

The Fourth Swedish National Pension Fund's (AP4) fund capital increased to SEK 334 billion in 2016. Total return was 10.0 percent after expenses. AP4 outperformed both the long-term return target and the income index by a wide margin. AP4 thus contributed positively to the pension system's financial strength.

Fund governance report

AP4 publishes an annual fund governance report that describes elements of the work performed by the Board and AP4 during the year. The fund governance report follows applicable parts the Annual Accounts Act and the Swedish Code of Corporate Governance (the Code), which provides guidance concerning good practices regarding Swedish listed companies. AP4 is, however, a government agency, and differences between public law and corporate law are substantial. Therefore, the fund governance report is limited to the elements that may be considered relevant to AP4.

The fund governance report has not been reviewed by AP4's external auditors.

Governance of AP4 - an authority regulated by law

AP4 is a government agency whose business activities are regulated by governmental law (2000:192) regarding the public pension funds (hereinafter "LAP"). The law provides that AP4's capital may only be utilized by the State to finance income-related retirement pension, unless Parliament resolves otherwise. AP4's investment rules are specified in LAP.

In accordance with LAP, AP4 has its own Board of Directors, which is responsible for the organization, operations and management of the funds. AP4's Board of Directors and business operations, under LAP, are by law not controlled by government directives or by business policies or economic political interests.

AP4's mission

AP4's mission is to manage the fund's assets to achieve the highest long-term returns and thus provide the greatest possible benefit for the pension system. Environmental and ethical issues must be accounted for without compromising the goal of the best possible return. AP4 shall independently formulate its objectives and strategies.

External evaluation

The AP funds are evaluated on behalf of the government each year. This evaluation is presented in a letter to Parliament.

External and internal regulations, as well as letters that affect the governance and operations

- Law (2000:192) regarding the public pension funds (LAP)
- Laws such as the Administrative Procedure Act and the Act on public procurement.
- The principle of public access to information
- The Governments evaluation and report to the Parliament
- The AP Funds joint policy and joint accounting and valuation principles
- AP4's internal policies and valuation principles
- AP4's ownership policy
- Swedish Code of Corporate governance (the Code)

The Board has nine directors

AP4's Board of Directors shall consist of nine ordinary members appointed by the government, and no deputies. Of the nine members, two are nominated by representatives of the employers' organization and two members are nominated by representatives of the employees' organizations. The government appoints the Chairperson and Vice Chairperson from among the members not nominated by the employer/employee organizations.

Board Directors

On April 28, 2016 Sarah McPhee was appointed as Chairwoman, replacing Monica Caneman. On May 19, 2016, the government re-elect all of AP4's appointed board directors.

On December 31, 2016, the Board consisted of the following members: Sarah McPhee, Chairwoman, Jakob Grinbaum, Vice-Chairman, Helene Fritzon, Ing-Marie Gren, Sven Hegelund, Stefan Lundbergh, Erica Sjölander, Maj-Charlotte Wallin and Göran Zettergren. AP4's Board members are presented in more detail on page 6.

The Board's mandate remains in force until AP4's balance sheet and income statement for 2016 have been adopted.

The Board's three committees

The Board has established three committees; Remuneration, Risk and Audit, which prepare various matters for the Board.

Remuneration Committee

The task of the committee is to advise the Board and prepare remuneration matters regarding the CEO and Senior Management. The Remuneration Committee also addresses issues relating to AP4's remuneration principles and other terms of employment for all employees.

The Remuneration Committee consists of three Board members: Jakob Grinbaum - committee Chairman, Maj-Charlotte Wallin and Göran Zettergren.

Risk Committee

The task of the committee is to further improve communication and understanding of the financial risks of the business. The Risk Committee was established when the Board delegated an extended mandate to AP4's Strategic management.

The Risk Committee consists of three members: Jakob Grinbaum - committee Chairman, Sven Hegelund and Stefan Lundbergh.

Audit Committee

During 2016, the Board established an Audit Committee. The Audit Committee, on behalf of the Board, is tasked with preparing and monitoring AP4's external financial reporting, accounting, external audit, follow up on AP4's risk management, operational risk and compliance.

AP4's external auditors participates at the meeting when there are issues concerning the external audit.

The Audit Committee consists of three members: Maj-Charlotte Wallin - committee Chairwoman, Stefan Lundbergh and Erika Sjölander.

