

Interim Report 2020

AP4's mission is to contribute to the financial security of current and future pensioners by managing part of the Swedish national pension system's buffer capital.



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This half-year report has been prepared in accordance with the accounting and valuation principles jointly adopted by the AP Funds. These are described in AP4's 2019 Annual Report. Unless specifically indicated, the same accounting principles and calculation methods have been used as for the 2019 Annual Report.

The figures in the half-year report's tables and charts have been rounded separately, which is why their sum does not always exactly match their constituent parts. Figures in parentheses refer to the first half of 2019 unless indicated otherwise.

This half-year report has not been reviewed by AP4's auditors. No significant events have taken place after the end of the reporting period. AP4's annual report for the 2020 financial year will be published in February 2021.



403

SEK billion in fund capital

-10.6

SEK billion half-year result

4.2

SEK billion paid out to the pension system

-2.5

% return after costs

-0.7

% active return

0.09

% in management costs

Weak negative return in the light of covid -19

- **The Fourth Swedish National Pension Fund's (AP4) return** for the first half of 2020 was -2.5% before and after costs.
- **AP4's total fund capital** at 30 June 2020 amounted to SEK 403.2 billion, compared with SEK 418.0 billion at the start of the year.
- **The result** for the first half of the year was SEK -10.6 billion. During the same period, net payments from AP4 to the pension system totalled SEK 4.2 billion.
- **The portfolio's active return** during the first half of the year was lower than the return for AP4's benchmark portfolio, by -0.7 percentage points.
- **Currency exposure** at the end of the period was 19.7% of fund capital.
- **Total costs** indexed on a full-year basis amounted to 0.09% of average assets under management. AP4's cost level is approximately half of what corresponding pension funds are, in an international comparison.
- **In response to the Covid-19 crisis** and the uncertainty it has created for companies' development, AP4 has taken active owner responsibility and engaged in proactive dialogues with companies and owner groupings, resulting in AP4's participation in a number of new share issues to provide long-term support to sound companies in this very uncertain situation. AP4 is also contributing to the establishment of an investment company whose purpose is to serve as a minority owner and support primarily unlisted medium-sized Swedish companies in the current situation.
- **AP4 took its active owner responsibility** during the first half of the year by voting at the annual shareholder meetings of 82 Swedish and 873 international companies. Ahead of the 2020 AGM season, AP4 participated on the nomination committees of 38 companies.

Portfolio and return

AP4's return after costs for the first half of 2020 was -2.5%. AP4's considerable exposure to equities – both globally and in Sweden – was the main reason for the negative return. Real assets, consisting in part of equities in listed property companies, also contributed to the reduction in AP4's total return during the first half of the year. Fixed income investments made a positive contribution to the AP4's return, however. AP4's currency exposure of 19.7 percent by the end of the first half of 2020 resulted in a negative return contribution of -0.4 percentage points, owing to a strengthening of the Swedish krona during the first half of the year.

Long-term perspective warrants substantial equities allocation

AP4's long-term assignment and a higher expected return over time for equities compared with other asset classes warrants a high equities allocation, despite the relatively higher level of risk. Substantial exposure to Swedish equities and fixed income investments is warranted by a higher expected return relative to many other markets, favourable opportunities for AP4 to generate excess returns through active management, and lower currency hedging costs.

AP4 exceeding long-term return target despite negative return

The portfolio return of -2.5 percent for the first half of 2020 was lower than AP4's long-term return target of the Consumer Price Index (CPI) plus three percentage points per year. Over the ten-year evaluation horizon the average return has been 9.5 percent per year, which exceeds the return target, which has averaged 5.2 percent per year. Since the Fund's inception in 2001, the return

has averaged 6.2 percent per year, which is higher than the target return, which has been 5.6 percent per year.

Negative active return contribution

Active management made a negative return contribution of -0.7 percentage points during the first half of the year. A decline in share prices for listed property companies was the main reason for this. At the same time, listed property companies are included in the overall asset class of real assets, which is evaluated comparative to a real return requirement of the CPI plus three percentage points per year. However, over AP4's five-year evaluation horizon, AP4's active return has been positive, averaging 1.7 percentage points per year, compared with the target, which has averaged 1.0 percentage points per year.

