as a well thought-out solution for managing large inflows of commodity revenue in a relatively small economy. The apparent success seems to have shaped a more general understanding of cleverness and foresight in the making of the fund, and, in a larger perspective, of the Norwegian State’s handling of petroleum incomes in general.²

The fund was established by the Norwegian Parliament rather late in the Norwegian oil history, in 1990. This means that the relevant bill was prepared at the same time as Johan P. Olsen (1989) edited the Norwegian anthology Petroleum og politikk: Det representative demokratiets møte med oljealderen (“Petroleum and politics: Representative democracy’s

¹ Fund rankings are available from the Sovereign Wealth Fund Institute’s website, http://www.swfinstitute.org/fund-rankings/.
² David Chambers, Elroy Dimson, and Antti Ilmanen, "The Norway Model."; Richard Milne, "Investment: Norway’s nest egg."
encounter with the Oil Age”). This anthology, well known to a Norwegian audience, integrates the research programme outlined both in a number of articles and in the book *Rediscovering Institutions* with an analysis of the Norwegian political and administrative systems’ encounter with the oil riches.\(^3\) One of the anthology’s main contentions is that Norwegian society once had an historic opportunity to shape its future and destiny, but institutionalised norms and routines, strong pressure groups, and a number of other limitations on the political systems’ ability to conduct rational social and economic planning led to a result that no one really wanted. Olsen found strong elements of “petrolisation”, a development driven by interest groups and the dynamics of the oil sector rather than the aims and values targeted by representative democracy.\(^4\)

The starting point for the present article has been the following puzzle: How are we to explain that a celebrated institution, created to ensure a long-term perspective in policy-making, was launched at the same time as Olsen’s books and their more pessimistic view of planning? Is Olsen’s analysis wide of the mark in regard to understanding how Norway managed its oil wealth? Or does the fund’s background and origins allow for greater concessions to the historically and institutionally based interpretations that underlay the organisational analysis that characterises the tradition that Olsen is an important contributor to?

This article deals in essence with a piece of administrative history, analysing the establishment of the Norwegian petroleum fund during a period of general pessimism on behalf of the political and administrative institutions’ ability to manage the new riches. The following is based on interviews and especially archive material from the Norwegian government and the ministries involved in the preparation of the fund, which took place throughout the 1980s. When

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\(^3\) James G March and Johan P Olsen, *Rediscovering Institutions*.

examining the arguments and positions in the intense struggle around the fund, I soon realised that the various actors’ experience with similar events played an important role. The idea of setting up a fund appeared in the Norwegian public in the early 1980s, mainly as a buffer between the State’s volatile oil revenue and its running expenditure. However, the bureaucracy in the Ministry of Finance was intensely afraid of repeating previous failures, and their attitude both delayed and informed the new fund structure. The relevant experience, the perceived failure, was the establishment of the national insurance fund (Folketrygdfondet), once presented both as an engine of growth and a cornerstone in the financing of pensions and social insurance benefits. In the first part of this article, the preparation of the national insurance fund will be described in some detail, as it both represents the present experience and provides an excellent entry into the institutional and professional logic of the government’s senior advisors.

I will begin by briefly presenting the historical and theoretical background for how the fund was set up. The subsequent analysis of failure, learning, and fund creation will start with the anatomy of the perceived failure, the national insurance fund from the mid-1960s. I will then analyse this fund’s consequences for the later construction of the oil fund, before discussing how the historical experience and intuitional context together led to the present oil fund.

**New institutionalism, rational planners, and the Ministry of Finance**

The *Petroleum og politikk* anthology offered a variety of perspectives on how Norwegian oil policy was shaped during the pioneer phase of the 1960s. The main perspective, however, was not highly optimistic in regard to rational social planning. Historical and institutional factors influence which options are available to democratically elected bodies and how these options are used. According to Olsen, Norwegian petroleum policy “has been adapted to the established
institutions and conflicts in Norwegian politics, while such institutions and conflicts have only to a lesser extent been altered as the result of the petroleum activities”.

