FJÄRDE AP-FONDEN

ANNUAL REPORT 2007

The Fourth Swedish National Pension Fund (AP4) is one of five buffer funds in the national pension system. Together with the capital of AP1, AP2, AP3 and AP6, AP4's fund capital is used to offset temporary fluctuations in pension system contributions and disbursements. **The objective of the buffer funds** is to invest capital to generate optimum returns for the long-term health of the income pension system.

AP4 had **more than SEK 200 billion** in assets under management at year-end 2007.

TABLE OF CONTENTS

2007 HIGHLIGHTS	2
LETTER FROM THE CEO: A tough first year	4
MARKET:	
Turbulent finance markets	8
Credit crisis with serious ripple effects	9
THE BUFFER FUNDS' MANDATE AND OBJECTIVES:	
A long-term approach	10
High returns and low risk	11
MANAGEMENT: Sharper focus on strategic allocation and passive management	12
CORPORATE GOVERNANCE: Active shareholder responsibility	16
SOCIAL AND ENVIRONMENTAL RESPONSIBILITY:	
Social and environmental initiatives create higher shareholder value	18
The Ethical Council in China	19
ORGANISATION AND EMPLOYEES: Leadership with distinct values	20
REPORT OF THE DIRECTORS	22
Five-year summary	31
Income statement	32
Balance sheet	32
Accounting and valuation principles	33
Notes to the income statement and balance sheet	34
Auditors' report	39
ADMINISTRATION REPORT	40
BOARD OF DIRECTORS AND AUDITORS	42
EXECUTIVE MANAGEMENT COMMITTEE	43
GLOSSARY	44

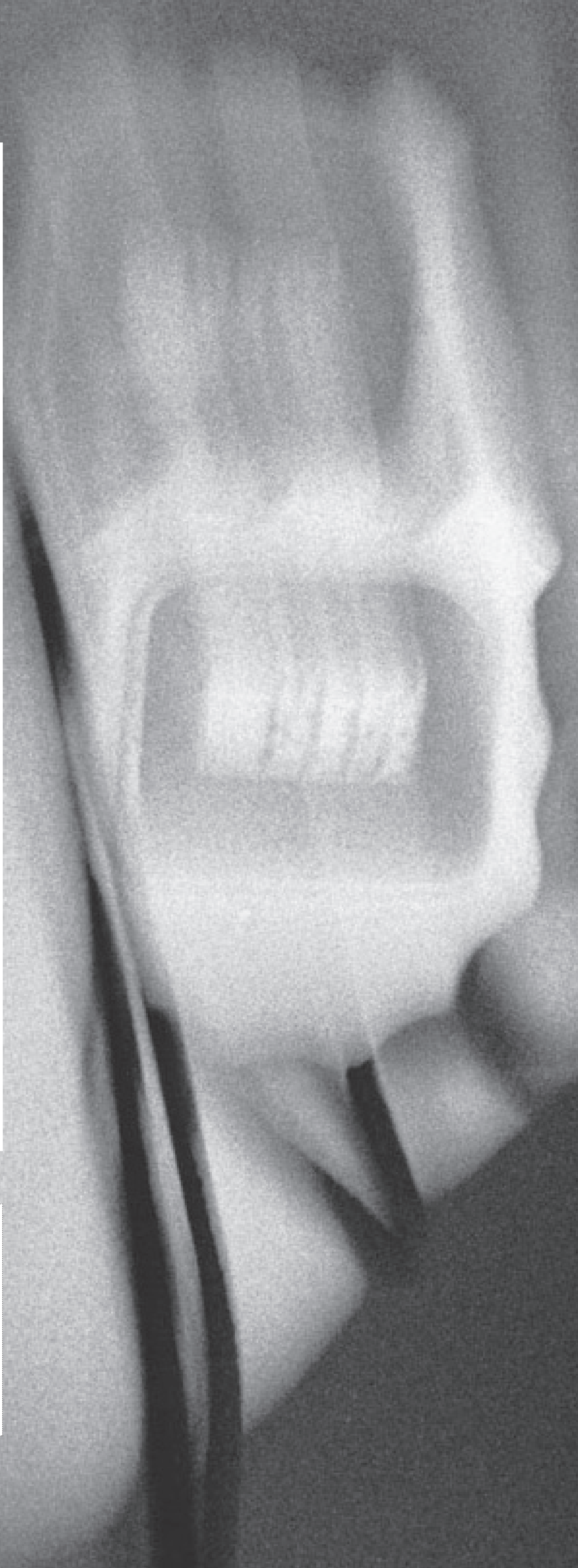
INFORMATION

For further information, please visit the AP4 website at www.ap4.se. The following publications are available online:

- Annual and interim reports from recent years
- AP4's key public documents, including the governance policy

Annual reports and other reports may be also be ordered directly from the Fund. Phone +46 8 787 75 00.

Further information about the national pension system is available online from the Swedish National Social Insurance Agency, www.forsakringskassan.se.



AP4 AT A GLANCE

The Fourth Swedish National Pension Fund (AP4) is one of five buffer funds in the national pension system. Together with the capital of AP1, AP2, AP3 and AP6, AP4's fund capital shall be available to offset temporary fluctuations in pension system contributions and disbursements. The objective of the buffer funds is to invest capital to generate optimum returns for the long-term health of the income pension system. The five buffer funds combined had about SEK 850 billion in assets under management at year-end 2007.

> **Financial security for Swedish pensioners.**

VISION

Asset management at AP4 is governed by laws, investment rules and internal guidelines. A comprehensive change and strategy initiative was commenced in 2007. The results thus far include formulation of the Fund's vision: Financial security for Swedish pensioners.

The vision is meant to clarify the central role and key mandate of AP4 and the other buffer funds to secure and increase the value of the public income pension.

INVESTMENT GOALS

With a view to realising the vision, AP4 has formulated two overriding objectives for the period up to 2010:

- The Fund shall generate average real (inflation-adjusted) return of 4.5% per year over a five-year period.
- The Fund shall achieve annual active return (return that outperforms the index) of 0.5 percentage points. Opportunities to achieve active return vary from year to year. The Fund has lowered its risk and consequently lowered the target to 0.4 percentage points for 2008.

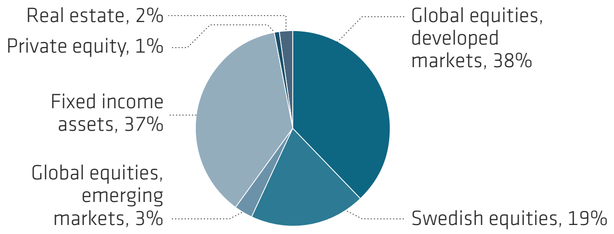
STRATEGIES

- The Fund will devote greater resources to the allocation function, that is, to the allocation of capital among asset classes. The Fund will apply three time perspectives to capital allocation, long-term (40 years), medium-term (3–5 years) and short-term (6–12 months), with greater emphasis on the medium-term investment horizon.
- The Fund will increase the percentage of passively managed assets and engage in active management only in clearly justified cases.
- The Fund will increase the percentage of external management mandates.

FUND CAPITAL

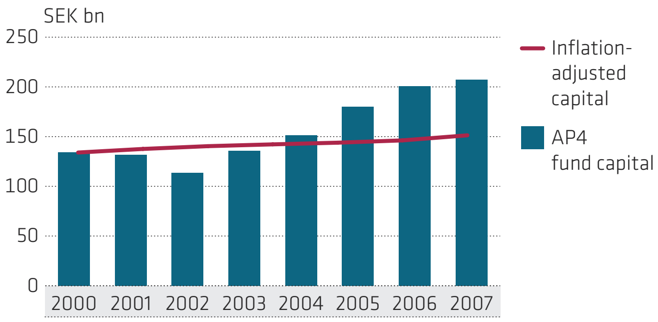
Fund capital was SEK 207.3 billion at 31 December 2007. Nearly 97% of the Fund's investment assets are listed, of which 61% equities. The Fund has delivered average annual return of 11.4% for the last five years, corresponding to average real return after management expenses of 9.7%. The Fund has thus outperformed its target for absolute return, but has not met the target for active return.

ACTUAL PORTFOLIO, 31 DEC 2007



Equities are the predominant component of Fund assets. Global equities, emerging markets was a new and growing sub-portfolio in 2007.

FUND CAPITAL AND INFLATION



Fund capital developed well and growth outpaced inflation by a healthy margin.

2007 HIGHLIGHTS

2007 will go down in economic history as the year of the global liquidity crisis. The crisis helped put an end to the very strong bull run of several years' standing in developed equity markets. The year was one of renewed struggle for AP4 that brought slim returns and a comprehensive change initiative.

TURBULENT MARKETS

Overall, 2007 can be summed up as a turbulent year. The financial markets demonstrated a highly fragmented picture. The most unexpected and dramatic aspect was the global liquidity crisis in the wake of the American mortgage lending crisis. The credit and liquidity crisis brought not only substantial credit losses, but also helped put an end to the very strong bull run of several years' standing in developed equity markets.

Despite these circumstances, equity markets still delivered share growth over the calendar year. Including dividends, world equity markets rose by more than 5% in 2007 to slightly outperform the bond markets.

COMPREHENSIVE CHANGE INITIATIVE

Internal change set the tone for AP4 in 2007. Several years of underperformance have sharpened demands and a comprehensive change initiative was commenced in early 2007, aimed at creating a management organisation that attains its objectives. The Fund has reviewed its management process and strategy and clarified areas of responsibility. In response to market turbulence in the second half, the Fund also reduced risks by heightening concentration on passive and external management.

NET PROFIT: SEK 4.8 BILLION

Net profit at market value for 2007 totalled SEK 4.8 billion (18.8). Weak second-half trends in the equity and fixed income markets in which the Fund invests were the primary cause of the decline.

FUND CAPITAL INCREASED TO SEK 207.3 BILLION

At market value and after transfers, Fund capital rose during the year from SEK 200.5 billion to 207.3 billion.

TOTAL RETURN: 2.5% BEFORE EXPENSES

Total return before expenses was 2.5% (10.5). Of the sub-portfolios, the Swedish listed equity portfolio posted a negative return of –1.6%, while positive returns were generated by the global equity portfolio, at 2.1%, and the fixed income portfolio, at 1.3%. Foreign assets were fully hedged in all portfolios.

Total return after expenses was 2.4% (10.4). AP4's target is to generate minimum annual average real return (inflation-adjusted) of 4.5% over five years. The Fund has delivered average real return of 9.7% a year after expenses for the last five-year period – despite the modest outcome of the last financial year.

OPERATING EXPENSES: SEK 139 MILLION

Operating expenses for 2007 were SEK 139 million (133), or 0.07% (0.07) of the average value of Fund capital.

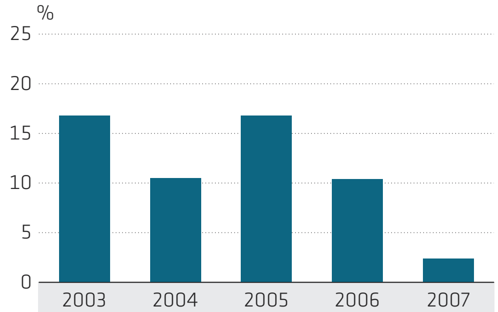
LOWER CURRENCY EXPOSURE

Currency exposure at 31 December 2007 was 14.2% (15.1).

ACTIVE RETURN: –1.0%

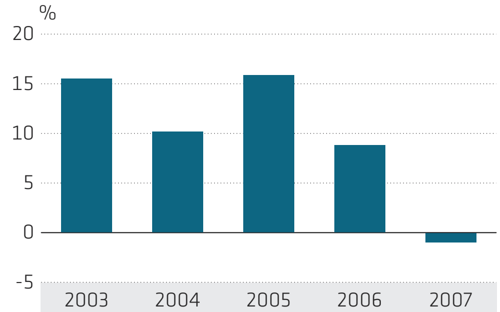
Active return before commission expenses for 2007 was –1.0 (–0.6) percentage points.

TOTAL RETURN AFTER EXPENSES



While net profit was slim for 2007, total returns for major asset managers must be assessed over periods of longer than one year ...

REAL RETURN



... AP4 has generated average real return of 9.7% over the last five years, substantially outperforming the minimum annual target of 4.5%.

INVESTMENT ASSETS, ALLOCATION AND RETURNS

Asset class	Return and contributions to Fund performance, Jan–Dec 2007					Asset mix, 31 Dec 2007		
	Portfolio return, %	Active return, %	Contri-bution to portfolio return, %	Contri-bution to net profit, SEK bn	Contri-bution to active return, %	Market value, SEK bn	Expo-sure[2], %	Strategic portfolio, %
Swedish equities	–1.6	1.0	–0.1	–0.1	0.2	38. 1	18.7	18.8
Global equities	2.1	–2.0	1.0	1.9	–0.8	84.7	41.2	41.0
Fixed income assets	1.3	–2.1	0.5	0.9	–0.8	76.3	36.9	36.9
Currency, Tactical asset allocation, Cash	–	–	0.4	0.9	0.2	1.3	–0.2	0
Total listed assets	**1.8**	**–1.2**	**1.8**	**3.6**	**–1.2**	**200.4**	**96.6**	**96.6**
Real estate	21.4	0.0	0.4	0.8	0.0	5.0	2.4	2.4
Private equity	40.4	32.5	0.3	0.5	0.2	2.0	1.0	1.0
Total investment assets	**2.5**	**–1.0**	**2.5**	**4.9** [1]	**–1.0**	**207.4**	**100.0**	**100.0**

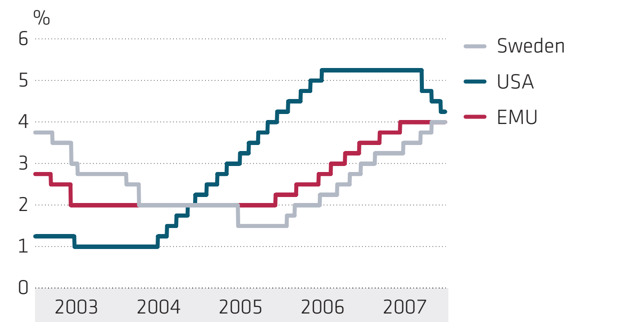
1) Before expenses; profit after expenses was SEK 4.8 billion.
2) Exposure includes the underlying value of derivatives for each asset class.

NET PROFIT BY ASSET CLASS

The Fund's net profit of SEK 4.8 billion for 2007 presents a meagre and fragmented picture. As shown in the table, the highest contributions to net profit were generated by global equities and fixed income assets, the two largest portfolios, at SEK 1.9 billion and 0.9 billion, respectively. The Swedish equity portfolio made a negative profit contribution of SEK –0.1 billion due to the share price downturn on the Stockholm Stock Exchange in 2007. It should be noted that the Fund's private equity holdings, which account for only 1% of Fund assets, contributed SEK 0.5 billion to total profit.

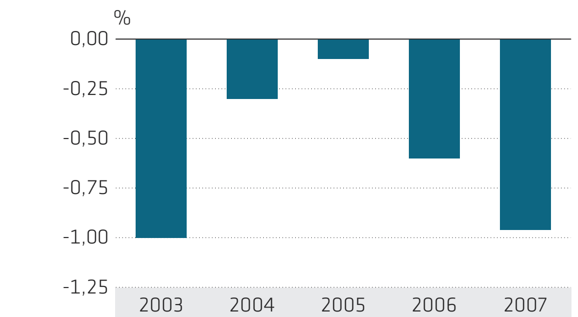
In terms of active return, the Swedish equity portfolio outperformed the index and provided a positive contribution of 0.2 percentage points, while contributions to the Fund's active return were negative for the global equity portfolio and fixed income assets, at 0.8 percentage points each. As shown, the small private equity portfolio also delivered a significant contribution to active return.

BASE RATES 2003–2007



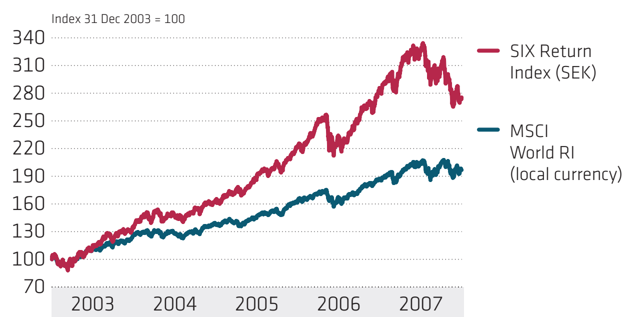
The US Federal Reserve initiated vigorous measures in autumn 2007 to stave off an international liquidity crisis and an impending economic downturn. Source: Reuters EcoWin

ACTIVE RETURN



The fund has not attained its active return target.

EQUITY MARKETS 2003–2007



Credit market turbulence in the second half of 2007 stopped the long bull run that had characterised the major equity markets since early 2003.
Source: Reuters EcoWin

A TOUGH FIRST YEAR

The improvements achieved in the first half of 2007 were erased by the turbulence in the credit market and the year ended in great disappointment. We did not meet our targets for absolute return or active management. The Fund's weak performance has compelled more in-depth analysis and comprehensive measures.

I would sum up 2007 as a very tough year at the helm of the Fourth National Pension Fund. The Fund's performance is not satisfactory. We did not meet our targets for absolute return or active management.

While AP4 delivered positive absolute return, it only reached a modest 2.5%, considerably underperforming the past few years. The primary explanation is the turbulence that hit the financial markets in the second half in response to the US mortgage lending crisis. It is to be expected that absolute return will end up around zero or even be negative in isolated years, since the Fund has nearly two thirds of its assets invested in equities. When world equity markets decline as they did in the second half of 2007, an asset manager like AP4 has very limited opportunities to withstand a downturn. Thus, absolute return for major asset managers must be assessed over longer periods than a single year. From that perspective, the Fund's situation looks brighter. Average absolute return was 11.4% for the last five years. Adjusted for inflation and management expenses, the Fund delivered annual return of 9.7%, outperforming the 4.5% target for real return (inflation-adjusted) by a wide margin.

MAIN PROBLEM

AP4's main problem is that the outcome for active management – that is, the capacity to outperform the market measured by the index – remains negative, year after year. The past year was yet another setback. The improvements achieved in the first half of 2007 were erased by the turbulence in the credit market and the year ended with active return of –1.0 percentage points and deep disappointment.

For the last five years, AP4 has generated average active return, before expenses, of –0.6 percentage points a year. Without question, this is wholly unacceptable. The Fund's weak performance has compelled us to implement more in-depth analysis and comprehensive corrective measures in 2007. Allow me to point out the main ingredients of the change initiative thus far and present a few key differences between the management strategy as it was, and as it is now.