Government's evaluation for 2019 positive

The government's annual evaluation of the AP Funds for 2019 was submitted to the Riksdag (Swedish Parliament) in May 2020. It includes a summary evaluation of AP4 and states that AP4 has



managed net flows between incoming and outgoing payments in the income pension system as intended, that AP4 has generated a return that is contributing to the income pension system's long-term funding, and that AP4 has worked actively with sustainability issues. In summary, it states that AP4 has met the government's expectations for AP4.

Changed investment rules for the AP Funds

On 1 May 2020, Step 2 of the changed investment rules took effect, which gives AP1-AP4 greater flexibility to make investments in unlisted assets. An AP Fund's maximum share of voting rights in a private equity company was thereby raised from 30 percent to 35 percent and such private equity company has been given the opportunity to now invest also in illiquid credits. In addition, the AP Funds have been given the opportunity to make discretionary investments in unlisted companies together with private equity funds that an AP Fund has already invested in.

Legislative review regarding easing of voting rights limitation for the AP Funds

In June the Ministry of Finance issued a legislative proposal for consultation calling for a temporary easing of the limitation for an AP Fund's maximum ownership stake in a listed company from 10 percent to 15 percent when participating in a new share issue. The easing of the limitation would give the AP Funds a better opportunity to support companies in which a Fund is already a major owner. It has been proposed that the rule applies during a limited period from 1 November 2020 through 30 June 2021 at the latest, and that holdings exceeding the 10 percent threshold be divested within a seven-year period thereafter.

Continued net payments to the pension system

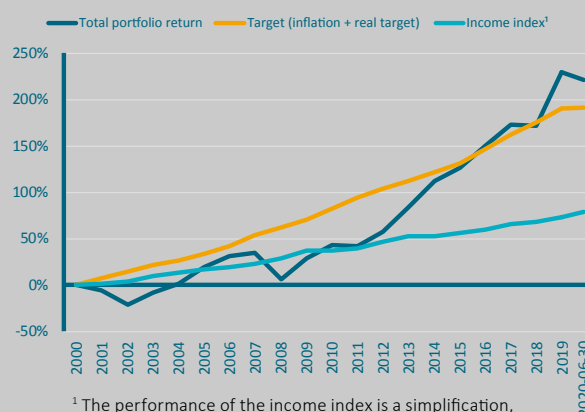
AP4's net payment to the pension system during the first half of 2020 amounted to SEK 4.2 billion. Since 2009, when net payments from the AP Funds to the pension system were begun, through the first half of 2020, AP4 has paid out SEK 61 billion to the pension system. These payments have been made mainly as a result of demographic factors, such as the generationally large number of people who are now pensioners. The pension system is designed specifically to withstand this, and net payments from the AP Funds to the pension system are expected to continue until around 2040.

Three new members on AP4's board

In May 2020 the government appointed Helén Eliasson, Monika Elling and Aleksandar Zuza as new members on AP4's board. The three new board members succeed Sven Hegelund, Erica Sjölander and Katrin Stjernfeldt Jammeh.

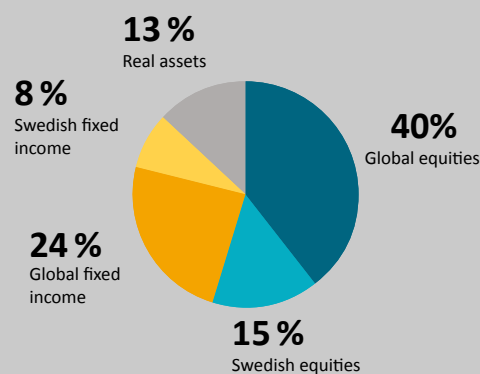
Portfolio and return, 30 June 2020

AP4's return, after costs, since start 2001



¹ The performance of the income index is a simplification, where the performance over a full year has been distributed equally over the respective half years.

