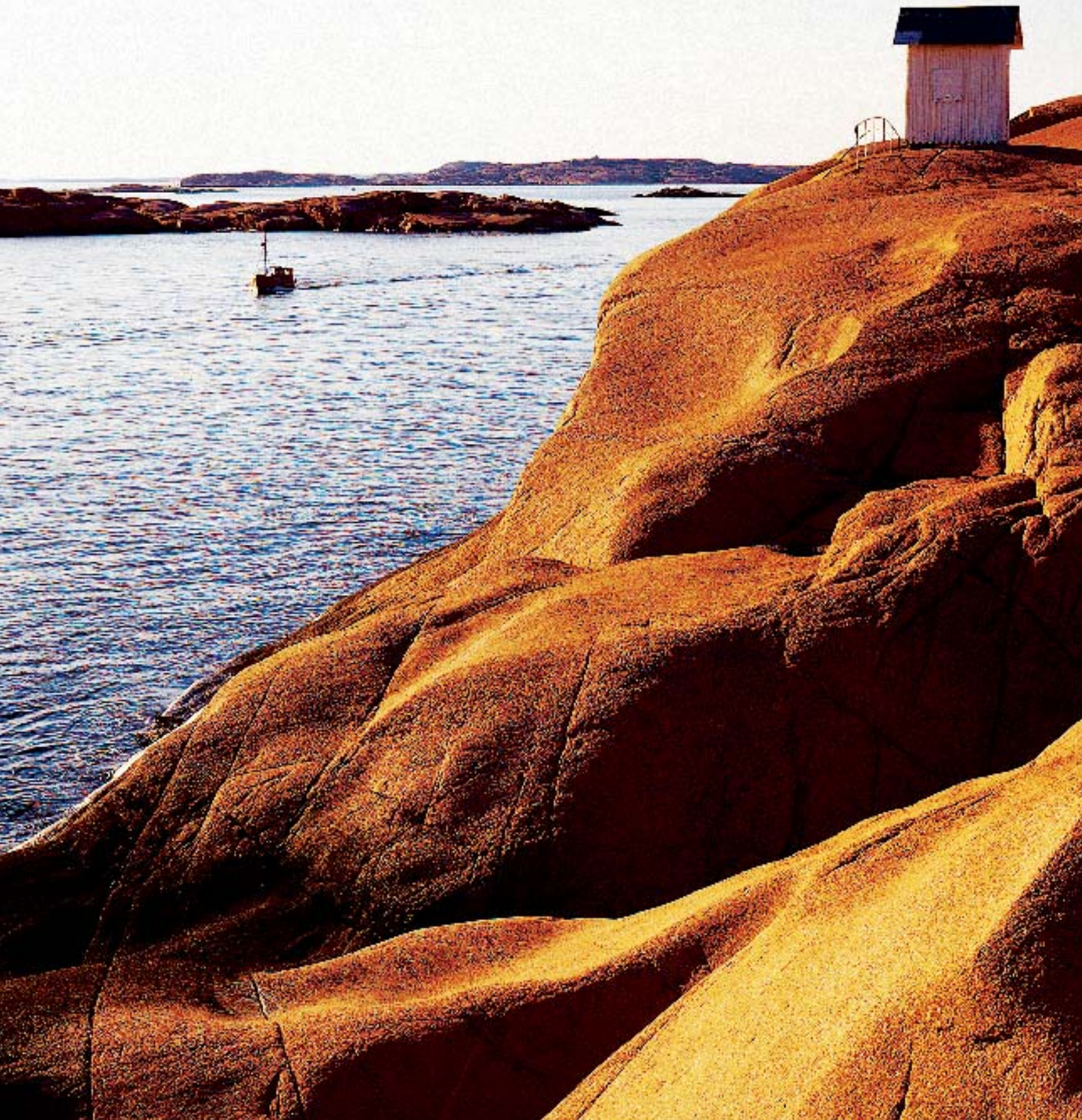




Andra AP-fonden
Second Swedish National Pension Fund - AP2

Annual Report 2003



Presenting the Second AP Fund

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Theme for the year: the Second AP Fund's combined holdings represent a local presence on the Swedish market as well as a global presence on the world's international stock markets.

The stock exchanges featured in the 2003 Annual Report are a selection of stock exchanges in different parts of the world on which the Fund is represented. Turnover 2003 translated into SEK (translated at the rate applied on December 31st 2003). Source: World Federation of Exchanges (FIBV).