MANAGEMENT DECISIONS ON THREE LEVELS

The basis of all asset management is selection among various asset classes – allocation decisions. In theory and in practice, the accepted wisdom is that the allocation decision determines 80–90 per cent of the manager's returns. Consequently, AP4 reinforced both human resources and system support in the allocation function during 2007. We have also clarified how the Fund allocation function must work with its three dimensions: the normal portfolio for the very long-term perspective, the strategic portfolio for the medium-term perspective and the actual portfolio for the short-term perspective (see also page 12).

The next step in the fund manager's process is to decide whether investments should be actively or passively managed. In this respect, AP4's current standard is that management should be passive – that is, with no ambitions to outperform the market average – once the return-critical mix of asset classes has been decided. Up to this point, the Fund's strategy has been to manage essentially all assets actively.

I still believe that large asset managers can outstrip the average. A visit to Norges Bank Investment Management (NBIM, the former Petroleum Fund) in 2007, along with the Fund's Board of Directors, served to strengthen my conviction on this point. But to achieve success, we must have a sound understanding of the areas amenable to active management and carefully thought-out processes for how such mandates should be assessed and followed up.

The third and final step in the fund manager's decision process applies to the choice between internal and external management. Historically speaking, AP4 has had the highest share of internal management of the buffer funds. I am not convinced this has been the right approach. In an increasingly developed and specialised capital market, I believe it is logical to look for the managers that, after expenses, can give the Fund the best return – regardless of whether the resources we utilise are internal or external.

GREATER CLARITY

One interim goal for AP4's ongoing change initiative is to create greater clarity in the organisation, particularly with respect to responsibility. This will build a solid platform for higher quality in management and follow-up.

Changing a knowledge-based enterprise is a process that is both sensitive and time-consuming. But the changes we are facing are neither revolutionary nor innovative. I am convinced that the main keys to success are thorough and sound analysis followed by a consistent and unambiguous implementation process. AP4 has devoted 2007 to analysis and to creating structures. Implementation and follow-up are that which remains ahead.

> My conviction that large asset managers can outstrip the average holds firm.

We can already provide examples of how management is changing at AP4 in this annual report. Perhaps the most obvious is that assets under passive management have increased from 15% at the outset of 2007 to 30% one year later. I do not preclude the possibility that the figure may increase further.

DISAPPOINTMENTS

As I analyse our performance in 2007, three management areas stand out as particularly negative:

The outcome was especially weak in the second half for fixed income management, which has performed well in previous years. As a result, active return from fixed income management for the entire year added up to a negative figure of more than 2 percentage points. The Fund's performance must be seen in light of the turbulence in the fixed income market, a crisis that not only compelled the world's central banks to take extraordinary measures and which led to enormous credit losses, but which also rocked the foundations of large and reputable financial institutions. The Fund's fixed income management was hit hardest by the dramatic increase in credit spreads (the difference between corporate and government lending rates). The level of risk in the Fund's fixed income portfolio was reduced substantially in the latter part of the financial year.

Global equities management was another disappointment. Both the internally and externally managed portfolios underperformed the benchmark indices, but absolute return was positive. Externally managed equity mandates were in large part transferred to passive management in the fourth quarter. Internal management is also undergoing thorough review. Lower risk and a higher component of passive management are the main points in the ongoing action programme.

SWEDISH EQUITIES A BRIGHT SPOT

There were also some bright spots in 2007, which should not be ignored.

Swedish equity management, the Fund's problem child for many years, has been remodelled, including certain staff changes. The results are promising, albeit the evaluation period is thus far brief. Swedish equity management met its active return target despite the troublesome state of the market in 2007.

Private equity is a small but highly interesting asset class for AP4. The outcome in 2007 seems very good, but here as well, patience and endurance are required before any more definite assessments can be made.

Currency management can also claim a good year, along with the Fund's tactical asset allocation operations.

RISK LOWERED

But the bright spots do not change the overall assessment. All told, 2007 was a very tough year for the Fourth National Pension Fund. The organisation's main focus in 2008 will be on active return. As the level of risk in the portfolio was reduced, a logical step after the miscalculation in 2007, the Fund's target for active management was reduced from 0.5 percentage points to 0.4. This is a consequence of the Fund scaling back its assumption of risk and not an expression of lower ambition. In future, the active management target is likely to fluctuate from year to year, since opportunities to generate excess return usually vary from year to year as well.

It is both my hope and my conviction that AP4 will reverse the negative outcome for active management in 2008. I have already described various actions in the ongoing change processes. The crucial points are that structures and responsibilities have been clarified while human resources and other resource issues have been revamped.

DRAMATIC ENVIRONMENT

Understandably, the focus of my letter this year has been on internal matters. But the investment environment has been dramatic, to say the least, and thus must be accorded a few concluding remarks.

The first half of 2007 was largely reminiscent of the trend in recent years. Our investment environment was one in which economies continued growing at a healthy clip, with China leading the way. Listed companies continued reporting above-forecast profits and their performance was reflected in the sustained price upturn in world equity markets. Inflation was held in check, despite surging prices for energy and primary products.

The clouds began gathering on the horizon in late summer. The mortgage lending crisis in the United States triggered the downturn. Although there was no lack of warning signals, the extent was far greater and the ripple effects far more serious than anyone had anticipated.

In hindsight, we now know that yet another bubble has burst. People had been able to borrow money far too easily, at far too low a price, and these practices had gone on for far too long a time. By means of the so-called art of financial engineering, new investment instruments had been created that neither investors, banks nor regulators fully understood and whose ripple effects could not be foreseen and grasped in a global capital market. For these reasons, it has also taken longer to ride out the storm than at first predicted by the experts. As I write this at the cusp of 2007/2008, no one yet knows when the crisis will be overcome and even less how much it is going to cost.

DOWNWARD-ADJUSTED FORECASTS

The assessment of where the world's economies are going currently hangs in the balance. Expectations for 2008 have been successively toned down, especially in the United States. In recent years, we have enjoyed the fruits of synchronised and strong growth in every region of the world. An entirely new economic power in the form of the BRIC countries (Brazil, Russia, India and China) has emerged. The test will now be to see how the world's economies weather the impact of a United States that has entered a phase of slower economic growth in parallel with rising pressure on the global financial system.

Despite all, the longer-term perspective must govern the direction of management at AP4. The Fund's long-term (ten years or more) capacity to deliver returns to the Swedish pension system is dependent on long-term allocations. As I said, how investment assets should be allocated is the most crucial decision an investor must make. The analysis performed by the Fund in 2007 within this area once again indicates that the long-term weight in equities should be higher than the 60% currently in effect at AP4.

TIME TO REVISE THE REGULATIONS

If the equity component in the four buffer funds had been five percentage points higher for the last five years, their combined return would have been about SEK 25 billion higher. Stakeholders often forget that the buffer funds, combined, account for no more than 12–13 per cent of the assets of the income pension system. If the buffer funds' risk mandate is formulated based on an overall perspective, there seems to be virtually no rational argument for the current limitation rule, which stipulates that the funds must have at least 30% of their assets invested in fixed income securities with low credit and liquidity risk.

Against this backdrop, I believe there is reason to review the regulations, now nearly seven years old, governing the AP funds. The hallmark of global financial markets – rapid development – is yet another reason for regularly reviewing and adapting regulations as required.

Mats Andersson
CEO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TURBULENT FINANCIAL MARKETS

The financial markets presented a turbulent and fragmented picture in 2007. The most unexpected and dramatic was the global liquidity crisis in the wake of the US mortgage lending crisis. The credit and liquidity crisis brought not only enormous credit losses, but also helped put an end to the very strong bull run in the developed equity markets of several years' standing.

Overall, global economic growth remained strong in 2007. Extremely favourable development in emerging economies compensated for weaker economic trends in OECD countries, where the growth rate gradually slowed to an estimated 2% by the end of the year. The growth rate within the OECD is now the lowest in five years.

Continued strong momentum in the global economy set the tone for the first half of the year, despite the relatively weak US economic trend. Growth was driven by leading emerging economies, but the economic recovery also continued in Europe and Japan. Corporate earnings reports outperformed expectations and significant price upturns were recorded in world equity markets. Strong global demand triggered successive base rate hikes in Europe and rising short-term and long-term bond rates worldwide.

Market trends reflected a growing appetite for risk based on increasing confidence in the capacity of new economies to compensate for weaker trends in the west. Equity trends were extremely favourable in emerging markets. The Swedish equity market, which has significant exposure to emerging markets via Swedish engineering companies, also benefited during the first half.

THE TURNING POINT

The outlook for the US housing market darkened in the summer. Rising credit losses revealed questionable lending practices in the mortgage lending market. Burgeoning concern about ripple effects triggered rising credit spreads and greater pessimism about the future development of the US economy. Share price upturns reversed into steep declines on world equity markets. A continuation of strong profit trends seemed doubtful and relatively good returns on fixed income investments attracted investors to less risky alternatives.

The scope of the credit crisis grew rapidly. Banks and other financial institutions began reporting heavy losses. Growing uncertainty spread in the financial system with respect to the extent of total losses, as well about where the problem loans actually were. The uncertainty caused a liquidity crisis, investor flight to relatively safe assets such as short-term government bonds and significant difficulties in financing operations for banks and other financial players. (See the article on the next page for a more detailed account.) Credit spreads widened and reached levels last recorded in conjunction with the economic downturn of 2000.

By autumn, the situation had led to repeated interest rate reductions by the Federal Reserve and other actions by central banks designed to increase access to liquidity. Volatility rose significantly in both the bond and equity markets during the period.

FRAGMENTED TREND

Despite the circumstances, equity markets still delivered a positive share-price outcome for the calendar year. Including dividends, world equity markets rose by more than 5% in 2007, slightly outperforming the bond markets. But the spread was remarkably wide. Equities in emerging markets returned an impressive 33% on average, while the Swedish equity market returned -2.6% (including dividends).

Sector trends were also sharply divergent. The growing uncertainty in the credit market combined with poorer earnings outlooks caused financial stocks to drop by about 14% during the year, while the rising oil price and continued profit growth in primary goods companies supported the robust trend in those sectors.

The picture of the 2007 market year changes if share price performance is measured according to the respective highest price paid. At least for the developed equity markets, 2007 is starting to look like a trend-breaker. Six months after the outbreak of the US mortgage lending crisis, it has become clear that the global ripple effects of the crisis have broken the strong and steady price upturn experienced by virtually all equity markets since early 2003.

The currency markets were characterised by the continued anaemic trend for the US dollar. Low growth, the credit crisis and interest rate-slashing in the second half weakened the dollar in trade-weighted terms by more than 7% in 2007. The oil price jumped to about USD 92 a barrel by the end of the year. The increase expressed as a percentage was thus nearly 60% over the full year. But prices fell for a number of base metals, such as lead, zinc, nickel and copper.

OUTLOOK

In the Fund's judgement, the negative impact of the liquidity crisis on growth has created latitude for lower short-term interest rates. Market anomalies of the kind recently experienced customarily represent an opportunity for higher expected returns for long-term asset managers. But this must be considered in light of the extremely high volatility, which generates a risk contribution higher than desirable. Leading indicators for the OECD have declined sharply since summer and now indicate a significant slowdown in the industrial economy over the next six months. Growth forecasts for Japan, Europe and the US have been successively adjusted downward and by the end of 2007, highly reputable forecasters had also begun predicting a recession in the US. The big question right now has to do with development in emerging economies. Can sustained strong trends for domestic demand in these countries compensate for the decline in demand that is likely in western countries in 2008? Market opinion, as reflected in share price performance near the end of 2007, was distinguished by growing pessimism. Thus, it seems that actual economic development in the next few months will determine market trends for the rest of 2008.

CREDIT CRISIS WITH SERIOUS RIPPLE EFFECTS

The world was hit by a significant credit and liquidity crisis in summer 2007, which has since had a dominating impact on the financial markets and the global economy. The crisis brought a shortage of liquidity and significantly higher costs for short-term financing, which had direct impact on the Fund.

UNIQUE LIQUIDITY CRISIS

Sustained appreciation in US housing prices, investors' higher appetite for risk and new financial constructions paved the way for households with poor credit scores to obtain home mortgages. When the US housing market sagged further in summer 2007, payment defaults on high-risk mortgages followed almost immediately. Uncertainty about the credit quality of assets deepened, and when it became increasingly difficult to sell the assets in the market, the holders' losses accelerated. The dearth of knowledge about who was exposed to these losses engendered distrust between financial players, which manifested in greater reluctance to lend liquidity. There is nothing unusual about the market adjusting the price of credit risk after a long period of falling risk premiums. The unexpected and dramatic feature of this crisis is that it initially, and to such a large extent, revolved around the liquidity shortage that ensued upon the drastic decline in willingness to extend credit to other financial institutions.

> **"The liquidity crisis in autumn had severe impact on the Fund's fixed income portfolio.**

Several times during the autumn, access to liquidity was so tight that the market began fearing for the stability of the entire financial system, an event not seen for many decades. One reflection of the surprise and the severity of the crisis is the extraordinarily large injections of liquidity and the sudden reversals in monetary policy implemented by the leading central banks in the autumn.

Although the immediate crisis was triggered by an increasingly widespread price depreciation for US residential real estate, it was based on several interacting factors. Protracted strong economic trends with low base rates and moderate inflation expectations combined with a low loan-to-value ratio and strong corporate and bank earnings caused a market situation in which investors felt comfortable increasing the credit risk. In parallel, demand for credit assets was also driven by a trend in which increasing numbers of investors transferred portions of their capital to credit assets.

During phases of similar strategic reallocation, investors tend to become less sensitive to historical valuations. Historically low interest rates combined with shrinking risk premiums also encouraged investors to seek out even riskier investments. The new structured products were assigned high credit ratings by established credit rating institutions, which probably lulled investors into a false sense of security and thus less stringent valuation of underlying assets. This is one of many areas where the crisis and subsequent crisis management led not only to altered pricing structures, but to new playing rules, stricter procedures and staff changes at the highest levels.

AP4 INDIRECTLY AFFECTED

While not directly exposed to the relevant type of US housing assets, the liquidity crisis in the autumn nonetheless had severe, albeit indirect, impact on the Fund's fixed income portfolio. Even though the Fund was positioned for rising credit risks, the result was entirely overshadowed by the severe impact of the lack of short-term financing for high-quality assets with shorter maturities.

A LONG-TERM APPROACH

AP4 is one of five buffer funds whose purpose is to offset temporary fluctuations between pension contributions and disbursements to and from the public pension system. The overarching mission of the buffer funds is to secure the income pension in the Swedish pension system in the long term, by means of carefully risk-weighted management of investments in equities, fixed income assets and real estate. AP4 currently has more than SEK 200 billion of the Swedish public's pension assets under management.

There are three components to the Swedish pension system: the guarantee pension, the income pension, and the premium pension. The income and premium pension components are part of the public pension system and are financed via pension contributions from people in work, while the guarantee pension is financed via the central government budget.

The income pension is structured as a distribution system, with pensions financed by pension contributions. But paid-in pension contributions do not always match pension distributions, which is why the AP funds were allocated buffer capital to offset temporary fluctuations between contributions and disbursements. Payment flows in the system are forecast with reference to demographic factors such as average lifespan, age of retirement and the employment rate. At present, buffer fund capital accounts for between 12 and 13 percent of the total pension commitment.

Premium pension disbursements are directly connected to the individual's personally allocated funds, which accrue from the premium pension contribution. Premium pension assets are managed by private fund managers and the Seventh National Pension Fund. Please refer to AP7 and the Premium Pension Authority for further information.

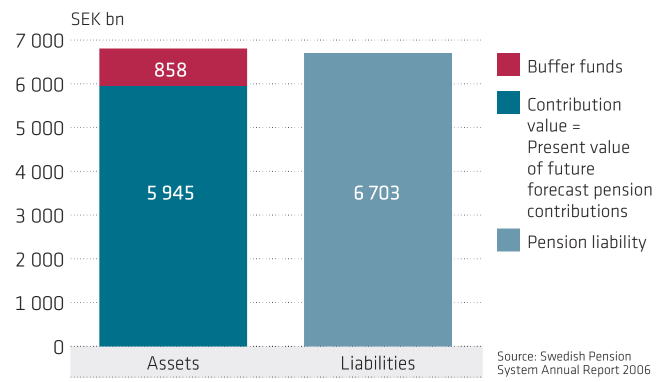
A FINANCIALLY STABLE SYSTEM

To ensure the financial stability of the income pension system, disbursed pensions are adjusted through a balancing procedure, if assets fall below liabilities. The greatest threat to the value of pensions in the next 20–30 years is that the labour force activity rate may decline, while the greatest long-term risk will arise upon unfavourable demographic trends expressed as a low birth rate or low net immigration. There are additional risks in the form of low returns on the buffer funds and low economic growth.

FIVE BUFFER FUNDS SPREAD THE RISKS

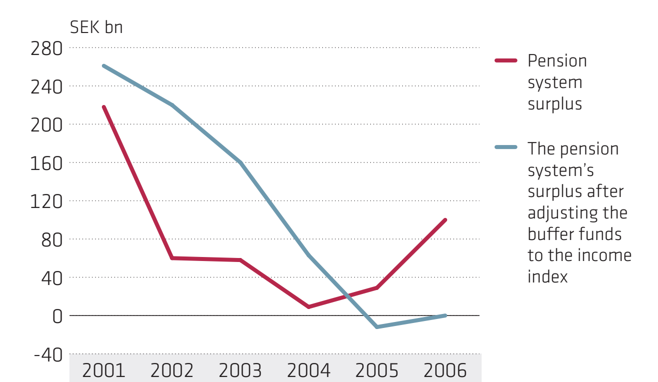
Buffer fund operations are governed by the Swedish National Pension Funds Act. Under the law, the funds shall "manage fund assets to generate maximum utility to the insurance scheme for earnings-related pensions" and "the overall risk level in fund investments shall be low." The Riksdag has further reduced the risk in managing income pension assets by dividing the management mandate among five funds. Each fund is mandated to act independently and, based on the investment rules, determine the allocation of assets for the long, medium and short terms.

PENSION SYSTEM BALANCE SHEET DEC 2006



The National Pension Funds have vast assets under management, but seen in their context – as buffers in the Swedish pension system – the Funds account for only 12–13% of total pension liability.

THE BUFFER FUNDS SAVED SWEDISH PENSIONS



The severe market downturn in the early 2000s meant heavy going for the new buffer funds. But the strategies to maintain a high weight in equities were adopted, which "saved" Swedish pensions over the last year or two.