A diversified portfolio



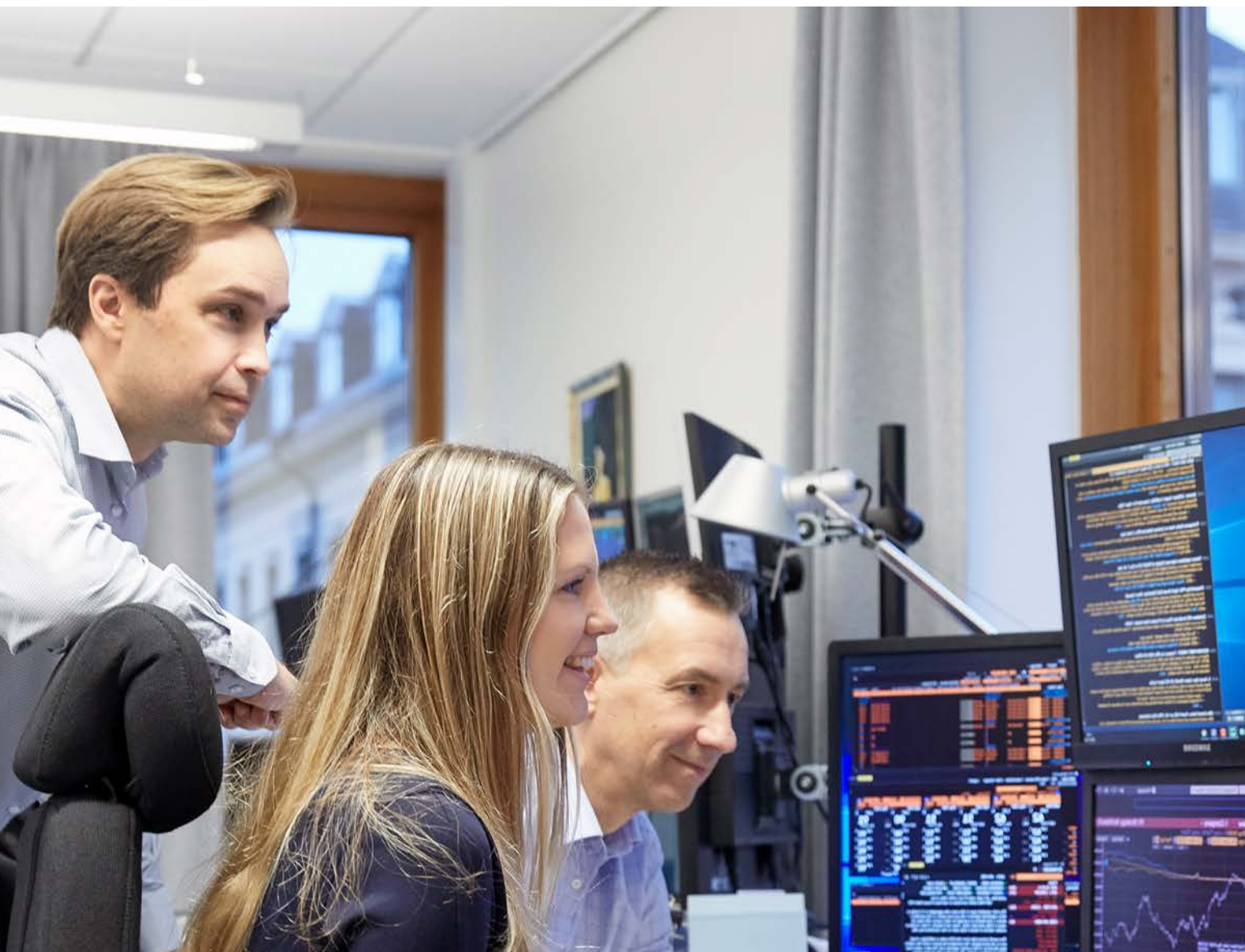
Asset class

Asset class	Market value, SEK bn	Portfolio return ¹ , %	Exposure ² , %
Global equities	159.7	-6.4	39.6
Swedish equities	61.7	-2.0	15.3
Global fixed income	96.6	2.7	24.0
Swedish fixed income	32.4	1.0	8.0
Real assets	52.8	-4.0	13.1
Other assets ³	0.0	0.2	0.0
Currencies	0.0	-0.4	0.0
TOTAL INVESTMENTS	403.2	-2.5	100.0

¹ Portfolio return before costs.

² Underlying values of derivative instruments in the passive allocation are distributed among the respective asset classes.

³ Consists mainly of various overlay mandates.