Unless otherwise stated, the portfolio assets referred to in this report are "allocated exposures". In addition to booked market values, these also refer to allocated (but not yet invested) liquidity for the specific class of asset, and the liquid funds held as collateral for positions already taken in derivative instruments. Classes of asset, derivative instruments and liquid funds are reported individually in the balance sheet at market values.

The capital assets invested in Sweden's publicly financed national pension system are managed by "buffer funds", which invest these assets in the capital markets. The joint regulations governing investment by the First to Fourth AP Funds permit investment in several different classes of asset and on different markets.

The Second Swedish National Pension Fund/AP2, located in Gothenburg, started operations on January 1st 2001. During 2002 and 2003, the Fund has progressively developed and implemented its strategies and infrastructure to become a modern and internationally focused asset management organisation.

The Board of the Second Swedish National Pension Fund/AP2 is appointed by the Swedish Government. Each director is appointed on the basis of his/her individual ability to further the Fund's management goals.

The aim of the Second Swedish National Pension Fund/AP2 is to ensure that the Swedish pension assets for which the Fund is responsible are invested to generate a maximum long-term return at minimum risk, supported by efficient and professional asset management techniques.

The Second Swedish National Pension Fund/AP2 is determined to be the most successful Swedish pension fund manager, with respect to the long-term return generated on invested assets. The Fund shall achieve this through the successful in-house management of assets and skilled "management of managers".

2003

in brief

- The capital assets of the Second Swedish National Pension Fund/AP2 totalled SEK 140.4 billion on December 31st 2003, an increase of SEK 23.3 billion compared with the preceding year. During the year, the Fund noted a net inflow of SEK 2.6 billion. The Fund posted a total return on invested assets of 17.7 percent for the full year 2003. Net profit for the year totalled SEK 20.7 billion.
- The sharp growth in Fund capital may be attributed in part to the fact that it maintained a high allocation of equities throughout the year, in conjunction with sharp upswings on the world's leading stock markets.
- During 2003, portfolio management of market listed assets has focused increasingly on active management and absolute yield requirements. This has applied both to the Fund's internal asset management activities and to its substantial portfolio of externally managed assets. Fund management of equity and fixed-income portfolios has focused on steady diversification, both in classes of asset and geographical markets. The intention is to secure a stable return on investment and further diversification of risk.
- Towards the end of 2003, the Second Swedish National Pension Fund/AP2 finalised its strategic portfolio for 2004. The general allocation of approximately 60 percent equities and about 40 percent fixed-income instruments remains valid.

Three-year review

	2001	2002	2003
Fund capital, SEK bn	133.5	117.1	140.4
Inflows ¹⁾ , SEK bn	4.5	5.0	2.6
Net result, SEK bn	- 5.0	- 21.4	20.7
Total ROI, %	- 3.7	- 15.3	17.7
Active return incl.			
Fund operating expenses, %	1.7	0.4	- 0.8
FX exposure, %	10	7	8
Under active management, %	37	62	89
Under external management, %	82	38	45

1) Comprised partly of the Fund's share of the annual surplus in the national pension system, partly of inflows from the Liquidation Fund and special funds.

Amounts in Swedish kronor are given as SEK k (thousand), SEK million or SEK m (million) and SEK billion or SEK bn (thousand million).

Andra AP-fonden is officially translated as the Second Swedish National Pension Fund/AP2. In body text, for convenience, this is shortened to the Second AP Fund.

Chief Executive's review

After three years of declining stock markets, 2003 marked something of a turnaround. The Second Swedish National Pension Fund/AP2, which has maintained its consistent commitment to a policy of long-term investment, has been able to report a highly satisfactory result for 2003. The net result for the full twelve months is SEK 20.7 billion. The implementation of a consistent and long-term policy, and the exercise of patience, produces results when the fundamental analysis is correct.



The financial industry has had a difficult time in the past few years, with many players finding themselves forced to post negative results. This has also led to partially justified criticism that the industry often acts too independently and uncritically, intensifying negative stock market trends, while positive movements can result in explosive growth. There are, of course, good reasons for increased clarity and openness, more qualified advice and some serious soul-searching and increased humility on the part of the financial industry, when it comes to conditions and professional practice within the field of asset management. At the same time, it is equally important to remain aware of the fact that, over the long term, a well-functioning market economy with clear principles and fixed game rules can adjust excesses in market rates. Which is precisely what has happened in the past few years.