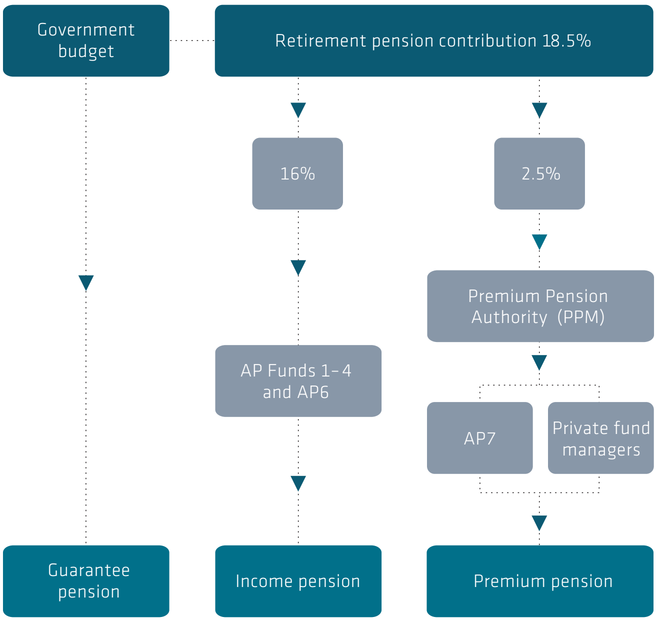
HIGH RETURNS AND LOW RISK

The overriding objective of AP1–AP4 is to generate the best, risk-adjusted long-term returns in relation to the funds' mandate. The Funds are barred from taking national business or other economic policies into account. Environmental and ethical considerations must be taken into account without compromising the objective of high returns.

The overriding objective of AP1–AP4 is to manage fund capital so that it provides maximum benefit to the national pension system. AP6 has a specialised mandate to invest a minor portion of the pension system's funded capital in the private equity market.

The fundamental principle of the income pension system, which includes AP1–AP4 and AP6, is that current pension disbursements are financed by guarantee pension contributions in the same year from people in work, at a rate of 16% of salary. The income pension system's most important asset consists of projected future contributions. The assets of the buffer funds correspond to 12-13% of total pension liability.

Pension disbursements in the premium-funded system are based on the individual's personally allocated funds, which accrue from the premium pension contribution (2.5% of salary). The premium reserve is managed by private fund managers and AP7.



There are three components to the Swedish pension system:
- Guarantee pension
- Income pension
- Premium pension

INVESTMENT RULES

The investment rules for AP1–AP4 are relatively flexible and permit investments in various asset classes. Each fund is mandated to act independently and, based on the investment rules, determine the allocation of assets for the long, medium and short terms. Management is governed by certain restrictions.

The Riksdag (the Swedish parliament), drew up new investment rules for AP1–AP4 in conjunction with the reorganisation of the funds. The rules came into effect on 1 January 2001 and are identical for each of the four funds.

The investment rules allow the funds to invest in most asset classes other than commodities. The restrictions are as follows:

- The funds may invest in all listed and liquid securities traded in the capital market.
- At least 30% of fund assets must be invested in fixed income securities with low credit and liquidity risk.
- A maximum of 40% of fund assets may be exposed to currency risk.
- A maximum of 10% of fund assets may be exposed to a single issuer or group of issuers with mutual links.
- Equities held in listed Swedish companies may not exceed 2% of total market capitalisation.
- The fund may own shares corresponding to no more than 10% of voting rights in any single listed company.
- No more than 5% of fund assets may be invested in unlisted securities. Such investments must be made indirectly via venture capital firms or the equivalent.
- At least 10% of fund assets must be managed by external asset managers.

SHARPER FOCUS ON STRATEGIC ALLOCATION AND PASSIVE MANAGEMENT

Since the inception of the Fund, AP4 has had distinct focus on tactical and active management. The strategy has not delivered the expected return and the Fund has not achieved positive active return. A change initiative was intensified in 2007 with a view to developing a management model with sharper focus on strategic allocation and a decreased component of active management.

THREE-STEP MANAGEMENT DECISION PROCESS

The Fund's management is determined in a three-step decision process where allocation – the mix of assets and markets – is the most crucial decision and has the greatest impact on the Fund's total return. In the Fund's assessment, this decision determines 80 to 90% of the expected return.

Active or passive management

The second step in the management process, once the strategic portfolio has been implemented, is the Fund's choice between active or passive management alternatives. To the extent the Fund deems that conditions exist for enhancing returns by means of active management within a particular asset class or market, active management may be selected. This assessment is made on grounds including analysis of institutional conditions (including political and legal risks) in various asset markets and of how well various fund managers have succeeded in generating good active returns from a longer-term perspective.

The Fund has historically prioritised active management, but decided in 2007 to increase the share of passive management mandates, which should also be the standard unless the Fund has objective reason for instituting active management.

Internal or external management

The strategic portfolio is implemented in step three through internal or external management mandates. The choice between internal and external mandates is always determined by the expected return after expenses.

The Fund must regularly evaluate both internal and external alternatives, but from the short-term perspective, the Fund will be increasing the share of external management mandates.

THE AP4 ALLOCATION FUNCTION

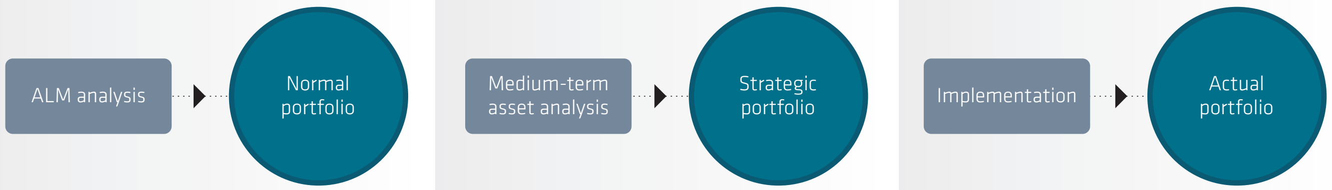
The Fund's allocation function is tasked with using ALM (Asset Liability Modelling) and medium-term asset analysis to identify the level of risk that the Fund should permit for long-term and medium-term asset management. The chosen level of risk is expressed in the Fund's normal portfolio and in the strategic portfolio.

The strategic allocation and analysis function is in the build-up phase. Key clarifications have been made during the year in respect to responsibility for analysis and the role of the strategic portfolio in Fund management. Additional resources have also been allocated to strategic analysis to ensure that the portfolio proposed to the Fund's board of directors is optimal in relation to the Fund's expectations.

Long-term asset allocations

Long-term asset allocations are described by the normal portfolio, which shows how the Fund should allocate its capital among the general asset classes. It is based on analysis of the public pension system and the asset classes, with the objective of identifying the assets that will give current and future Swedish pensioners the highest pensions possible, while observing the goal of limiting the

THE FOURTH NATIONAL PENSION FUND ALLOCATION FUNCTION

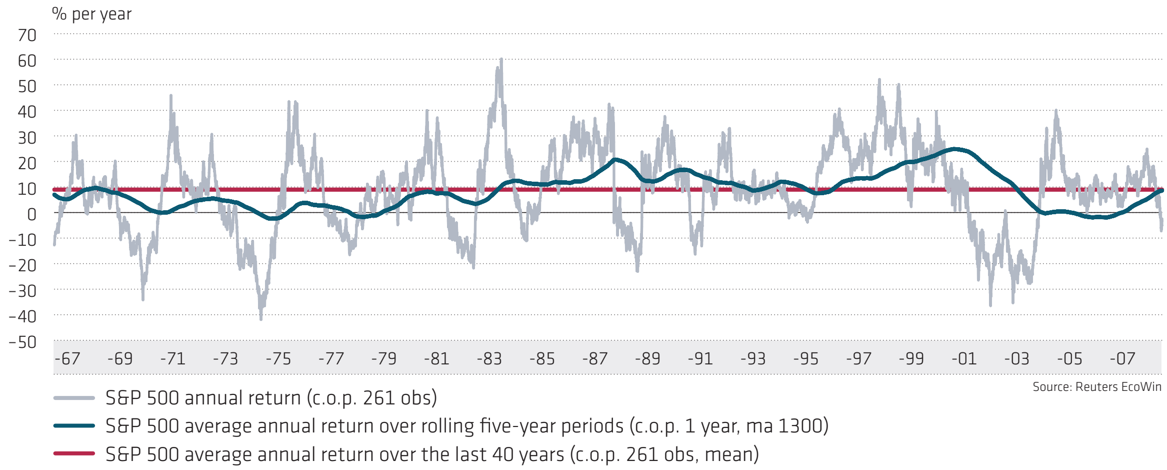


The normal portfolio is adopted by the board of directors once a year.

The strategic portfolio is revised on an ongoing basis and adopted by the board.

Executive management is responsible for asset management, including decisions on active versus passive and internal versus external management.

US EQUITY MARKET RETURNS OVER THREE INVESTMENT HORIZONS



A retrospective look at the US equity market may be used to illustrate the Fund's approach to the three investment horizons. The graph above shows how average return on the US equity market has varied depending on the investor's investment horizon. The truly long-term investor (red curve) has achieved an average annual return of 8.7% over the last 40 years, while the short-term investor's returns have depended entirely on when the investment was made and how long it was maintained.

The most relevant aspect to the long-term investor with an investment horizon of 40 years is expected average return across the entire period. From this perspective, variations in return during the investment period lack significant import. When performing the ALM study, AP4 uses expected average returns for various assets over the next 40 years. The Fund's asset mix of the normal portfolio expresses the outcome of the study.

The picture changes dramatically from the medium-term perspective. The dark blue curve illustrates average return from a rolling five-year perspective and shows that during certain periods, returns on equities fell below the average of 8.7% for investors who entered the market at the wrong time. The purpose of strategic analysis and the strategic portfolio is to enhance returns by factoring in the deviations in expected return that can arise during five-year periods.

Short-term – up to five years – there are opportunities to add value by taking advantage of short-term movements in the markets.

risk of pension cutbacks or weak trends in purchasing power for pensioners.

The normal portfolio – which is structured using ALM and based on assumed average return and risk over the next 40 years – is defined in terms of broad asset classes, duration and the currency basket. The structure of the normal portfolio is significant to the Fund's choice of risk level and thus long-term return.

The ALM analysis is refined and updated annually. The normal portfolio is adopted by the board of directors.

Medium-term asset allocation

Assets are also analysed based on an investment horizon of three to five years. This analysis covers more asset classes and more geographical markets than the long-term analysis and provides a basis for deciding which strategic portfolio the Fund should be invested in during the next five-year period.

The analysis from the 40-year perspective must be supplemented with a medium-term analysis because returns on assets vary considerably over time. With a five-year investment horizon, the Fund can take advantage of investment opportunities that arise when asset valuations appear unreasonably high or low in relation to the long-term average levels applied in the ALM analysis.

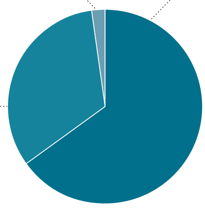
The strategic portfolio must contain asset classes and markets in the proportion that will in the Fund's judgment generate optimal return over the next five years at reasonable risk. It also serves as the reference portfolio for active management at AP4. Indices are assessed and selected in conjunction with strategic portfolio analysis.

The analysis is an ongoing process. The strategic portfolio mix is also adopted by the board of directors.

Implementation

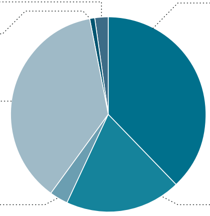
In purely practical terms, the strategic portfolio is implemented by the management organisation. The decision on whether investment mandates will be managed actively or passively and internally or externally is taken in this step. The Fund's longstanding strategy has included significant elements of active management, with external

NORMAL PORTFOLIO, 31 DEC 2007



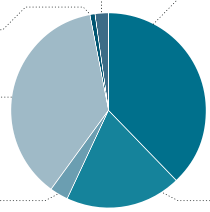
The Fourth National Pension Fund applies a 40-year investment perspective to the normal portfolio. With a horizon of this duration, the equity component of the portfolio becomes very high.

STRATEGIC PORTFOLIO, 31 DEC 2007



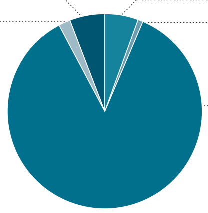
A medium-term (3–5 years) perspective is applied to the Fund's strategic portfolio. As a result, additional asset classes and several markets are considered in the Fund's allocation process.

ACTUAL PORTFOLIO, 31 DEC 2007



Unusually, the Fund's actual portfolio was identical to the strategic portfolio at year-end 2007.

CURRENCY EXPOSURE IN THE ACTUAL PORTFOLIO



There was a marginal drop in currency exposure during 2007 from 15.1 to 14.2%.

management serving mainly as a complement to internal management. AP4 has reconsidered that strategy. The standard approach in future will be oriented towards passive management. Active management alternatives will be considered only if conditions are assessed as highly favourable. In the choice between internal and external management, an objective comparison will be made between the expected returns after expenses for the two options.

At present, internal management is divided among seven areas of responsibility: fixed income, global equities, Swedish equities, private equity, tactical asset allocation, currency management and external management. The tasks of the internal organisation include managing some of the mandates to be managed actively within certain selected areas, aimed at achieving return targets that exceed strategic portfolio return.

AP4'S CURRENT PORTFOLIO

The three time perspectives applied to Fund management are represented by AP4's three portfolios: the normal portfolio, the strategic portfolio and the actual portfolio. The first two are model portfolios, while the third represents the Fund's current assets.

Normal portfolio

A general conclusion of the ALM analysis is that with the very long investment horizon and with pension commitments that entail few restrictions on the Fund's investment opportunities, the Fund has the latitude to assume relatively high risk when the expected return is assessed as favourable. A premium is put on riskier assets in the model because they are expected to deliver higher returns in the long term. Thus, one conclusion of the ALM analysis is that the equity component of the normal portfolio should be high. In respect to fixed income assets, the ALM study findings are that the Fund's normal portfolio should have a low weight in government bonds and a high weight in investment grade corporate bonds. The Fund's fixed income portfolio should also be of long duration.

The Fund's long-term currency exposure is designed to offset the effects of exchange rate fluctuations on inflation and thus on the debit side of the public pension system. In the Fund's judgement, this will be achieved if total currency exposure is 20% and the currency basket corresponds to the currency mix of imports to Sweden.

Strategic portfolio

The strategic portfolio is structured using various portfolio selection models, which are based on the Fund's internal risk and return forecasts for the next five years.

The strategic portfolio differs from the normal portfolio on a number of points. At present, the Fund has a lower equity

ACTIVE RETURN TARGETS AND RISK MANDATES AS OF JANUARY 2008

	Weight, %	Benchmark and reference index	Excess return target per year, % points	Active risk guide-line, %
Global equities, developed markets	39	MSCI World Gross [1)]	0.4	4.4
Global equities, emerging markets	3	MSCI Emerging Markets Net [1)]	–	–
Swedish equity portfolio	19	SIX Return Index	0.6	6.0
Fixed income portfolio	37	Handelsbanken Markets Obl.Index/ Merrill Lynch GBI (SEK) [1)]	0.3	2.0
Active currency management	–		0.1	0.5
Active tactical asset allocation	–		0.1	0.6
Real estate	2	Return on holding in AP Fastigheter Holding AB	–	–
Investment assets	**100**	**Index weighted as per strategic portfolio**	**0.4**	**4.0**

[1)] = *Hedged in SEK*

component. The Fund has also excluded Japanese bonds and British long-term bonds because these investments are expected to deliver low returns for the next five years. Strategic currency exposure is lower than the corresponding exposure in the normal portfolio, which reflects expectations that the Swedish krona is set to appreciate. From the strategic perspective, the currency basket entails an overweight in yen against the euro and GBP, based on forecasts that the Japanese currency is going to strengthen.

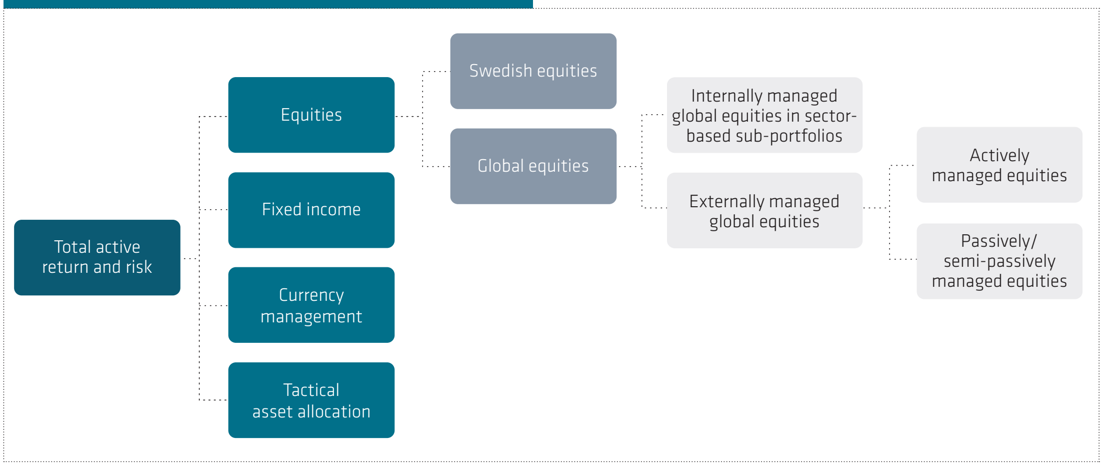
Actual portfolio

The main difference between the actual portfolio and the strategic portfolio is that the actual portfolio has a lower equity component to provide scope for actual allocations among asset classes. The bond component is also lower.

At present, 70% of the Fund's assets are managed actively and 30% are managed passively or semi-passively. With the exception of active tactical asset allocation and active currency management, the bulk of AP4's active asset management operations are index-tracking, meaning risk and return targets are set, measured and assessed against a benchmark index.

The Fund has elected to reduce active risk in management in 2008 because active risk assumption has generally not met expectations for return. The table above shows the current distribution of expected return contributions and active risk.

RETURN AND ACTIVE RISK BY PORTFOLIO



Schematic distribution of return contributions and active risk among sub-portfolios.

ACTIVE SHAREHOLDER RESPONSIBILITY

With their very broad equity portfolios, financial institutions must prioritise in order to gain shareholder influence. AP4 believes that sound companies are created and developed by people, not codes. For that reason, the Fund invests considerable resources towards ensuring that Swedish listed companies have the best possible boards of directors.

Business ownership and power has been a central theme in economic policy debate for more than a century. At first, the discussion revolved mainly around the entrepreneurs, but focus later shifted to the stock market and big business. Gradually – in pace with economic growth, political changes, deregulation and globalisation – new owners, such as financial institutions, have gained increasing influence.

These days, traditional entrepreneurs are respected in most social systems. The general opinion today is that hardworking entrepreneurs are a tremendous boon to employment and social welfare. Other forms of ownership are routine targets of other criticism – they are too faceless, too passive, too inefficient, too short-sighted, too greedy, and so on.

COMPLEMENTING OLDER FORMS OF OWNERSHIP

The most intriguing aspect of modern ownership is the dynamic. When deregulation and globalisation have revealed the shortcomings in established forms of ownership, the market has generally developed new ownership roles – primarily as a complement to the older forms, not a substitute – aimed at facilitating more rapid company development. One distinct example of this in recent decades is the emergence of private equity where shareholder involvement is both active and temporary.