Key ratios for AP4's operations

	30 June 2020	30 June 2019	2019
Fund capital at start of period, SEK bn	418.0	349.3	349.3
Net result for the period, SEK bn	-10.6	45.2	75.2
Net flow to national pension system, SEK bn	-4.2	-3.0	-6.5
Fund capital at end of period, SEK bn	403.2	391.4	418.0
Asset management costs, operating expenses, %	0.06	0.06	0.06
Asset management costs, commission expenses, %	0.03	0.04	0.04
Total asset management costs, %	0.09	0.10	0.10
Return, total portfolio, before costs, %	-2.5	13.0	21.8
Return, total portfolio, after costs, %	-2.5	13.0	21.7
Real return after costs, % ¹	-1.6	11.7	19.9
Annualised return after costs, 5 years, %	7.4	9.3	9.3
Annualised return after costs, 10 years, %	9.5	10.4	9.9

¹ The CPI for June 2020 is an estimate, since this figure was not yet available at the time of publication of this report.

Letter from the CEO

The first half of 2020 will go down in history as the time in which the world came under the onslaught of Covid-19. The pandemic and the measures taken to limit the spread of the disease have put great a great strain on the global economy. The situation remains hard to predict, with major uncertainty about future development.

Even though it now feels distant, the year started out with a positive macroeconomic trend with indications for a recovery following a weak 2019. The comparatively positive start to the year then abruptly changed over to near panic in March. We saw an extreme drop in the stock markets in pace with the spread of Covid-19 to Europe and the USA. We also saw movements in the financial markets that were greater than what we saw during the financial and euro crises along with marketability that was very limited – or lacking entirely – for most securities. What we experienced in March with a long succession of days of market reactions can be most closely equated with what we had following the terrorist attack on 11 September 2001. To give an illustration of the scope of the stock market decline in March, the market capitalisation in the US stock market fell by nearly 11.000 billion dollars from top to bottom. This corresponds to nearly 50% of the USA's annual GDP!

The political system has on the whole acted swiftly and resolutely in response to the pandemic. First came the imposition of various restrictions to slow the spread. These gradually grew very extensive in many countries in Europe and parts of the USA, with very large real economic consequences. To counter the negative consequences of the restrictions, central banks and governments began at an early stage deciding on various types of support measures. During the spring these monetary and finance policy programmes also grew increasingly extensive and are now at historically high levels; the fiscal policy stimulus measures alone are expected to amount to a whopping 15% of GDP as an international average in total over this and next year.

Owing to a combination of strong support and stimulus measures, gradually improved control over spread of the disease, gradually improved knowledge about Covid-19 in general and the successive easing of restrictions, since early April the financial markets have recovered considerably. Now at mid-year, looking at the combined changes in asset prices since the start of the year, they are in many cases astoundingly small given the extreme period we have endured.

The scope of the impact on the real economy during the

first half of 2020 has been brutal. The speed and depth of the economic slowdown far exceeds what we saw during the financial crisis. For 2020, GDP is expected to fall in the range of -8% in Europe and the USA compared to what was expected before the pandemic. Following such an historically dramatic slowdown, it is natural that we will have a rebound in 2021, but according to our main scenario we do not believe that we will be back to the same GDP level as before the pandemic struck until around 2023.

A historically large drop in GDP this year and thereafter a rebound in 2021 notwithstanding, the long-term key question is whether the pandemic will cause structural and permanent damage to the world economy, and if so, how much. Revolving around this question, undoubtedly there is no lack of areas of concern, including the risk for permanently high unemployment, a new crisis in the financial system, a halt to globalisation and increased regional tensions, and a sharply higher level of debt that may lead to structural problems in the future. On the other side of the scale, and more positively, are other factors that over time may strengthen the economy's way of functioning and productivity. Examples of such factors are an acceleration of digitalisation, investments in neglected infrastructure, the shift to a sustainable society, and the potential for positive structural reforms.

Ultimately much will be determined by whether the resources that will be invested into restarting the world's economies succeed in steering towards long-term productivity improvements and that the leading economies have the continued resilience to embrace the belief in the benefit of global cooperation and global economic collaboration. Our current assessment is that the pandemic will certainly lead to permanent damage to the world economy, but that this damage will not necessarily be as hard to repair over the long term as after the financial crisis. The financial crisis entailed a meltdown of the world's banking system, with an essentially broken credit system for a long period of time. In Europe the crisis in the banking system subsequently gave way – through very strained state budgets – to a deep and paralysing euro crisis which parts of Europe have still not recovered from. The situation is very hard to predict however, and it is certainly



possible to conjure especially more negative scenarios, but also some that are more positive.