The Second Swedish National Pension Fund/AP2 is one of the four large “buffer” funds that make up the Swedish national pension system. The task of these funds is no easier but is more clearly defined than may perhaps be the case for many other fund managers. Our task is to maximise the return on invested assets at a minimum of risk, while addressing the increasing importance of environmental and ethical issues related to these assets. We also benefit from being able to operate on a long-term basis. In broad terms, this means that, seen in the context of the national pension system, where some 90 percent of the assets may be considered as a real-interest bond, the remaining portion shall be exposed to a certain equity risk – although not more than required to satisfy the established target of an annual real return on investment of not less than 3.5 percent. In the case of the Second Swedish National Pension Fund/AP2, this has involved the following diversification of risk

over the twelve month period: about 60 percent in equities and 40 percent in bonds and real estate.

To ignore such an investment strategy, geared to long-term objectives, when the task and goal have already been clearly established, would deny the very purpose of the buffer funds. Quite apart from the issue of a required return on investment, the Fund would be operating on the basis of a false risk profile, and investment activities would become too subject to an opportunistic approach. This would not benefit the pension system as such or create any added value for current or future pensioners. Furthermore, it would risk discrediting one of Europe's most stable pension systems.

The net result (SEK 20.7 billion) is more than double the Fund's anticipated long-term return on investment with the current portfolio of assets.

A solid return ensures future stability

2003 was a good year for the Fund, which generated a 17.7 percent return on reported total assets of SEK 140.4 billion. The dramatic nature of the Fund's performance is reflected in the approximately SEK 40 billion improvement, compared with the result for the preceding year. The result for the full twelve months was SEK 20.7 billion. The Fund's chosen benchmark index reflects the composition of the strategic portfolio, which has generated a better absolute return than portfolios more closely linked to the broad



indexes (SIXRX and MSCI World) would have done. Compared to the Fund's overall index for market-listed assets, the relative return amounted to minus 0.5 percent. If we compare our return to the "broad" indexes, the Fund would have shown a positive return on investment. The net result is more than double the Fund's anticipated long-term return on investment with the current portfolio of assets. Since its inauguration, the Fund has achieved a surplus return on investment of 0.6 percent per annum, relative to benchmark index.

An open culture promotes commitment and a will to succeed

Successful asset management relies on effective interaction between individual staff members on a day-to-day basis. It is also the result of a holistic and professional approach, founded on solid values. The intention is that each and every Fund employee shall strive to create a positive and open corporate culture, establishing an appropriate climate for the development of responsible and dynamic staff. During the year, the Fund has conducted an in-house project to clarify its strategy for the future. This project, entitled "Målbild 2006" (Goals 2006), aims to clarify the Fund's goals over the next three years and to establish a joint vision and set of values for all employees.

Asset management in focus

The Fund has maintained its revised management strategy, involving an increased degree of active asset management, throughout the year. Increased diversification of risk, well-developed control routines and thorough analysis are central to the Fund's asset management operations – whether under internal or external management.

The Fund has started to cooperate with a number of new partners during the year, while others no longer par-

ticipate in its activities. Still others have had their mandates and contract conditions changed. All this forms a natural part of a process that is continuously focused on developing the best solutions. Continuing this policy, the Fund plans to focus on consolidating its role as professional investment manager in 2004. This will involve raising the quality of both the internal and external management of assets, clearer definition of that aspect of Fund activities conducted in compliance with the demand for an absolute return on investment, increased exposure to "growth markets" and the adoption of a more active approach to tactical allocation.

Active shareholders wanted

Definitions of "active shareholders" and views about their role in a globalised world differ sharply. There is no doubt at all, however, that the way shareholders exercise their power has a decisive impact on companies and on their economic growth. The Fund's recipe for better shareholder control is transparency, accountability and reasonableness. In connection with specific issues relating to the good conduct, ethics and appropriate business practice of individual decision-makers, personal responsibility is the most important. "Shifting the blame" onto someone else can never be acceptable.

The Fund's position on various shareholder issues is stated in the corporate governance policy, which is subject to annual revision. The Fund's policy with respect to governance issues is to progress steadily towards a more explicitly active approach.

Looking ahead

Normally speaking, we know very little about the future. Having said this, there are grounds for increased optimism over expectations that 2004 will see an economic recovery with relatively solid growth, led by the USA and China. The economic picture in Europe continues to be more fragmented. This optimism must nevertheless be tempered by the possibility that a number of large national deficits, in particular the US deficit, could limit both the vigour and duration of any economic recovery. This said, financial market indicators also point towards an ongoing positive trend.

At the Fund, the work of refining our professional skills continues. We are not afraid to test the limits in our approach to "conventional" asset management. We believe in our chosen strategy and working methods, but we retain an inherent flexibility that allows us to respond to change and to develop new solutions.