The shareholder's role has thus undergone major changes and become considerably more multi-faceted in the last quarter-century. Various shareholder categories define and exercise their ownership functions in many different ways, depending on things like their purpose, mandate, investment horizon, capital strength, expertise and commitment.

In ownership contexts, AP4 is considered a financial institution, a growing group that began to recognise and accept shareholder responsibility 15 or 20 years ago. The 15 largest financial institutions in Sweden now account for more than 20% of the capital invested in the OMX Nordic Exchange, Stockholm.

LIMITED OWNERSHIP ROLE

The law prohibits the buffer funds from acting as an instrument of national business or economic policy. But, through their ownership role and without setting aside the return objective, the buffer funds should be able to promote the public interest by encouraging compliance with environmental and ethical standards adopted in the investment policy.

" AP4 was represented on 28 nominating committees in 2007.

The law stipulates that return is the overriding objective, but other restrictive regulations show in parallel that an AP fund - regardless of its vast capital – must exercise its ownership role in a different, more indirect way than an entrepreneur, a principal shareholder, or an investment firm. The bare fact that an AP fund is prohibited by law from owning more than 10% of voting rights in a listed company demonstrates the legislative intention to limit the ownership power of the funds. If financial institutions, with their very broad equity portfolios, are going to gain noticeable shareholder influence, they must either prioritise and/or work together. The priorities of Swedish institutions differ rather widely in this respect. Some emphasise general questions and others company-specific issues; some try to exercise the ownership role via the media and others work mainly in the background, etc.

FOCUS ON BOARD ELECTIONS

AP4's first priority in respect to corporate governance remains the Swedish equity portfolio, although the Ethical Council has resulted in sharper attention to governance in relation to the global equity portfolio than in the past (see separate article on the next page). While the Swedish equity portfolio accounts for only about 20% of the Fund's assets, it nonetheless gives AP4 an adequate platform for actively influencing the most critical ownership decision faced by a listed company – electing the board of directors. Accordingly, in the course of exercising its ownership role, AP4 invests considerable resources towards making sure Swedish listed companies have the best possible boards of directors.

From the shareholder perspective, the financial year may be summarised as follows: The Fund was a member of 28 nomination committees in 2007 and acted as chairman in five cases. AP4 thus had a significantly higher number of nominating committee mandates than all other buffer funds combined. The nominating committee's most important task is to nominate directors for the new board and present them to the annual general meeting for consideration.

As discussed in previous annual reports, nominating processes often vary widely as the companies' situations differ in key respects. Sometimes a great many meetings are required, interspersed with interviews of former and potential directors. In other cases, one or two meetings may suffice in a well-managed company with an efficient board and a principal shareholder with a distinct and long-term approach.

One tendency seen in nominating committees in 2007 was that board service in private equity companies seems more appealing than serving on the boards of listed companies. AP4 has attempted to factor in this risk in the revised governance policy adopted by the Fund's board of directors in October 2007. It stipulates that board remuneration may include both a fixed component and an incentive-based component. But the Fund's revised governance policy specifies that such departures from the tradition of fixed remuneration only in Swedish listed companies must be justified prior to any resolution by the AGM.

ACTIVE AGM PARTICIPANTS

Attending and exercising voting rights at the AGMs of companies in which the Fund enjoys significant influence is and will remain a key aspect of AP4's ownership role. The Fund was represented at 51 annual general meetings in 2007. To ensure that AGMs are not dominated by the formal requirements of the Swedish Code of Corporate Governance or detailed questions about complex incentive schemes, the Fund maintained its active approach during the financial year, primarily by allowing its AGM representatives to ask the CEO specific questions about operations.

JOINT SHAREHOLDER INITIATIVES

In recent years, "joint shareholder initiatives" has become an expected sub-heading in the annual reports of Swedish financial institutions, and 2007 is no exception. We present two cases that illustrate the value of institutional cooperation:

The first case has to do with more stringent merger regulations, which was also discussed in the Fund's 2006 annual report. In late 2006, the largest financial institutions in Sweden jointly wrote a scathing dissent to a proposal that would allow more than 10% of outstanding shares to be acquired through forced sale in a takeover. The reason for the financial institutions' mobilisation was that the proposal could sharply reduce the bid premium in company acquisitions.

The action persuaded the Ministry of Finance to withdraw the proposal. Instead, a temporary suspension was incorporated into the law, requiring the consent of at least 90% of the shareholders to a merger. This suspension rule, which went into force at 30 June 2007, was an important partial victory for the institutions. The next partial victory came in the autumn, when a new report was presented and showed that the opinions of bidding interests had not garnered support in an international study. The Government is expected to present a bill on this issue to the Riksdag in spring 2008.

REVISED GOVERNANCE POLICY

AP4 carried out in 2007 its first comprehensive revision of the governance policy since the Code was implemented. A few of the new points are:

- The Fund is amenable to allowing an incentive-based component to board remuneration in Swedish listed companies.
- The Fund declares that there should be no premium for voting shares in connection with takeover bids.
- Directors should be shareholders in the company, as the purpose is to create a common interest between the board and shareholders.

The complete governance policy is available online at www.ap4.se.

The other case from 2007 involving a joint institutional shareholder initiative has to do with takeover regulations and equal treatment of shareholders.

The background was the 2007 bid for Invik by Iceland-dominated Racon Holdings. Racon offered a lower price for class B shares than it had recently paid for the class A shares and the voting rights attached to them. Invik's largest institutional shareholders, Alecta, AP4, Nordea fonder and Swedbank Robur, believed this was a violation of generally accepted practices. The institutions lobbied the buyers, the sellers, advisers and other stakeholders and expressed their objections, but to no avail, and the bid was successful. The institutions accepted under protest, since they did not want to risk ending up in the minority in an unlisted company.

AP4 and a large cadre of Swedish institutions thus lost the immediate battle, but decided to work further on the issue of equal treatment of class A and B shares in connection with takeover bids. The first interim goal in the process was to garner support for institutional opinions in the international capital investment community, which succeeded in remarkably short order. As a result, a carefully considered letter could be submitted to the Swedish Industry and Commerce Stock Exchange Committee (NBK) and OMX, which petitioned for the clarification/amendment of takeover regulations so that the same price would apply to class A and B shares in connection with takeover bids. Twelve Swedish and twelve foreign financial institutions signed the letter, including the American CalPERS, English Hermes, German DWS Investments and the Norwegian NBIM (formerly the Petroleum Fund) – in other words, some of the largest capital investors in the world.

The first reaction to the letter among the traditional special interest groups within NBK was negative, in part because the institutional petition had been misinterpreted as a criticism of the entire Swedish corporate governance system of differentiated voting rights. Even after the institutions made it clear that the demand for amendment/clarification of the rules applied only to pricing in connection with takeover bids, the conflict of interests probably remains. NBK, as a self-regulation body, thus has a thorny issue to resolve in 2008. For the first time, the international capital investment community has joined Swedish financial institutions in a joint initiative to bring about change.

SOCIAL AND ENVIRONMENTAL EFFORTS CREATE HIGHER SHAREHOLDER VALUE

The Fund believes that companies which practice social and environmental responsibility enhance shareholder value. Accordingly, AP4 integrates CSR and environmental analysis in ongoing management operations and has joined global initiatives such as Principles for Reasonable Investment and the Carbon Disclosure Project.

The Fund believes that companies which practice social and environmental responsibility enhance shareholder value. An internal discussion of social and environmental responsibility was begun in 2006 to create a more proactive process aimed at becoming a more responsible investor while contributing to improving returns on investments.

The Fund's first step was to join two important global initiatives: Principles for Reasonable Investment (PRI) and the Carbon Disclosure Project (CDP). For the third consecutive year, the Fund is also supporting Amnesty Business Group's rating of Swedish companies in relation to human rights.

The next step was to begin the process of refining social and environmental responsibility analysis in internal management. The objective is to become still better at identifying companies that create or destroy value through their actions in the areas of social and environmental responsibility. A further objective is to highlight these areas in meetings with companies aimed at improving the Fund's knowledge, but also to emphasise the importance of corporate social responsibility.

AP1–AP4 formed a joint Ethical Council in 2006 to more proactively promote social and environmental responsibility in asset management. The Ethical Council is accomplishing this by more forcefully and cost-effectively pursuing issues of social and environmental responsibility in connection with foreign investments. For instance, the Ethical Council commissioned a systematic review of the equity portfolios of the four buffer funds to identify companies that may be violating international conventions. The results were promising. The Ethical Council has made AP1–AP4 more influential players with greater opportunities to influence companies to take greater social and environmental responsibility.

Efforts were intensive in 2007. The Ethical Council held eight meetings, at which representatives of the AP funds discussed the companies flagged as being of concern in the screening process. The Council contacted about 15 companies in response to the screening. Further information about the work of the Ethical Council will be provided in its annual report, which will be published in spring 2008 on the Fund's website, www.ap4.se.

ethical council

A COLLABORATION BETWEEN FIRST–FOURTH AP-FUND

DETAILS

The Ethical Council – A joint initiative of the First through Fourth Swedish National Pension Funds. The four funds had total assets under management worth approximately SEK 850 billion. Each fund has a representative on the Ethics Council. The purpose is the joint pursuit of positive change in foreign companies linked to violations of international conventions for environmental protection and human rights, including the ILO Core Conventions and the UN Declaration on Human Rights.

Global Compact – A voluntary initiative aimed at enlightening businesses and stimulating them to take active responsibility for ten universally accepted principles in the areas of human rights, labour, the environment and corruption.

PRI – Principles for Responsible Investments. The institutional investors' equivalent to the Global Compact. Introduced in 2006 at the initiative of Kofi Annan, former Secretary-General of the United Nations. PRI has adopted six principles for how institutional investors should act with respect to human rights, labour, the environment and corruption. PRI signatories represent investments of more than USD 1,000 billion.

CDP – Carbon Disclosure Project. A partnership among a large number of investors worldwide aimed at facilitating a dialogue with leading corporations in respect of their impact on the climate and their opportunities to act to reduce the risk of climate change.

ABG – Amnesty Business Group. Part of the Swedish section of Amnesty International. A member organisation whose vision is that no human rights will be violated anywhere in the world due to the ignorance of Swedish companies or unwillingness to comply with internationally established principles of human rights.

CSR – Corporate Social Responsibility. Voluntary corporate involvement in social development through focus on assuming responsibility in areas ranging from environmental protection to human rights.

THE ETHICAL COUNCIL IN CHINA

The Ethical Council's trip to China to learn more about the views of Chinese companies on social responsibility gave representatives of AP1-AP4 a fascinating first look at business practices in the country. The visit also sent a clear signal that there are foreign investors who consider it a matter of urgency that China resolves its environmental problems and improves working conditions in the manufacturing sector.

Rapid economic development in China is creating widening gaps between the rich and the poor and between urban and rural regions. In parallel, the Chinese government is intent on preserving China as a "planned economy", rather than a market economy.

FOREIGN INVESTORS A NEW ELEMENT

Focus in recent years has been on China's widely criticised environmental problems and working conditions in the manufacturing sector. Greater attention is being paid to these issues as consumers and investors strengthen their commitment to Corporate Social Responsibility (CSR).

Only one of the dozens of companies the Ethical Council met with in China had been visited by foreign investors who addressed the issue of corporate social responsibility. The Chinese companies we visited know that foreign business partners are putting stronger emphasis on CSR, but it was news to them that financial investors, such as the Swedish buffer funds, are also prioritising these issues.

> **There are foreign investors who are willing to assume their responsibility.**

SEVERE ENVIRONMENTAL PROBLEMS

Environmental problems made the greatest impression on the Ethical Council when it visited China. After having discussed the environmental threats on-site with companies, economists, journalists and voluntary organisations like Greenpeace, the Council concluded that various Chinese stakeholders are keenly aware of the seriousness of the situation.

Several measures have been taken and more are being planned to reduce emissions to air and water and cut energy consumption. But the actions taken thus far are inadequate. The smog choking the cities and causing respiratory problems is palpable evidence that much remains to be done.

WORKING CONDITIONS VARY WIDELY

After the Council visited several factories in various sectors, it was obvious that working conditions vary widely. There were state-of-the-art factories boasting the latest technology cheek-by-jowl with primitive factories still living in a primitive age.

However, the good examples are clear indications that it is possible to manufacture goods responsibly and sustainably while remaining a competitive supplier to foreign customers.

NEED FOR FOREIGN PRESSURE

One representative of a Swedish company doing business in China insisted that "all Chinese companies can have a good manufacturing environment." Another said "there is no excuse for poor working conditions." These remarks engender hope.

After the visit to China, the motivationto work within the framework of the Ethical Council to promote better environmental and working conditions is even greater. Obviously, foreign investors and business partners are playing vital roles in hastening China's development in these areas.

LEADERSHIP WITH DISTINCT VALUES

AP4 is a knowledge organisation. The Fund's opportunities to fulfil its mandate are highly dependent on its capacity to attract, develop and retain skilled employees. In order to implement adopted strategies and attain our objectives, we must also have strong leadership, with sound and clearly communicated objectives.

In a world where the winds of change are blowing ever harder, demands on AP4 and its employees are also increasing. Competition for key employees is increasing even as it becomes more crucial to ensure that a knowledge organisation like AP4 is capable of attracting, keeping and developing skilled employees. Things like leadership, organisational culture, the working climate and employee skills development are key factors in attaining that objective. Aimed at ensuring effectiveness in this area, the Fund has a number of employee-related processes in progress throughout the year. The most important links in the chain are described below:

CHANGE INITIATIVE

The Fund implemented a number of change processes in 2007 as part of a "LOTS" project. The main objective is to improve conditions for meeting the Fund's targets for absolute and active return. The change initiative has entailed a comprehensive examination of operations, whose results included:

- A revised management strategy with more distinct focus on allocation decisions and passive/external management
- Review and clarification of responsibility for current management mandates
- Implementation of a new performance assessment system
- Outsourcing of IT operations and support

Strong emphasis was also put on improving internal information while the change initiative is in progress so that employees are encouraged to participate actively. The employees clearly understand and accept how and why the various aspects of operations must be further developed so that the Fund can achieve its return targets.

LEADERSHIP

Managers at AP4 are responsible for ensuring that their employees clearly understand the organisation's strategies and goals – and how everyone must contribute to implementing and attaining them.

In order to enhance existing leadership and ensure the development of future leaders, the Fund is investing in management training. Fund executives began external management training in 2007.

SKILLS

AP4 is a typical knowledge organisation. A high percentage of employees are university-educated, most of them within finance and financial accounting.

The Fund provides its employees comprehensive opportunities for developing their skills, through both internal knowledge transfer and relevant external training.

WORKING CLIMATE

AP4 considers employee surveys and the subsequent feedback processes the essential ingredients for enhancing the quality of leadership and increasing employee commitment. The organisation carried out the annual employee survey in October 2007.

The results of the employee survey were used as a basis for continued efforts to improve in the context of special group exercises as well as within the framework of the annual, individual performance dialogues.

GENDER EQUALITY AND ETHNIC DIVERSITY

The Fund supports gender equality and diversity and endeavours to maintain a carefully balanced mix of employees with respect to gender, sexual orientation and ethnic background. At 31 December, 17 of the Fund's 45 employees were women.

HEALTH

AP4 encourages wellness activities to promote personal well-being and minimise sickness absence. For that reason, our employees are offered subsidised wellness activities. The Fund has a low sickness absence rate and absenteeism is not generally considered a problem.

THE FOURTH NATIONAL PENSION FUND'S VALUES

CORE VALUES

Operations must be founded on clearly communicated core values in order to build a strong organisation. The words themselves are not the important thing, living by them is. AP4's core values are:

Respect

- We demonstrate compassion, empathy and respect towards each other
- We demonstrate understanding for each other's tasks and responsibilities

Openness

- We are all free to express our opinions
- We listen to each other

Professionalism

- The best interests of Swedish pensioners are our foremost concern
- We always do our utmost
- We have the courage to err and we accept our own and others' mistakes

Cooperativeness

- We act as a team, helping and supporting one another

REPORT OF THE BOARD OF DIRECTORS

The Board of Directors and CEO of the Fourth Swedish National Pension Fund (AP4) present herewith the annual report for the financial year beginning 1 January 2007 and ending 31 December 2007, the Fund's 34th year of operation and the seventh since the reorganisation of the Swedish pension system. Accounting and valuation principles are described in a separate section.

FUND CAPITAL PERFORMANCE

Total return and fund capital

AP4 generated a total return after expenses of 2.4% (10.4) in 2007, corresponding to a net profit of SEK 4.8 billion (18.8). This modest return from the historical perspective is primarily attributable to the weak performance of the equity and fixed income markets in which the fund invests. After a strong first half, share prices fell in developed equity markets around the world, including the Swedish market, and returns on the Fund's benchmark indices for the full year were 4.1% for global equities and –2.6% for Swedish equities. Performance growth occurred in the fixed income markets between the first and second half, but return still did not exceed a modest 3.4% (0.6) for 2007. In addition to the weak market trend, the negative active return before management expenses of –1.0 (–0.6) percentage points was contributed to the Fund's low return.

CHANGE IN FUND CAPITAL

SEK bn	2007	2006
Fund capital at 1 January	200.5	180.1
Net payments from the national pension system	1.0	1.6
Transfers from special management funds	1.0	0.1
Net profit for the year	4.8	18.8
Fund capital at 31 December	**207.3**	**200.5**

AP4's objective is to generate a minimum annual average real total return (inflation-adjusted) of 4.5% over five years. The Fund has delivered average real return of 9.7% after expenses for the last five-year period, 2003–2007, and thus outperformed the target by a healthy margin despite the low return of the latest financial year.

Fund capital at year-end totalled SEK 207.3 billion (200.5). Fund capital increased during the year by SEK 6.8 billion (20.4). Net profit for the year provided SEK 4.8 billion (18.8) of the increase, net payments from the pension system accounted for SEK 1.0 billion (1.6) and transfers from the special asset management funds provided SEK 1.0 billion (0.1).

Income and expenses in 2007

Operating income consisted of net interest income, dividends received, net income per asset class and net commission expenses amounting to SEK 4.9 billion total (18.9). The sharpest decline compared to 2006 was in the net result from listed shares and investments, which was SEK –0.1 billion (19.0).

Operating expenses were SEK 139 million (133). Personnel costs of SEK 87 million (86) included SEK 4 million (3) arising from reductions in the workforce. Other administrative expenses amounted to SEK 52 million (47). The increase is attributable to information and IT expenses.

Excluding commission expenses, the percentage of costs attributable to management (operating expenses in relation to

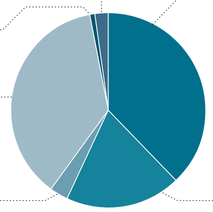
ABSOLUTE RETURN 2007

The sustained strong market trend in the first half of 2007 contributed not only to robust absolute return ...

ACTIVE RETURN 2007

... but also to positive active return for AP4. Turbulence in the financial markets during the second half triggered a steep decline in both yield curves.