Board Remuneration

The government determines the Board members' fees. Full-year remuneration amounted to SEK 100 000 for the Chairwoman, SEK 75 000 for the Vice Chairman and SEK 50 000 for each of the other members. The remuneration fees are unchanged since 2000.

The government also set an annual limit of SEK 100 000 for committee assignments, which the Board has resolved to distribute in the amount of SEK 11 100 per member, including the Chairperson, for committee work.

The Board's work 2016

The Board's responsibility

The Board is responsible for AP4's organization and for the management of the fund's assets; the Board has delegated the daily responsibility of the management to the CEO.

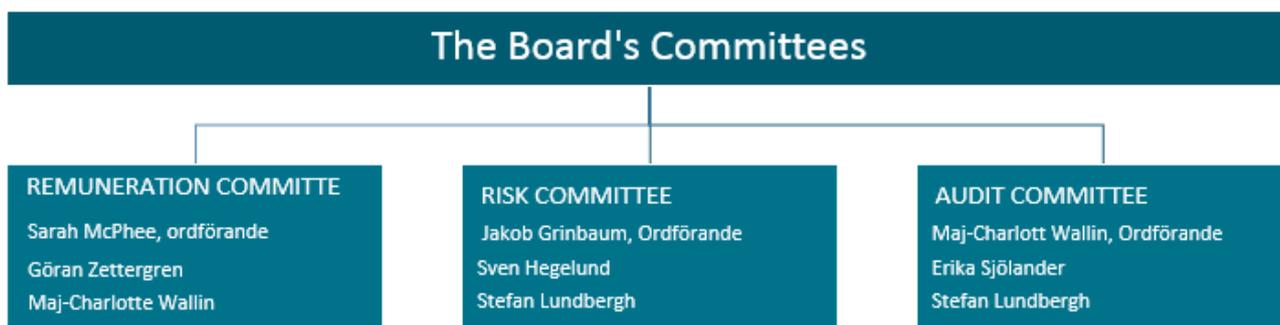
Management - Niklas Ekvall appointed new CEO

In June 2016, the Board appointed Niklas Ekvall as the new CEO of AP4, following Mats Andersson's departure after ten years as CEO. Niklas Ekvall assumed the role of CEO on October 1, 2016.

The CEO has a management team to support decision-making, which at the end of 2016 consisted of the CEO and six employees. The management team as per December 31, 2016 is presented in the annual report found at www.ap4.se.

Rules of Procedure and CEO instructions

The Board establishes guidelines for its work as well as instructions for the CEO. These basic documents, together with ethical guidelines for employees and rules regarding own transactions with financial instruments, are adopted by the Board annually.



12 protocolled meetings

During the business year, the Board held 12 formal protocolled meetings. As shown in the table below, attendance remained high and averaged 93 percent.

In addition to members of the Board and the board secretary (who is also AP4's General Counsel), the CEO and other employees of AP4, presenting at the meetings, have participated.

The Board of Directors' duties

The Board is utmost responsible for AP4's organization and the management of the fund's assets. Important tasks include establishing:

- procedures for the Board's work
- policies and regulations regarding, among others, the business, personnel (including principles for remuneration and terms of employment), financial- and operational risk, as well as the personnel- and ethics-related policy
- long-term business goals
- the long-term asset allocation of AP4's reference portfolio, the Normal portfolio
- instructions for the CEO
- an annual business plan for the coming year.

The Board of Directors is also responsible for hiring and evaluating the CEO; assessing overall strategic issues; ensuring Board decisions are implemented; and checking and monitoring that the business and its risks are managed appropriately.

Focus areas 2016

In addition to the ongoing work in 2016, the Board primarily focused on:

- the recruitment of the new CEO, Niklas Ekvall, who assumed the role October 1, 2016, following Mats Andersson's announcement that he would leave the fund during the Summer of 2016.
- issues regarding the independent review of the company Rikshem, which AP4 owns jointly with AMF.
- conducting a salary survey based on the Discrimination Act and an external market comparison of salaries.
- establishing the Audit Committee.

Evaluation of the Board's work

The Board's work is evaluated annually. In late 2016, the Board conducted the annual evaluation of its work in which all board members participated. The evaluation was performed by means of a written questionnaire, which was the basis for a discussion within the Board. The discussion covered, among other things, how the work was conducted during the past year and how it can be further developed.