Gothenburg, February 2004

Lars Idermark
CEO

Greetings from Tokyo



Tokyo Stock Exchange

The Tokyo Stock Exchange was formally established in May 1878, and trading started on June 1st of the same year.

Turnover 2003: SEK 15,331 billion.

The Second AP Fund has assets amounting to approximately SEK 5 billion invested in the Tokyo Stock Exchange.

Investment strategy with increased focus on active asset management

The Second AP Fund's board of directors evaluates investment policy on an ongoing basis. The revised ALM (Asset Liability Modelling) study forms an important part of this work, providing the basis for the board's decision regarding the composition of the Fund's benchmark portfolio. The study conducted in 2003 has led only to minor changes in the composition of this portfolio. The proportion of assets under active management and subject to an absolute return on investment will continue to increase.

When the new AP funds were formed in 2000, one important difference was the freedom to invest a substantially greater proportion of the assets in equities markets and foreign markets. These new investment regulations were a response to the fact that funds with investment portfolios totally dominated by fixed-income instruments were judged incapable of generating the required long-term return on investment. During 2001, its first full operating year, the Second AP Fund conducted a comprehensive reallocation of its portfolio assets, involving sales of Swedish fixed-income instruments and purchase of foreign equities. By the late autumn of 2001, the Fund had achieved parity between the composition of the actual portfolio and the benchmark portfolio approved by the board. Described in the simplest terms, the composition of the portfolio during 2001 was 60 percent equities and 40 percent fixed-income instruments and real estate.

In 2002, despite the continuing decline of global stock markets, the Fund's board decided to maintain the high allocation of equities featured in the benchmark portfolio for 2003. The new benchmark portfolio was refined in terms of asset allocation on different markets and the asset management style to be adopted. In light of the sharp recovery staged by the world's stock markets in 2003, it is

now clear that this was the correct strategic decision – and one that has contributed SEK 21 billion in capital growth.

The board's decision concerning the Fund's benchmark portfolio for 2004 was preceded by a new analysis and

In light of the sharp recovery staged by the world's stock markets in 2003, it is now clear that this was the correct strategic decision...

review of the factors that are thought to promote successful asset management. The most important part of this process has been the revised ALM study produced at the end of 2003. The new study concludes that there are no changes in the liability or asset side of the national pension system that would justify any significant changes in the composition of the current portfolio. In broad terms, therefore, the 60/40 ratio between equities and fixed-income instruments remains valid, apart from certain adjustments concerning the definition and content of each class of asset, and the way various classes of asset are to be managed. The process of increasing the degree of active asset management, initiated

in 2003, continues. The policy of coopting external fund managers to handle a substantial share of the Fund's assets is also being maintained.

The role of the AP funds in the new national pension system

It is worth stressing that the AP funds, although important, form only a limited part of the overall pensions system. A rough calculation shows that Sweden's combined pension liability amounts to approximately SEK 5 000 billion. Some 90 percent of this liability will be financed from taxation and other charges levied at source, according to the "pay-as-you-go" approach, whereby the economically active section of the population pays on an ongoing basis for those that have already retired from employment. The remaining amount, about 10 percent or SEK 500 billion, consists of assets that have been invested by the AP funds. The first net disbursements from these funds are expected to be made around 2010. By then, forecasts suggest that the ongoing payments to the national pension system will no longer be adequate to cover pension entitlements. Consequently, only a very small proportion of the Swedish pension system's total assets, currently about five percent, are placed in equities. If the AP funds are to meet their long-term commitments, they must generate an average real annual return of some 4–5 percent. Historical data clearly demonstrates that such a high long-term return can only be achieved with a portfolio that features a relatively high percentage of equities.

The new benchmark portfolio

The changes in the strategic allocation of assets for 2004, compared to earlier, are relatively small. The difference between the benchmark portfolios for 2003 and 2004 is that Alternative Investments are now defined as a new class of asset that comprises asset classes Real Estate, Private Equity Funds and Hedge Funds, and that the Fund's assets will be broken down into liquid and non-liquid assets. The intention is to facilitate a more accurate ongoing attribution of asset management performance.

Asset class Alternative Investment will constitute five percent of the Fund's benchmark portfolio. The asset class includes Real Estate (3%), Private Equity Funds (1%) and Hedge Funds (1%). These are not new investments. They already formed part of the Fund's portfolio, but have now been gathered together to form a separate asset class. Consequently, the new benchmark portfolio will feature one-percent declines for asset class Equities and asset class Fixed-Income Instruments respectively.