ACTUAL PORTFOLIO, 31 DEC 2007



total average fund capital) was 0.07% (0.07). Including commission expenses, the figure was 0.10% (0.11).

Portfolio structure

The market value of the Fund's investment assets was SEK 207.4 billion (200.6) at 31 December. The Fund's assets were allocated as follows in 2007, with underlying values for derivatives in tactical asset allocation distributed per asset class: global listed equities, 41.2% (41.8), which includes equities from emerging markets at 3.0 percentage points (0.0); Swedish equities, 18.7% (19.7); fixed income assets 36.9% (36.3); cash, unrealised losses/gains from hedging, etc., –0.2% (–0.7); real estate 2.4% (2.3); and private equity, 1.0% (0.6).

Return and risk

AP4 generated total return before expenses of 2.5% (10.5) in 2007. Of the sub-portfolios, the Swedish listed equity portfolio posted a negative return of –1.6% (25.8), the global listed equity portfolio returned 2.1% (13.6) and fixed income returned 1.3% (0.6), in all cases with foreign assets fully hedged. Equities from emerging markets delivered strong returns, but the Fund did not have any significant weight of investment assets in this asset class until the last quarter of the year.

The Fund's active return (return against the benchmark index) was very weak, at –1.0 (–0.6) percentage points. Active return for listed global equities was –2.0 (–0.2) percentage points and for

RISK AND RETURN FOR INVESTMENT ASSETS

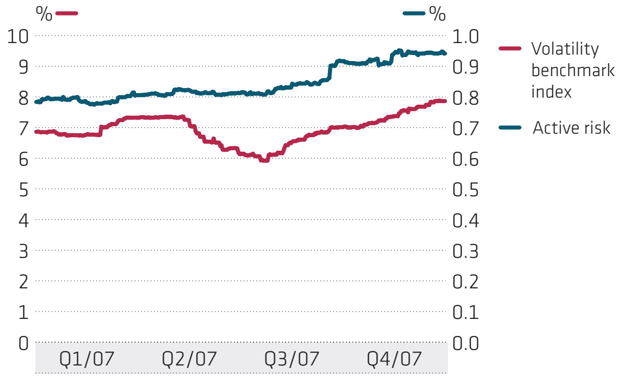
	Portfolio return, %	Active return, %	Volatility, % 12 months portfolio	Active risk, % 12 months	Sharpe ratio, 12 months portfolio	Information ratio, 12 months
Swedish equities	-1.6	1.0	18.7	1.8	-0.3	0.6
Global equities	2.1	-2.0	13.5	1.0	-0.2	-2.1
Internally managed	3.5	-1.3	13.5	1.4	-0.1	-0.9
Externally managed	0.2	-3.5	14.3	1.6	-0.3	-2.3
Fixed income assets	1.3	-2.1	2.0	1.0	-1.7	-2.1
Currency, Tactical asset allocation, Cash	–	–	–	–	–	–
Total listed assets	**1.8**	**-1.2**	**8.6**	**0.7**	**-0.5**	**-1.7**
Real estate	21.4	0.0	–	–	–	–
Private equity	40.4	32.5	–	–	–	–
Total investment assets	**2.5**	**-1.0**	**8.6**	**0.7**	**-0.2**	**-1.4**

CONTRIBUTIONS TO FUND PERFORMANCE AND ASSET ALLOCATION

	Contribution to portfolio return, %	Contribution to net profit, SEK bn	Contribution to active return, %	Market value, SEK bn	Exposure[2], %	Strategic portfolio, %
Swedish equities	-0.1	-0.1	0.2	38.1	18.7	18.8
Global equities (including emerging markets)	1.0	1.9	-0.8	84.7	41.2	41.0
Fixed income assets	0.5	0.9	-0.8	76.3	36.9	36.9
Currency, Tactical asset allocation, Cash	0.4	0.9	0.2	1.3	-0.2	0
Total listed assets	**1.8**	**3.6**	**-1.2**	**200.4**	**96.6**	**96.6**
Real estate	0.4	0.8	0.0	5.0	2.4	2.4
Private equity	0.3	0.5	0.2	2.0	1.0	1.0
Total investment assets	**2.5**	**4.9** [1]	**-1.0**	**207.4**	**100.0**	**100.0**

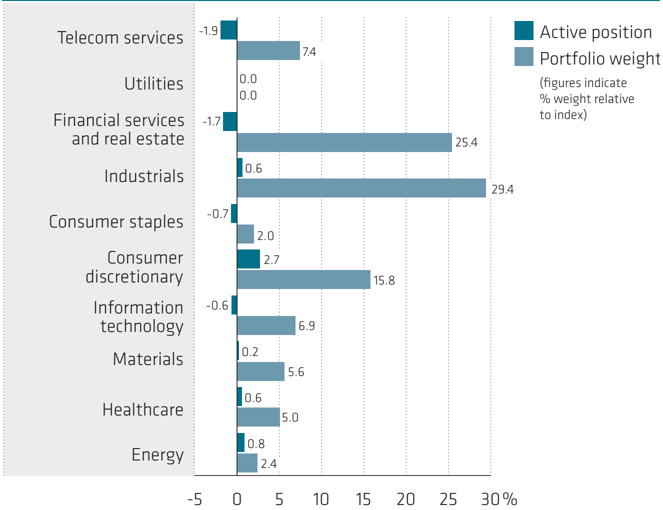
1) Before expenses; profit after expenses was SEK 4.8 billion.
2) Exposure includes the underlying value of derivatives for each asset class.

ACTIVE RISK AND VOLATILITY 2007



Active risk climbed behind rising market volatility.

SECTOR MIX IN THE SWEDISH EQUITY PORTFOLIO, 31 DEC 2007



Industrials were the heavyweight in the Swedish portfolio at year-end. Portfolio risks were lowered during the market turbulence in the second half.

fixed income assets −2.1 (0.1) percentage points. Management of listed Swedish equities generated positive active return of 1.0 (−2.4) percentage points. Currency management and tactical asset allocation also made a positive contribution to the Fund's active return totalling 0.2 (0.0) percentage points, as did private equity, which contributed 0.2 percentage points.

Overall, active management significantly underperformed the Fund's total active return target of at least one percentage point for a two-year period. In response to the poor management outcome, AP4 has reduced risks in active management and accelerated the restructuring of the management organisation.

Volatility rose in the financial markets in the second half. Average volatility for AP4's investment assets in 2007 was 8.6% (7.1) during the year. Active risk – risk versus the benchmark index – was driven upward by rising market volatility, but the increase was offset in equity management by a moderate reduction in position-taking. Within global equities, passive (index-tracking) management was applied to the Health sector as of 1 January and to sector allocation as of 30 June. AP4 reduced its portfolio positions for large cap equities in Swedish equity management, while small and midcap equities were under passive management for the first seven months of the year. The midcap portfolio was transferred to active management in August, with investment options expanded to Finland, Denmark and Norway.

Budgeted active risk for fixed income management increased from 0.75% in 2006 to 1.0% in 2007. Realised active risk was below budget during the first half of 2007, but credit nervousness and liquidity problems in the second half caused a marked increase in active risk. Average active risk for fixed income management was 1.0% (0.7) for the year. The severe negative active return triggered a red light in the Fund's internal "traffic light" system for loss containment in the autumn with regard to fixed income

FIVE LARGEST HOLDINGS IN THE SWEDISH EQUITY PORTFOLIO

Company	Market value 31 Dec 2007, SEK bn	Share of Swedish portfolio, %
H&M	3.2	8.4
NORDEA	2.4	6.4
VOLVO	2.2	5.8
TELIASONERA	2.1	5.4
ERICSSON	1.8	4.7
Total	**11.7**	**30.7**

LARGEST ACTIVE POSITIONS IN INTERNALLY MANAGED EQUITY PORTFOLIOS AT 31 DEC 2007

Company	Active weight, %	Portfolio weight, %	Index weight, %
Largest overweights (Sweden)			
SWEDBANK	2.0	4.3	2.4
VOSTOK NAFTA	1.5	2.2	0.7
RATOS	1.3	2.0	0.7
SANDVIK	1.2	4.5	3.3
SSAB	1.1	2.6	1.4
Largest underweights (Sweden)			
SHB	−2.4	0.8	3.3
ERICSSON	−1.5	4.7	6.1
TELIASONERA	−1.4	5.4	6.8
SKANSKA	−1.3	0.0	1.3
SKF	−1.0	0.2	1.2

management and certain externally managed global equity mandates (see also the section on risk management on page 30). Consequently, active positions in fixed income management were reduced and capital was transferred from actively to passively managed global equity mandates.

As mentioned, the Fund's total return was modest for the year. Global equities delivered the strongest positive contribution (see table, "Contributions to Fund performance and asset allocation", page 23), while investments in Swedish equities provided a negative contribution. Global equities and fixed income assets produced large negative contributions to the Fund's active return. Positive contributions came – for the first time since 2001 – from Swedish equities and private equity, currency management and, to a lesser extent, from active tactical asset allocation.

PERFORMANCE PER MANAGEMENT MANDATE

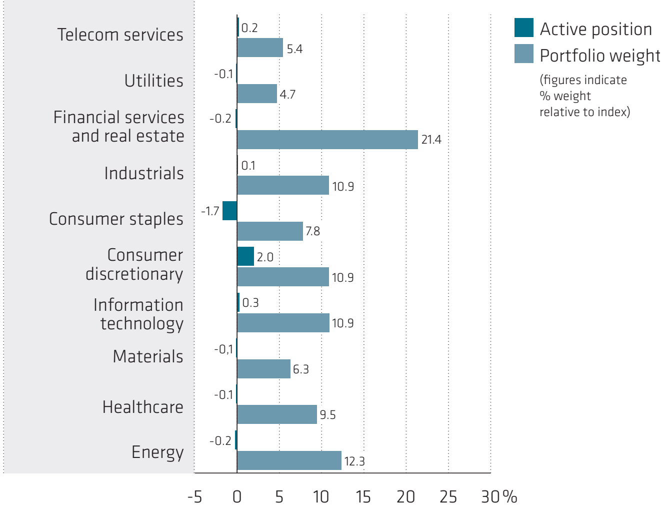
Swedish equity portfolio

At year-end, the market value of the Swedish equity portfolio was SEK 38.1 billion (41.1), excluding unlisted assets, corresponding to 18.4% of Fund assets (20.5). The five largest holdings in the portfolio were H&M, Nordea, Volvo, TeliaSonera and Ericsson, which together constituted about 30% of the portfolio. The portfolio posted a full-year return of –1.6% to outperform the reference index by 1.0 percentage points. Active risk was 1.8% on average for the year, slightly below budget. Swedish equity management was split at year-end 2006 into two portfolios: an actively managed portfolio of mainly large cap equities, which accounts for almost 85% of the Fund's Swedish equity investments, and a passively managed portfolio of small and midcap equities.

The large cap portfolio's concentration on companies benefiting from sustained strong demand in capital goods, energy and primary products was successful in the bull market during the first half. The portfolio's active positions were reduced during the summer, but active return was nevertheless adversely affected later in the year. Among the large cap equities, the underweight in Ericsson and the overweights in ABB, Sandvik, Vostok Nafta and Alfa Laval made a positive contribution. The overweights in Swedbank and Boliden and underweights in TeliaSonera and OMX had the most adverse impact on active return.

As of autumn 2007, the entire small and midcap portfolio is under active management. Up to 50% of the portfolio may be invested in Finnish, Danish and Norwegian equities. Active management of small and midcap equities has got off to a very good start, outperforming the reference index by 1.9 percentage points. Investments in Mekonomen, G4S, Lindex and Unibet provided the largest contributions to the positive outcome. However, the management mandate is still in the build-up phase

SECTOR MIX IN THE INTERNALLY MANAGED GLOBAL EQUITY PORTFOLIO AT 31 DEC 2007



Consequent upon the weak management outcome, indexing of the global portfolio increased in 2007.

FIVE LARGEST HOLDINGS IN THE INTERNALLY MANAGED GLOBAL EQUITY PORTFOLIO

Company	Market value 31 Dec 2007, SEK m	Share of global portfolio, %
EXXON MOBIL	1,005	2.1
MICROSOFT	857	1.8
GE	823	1.7
PROCTER & GAMBLE	634	1.3
VODAFONE	556	1.2
Total	**3,875**	**8.2**

LARGEST ACTIVE POSITIONS IN INTERNALLY MANAGED EQUITY PORTFOLIO, 31 DEC 2007

Company	Active weight, %	Portfolio weight, %	Index weight, %
Largest overweights			
SWEDBANK	1.1	1.1	0.0
NEW WAVE	0.7	0.7	0.0
WPP	0.6	0.7	0.1
PUBLICIS GROUPE	0.6	0.6	0.0
LVMH	0.6	0.7	0.1
Largest underweights			
TELEFONICA	-0.6	0.0	0.6
APPLE	–0.4	0.4	0.7
GOOGLE	–0.3	0.3	0.7
AT&T	–0.3	0.7	1.1
INTEL	–0.3	0.3	0.6

and the share of companies outside Sweden was less than 10% at year-end 2007.

Global equity portfolio

The market value of the global equity portfolio was SEK 84.7 billion (79.9) at year-end, excluding unlisted equities corresponding to 40.8% of Fund assets (39.8). Return for the year, including full hedging, was 2.1% (13.6), which resulted in active return of –2.0 (–0.1) percentage points.

The internally managed component, which consists of investments in North America and Europe, made up 56.4% of the global equity portfolio at 31 December. The management mandate is divided into sector-based equity mandates and one sector allocation mandate. At the beginning of the year, seven were active management mandates and three were passively managed.

The internally managed portfolio posted annual return, including full hedging, of 3.5% (16.8), representing an underperformance against the reference index of –1.3 (0.5) percentage points. The weak return from active management is primarily attributable to underweights in equities with exposure to consumer electronics, such as Apple, Nokia and RIM. Overweight positions in bank stocks, such as Citigroup and Swedbank, and a defensive sector positioning in the first half also had adverse impact on the result.

Consequent upon the weak management outcome, sector allocation and one additional sector portfolio were switched to passive management during the year and two of the remaining actively managed mandates were split into an active and a passive component. As a whole, these measures reduced the active management component from 80% of the internal global equity portfolio at 1 January 2007 to about 50% by 31 December.

At year-end, external management mandates made up 43.6% of the global listed equity portfolio. As the year began, the Fund's externally managed global equities consisted of four actively managed equity mandates – one global, one Japanese, and two Asia-Pacific (excluding Japan) – and three semi-actively and quantitatively managed mandates covering North American and European equities. Mainly in the second half of 2007, the Fund made phased investments of 3% of investment assets in two external, passively managed mandates for global emerging markets. The investments were financed by reducing the Fund's other holdings in listed global equities.

Fully hedged, the external mandates returned a total of 0.2% for the year (11.7). Active return was –3.5 percentage points (–1.8). Stock selection in Japan and Asia-Pacific was the main explanation behind the very negative outcome for actively managed mandates. The semi-active mandates delivered weak active return in conjunction with the market downturn in August, when trends were generally very poor for quantitative management strategies. In response to the substandard active management outcome, SEK 2.8 billion was transferred during the year from the actively managed external mandates to two passively managed external mandates, one for Japan and one for Asia-Pacific excluding Japan. Please see the table on page 29 for an overview of the Fund's externally managed global equity mandates.

Increasing the percentage of assets under passive management reduced total active risk towards the end of the year for both the internally and externally managed components of the portfolio.

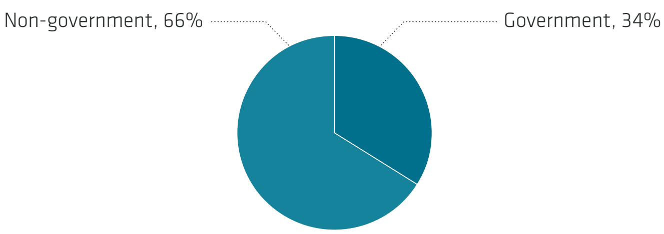
Fixed income portfolio

The Fund's fixed income portfolio had a market value of SEK 76.3 billion at year-end (69.6). Fully hedged, return for the year totalled

NET CONTRIBUTIONS FROM EXTERNAL MANAGEMENT OF LISTED ASSETS, 2007

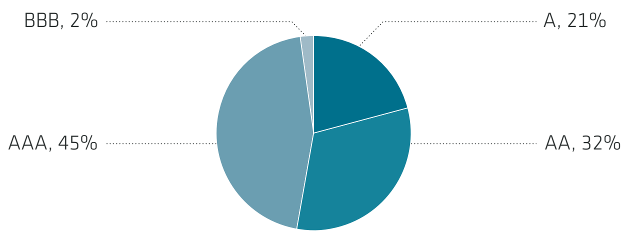
SEK m	Total listed assets
Gross income	278
Less performance-based fees	–1
Net	277
Fixed management fees	–58
Net contribution	**219**
Assets under management, 31 Dec 2007	30,665

FIXED INCOME PORTFOLIO BY ISSUER TYPE, 31 DEC 2007



High weight in corporate bonds.

BOND HOLDINGS BY RATING CLASS, 31 DEC 2007



Concentration in investment grade corporate bonds remains high.

CURRENCY EXPOSURE[1], 31 DEC 2007, SEK M

	USD	EUR	GBP	JPY	Other	Total
Shares and investments	44,341	16,624	7,732	7,634	7,810	84,142
Bonds and other fixed income assets	23,227	11,364	7,621	0	0	42,213
Derivatives excl. currency derivatives	152	127	–89	–36	–488	–334
Net other receivables and liabilities	222	200	51	173	541	1,187
Currency derivatives	–56,111	–16,148	–13,685	–3,874	–7,936	–97,754
Net currency exposure	**11,831**	**12,167**	**1,630**	**3,897**	**–73**	**29,454**

CURRENCY EXPOSURE[1], 31 DEC 2006, SEK M

	USD	EUR	GBP	JPY	Other	Total
Shares and investments	38,691	13,684	9,193	7,961	7,424	76,953
Bonds and other fixed income assets	20,507	10,304	7,032	0	0	37,843
Derivatives excl. currency derivatives	–36	127	–279	21	–205	–372
Net other receivables and liabilities	15	215	175	42	322	769
Currency derivatives	–50,830	–15,555	–20,017	–766	2,159	–85,009
Net currency exposure	**8,347**	**8,775**	**–3,896**	**7,258**	**9,700**	**30,184**

[1] *Currency exposure was formerly calculated on the basis of legal domicile. As of 2005, AP4 uses the MSCI currency domicile definition for equities and the denomination currency for fixed income assets.*

1.3% (0.6), significantly underperforming the Fund's reference index. The fixed income portfolio posted active return of –2.1 percentage points (0.1). Although the Fund has had no exposure to US housing assets, the liquidity crisis in the second half had tangible indirect impact. The shortage of short-term financing has had exceptionally adverse impact on high-quality assets with shorter maturities (such as Swedish housing bonds, interest swaps and deposit rates). The Fund had an overweight in these assets during the year against government bonds in several markets, which lay behind the bulk of the negative result. Other negative contributions resulted from the steeper drops in US and European interest rates compared to Swedish rates. As mentioned previously, the sharply negative active return triggered a red light in the Fund's internal traffic light system for loss containment (see also the section on risk management on page 30). Active positions in the fixed income portfolio were subsequently reduced to diminish the risk of further losses.