The anthology’s predominant perspectives, as well as its criticism of the unachievable goal of rational planning, can be recognised in an extensive literature that is known as, and that refers to itself as, new institutionalism. The new institutionalism sees the institution as an collection of rules and organized practices, embedded in structures of meaning and resources that are relatively invariant in the face of changing external circumstances. Constitutive rules and values prescribe appropriate behavior for specific actors in specific situations. An integrated part of this framework, is “the logic of appropriateness” as a perspective on human action. To act appropriately is to proceed according to the institutionalized practices of a collectivity and mutual understandings of what is true, reasonable, natural, right, and good. Actors seek to fulfil the obligations and duties encapsulated in a role, and a membership in a political community. Rules are primarily followed because they are perceived to be adequate for the task at hand and to have normative validity.

As was also largely done in both Petroleum og politikk and Rediscovering Institutions, the following analysis will contrast this perspective with that of the rational economic planning, which in theory is not limited by norms, traditions, and institutionalised routines.

The rational perspective is motivated and chosen mainly because it provides the normative basis for the architects of the fund – the elite economists of the central bureaucracy – who was fundamentally informed by their educational background and its tenets of instrumental reason, where the goal is to find the solutions that best respond to general goals for growth,

5 Ibid.
redistribution, stability, and so forth. This is the underlying norm of rational social planning, though everyone knows that ideals and reality do not always correspond with each other.

On the other hand, a petroleum fund is commonly viewed precisely as an efficient construction, a means that is well suited to the goal of managing a nation’s wealth as best as possible. Today, more or less a generation later, we find this understanding in international journals that are not directly linked to the specific institutional contexts that can be identified in Norwegian politics and bureaucracy in the 1980s.

That real life economic planning does not take place in a value-neutral space is a relatively trivial observation. In the following we shall use the available historical material to try to understand the functionality of the relevant arenas of policy-making. By far the most important arena here is the Norwegian Ministry of Finance, which remained invested with several partially overlapping functions that were mobilised in conjunction with the petroleum fund as well as its significant and instructive forerunner, the national insurance fund.

Some general characteristics of the Ministry of Finance should be underlined. It was a powerful force in the central bureaucracy through the “power of the purse”, as condensed in its work on preparing the government budget, controlling other parts of the bureaucracy, approving appointments, and so forth. Throughout the 50s and 60s, new functions connected to economic policy-making and short- and long-term planning had moreover been incorporated into the ministry rather than into specially created ministries or in separate planning units, as was the case in several other countries. Nor did Norway have an overarching Office of the Prime Minister, as was for example found in the United Kingdom.

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As a result of all this, the Ministry of Finance acted as a controlling and coordinating body at the very core of the civil service and wielded a corresponding amount of influence. The ministry was probably more influential than treasury institutions in most other countries. Still, the ministry’s civil servants shared the institutionalised fear one finds in most treasury institutions, that the sum of present and future plans and projects would increase inflation, or weaken state finances or balance of payments. This fear created a certain scepticism to new initiatives and a tendency to seek solutions that minimised the long-term risks for state finances and internal and external balances of the national economy.

In the construction of the petroleum fund and of its predecessor, the national insurance fund, the senior civil servants played an important and independent role (as they indeed did in a number of other major schemes). They were at the same time loyal both to political signals and decisions and to their own interpretation of what constituted the preferred or necessary solution for the common good. These loyalties and role perceptions are best described through their actions and manoeuvring in the relevant cases. We’ll start with the insurance fund, and then move on to the complicated internal disputes around the petroleum fund.

National saving in a regulated economy

Norway’s national insurance scheme and national insurance fund were set up in something of a rush in the mid-1960s following a long, drawn-out process. The new national insurance system

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would provide the elderly and their surviving dependents with annual pensions amounting to two-thirds of their earned income. The existing welfare schemes to be included in the new universal system were funded in different ways. Retirement pensions, disability pensions, and certain other schemes were jointly financed through members’ contributions and contributions from employers, municipalities, and the government. Some benefits were funded by contributions from employers, others directly by the treasury. This complex system was now to be extended and unified.

The Ministry of Finance set out the key principles in the preparatory work on a parliamentary bill. One requirement that stood firm throughout the preparatory process was that the national insurance scheme should be independently financed. The national insurance contributions, which would be paid partly by the employers, the individual wage earners and the State, were to be kept separate from ordinary taxes, so as to underline that such contributions were earmarked specifically for the great welfare reform that was to benefit all. Another point of departure for the ministry’s civil servants was that the nation’s aggregate saving should not decrease as the result of the introduction of the national insurance scheme – we will return to the reasons for this later. The calculations that were made assumed that there would be a substantial reduction in private pension saving following the introduction of a graduated old-age pension in the national insurance scheme. This would be offset by a substantial initial transfer to a new fund, which would then be built up rapidly.