2016 Board Meetings

	Remuneration Committee	Risk Committee	Audit Committee	Presence/total number of meetings	Received fees
Sarah McPhee, Chairman of the Board as of April 28, 2016	X			7/12	73 612 kr
Monica Caneman, Chairman of the Board ¹ until April 27, 2016	X			3/12	29 167 kr
Jakob Grinbaum, vice chairman ^{1 2}		X		12/12	92 051 kr
Ing-Marie Gren, director ²				9/12	62 501 kr
Stefan Lundbergh, director ^{2 3}		X	X	12/12	68 051 kr
Maj-Charlotte Wallin, director ^{1 3}	X		X	12/12	68 051 kr
Helené Fritzon, director				11/12	50 000 kr
Göran Zettergren, director ¹	X			11/12	52 775 kr
Sven Hegelund, director ²		X		12/12	65 276 kr
Erica Sjölander, director ³			X	12/12	52 775 kr

¹ Remuneration includes compensation from the Remuneration Committee.

² Remuneration includes compensation from the Risk Committee.

³ Remuneration includes compensation from the Audit Committee.

Employee Compensation

AP4's role as a manager of the State's pension assets presupposes that the benefits to employees, including the CEO, are reasonable, justifiable and explainable.

Generally, overall compensation levels should be in line with the market and should enable AP4 to attract and retain talented employees; however, compensation levels should not be market leading.

Since 2012, the AP Funds have a common policy for remuneration terms and conditions, employee benefits, representation and business travel, which have been adopted by the respective National Pension Fund's Board of Directors. This common overall policy is supplemented by AP4's more detailed internal personnel-related policies and guidelines.

Compensation policy

The Board has adopted a policy for remuneration and other employment terms for AP4's employees. The Board, through the Remuneration committee, determines the terms of employment of the CEO. All employees have individual employment contracts. The total compensation for an employee consists of a fixed salary, variable salary, pension and other benefits. Variable compensation is only paid if AP4's comprehensive income for the year is positive. The CEO, senior executives, the Head of Compliance and the responsible person for Risk Control do not receive any variable remuneration.

Variable remuneration may amount to a maximum of two months of an employee's salary. Variable compensation can be attained when clear and measurable objectives have been achieved. Variable compensation is based on group-oriented quantitative targets and the individual employee's measurable contribution, determined over a rolling three-year period. Other benefits constitute a very limited value and are offered to all employees. Examples include health insurance, group insurance and fitness contributions. AP4 also has four parking spaces that employees can use whereupon they are taxed on the benefit.

Details of the remuneration levels for the CEO, management team and other employees, and the outcome of variable salaries for 2016 are detailed in Note 6 of AP4's annual report. Furthermore, AP4's work with remuneration issues is presented under the section "Remuneration at AP4" in the Annual Report. More information can be found at www.ap4.se.

The Board's review 2016

During the year, the Board of Directors commissioned both a salary survey for all employees in accordance with the Discrimination Act as well as an external market comparison of both the management team and other employees, where a comparison has been made to the corresponding services in the financial sector in Sweden working with long-term management of capital.

The completed salary survey, from a gender perspective, concluded that there are no significant differences in pay either regarding equal work, work of equal value or in female-dominated groups.

External market comparison of salaries

The finalized external market comparison included all of AP4's employees, plus senior management. The market comparison of salaries was prepared with corresponding positions in the Swedish financial sector working with the long-term management of capital.

The objective of the market comparison was to ensure that the Fourth AP Fund's wage levels are in line.

The remuneration policy together with the government guidelines for terms of employment for senior executives of the AP Funds ensures that AP4's compensation levels are reasonable and defensible and not market leading, while at the same time the levels of remuneration should be market conforming and competitive.

The external consultant Willis Towers Watson conducted the comparison, analysis and compilation of the survey for the external market salary, whereby the base was drawn from their annual salaries and benefits survey for the financial sector in Sweden. Each employee's compensation was compared with the corresponding positions of a group in the financial sector in Sweden working with long-term capital management: Alecta, AMF Pension, AFA Insurance, the Second AP Fund, First AP Fund, Kammarkollegiet, Länsförsäkringar, SEB, Sixth AP Fund, the Seventh AP Fund, Skandia, Swedbank and the Third AP Fund. These were deemed to compete for staff with similar responsibilities, experience and skills that are required by AP4 to fulfill its mission.