The year-end duration in the fixed income portfolio was somewhat longer than the reference index. The table on page 26 provides a breakdown of bond holdings by rating class.

At year-end, the Fund was positioned for steeper yield curves in Australia and the UK and falling credit spreads for investment grade corporate bonds. The Fund was also overweight in Swedish bonds and underweight in dollar-denominated bonds.

Currencies

Active currency management made a positive contribution of 0.16 percentage points (–0.11) to the Fund's active return, corresponding to a profit increase of SEK 0.3 billion (–0.2). The favourable result is mainly attributable to the overweight in Swedish and Norwegian kronor against the euro. Strategic currency management, which refers to hedging foreign assets to achieve strategic currency exposure in accordance with investment decisions, also delivered positive active return. The relatively high transaction costs for strategic currency management were thus more than offset by fortuitous management of forward contract maturities and a successful rebalancing strategy.

Currency exposure was 14.2% of total assets at 31 December 2007, compared to 15.1% at 31 December 2006.

Tactical asset allocation

Active tactical asset allocation is an independent mandate with no direct links to the Fund's underlying asset allocation. The mandate provided a positive contribution in 2007 of 0.03 percentage points (0.12) to the Fund's active return, corresponding to a profit increase of SEK 0.1 billion (0.2). Long positions in the US and European equity markets in the first half made a positive profit contribution, but a long position in the Japanese equity market relative to the European markets in the autumn produced a negative contribution. Active risk in the portfolio remained low in 2007.

Passive tactical asset allocation aims – with reasonable transaction costs – to minimise the differences in allocations per asset class between the Fund's investment assets and the strategic portfolio. The mandate produced a contribution of −0.1 percentage points to the Fund's total active return in 2007. The negative outcome is due to transaction costs and deviations in return among strategic portfolio indices and forward contracts used in passive tactical asset allocation.

As of 31 December, the active tactical asset allocation portfolio had a long position in European bonds and a short position in the Hong Kong equity index versus long positions in the European and US equity markets.

Real estate

Along with AP1, AP2 and AP3, AP4 is an equal partner in AP Fastigheter Holding AB , one of Sweden's largest property groups, with a portfolio worth nearly SEK 40 billion. The group's main holdings are of commercial real estate and residential properties in Stockholm, Uppsala and Gothenburg.

Turnover in the Swedish property market set new records in 2007, but declined steeply toward the end of the year, reflecting the flagging economy. Share prices for Swedish and foreign real estate stocks decreased during the year.

At 31 December 2007, the Fund's stake in AP Fastigheter was valued at SEK 5.0 billion. Return for the year was 21.4%. AP Fastigheter's actual return is used as the reference index for the security holdings.

Private equity

At year-end, the market value of the Fund's private equity portfolio was SEK 2.0 billion (1.3), corresponding to 1.0% (0.6) of Fund assets. Private equity delivered strong total return of 40.4% to outperform the benchmark index by 32.5%. The excess return is attributable virtually entirely to the sale by EQT of Tognum, a German company, in summer 2007. The Fund made two additional commitments totalling SEK 0.3 billion to private equity funds during the year, Scope Growth II and Accent Equity 2008.

NET CONTRIBUTION FROM EXTERNAL MANAGEMENT, UNLISTED ASSETS (EXCLUDING REAL ESTATE), 2007

SEK m	Unlisted assets
Gross income	518
Management fees refunded at profitable exit	+55
Management fees reported as commission expense	−8
Net contribution	**565**
Receivables, management fees unlisted assets	42
Assets under management, 31 Dec 2007	1,980
Invested capital, 31 Dec 2007	1,848
Commitments, 31 December 2007	1,954

Strategic positions

The Fund applies a three-step investment process, which is described in greater detail on pages 12–15. In the first step, the structure of the Fund's long-term normal portfolio is decided based on an ALM study of the income pension system. The asset mix is adjusted to medium-term return forecasts in the second step. This is done in the strategic portfolio, for which the normal portfolio is used as the benchmark index to assess long-term performance. The differences between the strategic portfolio and the normal portfolio constitute the Fund's strategic positions. The strategic allocation function is in the build-up phase. It was operational for fixed income assets and currencies throughout 2007, but equity resources were not in place until late in the year. Accordingly, differences between the strategic and normal portfolios with regard to equity weights and equity portfolio structure will not constitute strategic positions until 2008. The following strategic fixed income and currency positions existed in 2007.

In respect to fixed income, the Fund has excluded British bonds with maturities of longer than ten years from the strategic portfolio due to systematic erroneous pricing. Japanese fixed income investments have also been excluded from the strategic portfolio based on the Fund's judgement that the country is in the midst of a process that will lead to increases in interest rates to levels comparable to those in other developed market economies. Finally, the Fund had a strategic underweight in Swedish corporate bonds and a corresponding overweight in Swedish government bonds during the year. The strategic fixed income positions provided a contribution in 2007 of 0.1 percentage points to strategic portfolio return.

Currency exposure in the strategic portfolio was 5 percentage points below the normal portfolio's 20% at the beginning of the year. Late in the year, strategic currency exposure increased somewhat and the underweight was 3.8 percentage points at 31 December. The Fund decided in May to increase the strategic portfolio's exposure against Japanese yen from 1% to 2% of the total portfolio and reduce the weight for euro and GBP to a corresponding extent. The strategic currency positions made no positive or negative contribution to strategic portfolio return in 2007.

The structure of the strategic equity portfolio was modified during the year through the phased transfer of about 7%, or SEK 6 billion, of the global equity portfolio to equities from emerging markets. For reasons reported above, the change did not make up any part of the Fund's strategic position-taking in 2007, but for

EXPOSURE AND RETURNS FOR EXTERNAL MANDATES, 2007

Global equities, developed markets

Asset class	Type of management	Region	Benchmark index [1]	Portfolio manager	Market value at 31 Dec, SEKm	Return, %	Return on index, %	Relative return, % points
Equities	Passive	Pacific ex Japan	MSCI Pacific ex Japan	BlackRock	1,746	–4.2	–2.4	–1.8
Equities	Passive	Japan	MSCI Japan	State Street	1,958	–9.3	–9.5	0.2
	Total passively managed mandates				**3,704**	**–9.9**	**–9.4**	**–0.6**
Equities	Semi-active	North America	MSCI North America	State Street	6,354	4.4	4.3	0.1
Equities	Semi-active	Europe	MSCI Europe	State Street	4,205	4.3	5.4	–1.0
Equities	Semi-active	World ex Pacific	MSCI World ex Pacific	BlackRock	7,447	3.5	4.7	–1.2
	Total semi-active mandates				**18,007**	**4.0**	**4.7**	**–0.7**
Equities	Active	Pacific ex Japan	MSCI Pacific ex Japan	APS	1,241	2.3	19.5	–17.3
Equities	Active	Pacific ex Japan	MSCI Pacific ex Japan	Capital	1,082	18.1	19.5	–1.4
Equities	Active	Japan	MSCI Japan	Martin Currie	5,677	–13.1	–8.3	–4.8
Equities	Active	World	MSCI World	Capital	952	–1.8	3.9	–5.7
	Total active mandates				**8,952**	**–4.2**	**1.7**	**–5.9**
Global equities, emerging markets								
Equities	Passive	World	MSCI Emerging Markets	Deutche Bank/ UBS	6,267	17.4	17.7	–0.3
	Total passively managed mandates				**6,267**	**17.4**	**17.7**	**–0.3**

[1] *All indices hedged to SEK.*

information purposes only, we are reporting a contribution of 0.1 percentage points to strategic portfolio return during the year.

SIGNIFICANT EVENTS

Management process, risk management and other information

The Fund has been engaged in a change initiative since mid-February 2007, guided by the "LOTS®" process, which is explained more fully in the Letter from the CEO and on pages 20–21. Within the framework of this process, the Fund has initiated a number of activities. Some of the most central are to develop a strategic allocation function, objectively analyse conditions for active management in each asset class, and adopt a new management structure based on the analysis. Efforts so far have entailed expanding resources for the strategic allocation function and increasing the passive management component in global equities.

The Swedish small and midcap equity portfolio, which was under a passive management mandate at the beginning of the year, was transferred in autumn to active management. In parallel, investment options were expanded to include companies listed in Denmark, Finland and Norway.

During the autumn, fixed income management and certain externally managed global equity mandates triggered a red light in the Fund's traffic light system for monitoring extreme outcomes in active management. Consequently, active positions in fixed income management were reduced and capital was transferred from actively to passively managed global equity mandates.

The Fund's new "Pearl" system for evaluating risk, returns and positions went operational in May. The new system has streamlined continual monitoring and reduced operational risks while offering new research options. Among else, the Fund can now perform a contribution analysis of active returns for equity mandates down to the securities level.

Organisational changes and employees

Mats Andersson took over as CEO of the Fund as of 1 January 2007. Prior to joining AP4, he was head of asset management at Skandia Liv.

As planned, the Deputy Managing Director of the Fund retired during the year.

Aimed at cutting the Fund's costs, responsibility for IT operation and system maintenance was outsourced to an external data support firm in November, which reduced the workforce by four people.

Several individuals were assigned to other tasks within the Fund during the year, consequent upon the ongoing change process.

New members of staff were recruited during the year in the Swedish Equities, Tactical and Strategic Asset Allocation, Currency Management and Performance and Risk Control departments

The average number of employees at the Fund in 2007 was 42 (44).

SIGNIFICANT EVENTS AFTER THE END OF THE FINANCIAL YEAR

Conditions have been turbulent going into the new financial year. Market movements have been extreme worldwide. Uncertainty about where the US economy is going, or rather how deep the slump is going to be, has become more intense. The US Federal Reserve has implemented several vigorous cuts in the base rate. Unsurprisingly, the equity markets have reacted adversely to the more severe uncertainty. Naturally, this is having an impact on AP4's absolute return from the short-term perspective.

Two changes have occurred in AP4's executive management committee since 1 January. The Head of Global Equities and the Head of Fixed Income and Securities have resigned their positions with the Fund. The process of finding their replacements has begun.

RISK MANAGEMENT

The board sets an annual risk management plan that details the main operational risks and how these risks should be managed. The principal risks are of a financial and operational nature. Financial risks consist of market risks, credit and counterparty risks and liquidity risks. Operational risks are defined as administrative risks, IT risks, other technical risks, legal risks and ethical risks.

Performance and Risk Control is an autonomous department that reports directly to the CEO and the Board of Directors. Its task is to ensure compliance with legal investment rules and the risk management plan throughout the Fund. This is accomplished mainly through careful evaluation and analysis and daily reporting of absolute return and risk and in relation to relevant indices.

In the current organisation, the CEO of the Fund has operational charge of investment operations. Rules under this organisation aimed at securing the principle of duality include that the CEO may not independently carry out transactions and all limit adjustments must be reviewed in advance and approved by Performance and Risk Control. Moreover, the head of Performance and Risk Control has the unrestricted right to submit any questions that arise within the department's remit directly to the board.

Financial risks

The core aim of AP4's investment operations is to generate an active return in relation to the benchmark and reference indices. Accordingly, risk is primarily determined in relation to the index (active risk). Currency, fixed income and equity risks in active management are managed by means including limitation of active risk, duration and permissible deviations from index weights.

During the 2007 financial year, the Fund also implemented a system for monitoring and containing extreme outcomes in active management, as a component of ongoing risk management. The aim is to initiate discussions about possible actions when active management outcomes are unexpectedly negative or positive, in order to clarify guidelines for the appropriate level of risk. The system is designed as a "traffic light" system, where an amber light indicates that the manager and his or her immediate manager/executive management must discuss the situation and the actions required to stop the undesirable trend. A red light requires transfer of responsibility for the portfolio to the CEO.

The use of derivatives is limited with respect to both nominal underlying value and market risk. All derivative positions and associated risks are subject to daily position and risk monitoring.

Credit and counterparty risks consist of the risk that individual counterparties will be unable to perform their obligations to the Fund. AP4 has established individual, continuously monitored counterparty limits in order to manage credit risks. Credit risks are limited by a rule that permits investments only in securities rated BBB or higher.

Liquidity risks are limited by special rules for investments in fixed income assets and careful monitoring of cash balances.

Operational risks

AP4 managers are responsible for taking requisite steps to identify, limit and control their departments' operational risks in accordance with the risk management plan.

ADMINISTRATION REPORT

The board of directors has provided a separate Administration Report in this annual report (page 40), which gives a more detailed account of the board's activities.

FIVE-YEAR SUMMARY

	2007	2006	2005	2004	2003
Fund capital, inflows and net profit, SEK bn					
Fund capital at 31 Dec	207.3	200.5	180.1	151.4	135.5
Net inflows from the pension system and special asset management funds	2.0	1.7	2.9	1.7	2.6
Net profit for the year	4.8	18.8	25.8	14.3	19.3
Return, %					
Return on total portfolio excluding expenses	2.5	10.5	16.9	10.6	17.0
Return on total portfolio including expenses	2.4	10.4	16.8	10.5	16.8
Return on total portfolio versus index excluding expenses	–1.0	–0.6	–0.1	–0.3	–1.0
Return on listed assets versus index excluding expenses	–1.2	–0.5	–0.1	–0.3	–0.4
Inflation	3.5	1.6	0.9	0.3	1.3
Real return after expenses	–1.0	8.8	15.9	10.2	15.5
Management cost quotient as % of assets under management					
Operating expenses	0.07	0.07	0.08	0.09	0.10
Operating expenses and commission expenses	0.10	0.11	0.13	0.15	0.16
Risk in total portfolio, %					
Portfolio, ex-post	8.6	7.1	4.7	6.0	9.0
Active risk, ex-post	0.7	0.8	0.8	1.0	0.9
Sharpe ratio	neg	1.0	3.1	1.4	1.6
Currency exposure at 31 Dec, %	14.2	15.1	10.1	20.4	18.5
Share of active management incl. enhanced at 31 Dec, %	94	100	100	100	100
Share of external management including investments in venture capital firms at 31 Dec, %	17.8	17.3	18.8	20.6	13.2
Number of employees at 31 Dec	45	46	50	50	51
Allocation of investment assets, % [1]					
Global equity portfolio	42.0	42.2	42.2	42.8	42.5
Internally managed	24.2	25.1	23.6	22.4	29.5
Externally managed	17.8	17.1	18.6	20.4	13.0
Swedish equity portfolio	18.8	19.9	20.0	19.3	20.1
Fixed income portfolio	36.9	36.3	36.4	35.8	35.0
Real estate	2.4	2.3	2.1	2.1	2.4
Currency/Tactical asset allocation/Cash [2]	–0.2	–0.7	–0.7	0.0	–
Total investment assets	100.0	100.0	100.0	100.0	100.0

1) Exposure per asset class; underlying values for derivatives have been distributed per asset class.
2) These items were included in the equity and fixed income portfolios in 2003.

INCOME STATEMENT

SEK m	Note	2007	2006
OPERATING INCOME			
Net interest income	1	1,972	555
Dividends received		2,800	2,436
Net income, listed shares and investments	2, 4	-138	19,031
Net income, unlisted shares and investments	3	963	839
Net income, fixed income management		21	-1,303
Net income, derivatives		-1,138	99
Net income, foreign exchange		519	-2,686
Net commission expenses	4	-72	-75
Total operating income		**4,927**	**18,896**
OPERATING EXPENSES			
Personnel costs	5	-87	-86
Other administrative expenses	6	-52	-47
Total operating expenses		**-139**	**-133**
INCOME IN 2007		**4,788**	**18,763**

BALANCE SHEET

SEK m	Note	31 Dec 2007	31 Dec 2006
ASSETS			
Shares and investments, listed	7	116,280	120,823
Shares and investments, unlisted	8	4,817	3,708
Bonds and other fixed income assets	9	77,020	70,389
Derivatives	10	8,526	4,757
Cash and bank balances		1,727	1,428
Other assets	11	999	63
Prepaid expenses and accrued income	12	2,527	2,148
Total assets		**211,896**	**203,316**
LIABILITIES AND FUND CAPITAL			
Liabilities			
Derivatives	10	2,374	1,247
Other liabilities	13	1,119	425
Deferred income and accrued expenses	14	1,058	1,107
Total liabilities		**4,551**	**2,779**
Fund capital	15		
Fund capital at 1 January		200,537	180,098
Net payments from the national pension system		991	1,568
Transfers from Liquidation Fund/ Special Asset Management Fund		1,029	108
Net profit for the year		4,788	18,763
Total fund capital		**207,345**	**200,537**
TOTAL LIABILITIES AND FUND CAPITAL		**211,896**	**203,316**
MEMORANDUM ITEMS	16		

ACCOUNTING AND VALUATION PRINCIPLES

In compliance with the Swedish National Pension Funds Act, the annual accounts have been prepared according to generally accepted accounting principles. The buffer funds have developed and put into practice a set of common accounting and valuation principles that accord with existing regulations for comparable financial institutions.

Transaction day accounting
Purchases and sales on the money, bond, equity and foreign exchange markets are reported in the balance sheet on the transaction date; that is, at the point when material rights, and therefore risks, are transferred between the parties. Receivables and liabilities that fall between transaction and settlement date are reported under other assets and other liabilities respectively. Net accounting is applied when permitted.

Foreign currency
Foreign currency-denominated assets and liabilities are stated at year-end exchange rates. Changes in the values of foreign-currency-denominated assets are divided between those attributable to the change in the value of the asset or liability in local currency and those stemming from fluctuations in exchange rates. Realised and unrealised changes in value arising from exchange rate fluctuations are reported in the income statement under "Net income, foreign exchange".

Shares and investments
Shares and investments are valued at fair value. Shares listed on an authorised stock exchange are valued primarily at the closing rate in local currency on the last trading day of the year or secondarily at the latest buying rate. Private equity holdings are valued in accordance with EVCA principles or equivalent standards. Fair value should primarily be calculated on the basis of transactions with third parties, though other valuation methods may be used.

Bonds and other fixed income assets
Bonds and other fixed income assets are valued at fair value. The market value of fixed income securities is determined primarily by the closing price on the last trading day or secondarily by the buying rate on the day preceding the last trading day. When instruments are not traded on an active market and listed market prices are unavailable, the instrument is valued using generally accepted theoretical models, by which cash flows are discounted using yield curves.