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11 Hermod Skånland, minutes from meeting at the first secretary’s office, 20 Nov. 1965; Eivind Erichsen’s archive, Ministry of Finance, box 37 (hereafter EE 37).

The core idea behind the fund was that government-mandated investment would be the path to robust economic growth. This approach to growth policy was well rooted in the economic policy pursued in Norway in the 1950s and 1960s. One key tenet was that low interest rates, a high rate of investment, and correspondingly low levels of private and public consumption were the best ways to build the country’s production capacity and future welfare capacity. This principle can be seen fairly clearly in all of the political parties’ views of the fund.\textsuperscript{13} In the debate on the national insurance bill in the summer of 1965, one Labour Party MP described the fund as “the grand vision on which the state pension builds […], namely that the fund itself will form the basis for an economically stronger and richer Norway”.\textsuperscript{14}

Within the Ministry of Finance, the fund’s true function gave rise to both discussion and doubt during the brief exploratory process. Internal memos soon posited a number of striking counterarguments to the reasoning presented in public. The most important was that high investment was hardly the best way to achieve higher growth in a Norwegian context. The very \textit{problem} with the Norwegian economy was that investment was record-high. For much of the post-war period, the country had tried to curb investment in order to avoid excessive imbalances between the domestic and external economies.\textsuperscript{15}

So why did the ministry go along with this fund structure? The reasoning about the fund within the ministry was both simpler and more complex than expressed in the public debate. One key problem in all of the years the country actively pursued a low interest rate policy was obtaining sufficient amounts of credit for state-owned banks lending at regulated low rates.\textsuperscript{16}

\textsuperscript{14} St.t. 1964-65, "Storting Gazette 1964-65: 4147."
\textsuperscript{15} Director General T. Glesne to the secretary general, 13 April 1964; 107.43, EP/NA.
\textsuperscript{16} Bernhard Nestaas, “Finansieringen av de offentlige investeringer i etterkrigstiden.”
Within the Bretton Woods system, it was not possible to finance state lending through monetary expansion or permanent fiscal deficits, as it would have created internal and external (balance of payments) imbalances. In the 1950s, around half of the capital for state bank lending had been created through a highly restrictive fiscal policy. Large operating surpluses made it possible to transfer capital as loans from the treasury to the state banks. The remainder was funded through bond loans from private banks and insurance companies to the government, which forwarded the money on to the state banks.

In the 1960s, however, the ability of fiscal policy to finance the state banks gradually deteriorated. Government expenditure grew much more quickly than in the 1950s, and revenue failed to keep up. At the same time, European interest rates started to rise, while Norwegian authorities insisted on keeping borrowing costs low. This made it more difficult to borrow money from private institutions in the market. In this context, the national insurance fund had the potential to be a useful, if not essential, instrument, precisely because it would accumulate large amounts of available capital administered by the state.

It was always the intention that the national insurance fund would be able to provide capital for investments that were a government priority, such as housing and regional industrial development, targeted by state banks.\textsuperscript{17} From late 1965, however, the Ministry of Finance’s memos to the government were portraying the fund not as an independent instrument for achieving general policy goals but as a means of getting other instruments to work. Now the role of securing reasonable funding for the state-run credit system was presented as the fund’s dominant practical objective.\textsuperscript{18} This met with resistance from the cabinet members. That winter

\textsuperscript{17} St.R. No 75, "Report to the Storting No. 75 (1963-64)."

\textsuperscript{18} Important in this respect is a government paper dated 4 January 1966 prepared by the Economic Policy Department. This outlines probable developments in the so-called surplus-before-loan transactions in the coming years, and compares these figures with estimates for how much borrowing could be expected from private
brought a heated debate about the guidelines for the fund. In the end, the ministry did get its way that the fund’s management should be given very limited scope to invest anywhere else than in the bond market. The ministry had close control over this market through rules in the Credit Act regulating what bonds could be issued. 19

This solution followed from a very basic institutional and systemic logic, in which the permanent staff in the Ministry of Finance felt committed to safeguarding state finances and honouring the state’s financial obligations: government policies were still committed to regulated low interests, and private savings were to a lesser extent available for state bank funding. Outside the Ministry of Finance, few people were concerned about how exactly public-sector growth was financed. Even though a key person like General Manager Skånland of the Economic Policy Department had grown sceptical of the wisdom behind the low, fixed interest rates, he obviously felt committed to finding solutions that hindered the very same policy from resulting in large budgetary or financial deficits. The only solution available was using the national insurance fund to fill the gap in the available financial resources. The fund was thus quietly enrolled into the wider system of providing funding for state banks.