In the type of extraordinary markets that we saw in March and April, AP4's asset management has moved in to what we call a state of readiness, since the external conditions require a different focus and set of dynamics than AP4's ordinary processes. A state of readiness entails, among other things, a considerably higher meeting frequency than normal – and flexible, specially adapted meeting constellations suited for this purpose – to ensure effective information-sharing, a cohesive grasp of the Fund's larger positions and focus on swiftly acting on business opportunities. In short, our state of readiness during the spring has involved maintaining full focus on the following main principles:

- Avoid forced trades in non-functioning markets – trade only when it is necessary and then underpinned by an investment analysis
- Dare to be long-term (one of the Fund's unique characteristics) – hold, and even increase, positions that we believe in long-term and act as a long-term and responsible owner
- Strive to take the offensive – seek out and take advantage of opportunities and imbalances that emerge in the market
- Support each other – stay positive and keep calm

Such a difficult, disorderly and nervous market that we have had during the spring entails challenges, but also opportunities, for a

long-term investor like AP4. For example, we began buying equities after the first, major initial drops to maintain our asset allocation. Another example is corporate bonds, the price of which fell indiscriminately in March, when the market in its hysteria could not manage to differentiate between various companies. Here we saw an opportunity as a long-term investor to increase our investments in corporate bonds issued by quality companies that structurally benefit – or at least are not put to a disadvantage – from the long-term impacts of the Covid-19 crisis.

“We have acted as a long-term and responsible owner in this extremely difficult and uncertain situation.”

We have also acted as a long-term and responsible owner in this extremely difficult and uncertain situation. This has been done, among other ways, by engaging in proactive dialogues with companies and with owner groupings on companies' need for capital, which has resulted in AP4's participation in several new share issues to support companies with sound long-term models. AP4 is also contributing to the establishment of an investment company



together with AMF, FAM, SEB and AFA Försäkring, whose purpose is to work in the prevailing, difficult market situation by injecting capital and serve as a minority owner in supporting primarily unlisted, medium-sized Swedish companies that have business models that will remain sound after the pandemic. It is also gratifying that a proposal for a temporary change in legislation that will allow the AP Funds to own up to a 15% voting stake in listed companies (it is currently limited to 10%) has been circulated for review.

“A negative result never feels satisfactory, but given the circumstances, our return for the first half of the year can still be regarded as a passing grade”.

AP4 reports a return of -2.5% for the first half of 2020. The main explanation for the negative return is AP4's substantial holdings of Swedish and global equities. But even real assets thus far this year have had negative returns, while fixed income assets have made a positive contribution. A negative result never feels satis-

factory, but given the circumstances, our return for the first half of the year can still be regarded as a passing grade for how we have managed to deal with the spring's market turbulence. The entire organisation has worked very resolutely and professionally throughout this difficult time.

In closing I want to direct great thanks to all of AP4's employees for how well you handled the work burden during the spring. The management and handling of AP4's portfolio have been conducted in a superb manner at the same time that our operations continued to develop with the goal over time to optimally perform the Fund's assignment to generate a long-term favourable return for today's and tomorrow's pensioners.

Stockholm, 13 July 2020

Niklas Ekvall, CEO

Active owner in a turbulent environment

AP4 is a long-term owner and embraces its responsibility to support companies in which we are an owner in good times and bad. It has therefore been natural for AP4 – in the face of Covid-19 and the uncertainty it has created for companies' development – to engage in proactive dialogues with companies and owner groupings.

This has resulted in AP4's participation in a number of new share issues to provide long-term support to sound companies in this uncertain situation. AP4 also took its active owner responsibility during the first half of 2020 by voting at the AGMs of 82 Swedish and 873 international companies. Ahead of the 2020 AGM season, AP4 participated on the nomination committees of 38 companies.

Transition Pathway Initiative provides documentation for active corporate governance

The Transition Pathway Initiative (TPI) is a global initiative led by institutional investors. It assesses how companies with a substantial carbon footprint are working to address climate change in line with the Paris Agreement as well as their public disclosures in accordance with the requirements of the Task Force on Climate-related Financial Disclosures (TCFD). AP4 has supported the TPI since its formation in 2016. In spring 2020 AP4 used the TPI's assessment as documentation for voting at company annual meetings globally. If a company's board does not clearly work for emissions reductions, climate action and transparency, AP4 weighs this in to its assessment of whether it will vote for or against re-election of senior persons on the company's board – the chairman, vice chairman and CEO. The TPI's assessments were used ahead of company annual meetings during the first half of 2020, and in 28 cases APR voted against re-electing said persons. To challenge companies to work more with this issue, AP4 clearly expresses its views and continually monitors developments.