Liquid and non-liquid assets

The Fund's portfolio comprises assets of varying liquidity. The liquid assets consist of equities, bonds and foreign exchange, while the non-liquid assets consist of real estate and private equity funds. To ensure that the ongoing review of yield levels and risk is accurate and fair, all assets should be assessed on the same occasion and with the same periodicity, which until now has not been possible. Non-liquid

The Fund's new benchmark portfolio

	Benchmark portfolio, %	Permitted interval, %
Swedish equities ¹⁾	20	15–25
Foreign equities, hedged	31	20–40
Foreign equities, non-hedged	5	4–17
Foreign equities, emerging markets	3	0–4
Swedish fixed income instruments, nominal	16	10–25
Swedish fixed income instruments, real	5	2–8
Foreign fixed income instruments, nominal	15	10–25
Real estate	3	0–5
Private equity funds	1	0–5
Hedge funds	1	0–2

1) Consists of the following: SBX (75%), OSX equally-weighted (25%) and Carnegie Small Cap Index (10%).

assets also pose a problem where rebalancing is concerned, as this is not so easily achieved with this type of asset.

To enable effective performance attribution of the active asset management process, the liquid portion of the portfolio, as well as the non-liquid portion, is monitored on the basis of their individual characteristics. The Fund's total reported return will include the yield on both portions of the portfolio, while the active return will be calculated in comparison with the liquid portfolio's development.

Active management ensures greater focus on absolute return

During 2003, the Fund has progressively implemented a style of management that has improved the diversification of risk while simultaneously satisfying the Fund's long-term return requirements. A consistent element of this strategy is the increase in the amount of capital under active management and subject to the requirement for an absolute return on investment. The increased focus on this type of asset management is dependent on access to skills which cannot be built up within the Fund. For this reason, the Second AP Fund manages a significant proportion of its assets, about 45 percent, with the assistance of external asset managers. During the year, the Fund has cooperated with more than 35 external managers, primarily in equities and private equity. During 2004, it is likely that the Fund will also initiate external management of certain fixed-income and tactical asset allocation mandates. Right from the start, the Fund's

IT system was complemented with a web-based system capable of importing trades conducted under external management. This means that all positions held on the Fund's behalf may be accessed on a day-to-day basis and subjected to the Fund's business control and performance-evaluation routines.

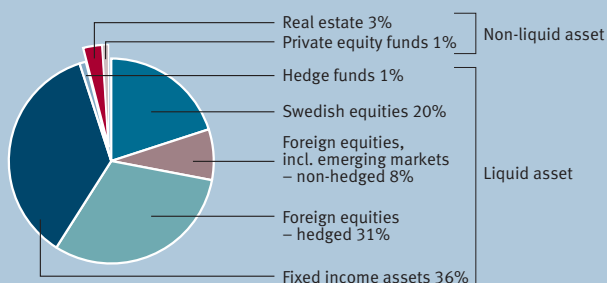
Quite apart from gaining access to specialist competence in the management of assets outside Europe, the significant proportion of assets under external management also offers

Although the cost of delegating such a substantial share of the portfolio to external fund managers is considerable, the advantages outweigh the cost.

opportunities for their speedy and flexible reallocation. One reason for implementing such a reallocation may be a more effective utilisation of the Fund's active risk, backed by a continuous risk budgeting process.

Although the cost of delegating such a substantial share of the portfolio to external fund managers is considerable, the advantages outweigh the cost. In addition to increased flexibility and diversification of risk, active management is expected to generate an excess return over time.

Benchmark portfolio 2004



Gradual implementation

The degree of active asset management and the focus on an absolute return will intensify over the next few years.

At the same time, the composition of the portfolio will be analysed and evaluated continuously, to determine the success of the Fund's active management. Another factor determining how fast the portfolio can be implemented will be the availability of specialised external asset managers with the appropriate expertise and experience.

Risk budgeting – essential to active management

The Second AP Fund believes that added value can be generated over the long term by actively deviating, to a greater or lesser extent, from the benchmark portfolio. Such active management is intended to generate returns that outperform the benchmark portfolio.

All positions that deviate from the benchmark portfolio involve an active risk. The Fund's total or absolute risk may therefore be considered to consist of two parts: a risk that derives from the composition of the benchmark portfolio (strategic risk), and the "extra" risk generated by temporary deviations from the benchmark portfolio, arising from active management of the assets (active risk). The strategic risk is the clearly dominant element in the Fund's overall risk profile.

The Second AP Fund's board of directors has determined that the Fund may deviate from the benchmark portfolio in an amount corresponding to a tracking error of three percent. The risk budgeting process is designed to optimise this mandate for exposure to active risk. The process aims to resolve issues such as in which asset classes deviations from the benchmark portfolio will offer the greatest potential gains, and the extent of the active risk that may be allocated to respective mandates to maximise the possibility of generating an active return on invested assets.