The deterioration of the national insurance fund

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19 “Recommendations of the government committee on the management of the state pension fund”, 21 Sept. 1966; EE 34.
This rescue mission for the policy of large-scale state lending at low interest rates set the direction for the use of the fund in the ensuing years. The Norwegian national insurance scheme also quickly proved more expensive than originally anticipated. Costs increased without financing keeping up – in fact, contributions were substantially reduced. The grandly envisioned fund therefore had far less money transferred to it than originally intended – and after a few years the inflow of new capital dried up altogether.

This is one side of the financial deterioration: the national insurance scheme’s expenditure moved entirely independently of current or future revenue. The principle of national insurance contributions being tailored to the need to build up a fund which, based on the views of the time, would help make it easier to pay future benefits, did not survive long. In 1973, the social security budgets were closely coordinated with the government budget. The year after, the budget presented pragmatic ideas that it was actually just a matter of expediency whether the national insurance scheme was funded through separate contributions or through ordinary taxes, so making it possible for the government to finance the scheme as standard expenditure through the government budget. In the years that followed, employers’ national insurance contributions were geographically differentiated as an instrument of regional policy. The mid-1970s saw Norway become one of several OECD countries to experiment with neo-Keynesian countercyclical measures. These included increasing wage-earners’ disposable income by lowering national insurance contributions in the hope that this would result in lower wage demand.\textsuperscript{20} With this, one of the main pillars of the fund’s concept – solid and stable contributions – was blown out of the water.

\textsuperscript{20} Svein Dahl, \textit{Kleppepakkene: feilgrep eller sunn formuft?}
Capital of some significance was still transferred by the Government to the national insurance fund through to 1975. Modest amounts were then transferred in three of the next four years, but after 1979 no capital at all went into the fund – employers and taxpayers still paid their contribution to the national insurance scheme but the Government stop transferring these means to the fund. At the same time, the return on the fund was very weak. In most years up until the low interest rate policy was abandoned in the 1980s, the real return was deeply negative. This was down to the fund’s main function of financing government lending of a type, and on terms, that the private market was unwilling to supply. This was very much on the cards from the outset, once the true function of the national insurance fund became to resolve the problems associated with funding the state banks.21

The more specific motivation behind this was to obtain capital for the state banks. This was also an important contributing factor in the long-term erosion of the fund. The shortage of funding for the state banks was no secret to political decision-makers. Looking at the newspapers and even parliamentary debates where ordinary members spoke from the floor, however, one is left with the impression that many truly believed that the intention was for the fund to grow to a large size and pave the way for the strongest possible economic growth.

Learning from history, confined by history

One of the first reviews of the finances of the national insurance scheme and the national insurance fund came with the Social Security Funding Enquiry of 1982, which was critical of the way that what

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was intended to finance future pensions was, in practice, being used to get other government instruments to work. However, the enquiry did not spark any major debate. A far bigger public issue was how the nation’s new-found oil riches could be saved in the long term for future needs and future generations. The national insurance fund and the oil fund were not linked together in the public debate. At the Ministry of Finance, however, the memories ran deeper.

The idea of investing oil wealth abroad was mooted as early as in a wide-ranging parliamentary report in 1974, although this did not look in detail at how this should be done. The actual practice in the years to follow was to spend revenue as it came in and instead control the rate of development and production. Unexpectedly large discoveries and another surge in oil prices in 1979/80 then created a strong impression that the government’s spending of this revenue was dependent on transitory external factors. A government-appointed committee, the so-called Tempo Committee, proposed a new principle for how accrued revenue and current government expenditure should be linked, or rather decoupled. Revenue should be determined by industrial considerations with respect to the rate of development and production, and then transferred to a fund that invested in global capital markets before being channelled back into the Norwegian economy at a tempo suited to fiscal and economic considerations.