Several thematic sustainability investments in unlisted companies

During the spring of 2020 AP4 made a number investments in unlisted companies based on identified sustainability trends. AP4 is participating in the establishment of an investment company that will support Swedish business by investing in medium-sized Swedish companies that were successful before the Covid-19 crisis and that are expected to be so again once the economy has returned

to a more normal situation. AP4 has invested in a fund focused on food supply that offers controlled environments for sustainable food production in advanced greenhouses. AP4 has also invested in a private equity fund that is investing on a commercial basis in unlisted medium-sized companies that are making positive contributions to the UN's Global Sustainable Development Goals.

Call to action from EU leaders for a sustainable restart of economies

In an open letter, AP4 together with more than a hundred institutional investors have urged the EU's leaders to act for a swift and sustainable recovery in the wake of the Covid-19 crisis. The investors, which have a long-term perspective of investments and returns, aim to contribute to a green and sustainable recovery. The EU's target to be climate neutral by 2050 entails that jobs need to be created with a focus on the sustainable infrastructure, industrial, construction and energy sectors. The path we choose today for restarting economies will have an impact on the global economy for generations to come.

AP4 participated in call to end deforestation in Brazil

Together with other Nordic and European investors, AP4 signed a letter to the Brazilian embassy in which concerns over increased deforestation primarily in the Amazon were stressed in response to a legislative proposal presented in Brazil. The deforestation presents risks to the climate, biodiversity and the rights of native peoples. Voting for more women on Japanese boards

During the annual meeting season in Japan in 2020, AP4 called attention to the importance of increased diversity on company boards in Japan. This was done by voting against re-election of board members who serve on the nomination committee for companies in which there are no women represented on the board. AP4 voted at the annual meetings of 261 companies in Japan in spring 2020, and in 40 cases there were no women serving on the board. AP4 will engage these companies in a dialogue and continually monitor developments.



AP4 took its active owner responsibility during the first half of 2020 by voting at the AGMs of 82 Swedish and 873 international companies. Ahead of the 2020 AGM season, AP4 participated on the nomination committees of 38 Swedish companies.

Income statement

SEK million	Jan-Jun 2020	Jan-Jun 2019	2019
OPERATING INCOME			
Net interest income ¹	820	1 084	2 027
Dividends received	2 761	4 299	6 035
Net income, listed shares and participations	-12 586	30 139	50 676
Net income, unlisted shares and participations	-262	162	5 589
Net income, fixed income assets	2 622	3 684	3 322
Net income, derivative instruments ¹	-1 190	1 708	2 018
Net income/loss, changes in exchange rates	-2 594	4 256	5 939
Commission expenses	-71	-66	-139
Total operating income	-10 500	45 266	75 467
OPERATING EXPENSES			
Personnel costs	-70	-66	-136
Other administrative expenses	-50	-47	-95
Total operating expenses	-120	-113	-231
NET RESULT FOR THE PERIOD	-10 620	45 153	75 236

Balance statement

SEK million	30 June 2020	30 June 2019	31 December 2019
ASSETS			
Shares and participations, listed	232 518	228 018	248 771
Shares and participations, unlisted ¹	45 215	37 258	42 897
Bonds and other fixed income assets	115 594	118 210	115 965
Derivative instruments	6 737	3 479	6 307
Cash and cash equivalents	4 335	3 767	4 496
Other assets	638	1 885	3 167
Prepaid expenses and accrued income	1 040	1 270	1 030
TOTAL ASSETS	406 077	393 887	422 633
LIABILITIES AND FUND CAPITAL			
LIABILITIES			
Derivative instruments	2 086	1 245	1 112
Other liabilities	381	622	2 865
Prepaid income and accrued expenses	402	595	628
Total liabilities	2 869	2 462	4 605
FUND CAPITAL			
Fund capital, opening balance	418 028	349 312	349 312
Net payment to the pension system	-4 200	-3 040	-6 520
Net result for the period	-10 620	45 153	75 236
Total fund capital	403 208	391 425	418 028
TOTAL LIABILITIES AND FUND CAPITAL	406 077	393 887	422 633