In other words, risk budgeting is about optimising the allocation of active risk to generate the best possible active return.

The risk budget process

The Second AP Fund's risk budget is based on the "top down" method. This process involves first dividing the active risk between those asset classes that may deviate from the benchmark portfolio – in principle, this applies solely to "liquid" investments. Later in the process, the active risk and/or capital is distributed among individual mandates according to a structured methodology. The latter part of this process is conducted in close consultation with in-house portfolio managers, to ensure that the quantitative and qualitative aspects of different external managers are evaluated in the most effective manner. The complete risk budget comprises risk limits, target intervals for active risk and target values for the active return on individual mandates.

Looking ahead

The factors affecting the benchmark portfolio's return are quite distinct from those that influence active return. The return generated by the benchmark portfolio is largely dependent on macroeconomic factors such as the rate of GNP growth and the interest rate, while the return generated on actively managed assets is entirely dependent on the skill of the chosen asset manager, and the opportunities offered on the markets in which individual managers operate. New opportunities are presented due to the mutual independence of the factors affecting respective sources of increased return on investment. By reducing risk in the benchmark portfolio and simultaneously increasing the level of active risk, the Fund's total risk can be reduced without compromising the anticipated return.



STOCKHOLMSBÖRSEN · SWEDEN

Stockholm Stock Exchange

Formal trading at the Stockholm Stock Exchange was formally established in 1863 by royal decree, which permitted the sale of bonds, promissory notes and equities.

Turnover 2003: SEK 2,195 billion.

The Second AP Fund's current holdings in the Stockholm Stock Exchange amount to about SEK 25.6 billion.

Structure and staff

The Second AP Fund currently has a staff of 45 people, 39 of whom are permanent employees, spread among three units. During the year, the Fund continued to implement a number of strategic measures within the personnel field, including the development of a joint vision for its HR activities. Other aspects highlighted during the period have been health, “on-the-job” training programmes and the establishment of guidelines with respect to business ethics and forms of remuneration.

In the three years since its inauguration, the Second AP Fund has established an organisation from the ground up, now comprising a staff of 45 people. Of these, 39 are permanent employees and 6 are employed on a project or hourly basis. The organisation consists of three units: asset management, business support and the executive management and staff functions. The Second AP Fund is actively committed to integrating the different units to establish a joint approach to processes and work flows.

Vision 2006 – joint values base

One of the in-house priorities of Human Resources (HR) during 2003 has been to establish a joint strategic vision for the Fund's activities up to the year 2006. This resulted in a project where all employees participated in four separate

seminars, addressing issues such as ethics, values, organisational structure and forms of cooperation. Based on the results of the consequent discussions, a number of in-house working committees were established and, during the autumn, developed proposals for routines that could be put in place to address these issues. These proposals refer partly to broader areas of concern, such as criteria for evaluating individuals and groups, or how various intra-Fund processes can be better coordinated and simplified, and partly to issues that are more narrowly focused on information and personnel amenities. The project is intended to establish a shared vision and set of values that can be endorsed by all employees, as well as to promote concrete improvements in a number of specific work processes.

“On-the-job” training programmes

The Fund's employees are able to participate in a range of short or extended training programmes to develop their professional skills. As well as participating in specialised



We here see 37 of the Second AP Fund's 45 employees, gathered on the steps of Gothenburg's Town Hall.

extension courses in their respective fields during the year, Fund employees have also attended educational seminars on broader topics such as Swedish and international politics, economic theory, ethics and the environment. Members of staff have also made several study visits to other pension funds, external asset managers, market analysts and other professional associates, mainly in Sweden, Great Britain and the USA. This ongoing exchange of professional experience and insights is essential to both the individual and collective “on-the-job” training process.

The entire staff meets at regular intervals to receive ongoing updates about relevant topics. As well as the type of information relating directly to employees’ specific job responsibilities, external speakers are also invited to come and address issues connected to the Fund’s sphere of activities. Guest speakers in the past twelve months have included Professor Thomas Hedner, who talked about the SARS epidemic, and Britt-Marie Mattsson, from Göteborgs-Posten (a major Gothenburg daily), who spoke on the global situation two years after the “9/11” terrorist attacks. Other speakers addressed topics ranging from vocational ergonomics and healthcare to drug abuse.