This proposal immediately found favour with a wide range of politicians and academic economists, but not the civil servants at the Ministry of Finance, who were quite determined to torpedo the Tempo Committee’s fund in 1984 and 1985. The background for their stance is partly provided by the experience from the fund, and partly from the changes in the regulation regime and general economic reasoning among the ministry’s economic advisors over the preceding five to ten years.
The Ministry of Finance and the Economic Policy Department had changed as an epistemic community, to use Peter M. Haas’ concept. Epistemic communities are groups or networks of experts characterised by shared beliefs about how to define problems, identify policy solutions, and assess policy solutions. In the 1960s, problems related to government funds and long-term fiscal balances were assessed in the light of an economic reasoning adapted to a strict regulatory regime developed in post-war Norway and a policy regime with limited room for market-based solutions.

However, the 1970s provided a series of shocks to the international and national policy framework. This decade was characterised by low productivity and high state subsidies in a number of industries, and by increasing rates of inflation.

The values, knowledge and theoretical orientation of the ministry’s advisors changed. Some changed their viewpoints on state intervention and demand management, and more importantly, new advisors with new ideas entered key positions. In political life, most of the 80s were used to delimit state intervention and transform the system of economic governance to more market-based solutions. Within the Ministry of Finance, the epistemic changes happened much more rapidly, and from the late 70s on the economic advisors were stern spokesmen for cutting subsidies and liberalising the Norwegian economy.

Another major issue in the early 80s was how the state could contribute financially to the internationalisation of Norwegian industry. As an extension of the Tempo Committee’s

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23 Some would say it’s the other way around, that policy was adapted to the reasoning of Norwegian economists, but we do not need to dwell on the genesis of the epistemic community within the framework of this narrative.


25 In 1980, neither the head nor the second in command of the Economic Policy Department was educated at the University of Oslo, the traditional source of candidates for such positions. They held PhDs in economic history/economics from Stanford and Utah State, respectively.
recommendations, key members of the Labour Party presented ideas for how oil money could be used to take the country forward with big industrial and infrastructure projects.\textsuperscript{26} The ministry’s fear was that the fund would become a readily available source of capital that could be used to finance measures through channels that were not controlled via the standard budgetary process, where the ministry was the coordinating hub. “An oil fund […] would seem deeply attractive to groups that consider themselves unfairly treated in the prioritisation of the government budget,” explained the Economic Policy Department in a memo to the secretary general and the finance minister. “All so-called non-inflationary expenditure proposals would see the oil fund as an alternative source of funding to the standard budget.”\textsuperscript{27}

Memos from the ministry portrayed experience from the national insurance fund as a dark scenario, and not without some reason. The national insurance fund was set up as a reserve outside the government budget. Proposals for new welfare measures were therefore tabled outside the budgetary process during its first years. What was left in the fund had been used to cross-subsidise popular programmes, at costs that were neither revealed nor fully known. The civil servants did not point out that it was their predecessors at the ministry who had consciously designed the fund with this in mind 20 years earlier, but this was, of course, well known to the key actors.\textsuperscript{28}

Ironically, the basic institutional norms and characteristics that had provided the structure of the old fund were similar to the ones that underpinned the hostility against a new fund. The ministry’s

\textsuperscript{26} Cf., for example, Finn Lied’s lecture “Norges valutareserver: Passiv plasserings eller vekstimpuls for landet” [Norway’s foreign exchange reserves: Passive investment or growth stimulus for the nation], manuscript, 11 Oct. 1984; Thorvald Moe’s papers, Ministry of Finance’s archives, box 8 (hereafter TM 8).

\textsuperscript{27} Economic Policy Department to the minister via the secretary general, 4 Sept. 1984; Svein Gjedrem’s papers, Ministry of Finance, box 2 (hereafter SG 2).

\textsuperscript{28} The Ministry of Finance had the same secretary general, Eivind Erichsen, in 1966/67 and in 1983/84. In a conversation between the author and Erichsen in 1996, Erichsen highlighted the significance of the national insurance fund’s “sad fate” in the ministry’s attitude towards the new oil fund.
traditional role in coordinating public policies was to safeguard state finances, control inflation, and keep an eye on the balance of payments. In the 60s, this led the ministry to use the new fund as a means of reallocation within the internal economy to provide the popular state banks with funding. In the 1980s, the same concern for state finance and internal and external balances led the civil servants to a position of extreme scepticism in the dispute over a new fund.