Net income is the difference between average accrued acquisition value and sales or fair value. Accrued acquisition value is the discounted present value of future payments where the discount rate corresponds to the effective interest rate at time of purchase. Acquired premiums and discounts are accrued until the coupon rate changes or the instrument matures. Changes in accrued acquisition values are reported as interest income.

Buybacks
In a true buyback (repurchase), the asset remains on the balance sheet and cash received is reported as a liability. The divested security is reported under pledged assets on the balance sheet. The cash value difference between spot and forward legs accrues during the maturity period and is reported as interest.

Derivatives
Derivatives are valued at fair value based on year-end market rates. When derivatives are not traded on an active market and listed market prices are unavailable, the instruments are valued using generally accepted theoretical models for which the input data consists exclusively of observable market data.

Derivative positions with a positive fair value at year-end are reported as assets, while positions with a negative fair value are reported as liabilities. The difference between forward and spot rates is accrued evenly over the term of the forward contract and reported as interest.

Securities loans
Lent securities are still reported in the balance sheet in a memorandum item as pledged collateral. Received and accrued premiums are reported as interest income.

Items reported directly against fund capital
Transfers to and from the national pension system, along with transfers from the liquidation and special asset management funds owned jointly by the four buffer funds, are reported directly against fund capital.

Performance-based fees to external managers
Performance-based fees, which are paid only if the manager produces returns above the agreed level, are reported in the income statement under net income per asset category.

Commission expenses
Commission expenses are reported in the income statement as a deduction from operating income. They consist of direct transaction costs, custody account expenses and fixed fees paid to external managers. Fees for external management of private equity assets, for which repayment is permitted prior to distribution of profit and where repayment is assessed as likely, are reported in the balance sheet as a receivable under "Other assets".

Operating expenses
All management expenses except brokers' commissions, fees to external managers and custody account expenses are reported as operating expenses.

Investments in property, plant and equipment and software, whether developed in-house or purchased, are customarily expensed as they are incurred.

AP4 is VAT-exempt since it is not classed as conducting business activities. Consequently, the Fund is not entitled to reimbursement of input VAT. VAT that has been paid or reserved for payment is reported under the relevant expense item.

Income taxes
AP4 is exempt from income tax on investments in Sweden. The tax liability on investments outside Sweden varies from country to country.

NOTES TO THE INCOME STATEMENT AND BALANCE SHEET

(SEK million, unless otherwise stated)

NOTE 1 Net interest income

	2007	2006
Interest income		
Bonds and other fixed income securities	3,475	2,523
Derivatives	3,968	4,097
Other interest income	154	173
Total interest income	**7,597**	**6,793**
Interest expenses		
Derivatives	–5,611	–6,230
Other interest expenses	–14	–8
Total interest expenses	**–5,625**	**–6,238**
Net interest income	**1,972**	**555**

NOTE 2 Net income, listed shares and investments

	2007	2006
Net income, listed shares and investments	12	19,179
Less brokers' commissions	–149	–129
Less performance-based fees	-1	–19
Net income, listed shares and investments	**–138**	**19,031**

NOTE 3 Net income, unlisted shares and investments

	2007	2006
Capital gain	400	76
Unrealised changes in value	563	763
Net income, unlisted shares and investments	**963**	**839**

NOTE 4 Net commission expenses

	2007	2006
External management fees (listed assets)	55	60
External management fees (unlisted assets)	8	7
Other commission expense, incl. custody account fees	9	8
Net commission expenses	**72**	**75**

Performance-based fees to external managers during the year totalled SEK 0 million (19) and are reported under net income for each asset class. External management fees for unlisted assets are reported under commission expenses to the extent agreements do not permit repayment prior to distribution of profits in connection with future profitable exits. Management fees totalling SEK 51 million (44) were paid during the year in respect of unlisted assets, including SEK 45 million (28) which has been assessed as likely for repayment in connection with future profitable exits and reported in the balance sheet under "Other assets". SEK 55 million (8) was repaid to the Fund during the year in conjunction with profitable exits.

NOTE 5 Personnel

NUMBER OF EMPLOYEES	2007 Total	2007 Women	2006 Total	2006 Women
Average number of employees	42	14	44	14
Number of employees at 31 December	45	17	46	18
Number of executive management committee members at 31 December	6	2	6	1

PERSONNEL COSTS, SEK '000	2007	2 006
Salaries and remuneration		
Chairman of the Board [1]	100	150
Other directors [2]	438	475
President	2,891	1,794
Other executive management committee members	8,057	8,986
Other employees [3]	36,182	32,299
Total salaries and remuneration	**47,668**	**43,704**
[1] Thereof additional remuneration for committee service	0	50
[2] Thereof additional remuneration for committee service	0	50
[3] Thereof employment termination costs for other employees	2,239	0
Incentive-based pay		
President	0	0
Other executive management committee members	695	487
Other employees	2,137	1,657
Total incentive-based pay	**2,832**	**2,144**
Pension costs		
President	560	2,091
Other executive management committee members	3,253	2,868
Other employees [4]	9,932	10,860
Total pension costs	**13,745**	**15,819**
[4] Thereof employment termination costs for other employees	556	2,560
Social security costs		
Chairman of the Board	10	48
Other directors	136	151
President [5]	1,073	3,714
Other executive management committee members [6]	3,627	4,283
Other employees [7]	14,553	13,373
Total social security costs	**19,399**	**21,569**
[5] Thereof costs for payroll tax not previously recognised as an expense on pension provisions for the President.	0	2,628
[6] Thereof costs for payroll tax not previously recognised as an expense on pension provisions for the Deputy Managing Director.	0	529
[7] Thereof employment termination costs for other employees	906	621
Other personnel costs	**3,354**	**3,424**
Total personnel costs	**86,998**	**86,660**
Thereof costs of employment termination	3,701	3,181

Note 5, cont.

Costs of employment termination

The costs total SEK 3,701,000 and relate to compensation for pension expenses, salary and severance pay in connection with outsourcing of IT. All employment termination costs were recognised as an expense in the 2007 accounts but will be disbursed in 2008.

Salaries and remuneration

The government sets remuneration for the Board of Directors. The Board of Directors determines the terms of employment of the President and Deputy Managing Director based on the recommendations of the Chairman and Deputy Chairman. Remuneration to the President and Deputy Managing Director is limited to base salary. Remuneration to other members of the executive management committee is made up of base salary plus incentive-based pay.

Incentive-based pay

The incentive scheme has been adopted by the Board and covers all employees who have been with the Fund for more than six months except the President and Deputy Managing Director. The basic principle is that employees earn incentive-based pay if the Fund outperforms the benchmark and reference indices. The maximum incentive-based entitlement for a full-year employee is two months' salary. The item includes provisions for incentive-based pay awarded in 2007 that will be paid in 2008, after the annual report has been adopted by the Board and estimated returns on investments have been examined by the Fund's auditors. In addition, particularly deserving efforts may be rewarded with performance bonuses, which are set by the President. The maximum performance bonus to individual employees is two months' salary.

Pensions and similar benefits

The President's pension benefits and severance package are specified in his employment contract. The provisions of the agreement include pension entitlement at age 65, with a pension provision of 20% of salary. The President is also entitled to a severance package equal to 18 months' salary.

Other executive management committee members have individual employment contracts including pension entitlements and severance notice as required by the relevant collective agreement.

Sickness absence

The sickness absence rate in 2007 was 1.8% (1.4) of normal working hours. The figures were 1.6% (2.5) for female staff and 1.9% (0.6) for male staff and 0.4% (0.4) of absences lasted 60 days or longer. The sickness absence rate was 1.2% (0.0) for employees aged 29 or younger, 1.6% (1.3) for employees aged 30–49 and 2.5% (1.5) for employees over 50.

NOTE 6 Other administrative expenses

	2007	2006
Costs of premises	8	8
Information and IT expenses	28	24
Services purchased	9	8
Other administrative expenses	7	7
Total other administrative expenses	**52**	**47**
Purchased services include fees to accounting firms as follows:		
Audit services, Öhrlings PwC	1.0	0.8
Audit services, KPMG	0.3	0.3
Other services, Öhrlings PwC	0.0	0.0
Other services, KPMG	0.5	0.0
Total fees to accounting firms	**1.8**	**1.1**

NOTE 7 Listed shares and investments

	31 Dec 2007		31 Dec 2006	
	Fair value	Acquisition value	Fair value	Acquisition value
Swedish equities	39 778	37 427	44 550	32 761
Foreign equities	55 583	55 843	55 582	50 575
Investments in foreign mutual funds	20 919	17 051	20 691	16 421
Total listed shares and investments	**116 280**	**110 321**	**120 823**	**99 757**

A detailed list of holdings is published on the AP4 website and printed copies may be ordered from the Fund.

NOTE 8 Unlisted shares and investments

Holding at 31 Dec 2007	Corp. ID no.	Number	Voting capital, %	Equity capital, %	Equity in total fund, %	Acquisition value
Swedish shares and investments:						
AP Fastigheter Holding AB	556650-4196	1,000,000	25	25		721
Innoventus AB	556602-2728	2,334	17	17		1
Innoventus Project AB	556616-8356	31,032	9	9		13
Accent Equity 2003 KB	969694-7739			19	6	56
BrainHeart Capital KB	969674-4102			21	19	195
HealthCap III Sidefund KB	969699-4830			20	20	41
HealthCap Annex Fund I-II KB	969690-2049			20	20	51
HealthCap IV KB	969683-6650			41	2	35
Innoventus Life Science I KB	969677-8530			16	16	24
Northern Europe Private Equity KB (EQT III)	969670-3405			10	1	36
Priveq Investment Fund III KB	969704-1524			19	12	31
Total Swedish shares and investments						**1,204**
Foreign investments:						
EQT IV LP				4	3	530
EQT V LP				2	1	171
EQT Opportunity LP				12	7	33
European Strategic Partners II				4	4	165
Goldman Sachs Multi-Strategy Fund				95	[1]	267
Goldman Sachs Vintage Fund IV Offshore LP				1	1	58
Goldman Sachs Distressed Opportunities Fund III Offshore LP				5	3	75
Goldman Sachs Private Equity U.S.Focused II Offshore Holdings LP				21	21	40
HealthCap V LP				12	12	18
Scope Growth II LP				10	10	8
Accent Equity 2008 LP				6	6	0
Total foreign investments						**1,365**
Total acquisition cost, unlisted shares and investments						**2,569**
Total fair value, Swedish shares and investments						3,219
Total fair value, foreign investments						1,598
Total fair value, unlisted shares and investments [2]						**4,817**

[1] AP4's shares of the underlying funds are 2% (GS Vintage III) and 4% (GS PEP 2004).
[2] The fair value of the holding has been reduced by SEK 42 million in balanced asset management fees, which are reported in the balance sheet item "Other assets."

NOTE 9 Bonds and other fixed income assets

	31 Dec 2007		31 Dec 2006	
	Fair value	Accrued acquisition value	Fair value	Accrued acquisition value
Issuer category				
Kingdom of Sweden	7,455	7,467	14,539	14,745
Swedish housing institutions	17,628	17,831	14,306	14,541
Other Swedish financial services companies	6,500	6,540	1,426	1,443
Swedish non-financial companies	2,614	2,628	2,080	2,078
Foreign governments	16,863	17,754	16,923	18,077
Other foreign issuers	25,960	27,764	21,115	22,674
Total fixed income assets *	**77,020**	**79,984**	**70,389**	**73,558**

	31 Dec 2007		31 Dec 2006	
	Fair value	Accrued acquisition value	Fair value	Accrued acquisition value
Instrument type				
Bonds	72,561	75,518	68,259	71,425
Promissory note loans	2,000	2,000	2,000	2,000
Subordinated debentures	378	385	130	133
Overnight loans	2,081	2,081	0	0
Total fixed income assets *	**77,020**	**79,984**	**70,389**	**73,558**
* Thereof assets valued according to a theoretical model.	551	579		

NOTE 10 Derivatives

	31 Dec 2007		
	Nominal value	Fair value Positive	Fair value Negative
Equity-related instruments:			
Options	6,267	6,267	0
Share futures	2,285	0	29
Total equity-related instruments	**8,552**	**6,267**	**29**
thereof cleared	2,285	0	29
Interest-related instruments:			
Swaps	81,598	376	1,015
FRA / Futures	199,227	379	321
Total interest-related instruments	**280,825**	**755**	**1,336**
thereof cleared	199,227	379	321
Currency-related instruments:			
Currency options	1,134	0	4
Currency forward contracts	116,187	1,504	1,005
Total currency-related instruments	**117,321**	**1,504**	**1,009**
Total derivatives *	**406,698**	**8,526**	**2,374**
thereof cleared	201,512	379	350
* Thereof assets valued according to a theoretical model.	198,919	1,880	2,024

NOTE 11 Other assets

	31 Dec 2007	31 Dec 2006
Receivables on unsettled transactions	953	6
Management fees receivable for unlisted assets	42	52
Other assets	4	5
Total other assets	**999**	**63**

NOTE 12 Prepaid expenses and accrued income

	31 Dec 2007	31 Dec 2006
Accrued interest income	2,449	2,075
Accrued dividends and repayments	73	67
Other	5	6
Total	**2,527**	**2,148**

NOTE 13 Other liabilities

	31 Dec 2007	31 Dec 2006
Trade payables	7	4
Pension provisions	3	15
Payables for unsettled transactions	1,106	401
Other liabilities	3	5
Total other liabilities	**1,119**	**425**

NOTE 14 Prepaid expenses and accrued income

	31 Dec 2007	31 Dec 2006
Accrued interest expenses	1,004	1,028
Accrued personnel costs	16	14
Accrued external management expenses	33	58
Other accrued expenses	5	7
Total	**1,058**	**1,107**

NOTE 15 Fund capital

	31 Dec 2007	31 Dec 2006
Fund capital at 1 January	**200,537**	**180,098**
Net payments to the national pension system		
Paid-in pension contributions	47,603	45,906
Disbursed pension payments	–46,405	–44,033
Transfer of pension rights to the EU	–8	–6
Settlement of pension rights for prior years	1	0
Administration fee paid to the Swedish Social Insurance Agency	–200	–299
Total net payments to the national pension system	**991**	**1,568**
Transfer from AP1 liquidation fund	961	63
Transfer from AP4 special asset management fund	68	45
Total transfers	**1,029**	**108**
Net profit for the year	**4,788**	**18,763**
Fund capital at 31 Dec	**207,345**	**200,537**
Assets under management, AP1 liquidation fund [1)]	0	3,643
Assets under management, AP4 special asset management fund [1)]	305	489

[1)] Annual reports may be ordered from AP1 and AP4.

NOTE 16 Memorandum items

	31 Dec 2007	31 Dec 2006
Lent securities for which collateral has been received		
Lent securities	28,822	18,358
Collateral received for lent securities	29,651	19,044
Collateral pledged for derivatives trading		
Collateral for equity options	6,087	0
Collateral pledged for derivatives trading		
Collateral for futures	1,823	1,112
Commitments		
Investment commitments, private equity holdings	1,954	2,140

NOTE 17 Related enterprises

AP4 rents its office premises from AP Fastigheter at market rates.

Stockholm, 14 February 2008

Birgit Friggebo
CHAIRMAN

Karl-Olof Hammarkvist
DEPUTY CHAIRMAN

Göran Johnsson

Kajsa Lindståhl

Charlotte Strömberg

Sture Nordh

Inga Persson

Ilmar Reepalu

Ulrik Wehtje

Mats Andersson
PRESIDENT

We expanded our audit remit to include examination of the administration report for the Fourth Swedish National Pension Fund in 2007. We found no cause for qualification in respect of our audit. Our auditors' report was submitted on

Stockholm, 14 February 2008

Anna Hesselman
AUTHORISED PUBLIC ACCOUNTANT
Appointed by the government

Anders Bäckström
AUTHORISED PUBLIC ACCOUNTANT
Appointed by the government

AUDITORS' REPORT

for the Fourth Swedish National Pension Fund
(corporate identity number 802005-1952)

We have examined the annual accounts, the accounting records and the administration of the Fourth Swedish National Pension Fund by the board of directors for the financial year 2007. The Fund's annual accounts are included in the printed version of this document on pages 22–41. These accounts and the administration, and the application of the Swedish National Pension Funds Act in conjunction with the annual accounts, are the responsibility of the board of directors. Our responsibility is to express our opinion on the annual accounts and the administration based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Sweden. These standards require that we plan and perform the audit to obtain high but not absolute assurance that the annual accounts are free from material misstatement. An audit involves examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and their application by the board of directors, the significant estimates made by the board when compiling the annual accounts and evaluating the overall presentation of information in the annual accounts. We believe that our audit provides a reasonable basis for our opinion set out below.

The annual accounts have been prepared in accordance with the Swedish National Pension Funds Act and give a true and fair view of the company's financial position and results of operations in accordance with generally accepted accounting standards in Sweden. The administration report is compatible with the other sections of the annual accounts.

The audit has given us no reason for qualification with regard to the annual accounts, the income statement and balance sheets, the accounting records, the inventory of assets or the administration of the company in general.

We recommend that the income statement and balance sheet be adopted.

Stockholm, 14 February 2008

Anna Hesselman
AUTHORISED PUBLIC ACCOUNTANT
Appointed by the government

Anders Bäckström
AUTHORISED PUBLIC ACCOUNTANT
Appointed by the government

ADMINISTRATION REPORT

The assets of AP1–AP4 and AP6 are state-owned and reserved by law for specific asset management purposes in accordance with chapter 9, section 8 of the Instrument of Government. The organisational structure and activities of the AP funds are regulated by the Swedish National Pension Funds Act. The law provides that the Government may not use fund assets for purposes other than those specified in the act, unless the Riksdag decides otherwise. The AP Funds are state bodies, but there are material differences between the Funds and other government agencies. The funds are more independent than most other agencies and have separate boards of directors and external auditors. The Government adopts the Funds' annual income statements and balance sheets and orders annual evaluations of the Funds' performance. The outcome of the evaluation is reported to the Riksdag in a written communication.

As a state body, AP4 is not directly covered by many of the provisions of the Swedish Code of Corporate Governance. In any case, there are substantial differences between public law and commercial law. This administration report is therefore limited to relevant areas. The report has been examined by AP4's auditors.

BOARD OF DIRECTORS

The AP4 Board of Directors is made up of nine directors with no alternates, all appointed by the Government. Two directors are appointed on the basis of nominations from employer organisations and a further two on the basis of nominations from employee organisations. The government appoints the chairman and deputy chairman from among its own nominees.

The Government took a decision in May on fund administration for 2007. Charlotte Strömberg, CEO of Jones Lang LaSalle, the Nordics, was appointed as a new director to succeed Marianne Nivert. The other directors were re-elected in May and their mandate runs until the Fund's income statement and balance sheet for 2007 have been adopted. More information is provided about the directors on page 42.

Board remuneration is set by the Government. The annual fees are SEK 100,000 for the chairman, SEK 75,000 for the deputy chairman and SEK 50,000 for other directors.