After review of the comparative analysis results, the Board could conclude that AP4 applies remuneration levels that are within established guidelines and that salaries are competitive, reasonable and defensible without being market leading. It was further found that senior executive benefits fit within the Government's guidelines for terms of employment for senior executives of the AP Funds.

Framework for AP4's risk management and risk control

The Board of Directors is ultimately responsible for AP4's risk management. The Risk Committee and Audit Committee prepare, on behalf of the Board, opinions regarding risk management and risk control. Annually, the Board adopts an investment policy and risk management plan for the business. Along with LAP, these governing documents form the framework for AP4's risk management and risk control. The risk and investment strategy has been designed in line with AP4's overall goal to maximize returns over time, thus contributing to the pension system's financial strength.

The investment policy describes, among other things, AP4's management focus based on: the Board of Directors resolved Normal portfolio (Reference portfolio); return targets; and risk profile and risk mandates for the Strategic and Tactical management. This represents an overall framework for the business. The Risk Management plan describes the division of responsibility and authority for the investment operations, the principal operational risks and the monitoring and control of the same. The main risks are financial and operational risks.

The returns, Risk and Control (ARK) unit

Financial and operational risks are monitored and controlled by an independent unit, Return, Risk and Control (ARK). The unit reports directly to the CEO and the Board.

ARK is responsible for, and develops, the risk analysis and control processes. ARK provides methods for risk identification, risk quantification, risk analysis and reporting of both financial and operational risks. ARK has the task to check that the statutory investment rules, investment policy, risk management plan and that the CEO's resolutions are complied with in operations.

ARK's work includes careful measurement and analysis as well as daily reporting of return and risk, both in absolute terms and relative to benchmark, and for the reporting of any violations of the applicable regulations.

ARK is divided into three functions: performance analysis, risk analysis and risk control.

Compliance function

AP4 also has a Compliance function, which is a separate unit that reports directly to the CEO and the Board. The Compliance function examines the business based on compliance with laws, regulations and other policies, instructions and rules, including the personnel and ethics-related policies.

The Compliance functions responsibility includes being a support for the activities regarding regulatory compliance issues and the analysis of operational compliance risks.

External audit of operations

AP4's auditors are appointed by the government. Peter Nilsson, of PwC AB, was the responsible accountant for 2016. The assignment applies until AP4's income statement and balance sheet are adopted for 2016; this also implies a special appointment of PwC AB to coordinate the audit of all the AP Funds.

The auditors submit an audit report based on their audit. The auditor's report directly to the Board through a written audit report and by oral presentation. The auditors attend at least one Board meeting per year.

The auditors also report annually to the Ministry of Finance. AP1-AP4 have jointly developed accounting and valuation principles, which aim to ensure that they apply the same valuation principles and that the financial statements are therefore comparable. The document is updated regularly and is reviewed annually with the external auditors.

More information can be found at www.ap4.se

A more detailed description of AP4's operations and management can be found in AP4's Annual Report, which is available at www.ap4.se.

Board of directors

AP4's Board of directors consists of nine members. All members are appointed by the government. Two members are appointed by proposal from the employees organization and two members are appointed by proposal from the employers organization. The government appoints the chairman.



Sarah McPhee

Chairman of the board since 2016.
Born 1954.

Other board assignments

Chair: SNS, The Royal Swedish Academy of Sciences Investment Committee.

Director: Klarna AB, Axel Johnson Inc., Bure Equity AB.



Jakob Grinbaum

Vice chairman since 2011.
Born 1949.

Other board assignments

Chair: Oscar Properties Holding AB.

Vice Chair: SBAB.

Board Director: IK Sirius, Jernhusen AB, Östgötagarde Uppsala Foundation, ATS Finans Holding AB, ATS Finans AB.



Heléne Fritzon

Director since 2015.
Born 1960.

Local Government Commissioner, Kristianstad Municipality

Other board assignments:

Chair: Koncernbolaget KKF, SKL:s förhandlingsdelegation

Director: SKL, EU - Committee of the Regions.



Ing-Marie Gren

Director since 2011.
Born 1951.
Professor.



Sven Hegelund

Director since 2012.
Born 1947.
Master in Political Science.