This fear of a fund to serve domestic objectives became more acute when a parliamentary report from the Ministry of Petroleum and Energy presented paragraphs on how oil revenue could be used to boost Norwegian infrastructure, growth capacity, industrial expansion abroad, and so on. Following sharply worded counterarguments from the Economic Policy Department, the Ministry of Finance was asked to set up a ministerial committee with two civil servants from its own ranks, two from the Ministry of Petroleum and Energy, and a chairman from a third ministry.

The mandate from the government was not whether there should be a fund but what kind of fund there should be. The majority returned with a recommendation to set up a fund that was not really a fund: it should take the form of a standard government deposit account at the central bank under ordinary fiscal policy control. Alternatively, the fund could invest its money in foreign currency purchased from Norges Bank at market rates, which was effectively the same thing. Oil revenue would be transferred to a (foreign currency) account managed outside the existing administrative apparatus.

The minority, two department heads from the Ministry of Petroleum and Energy, presented an institutional solution which was a fund in the normal sense of the word. This would be organised as a separate organisational unit and serve partly as a buffer fund for fluctuations in government revenue and partly as a long-term investment fund if the assets under management grew to a large size. The main thrust of this proposal was that capital should be invested abroad in fixed-income securities or
shares in large companies. However, their suggestion opened up the possibility of domestic investments, as the fund should be allowed to allocate funds to development contracts for foreign companies wishing to invest in Norway, and less specifically for “purchases of large shareholdings/corporate takeovers”.

While the Ministry of Finance made little reference to international models, the Ministry of Petroleum and Energy produced an extensive annex with international experience of commodity funds. These funds, the bulk of them in the Middle East, were divided into three types according to whether they were to (i) replace oil revenue once it came to an end, (ii) even out fluctuations in oil revenue, or (iii) be used here and now to develop the domestic economy.

The proposal from the mandarins at the Ministry of Petroleum and Energy embraced all three variants, and representatives of the Ministry of Finance were dismissive of a model where the fund would play any role at all in doing anything “strategic” in the domestic economy. Memos written while the committee was at work suggest, however, that the Economic Policy Department did not actually fear a consistent realisation of the original model from the Tempo Committee. What they really feared was that the popular variant, a fund that would invest in infrastructure and Norwegian industry, and at the same time escape the process for State budgeting, would win acceptance. And in their concrete advice, the baby went out with the bathwater.

The experience from the National Insurance Fund formed the stance and arguments of the high-ranking bureaucrats in the Ministry of Finance. They learned from historical experience, and they

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29 “Petroleumsfond som styringsinstrument i finanspolitikken” [A petroleum fund as an instrument of fiscal policy], report from the civil service committee appointed by the Ministry of Finance, 23 Jan. 1985; ØA box D9-442. Petter Nore was also one of the secretaries in the Tempo Committee. His loyalty to its conclusions was therefore not that surprising.

30 Marit Engebretsen and Petter Nore, “Internasjonale erfaringer med petroleumsfond” [International experience of oil funds], annex 1 to the report cited above.

31 For example, Economic Policy Department to the Minister, 27 Sept. 1984; TM 8.
were confined by historical experience. Their logic was undoubtedly rationalistic, in the sense that they systematically discussed ends and consequences related to the proposed means. But the judgements made were deeply coloured by their institutional commitment, as they saw it, by their available experience, and by their specific interpretations of the role as protectors of long-term balance in economic development and state finances.

Consequently, they did what they could to block the proposals for a new fund. After the first heavy objections from the Ministry of Finance, a protracted internal debate followed. One of Prime Minister Kåre Willoch’s high-profile political advisors was a clear advocate of establishing an oil fund.\textsuperscript{32} The Ministry of Finance’s parliamentary secretary, however, was clearly behind the civil service view.\textsuperscript{33} And it was this view that had the greatest influence over the formulation of the new bill for a Petroleum Fund Act following lengthy internal discussion within the government apparatus. This stated that “the fund’s assets will be managed in the same way as other government capital”, in other words placed in government accounts at Norges Bank in line with existing deposits.\textsuperscript{34} Not only had the Tempo Committee’s idea been diluted, but the solution had taken its time.