Multi-year summary

Multi-year summary	30 June 2020	2019	2018	2017	2016
FUND CAPITAL, FLOWS AND RESULT, SEK BILLION					
Fund capital	403.2	418.0	349.3	356.6	333.9
Net flows to the pension system	-4.2	-6.5	-6.8	-7.4	-6.6
Net result for the period	-10.6	75.2	-0.5	30.1	30.5
RETURN, %					
Return, total portfolio before costs	-2.5	21.8	-0.1	9.2	10.1
Return, total portfolio after costs ¹	-2.5	21.7	-0.2	9.1	10.0
Return, total portfolio after costs, annualised 5 yrs	7.4	9.3	8.1	11.5	12.0
Return, total portfolio after costs, annualised 10 yrs	9.5	9.9	9.9	7.3	6.7
OPERATING EXPENSE RATIO AS % OF AuM (ANNUALISED)					
Operating expenses	0.06	0.06	0.06	0.06	0.06
Operating expenses and commission expenses	0.09	0.10	0.10	0.10	0.10
RISK, % ¹					
Standard deviation ex-post, Total portfolio	18.0	5.3	6.4	4.1	7.3
Standard deviation ex-post, Liquid portfolio ²	20.8	5.8	7.0	4.5	7.8
Standard deviation ex-post, Liquid portfolio, 10 yrs ³	8.2	6.7	7.5	8.6	8.8
Sharpe ratio, total portfolio ex-post	neg	4.2	0.1	2.5	1.5
Sharpe ratio, liquidity portfolio ex-post ³	neg	3.9	neg	2.0	1.2

¹ Refers to daily return data, unless otherwise indicated. The higher daily market movements during the first half of 2020 explains the higher reported risk level.

² Refers to liquid assets excluding unlisted real estate, private equity funds and high-yield fixed income assets. ³ Refers to quarterly data for total assets.

³ Refers to quarterly data for total assets.

Other key ratios, as per closing date	30 June 2020	2019	2018	2017	2016
Active return, strategic management before costs, % ^{1, 2}	-0.7	4.4	2.3	-1.1	1.0
Inflation, % ³	-1.0	1.8	2.0	1.7	1.7
Real return after costs, % ³	-1.6	19.9	-2.3	7.4	8.3
Active risk ex-post, active management, % ⁴	1.7	1.2	1.5	1.7	2.7
Currency exposure, %	19.7	19.8	18.4	18.4	26.9
Proportion external management incl. investments in private equity companies, % ⁵	14.5	14.7	16.2	17.0	22.7
Number of employees on balance sheet date ⁶	64	53	52	53	54
ALLOCATION OF INVESTMENT ASSETS, % ⁷					
Global equities	39.6	39.3	38.9	40.8	40.2
Swedish equities	15.3	15.6	14.6	16.6	17.6
Global fixed income	24.0	21.0	22.0	21.1	22.7
Swedish fixed income	8.0	11.4	12.2	11.6	10.6
Real assets	13.1	12.7	12.1	9.6	8.6
Other	0.0	0.0	0.3	0.3	0.3
TOTAL INVESTMENT ASSETS, %	100.0	100.0	100.0	100.0	100.0

¹ The Fund's operative portfolio is evaluated against a reference portfolio made up of a number of benchmark indexes with set asset weights. The benchmark indexes used are standardised and currency-hedged to SEK in order to simplify and increase transparency. The Fund can use its tax status as a state pension fund, and during the first half of 2020 this gave a positive contribution of 0.10 percentage points.

² Active return, calculated as the difference in returns between the operative portfolio and the benchmark portfolio.


³ The CPI for June 2020 is an estimate, since this figure was not yet available at the time of this report's publication.

⁴ Active risk, calculated as standard deviation, measured on a yearly basis, in the difference in the return between the operative portfolio and the benchmark portfolio.

⁵ Wholly or partly owned property companies are reported as internally managed.

⁶ The higher number of employees on the end of the first half of 2020 is mainly related to seasonality, with a higher number of hourly employees during the summer.

⁷ Refers to exposure; underlying derivative values in the passive allocation have been distributed among the respective asset classes.



AP4's long-term perspective, responsibility as owner and great commitment to sustainability create opportunities for high returns at a low cost. In this way AP4 works for more secure pensions.