Health – creating long-term value

The Second AP Fund is actively engaged in ensuring that physical exercise and health forms an integral part of its corporate culture, and they are included among the goals established for individual job development plans. The Fund supports a variety of activities that may inspire and encourage members of staff in their wish to enjoy a healthy lifestyle. During 2003, for example, members of staff have participated in a range of sporting activities. More than two-thirds of Fund employees exercise regularly at various training facilities. Topics such as work environment, health and lifestyle issues are addressed in close cooperation with the Fund’s occupational health service. The number of days lost to ill health is extremely low, and no employee sought extended sick leave during 2003.

Guidelines on ethics, personal trading in securities and forms of remuneration

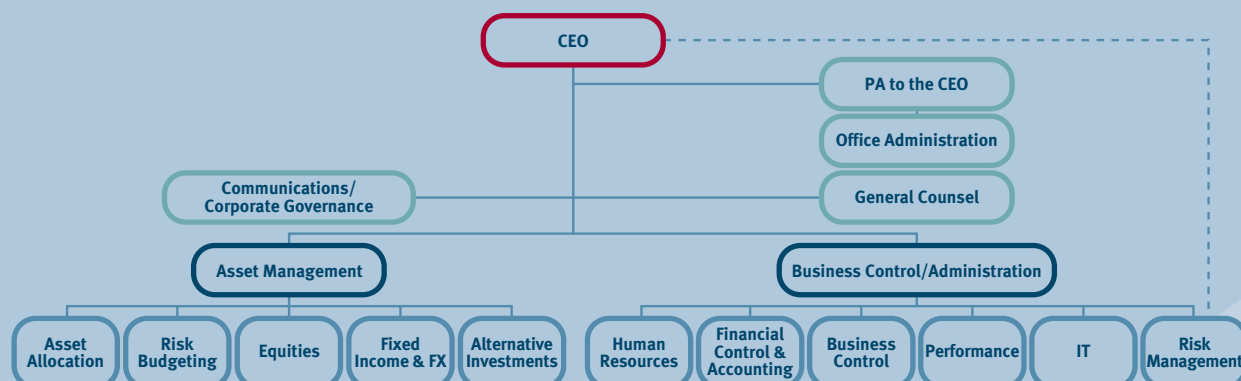
In the past year, the Swedish business community has been engaged in an intense debate concerning business ethics, morality and executive compensation programmes. In view of the fact that the AP funds are charged with managing public assets, and have interests in many Swedish and foreign companies, it seems only reasonable to briefly review the Fund’s own in-house guidelines concerning these areas.

In recognition of the Fund’s status as a public authority, it must comply with the guidelines established for other public organisations, which for example include special regulations governing challengeability (conflicts of interest), the giving and receiving of gifts, public disclosure and control. Furthermore, the employees of an organisation engaged in the management of capital assets must comply with the profession’s own rules of conduct. Implementation of so-called “insider” legislation is crucial, both in terms of the Fund’s professional role and when its own staff engages in securities trading. In cases where Fund employees trade in securities on their own behalf, the Fund applies the regulations adopted by the Swedish Association of Stockbrokers, in addition to the general regulations governing insider trading. Complemented by a number of additional clauses relating specifically to the Second AP Fund, its employees and board directors shall submit regular reports of all trades in securities.

The only form of remuneration awarded in the Second AP Fund is a fixed salary. The Fund has no bonus system.

HR activities in 2004

A new personnel strategy will be implemented in 2004. This new strategy comprises long-term guidelines for leadership, recruitment, skills development and communication. This personnel strategy is designed to contribute to a more efficient organisation and to help realise the Fund’s ambition of becoming a modern and attractive employer. Special emphasis will be placed on leadership issues.





Every year, the Annual Report of the Second AP Fund features an article written by an independent external contributor. This year, our contributor is Ole Settergren, who describes how demographic changes will affect future pensions.

Ole Settergren, 39 years old, is an economist and director of the pensions department at the Swedish Social Insurance Board. As First Secretary to the Swedish Ministry of Health and Social Affairs, he was one of those who designed Sweden's new national pension system.

Gale warning for global pensions?

Factors such as longer life spans, falling birth rates and the fact that persons born in the “baby boom” following World War II are now approaching their 65th birthday have all contributed to gloomy forecasts about the threat to the pension systems of the world’s developed economies. This issue has long attracted considerable attention, since the national pension systems constitute both the largest financial commitment of these countries and the one most clearly affected by demographics in terms of age distribution. The number of voters of pensionable age is another significant factor.