BOARD MEETINGS IN 2007

	Feb 15	April 23–24	June 07	Aug 29	Oct 17–18	Dec 07
Birgit Friggebo, chairman	x	x	x	x	x	x
Karl-Olof Hammarkvist, deputy chairman	x	x	x	x	x	
Göran Johnsson	x	x	x	x	x	x
Kajsa Lindståhl	x	x	x	x	x	x
Sture Nordh	x		x	x	x	x
Inga Persson	x	x	x	x	x	x
Ilmar Reepalu	x	x	x	x	x	x
Ulrik Wehtje	x	x	x	x	x	x
Charlotte Strömberg			co-opted	x	x	x
Marianne Nivert	x	x				

Marianne Nivert left the board in 2007 and was replaced by Charlotte Strömberg.

RULES OF PROCEDURE

The board is responsible for the Fund's organisation and management of its assets. The Board has adopted a charter for its work and a charter for the CEO. These documents are revised annually, as are the ethical guidelines for employees and rules for reporting holdings of financial instruments.

BOARD ADMINISTRATION IN 2007

The Board held six minuted meetings in 2007. As shown on the table, average attendance was high, at 94%. A seventh meeting was held to evaluate board activities. The CEO and other AP4 staff also attend board meetings in the role of reporter and secretary. The Board has not found it necessary to appoint standing sub-committees to handle specific tasks. The temporary recruiting committee appointed in 2006 after the resolution to appoint a new president was dissolved after the matter was settled.

The Board's focus in 2007 was on supporting and following up the Fund's new CEO, Mats Andersson, in his comprehensive change initiative aimed at enhancing the Fund's active return. In order to increase the flexibility and distinctiveness of asset management, the Board has resolved that the Fund's long-term normal portfolio, which has a 40-year perspective, will be supplemented by a medium-term strategic portfolio for which the investment horizon is 3 to 5 years.

In order to provide faster information to the Board, the CEO now issues a monthly newsletter between board meetings. Another new initiative during 2007 was the joint fact-finding trip carried out by Fund administration and the reinforced executive management committee. The purpose of the trip was to meet leading representatives of the successful Norwegian NBIM (a continuation of the former Petroleum Fund).

As in previous years, the Fund's positions on various matters of corporate governance were discussed on several occasions. AP4's Governance Policy was adopted in October following comprehensive revisions based on lessons learnt in the first few years following implementation of the "Swedish Code of Corporate Governance (the Code).

In accordance with its charter, the Board customarily adopts an operations plan for the following year during the latter half of the financial year. The document was reported at the board

meeting in December and, consequent upon the ongoing change initiative, will be adopted early in the 2008 financial year.

EXECUTIVE MANAGEMENT

The Board delegates responsibility for day-to-day management of AP4 to the CEO. The CEO has an executive management committee, which in 2007 consisted of five other employees, to support him in the decision process. Björn Franzon, former Deputy Managing Director of the Fund, retired in October and was succeeded on the executive management committee by Annika Andersson, Head of Corporate Governance and Communications. The executive management committee as of 14 February 2008 is presented on page 43.

SALARIES AND REMUNERATION

The Board of Directors determines the terms of employment of the CEO and Deputy Managing Director based on the recommendations of the Chairman and Deputy Chairman. All employees have individual employment contracts. The Board has also adopted an incentive scheme for all employees who have been with the Fund for more than six months (apart from the CEO and Deputy Managing Director). Bonuses under the scheme are limited to an amount equal to two months' salary.

Detailed information about salary and remuneration paid to the CEO, members of the executive management committee and other employees and the outcome of the incentive scheme is provided in Note 5 on page 34.

AUDIT

AP4's auditors are appointed by the Government. The current audit mandate came into effect in 2005 and is shared between Anna Hesselman of Öhrlings PricewaterhouseCoopers and Anders Bäckström of KPMG. The mandate runs until the Fund's income statement and balance sheet are adopted in 2008. Anders Bäckström is also responsible for coordinating the audit process across all AP funds.

The auditors submit a report based on their audit. They report directly to the Board by way of the written report and an oral presentation. The auditors attend at least one board meeting per year. An additional minimum of two meetings are held each year between the auditors and the chairman and deputy chairman. The auditors also provide report annually to the Swedish Ministry of Finance. The practical examination of the accounts and procedures is performed by a team of auditors from Öhrlings PricewaterhouseCoopers.

INTERNAL CONTROL

The Board of Directors produces an annual Risk Management Plan in accordance with generally accepted financial market standards and the Swedish National Pension Funds Act. The plan is meant to ensure effective internal risk control and that the duties of the Performance and Risk Control Department – which has independent status – are clearly stipulated and attached to the appropriate powers.

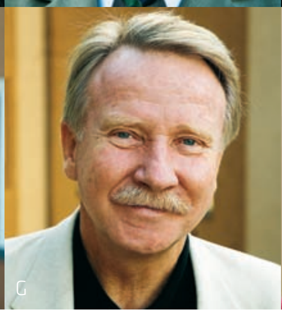
Performance and Risk Control is independent of the Fund's other operations and reports directly to the CEO and, if so required, directly to the Board. The plan states that the executive management committee must be aware of risks arising within the Fund's operations and how the risks are managed. The committee must also ensure that procedures are in place to make certain that AP4 complies with relevant legislation and decisions taken by the Board and CEO.

The Head of Performance and Risk Control submits written and oral reports to the Board at every board meeting. The Board believes the structure outlined above is adequate to ensure the Fund meets its obligations.

OTHER DISCLOSURES

A more detailed explanation of various financial and operational risks is provided under "Risk management" in the Report of the Directors. The main Board documents referred to in this Administration Report are publicly available and may be accessed from the AP4 website at www.ap4.se.

BOARD OF DIRECTORS AND AUDITORS



BIRGIT FRIGGEBO (A)
Year of birth 1941. Chairman since 2000.
Other assignments:
Chairman: University College of Opera, Stockholm, and UR (Swedish public service broadcasting corporation).
Member of Smålands Akademi.

KARL-OLOF HAMMARKVIST (B)
Professor. Pro-Vice-Chancellor of the Stockholm School of Economics.
Year of birth 1945. Deputy Chairman since 2000.
Other assignments:
Member of the Board of the Stockholm Institute for Financial Research, Länsförsäkringar Liv AB, Swedish Royal Dramatic Theatre.

GÖRAN JOHNSSON (C)
Former Head of the Swedish Metalworkers' Union. Year of birth 1945. Member of the Board since 1997 and alternate director 1993–1996.
Other assignments:
Deputy Chairman of the Swedish Export Credits Guarantee Board
Director of Swedbank, Swedish Foundation for Strategic Research, Elanders AB, Sveriges Television (SVT – public service TV), and Umeå University.

KAJSA LINDSTÅHL (D)
Director. Year of birth 1943. Member of the Board since 2004.
Other assignments:
Chairman of the Board of Stiftelsen Tumba Bruk
Director of FPG (Försäkringsbolaget Pensionsgaranti), Länsförsäkringar AB, Bank of Sweden Tercentenary Fund, SWEROAD (Swedish National Road Consulting AB), Swedish Institute for Financial Research, and Södersjukhuset AB.

STURE NORDH (E)
Chairman of the Swedish Confederation of Professional Employees.
Year of birth 1952. Member of the Board since 1999
Other assignments:
Chairman of the Board of Karlstad University, Deputy Chairman of Folksam Liv
Director of the Swedish National Labour Market Administration, Riva del Sole Spa and the European Trade Union Confederation.

INGA PERSSON (F)
Professor. Year of birth 1945. Member of the Board since 2000.
Other assignments:
Member of the Board of the Sida/SAREC Research Board.

ILMAR REEPALU (G)
Member of the Malmö City Executive Board. Year of birth 1943. Member of the Board since 2000.
Other assignments:
Deputy Chairman of the Swedish Association of Local Authorities (SKL) and Regions and SKL Företag AB. Member of the Board of E.ON Sverige AB and KPA AB.

CHARLOTTE STRÖMBERG (H)
CEO of Jones Lang LaSalle, the Nordics. Year of birth 1959. Member of the Board since 2007.
Other assignments:
Member of the board of Gant Company AB and member of the executive council, Stockholm Chamber of Commerce.

ULRIK WEHTJE (I)
CEO Rydsgårds Gods AB, Master of Engineering. Year of birth 1956. Member of the Board since 2004.
Other assignments:
Deputy Chairman of the Swedish Bookbinders' Union, the Swedish Graphic Companies' Federation.
Member of the Board of the Confederation of Swedish Enterprise, the Confederation of Swedish Enterprise's SME Committee and AFA Trygghetsförsäkring and Livförsäkring.

Auditors

ANNA HESSELMAN
Authorised Public Accountant: Öhrlings PricewaterhouseCoopers

ANDERS BÄCKSTRÖM
Authorised Public Accountant: KPMG

EXECUTIVE MANAGEMENT COMMITTEE

MATS ANDERSON
Year of birth 1954
Chief Executive Officer and Chief Investment Officer. Employed at AP4 since 2006.
Bachelor of Science
Previous employment: Deutsche Bank, AP3 and Skandia Liv.

GÖRAN SCHUBERT
Year of birth 1953
Head of Performance and Risk Control. Employed at AP4 since 2004.
Bachelor of Science
Previous employment: Nordea and Alecta.

ANNIKA ANDERSSON
Year of birth 1958
Head of Corporate Governance & Communications. Employed at AP4 since 1994.
Bachelor of Science
Previous employment: Aktiv Placering, Bohusbanken and the Swedish Society of Financial Analysts.
Directorships: Deputy Chairman, Aktiefrämjandet.

AGNETA WILHELMSON KÅREMAR
Year of birth 1952
Director of Administration. Employed at AP4 since 2001.
Bachelor of Laws and DIHM Diploma in Business Finance
Previous employment: Nordnet, Swedbank Markets and Handelsbanken.

GLOSSARY

Active management
Asset management via a portfolio composed differently from the index in an effort to secure a higher return.

Active position
Difference between a portfolio and its reference or benchmark index, e.g. in terms of weighting in individual equities (in active stock selection), sector weighting (in active sector allocation) or duration (in active duration management).

Active return
Difference between the return on a portfolio compared to the return on its benchmark or reference index. Synonymous with relative return. See also Excess return.

Active risk
Risk that arises as a result of active management. Is defined as the standard deviation of the difference between actual performance and index performance (i.e. the standard deviation of the active return). Also known as tracking error.

Active stock selection
The taking of active positions in individual equities, aimed at outperforming the reference index.

ALM analysis
Asset Liability Modelling. Analysis model used for compiling AP4's strategic portfolio. An ALM analysis is premised on the Fund's long-term undertakings, forecast pension contributions and the expected return and risk of different asset categories. The model simulates theoretical portfolios to provide a basis for selecting a strategic portfolio that provides the optimum combination to meet the Fund's pension commitments.

Asset management cost quotient
Operating expenses as a ratio of average fund capital.

Automatic rebalancing
A mechanism that reduces pensions when pension liabilities exceed pension assets (see Balance figure).

Balance ratio
The total assets of the national pension system (excluding premium pensions) divided by pension liabilities. It is an estimate of the pension system's financial balance. If the balance figure falls below 1.0, the automatic rebalancing mechanism is triggered and pension disbursements are reduced.

Benchmark index
Combination of various reference indices. Is a series of index returns against which AP4's total risks and return is compared. Returns mirror those from the strategic portfolio.

Beta value
Denotes the portfolio's propensity to rise or fall when the benchmark or reference index rises or falls. It states the expected percentage change in the value of the portfolio given a change of 1% in the reference or benchmark index.

Buffer fund
The name for the First, Second Third, Fourth and Sixth National Swedish Pension Funds. The funds' purpose is to compensate for temporary deficits in pension contributions in relation to pension disbursements (i.e. periods when disbursements exceed contributions) and also to maintain the value of pension assets in relation to pension liabilities. See Balance ratio.

Contribution value
Estimate of the present value of future forecast pension contributions to the national pension system (excluding the premium reserve pension scheme). Calculated by multiplying a three-year average of contributions by the "turnover period", which measures the average time between acquired pension entitlement and disbursed pension payments.

Corporate governance
The sharing and exercise of rights and responsibilities in relation to the running of a company, notably between management and shareholders.

Country risk
A risk arising from differentials in yield spreads between countries in the context of an international bond portfolio.

Credit risk
Risk that a counterparty wholly or partly cannot perform his obligations due to financial incapacity.

Currency exposure
Denotes the proportion of the portfolio exposed to currencies other than the Swedish krona and for which currency risk has not been neutralised by hedging.

Currency risk
The risk of a change in value of the portfolio as a result of fluctuations in foreign exchange rates.

Derivatives
Collective term for financial instruments whose value is linked to the value of an underlying instrument. Government bond futures are an example of a derivative linked to government bonds as an underlying instrument.

Duration
Measure of interest rate risk. Measures the average outstanding life of all future cash flows (coupon yields and final maturity) for a bond or portfolio of bonds. Is also known as McCauley Duration. See Modified duration.

Enhanced index management
See semi-active management.

Excess return
Arises when a portfolio outperforms its benchmark or reference index. Is the same as active return where the latter exceeds zero.

Fixed income portfolio
Comprised of fixed income assets including interest rate derivatives. The foreign portion of the fixed income portfolio's reference index is hedged in Swedish kronor.

Fundamental analysis
Analysis aimed at predicting a company's future value. Is based primarily on information about companies and their markets, e.g. information about their executive management, strategy, earnings forecasts and financial status and performance.

Global equity portfolio
Consists of equities and equity-related instruments listed on global stock exchanges included in the MSCI World Index. (Note that a share listed on the Swedish stock exchange may be included in both the Swedish and global equity portfolios and such shares are allocated to the intended portfolio at the time of purchase.) The reference index for 2006 is the MSCI World Daily Net Return Index, hedged, and for 2007 the MSCI Daily Total Return Index, hedged.

Handelsbanken Markets Bond Index
Svenska Handelsbanken's return index for Swedish fixed income bonds.

Hedging
The removal of currency risk by swapping exposure to foreign currencies for Swedish kronor using currency futures.

Import basket
Basket of currencies weighted in relation to their respective share of Swedish import revenues.

Information ratio
A measure of risk-adjusted return. Measured as a portfolio's active return compared to its active risk.

Interest rate risk
Measurement of the change in value of a fixed income portfolio after a specified change (usually 1%) in market interest rates.

Investment assets
Used in the annual report to denote the Fund's total capital under management. In the balance sheet, however, investment assets are defined in accordance with generally accepted accounting principles. These require that buybacks, liquid assets and derivatives with negative market value are reported on the balance sheet under items other than investment assets.

Investment grade
Term to describe borrowers assigned an A-rating (A, AA, AAA or equivalent) or triple-B-rating (BBB or equivalent).

Legal risk
Risk of unforeseen losses arising because of legal errors in agreements and contracts, e.g. that an agreement proves invalid or less advantageous than intended.

Liquidity risk
Risk that a financial instrument cannot be divested within a reasonable period without significantly affecting its pricing.

Market risk
Risk of a change in the value of a financial instrument due to changes in equity prices, exchange rates or interest rates.

Merrill Lynch GBI
The Merrill Lynch Global Bond Index is a return index for government and non-government bonds. It is used as the reference index for the foreign part of the fixed income portfolio.

Modified duration
Measure of interest rate risk. Defined as the percentile change in value of a fixed income security as a result of a 1% parallel shift in the yield curve. Calculated by dividing duration (see definition) by the market interest rate plus 1.

MSCI World DNI
The Morgan Stanley Capital International World Developed Markets Daily Net Index. Is the reference index for AP4's global equity portfolio and charts global market performance, including dividends. For 2006, less estimated withholding tax (Daily Net Return, DNR) and for 2007 with no such deduction (Daily Total Return, DTR).

Net contributions
Difference between annual pension contributions to the national pension system and disbursed pension payments.

Non-government bond
Bond carrying a higher credit risk than a government bond, for instance a corporate bond.

Normal portfolio
The asset allocation assessed as most closely corresponding to the Fund's general long-term objective. The composition of the normal portfolio is decided by the Fund's Board of Directors following ALM analysis. See also strategic portfolio.

Operational risks
Collective term for risk of losses arising through operational disruptions, e.g. human error, deficient systems or shortcomings in instructions or procedures.

Passive management
Portfolio management where portfolio holdings mirror a chosen index in order to match the index return.

Pension liability
The financial commitment to current pensioners plus total pension entitlements accumulated by those in work.

Reference index
Index series against which a portfolio's return and risk is compared, e.g. the MSCI World DNR or SIX Return Index.

Return
Time-weighted return, excluding asset management costs, calculated on a daily basis and assuming that all transactions are carried out at the end of the day. Is used when reporting the financial performance of the portfolio and sub-portfolios.

Risk-adjusted return
The return on a financial instrument or portfolio divided by the level of risk (measured as volatility). If two portfolios offer the same return but differ in volatility, the one with the lower volatility offers the higher risk-adjusted return. This is often measured as an information ratio or Sharpe ratio.

Sector allocation
Active overweights or underweights in different equity market sectors relative to the index in order to outperform the index.

Semi-active asset management
Portfolio management with a somewhat higher active risk than passive management, i.e. resembling index management but with a limited active component. Also known as enhanced indexing/ management.

Sharpe ratio
A measure of risk-adjusted return. Calculated as portfolio return minus risk-free interest and divided by portfolio volatility.

SIX Return Index
Reference index for the Fund's Swedish equity portfolio. Charts the market performance of companies listed on the Stockholm Stock Exchange's A and O lists, including dividends.

Strategic allocation
Medium-term deviations from the normal portfolio's asset allocation, currency exposure, duration, etc., aimed at enhancing returns and risk characteristics in the strategic portfolio. Strategic allocations are decided by the board of directors based on the normal portfolio and medium-term risk and return forecasts. See also strategic portfolio.

Strategic portfolio
The distribution of assets deemed to correspond best to AP4's long-term objectives and targets. Its composition consists of the normal portfolio adjusted for strategic allocations. The strategic portfolio thus determines the benchmark index against which the Fund's risk and return are compared.

Swedish equity portfolio
For 2006, the portfolio consists of equities and equity-related instruments listed on the Swedish stock market and unlisted Swedish shares and investments other than holdings in AP Fastigheter. The reference index for 2006 is the SIX Return Index. In 2007, the Swedish equity portfolio will be divided into three components: large-cap listed companies with the SIX60 Return Index as reference index, other listed companies with the SIX60 Return Index excluding companies on the SIX60 Index as the benchmark index and unlisted companies, for which the SIX Return Index plus four percentage points will be the reference index.

Tactical asset allocation
Active position-taking between different asset categories or regions in order to outperform the index.

Tracking error
See Active risk.

Volatility
Risk yardstick that corresponds to the measured standard deviation of the return on an asset. It shows the extent to which returns vary.

Yield curve
Graph created by plotting the market interest rates of a particular class of security according to maturity.

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