It may seem paradoxical that the civil service backed a fund that was, in reality, nothing more than a formal structure for standard government reserves managed by the central bank. However, the fear was not only that the fund could pave the way for domestic use of oil revenue by financing measures outside the budgetary process, but also that it might help raise the profile and visibility of the capital available for public spending. This general scepticism from the early 80s is supported by international experiences from the last 20 years or so. A general feature of large sovereign wealth

\textsuperscript{32} Osmundsen’s memo to the finance minister of 6 Sept. 1984; SG. 2.
\textsuperscript{33} Reiten’s memo of 10 Sept. 1984; SG 2.
\textsuperscript{34} “Om lov om Petroleumsfond” [On a Petroleum Fund Act], Proposition to the Odelsting No. 53 (1985-86), draft.
funds is that the direct involvement of politicians in their management results in greater investment in local, domestic objectives.\textsuperscript{35}

The bill was completed just after the oil prices plunged in winter 1986. In this new situation, the Norwegian government feared that a fund could create the impression that this drop was only temporary, and this was not the kind of signal it wanted to put out ahead of the year’s pay talks. The bill therefore had to wait until the pay deals were done and dusted.\textsuperscript{36} By then, the government had changed. Thanks to these chance circumstances, the civil service’s original line won the first round.

The second round came in 1989 when a new centre-right government came to power. The Conservative finance minister was quick to announce that he wanted an oil fund set up, but without giving clear guidelines for what it should look like. A bill was prepared by the bureaucrats at the Ministry of Finance without any great enthusiasm. However, as the head of the Economic Policy Department put it in a memo when the government paper on the matter was drawn up, the political signals that a fund was coming were “so clear that there is no avoiding it”.\textsuperscript{37}

However, all of the civil service’s misgivings from 1984-86 were written into the new bill. The key principle, which has held to this day, is that revenue from petroleum activities should go straight to the fund. All investments from the fund’s holdings should be made abroad, without exceptions. All spending of the return of capital invested must be approved by parliament as part of the balancing of the government budget. Any route from fund to consumption other than through the government budget was expressly ruled out. These regulations would protect the domestic economy from the overspending of oil revenue and avoid making the fund a source of “cheap money” for political

\textsuperscript{35} Shai Bernstein, Josh Lerner, and Antoinette Schoar, "The investment strategies of sovereign wealth funds."

\textsuperscript{36} Presthus’ handwritten notes on the draft bill, 20 March 1983; SG 3.

\textsuperscript{37} Gjedrem’s memo to Skauge via Hermansen, 8 Sept. 1989; “SG memos 1989”.

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purposes. Again, the civil servants reminded their political superiors of the discouraging experiences from the national insurance fund in the 1960s and 1970s.\textsuperscript{38}

Those who created the fund had real doubts as to whether any capital would ever be transferred to it.\textsuperscript{39} The Norwegian economy was in a perilous state in 1989/90, with huge imbalances in the economy on the back of a strong credit-driven boom in the middle of the decade and a looming bank crisis. In the first half of the 1970s, there was extensive debate about how Norway could avoid going repeating the Dutch experience, with high Government spending, followed by a tightening of economic policies when the windfall gains came to an and, with high unemployment as a consequence. Experience from the previous 15 years had, however, demonstrated that Norway had been in a position to spend large amounts of oil revenue domestically, even though the macroeconomic consequences had been unfavourable. “We carefully plotted a course, and then immediately headed in a different direction,” as Hermod Skånland, then central bank governor, elegantly put it.\textsuperscript{40}

Expectations of substantial oil revenue had fuelled very high levels of public consumption and large trade deficits in the late 1970s. Policy was tightened, but from the early 1980s there was a further strong upswing in the domestic economy. The reasons were complex, but actual and anticipated oil revenue put constant pressure on the economy and policymakers, along with low prices for credit and a tax system that favoured borrowers. This was presumably a contributing factor in the fund turning out the way it did in 1990: the civil service did not actually want one at all, but would as an alternative accept a fund investing outside the Norwegian economy. There was limited interest among politicians,

\textsuperscript{38} Economic Policy Department to the minister, 27 Jan 1989; SG 1988/89.

\textsuperscript{39} Personal communication to the author from then head of department Tore Eriksen and Svein Gjedrem, Ministry of Finance.

\textsuperscript{40} Hermod Skånland, “Norge og oljen: gamle eller nye utfordringer; socialøkonomenes forening’s petroleumsseminar 2. 11. 1988.”
because there was such uncertainty about whether the fund would ever be of any real significance – nothing in the preparatory work suggests that the political leadership in 1989/90 was particularly closely involved in the discussions on the concrete design of the fund in the final phase. Neither did we have any broad public debate on the issue in the last phase of the preparation of the fund; the public interest seems to have veined after the large fall in oil price in 1986 followed by the large deficits in the Norwegian economy. Hence, the vital discussions that determined the fund’s fate and structure, took place within limited circles in the Government system.