Other board assignments

Director: Nordiska investeringsbanken (NIB).



Stefan Lundbergh

Director since 2011.
Born 1968.

PH D.

Director Cardano Insights.



Erica Sjölander

Director since 2012.
Born 1971.
Chief Investigator, IF Metall.



Maj-Charlotte Wallin

Director since 2014.
Born 1953.
MBA

Other board assignments

Director Kammarkollegiets Fund delegation, Heart-Lung Foundation och Specialfastigheter AB.



Göran Zettergren

Director since 2015.
Born 1958.
MBA
CFO Confederation of Professional Employees.

Swedish pensions

Swedish pensions are comprised of several parts: national pension, occupational pension and private savings. The pensions can be represented by a pyramid, where the national pension forms the base.



The Swedish state provides the **national pension** and it is administered by the Swedish Pension Agency. It consists of two parts, income pension and premium pension, both of which are based on an individual's income. Each month the employer pays in 18.5 percent of pensionable income to the state, where 16 percent is paid to the income pension system and 2.5 percent to the premium pension.

The national pension also includes so-called **guaranteed pension**. It is a basic protection to the persons entitled to a pension, but who have not had an adequate income. The guaranteed pension is financed by the state budget and is independent of the income and premium pension system.

The premium pension - 2.5 percent of the salary - allows the employees themselves to choose directly how it will be invested within the premium pension system. The governmental **AP7** manages the premium pension for those who do not make their own active choice. The premium pension is governed by how the equity and fixed income markets develop.

Today, most employable people receive **occupational pensions** through their employer, often governed by collective agreements. In addition, employees can subscribe, individually, to a private pension.

AP Funds in the pension system

Income pension is a 'distribution system' where the year's pension contributions paid by those who work are used to pay pensioners the same year. In return, those who are working receive something called pension entitlements. Current and expected future pension rights earned constitute the system's pension liability. Everyone's earned pension entitlements determine the size of the individual income pension received.

The system's assets consist partly of the so-called contribution assets (86 percent) and partly of the AP Funds' capital (14 percent). The contribution assets are calculated based on long-term forecasts regarding, among others, the number of employable people and income.

There will be an imbalance in the pension system if many employable people retire at the same time without new workers entering the labor market leading to fewer people employed than pensioners. This would mean pension contributions would not be sufficient to pay-out pensions. The AP Funds, which acts as a buffer to cover these imbalances, compensate for these imbalances that may arise between generations, which is why AP1- AP4 is often referred to as the pension system's so-called "buffer capital". The buffer capital is used to cover any deficits in pension payments.

AP6 differs from AP1-AP4 in that it is a closed AP Fund where capital is not either paid in or out. AP7 has a very different mission from the other AP Funds in that it manages premium pension capital.

Pension System, net flows

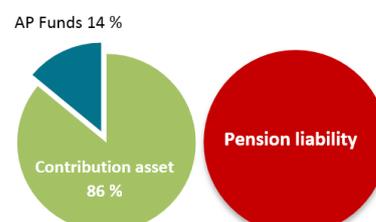
Since 2009, net flows in the income pension system have been negative, in other words payments to current retirees is greater than the contributions paid from today's wage earners. AP1- AP4 have therefore had annual outflows of capital to the pension system to bridge the generation gap that occurs when the so-called baby boomers retire.

The Swedish Pension Agency has predicted that AP1-AP4 will need to contribute capital to the pension system during the next more than 20 years to cover future pension payments.

The "Brake" balances pensions

The income pension is designed so that the capital will last over time and follows the income developments in Sweden. If the liabilities of the system should exceed its assets the so-called "brake" will be hit, or balancing - which is the real name. As such, income pensions are lowered when Sweden's economy slumps and are increased when the economy flourishes.

The increasing value of the AP Funds has contributed to that the automatic balancing mechanism has been avoided for several years. In connection with the financial crisis in 2008 and 2009 the "brake" point was reached. This was a result of severe economic- and employment-downturns and general declines in global equity markets.



AP4 manages buffer capital on behalf of the Swedish present and future pensioners with the goal to maximize shareholder value over time.

Fjärde AP-fonden
Regeringsgatan 30-32
Box 3069
SE-103 61 Stockholm

+468-787 75 00

info@ap4.se | www.ap4.se