There has since been a plethora of adjustments to the rules for managing the fund, especially when it comes to the types of assets in which oil revenue may be invested. The allocation to equities was introduced in 1998 and later increased, and the fund has moved into real estate. Ethical guidelines have been drawn up to stop the fund from investing in companies that sell arms or produce tobacco, or whose operations violate key ethical standards. Within this framework, the fund’s managers are to obtain the greatest possible return. But the principle that has been most widely debated – that the fund’s capital may only be invested abroad – has been unchanged. Over the last decades, advocates of spending oil money on industry, research, infrastructure, and suchlike have often argued that more should be invested domestically. This debate – which is outside the scope of this article – has been partly about securing capital for investment in infrastructure, and partly about financial investments in research foundations, innovation funds, and so on. But the distinction from the 1980s has held: investment must still be made exclusively abroad, and the way back into the Norwegian economy must be through existing or new rules and procedures in the budgetary process.

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Between past and present

The history of the national insurance fund and the subsequent petroleum fund shows how the wider system for economic policy-making had a decisive influence on each solution for fund structure, management, and investment strategy. And it reveals how historical experience from the first arrangement – the perceived failure of the national insurance fund – contributed to producing the opposite solution for the second fund. This is impossible to understand without the key role of the strong, integrated Ministry of Finance, at its previous experience with a national fund for public saving. Seen from a long-term perspective, the fear that the fund would lead to mission creep seems groundless, as the national institutions have proven itself capable of managing the wealth. But the fear of repeating mistakes was obviously strong in the mid-1980s, and encouraged the economists to work against a solution with characteristics similar to the ones of the National Insurance Fund. The resistance against any solutions that made it possible to invest in the domestic sphere, or to bypass the State budget process in political spending, was obviously inspired also by other sources, also foreign, mainly Dutch, experience. But the National Insurance Fund provided a relevant and very useful parallel with clear similarities in structure and purpose.

It is now time to return to the tiny puzzle that began this article: at a time when Olsen and other influential contributors to the Petroleum og politikk anthology feared, somewhat despairingly, that the state bureaucracy was ill-suited for managing Norway’s wealth, how did such as long-term-oriented petroleum fund come into being? Indeed, the fund’s history seems to corroborate Olsen’s analysis in two ways. First of all, it is not the case that the bureaucracy was
able to break from institutionalised attitudes and roles and point out a way for a long-term, rational management of the oil revenue. Rather, the bureaucracy hindered the fund as long as it could, with a pattern of action that was established prior to and independent of the oil wealth.

And second, had the government in 1989 not featured an experienced, energetic minister of finance, one who had himself encountered the civil servants’ opposition a few years before, it is unlikely that such a fund would have been established then either. It would probably have taken another decade, when the overwhelming amount of wealth would have necessitated some sort of fund. If it had been established within a different economic and political context, a fund could easily have been of an entirely different nature.

Upon closer inspection, the civil service’s opposition is linked to historical experiences from the recent past. Based on past experiences, where the previous fund was given a key role, they were highly critical of establishing channels for State financing outside the system for control and prioritisation that surrounded the annual State budget process. These experiences were incorporated into institutional roles and values that strongly emphasised the cautious expenditure of money, the idea that the ministry’s civil servants played a key in ensuring such caution, and a relatively explicit scepticism of the ability of politicians to take such a goal into consideration. This outlook shaped their assessments of institutional solutions and their enduring opposition to the petroleum fund.

In both content and expression, these assessments were characterised by a typical instrumental rationality. The outlook was consequentialist, not the result of rules of appropriateness or routinised behaviour. As such, it could have been explained within analytical frameworks more based on instrumental rationality, but where the understanding of reality and the assessments of various outcomes are strongly influenced by historically founded and
institutionalised attitudes. It is outside the scope of the present article to discuss this aspect. The goal here has rather been to discuss a retrospective understanding of why the fund was established as a reasonable answer to new challenges, as well as the late 1980s analyses of the inadequacy of Norwegian institutions to manage the new-found wealth. A key insight here is that the petroleum fund was established in spite of the efforts from the leading advisors and planners at the heart of Norwegian policy-making, and not because of their efforts.

Uncategorized References