In the age distribution of the national population, the trends are very similar throughout the OECD. On closer examination, however, the individual countries reveal some interesting national variations. Probably the greatest deviation from the general trend is in the USA, with its high birth rate (2.05 children per woman) and greater net immigration (0.33 percent of the total population). At the other end of the scale are Spain, Italy and Japan, with birth rates around 1.25 children per woman, and low net immigration. In Sweden, the corresponding figures are currently 1.6 children per woman, and a net immigration of 0.17 percent.

The general trend towards a larger proportion of elderly citizens also entails an increase in the number of non-productive citizens compared to those gainfully employed. The workforce as a whole may even decrease in absolute terms. Some countries, including Germany and Japan, predict that their overall populations will decline, an unprecedented development in countries at peace and with a high material standard of living.

The overhaul of Sweden’s national pension system – possibly the country’s most sweeping political reform since the end of World War II – was undertaken partly in response to demographic forecasts that warned of the population’s steadily rising average age and of “inadequate” replenishment with new taxpayers at the base of the population pyramid. The forecasts published in the early 1990s revealed that in proportion to GDP the disbursements of the national pension system would have risen in the next 50 years by 4–6 percentage points – an extremely sharp increase from an already high level. The reform of the Swedish pension system has limited the forecast increase in disbursements to just over one percentage point. Furthermore, the reform of the system has entirely eliminated the risk that the contribution rate will have to be raised to finance pension payments.

Political failures – not demographics

In parallel with the demographic ageing process and the maturing of the national pension system, there has been

a notable change in the willingness to continue gainful employment into old age. Paradoxically, as health has improved, as work has become less physically demanding, and as the average age of the population has risen, the age at which people retire from working life has fallen dramatically.

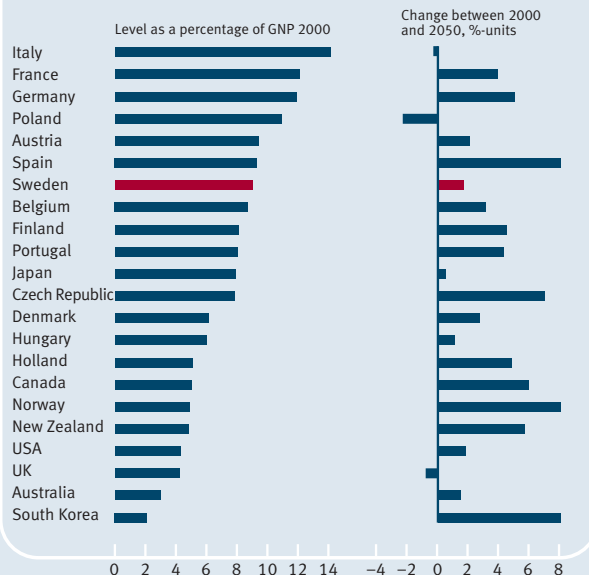
The tendency to early withdrawal from working life is at least partly due to the functioning of the national pension system, the tax system and supplementary pension schemes, which more or less subsidise early retirement.

Reforming the national pension system to remove the financial incentives for early retirement would make a substantial contribution to conserving public resources. The potential improvements are greatest in the major EU member states of France, Germany and Italy.

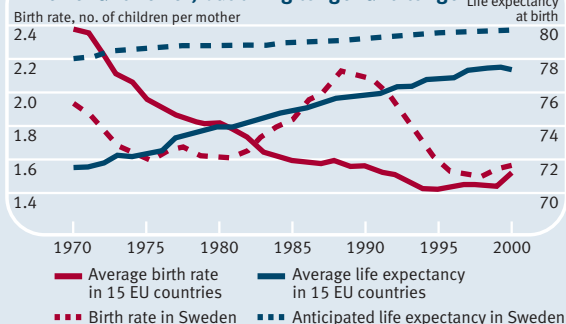
A financially stable system

In the reformed pension system, the capitalised value of the Swedish state’s pension liabilities, based on the current legislation and contribution rate, can never exceed the total value of the flow of contribution revenue and the combined assets of the AP funds. This statement remains valid whatever happens in terms of economic or demographic trends. Absolute financial stability has thus been assured. The system’s financial stability is partly due to its form of indexing. In the new system the pension credits are indexed by the growth/decline in average income, and the indexing of pensions is based on the change in average income. Probably the most important stabilising element of the system, however, is that pensions are calculated on the basis of actual average life expectancy, using so-called “annuitization divisors”. Every year, the Swedish Social Insurance Board calculates the annuitization divisors for the group, or birth cohort, of persons celebrating their 65th birthdays in that year. The annuitization divisor reflects the remaining average life expectancy of the cohort from 65 years onward, with no upper limit, and with interest of 1.6 percent included when the pension is drawn. The interest may be seen as an advance on future income growth. This

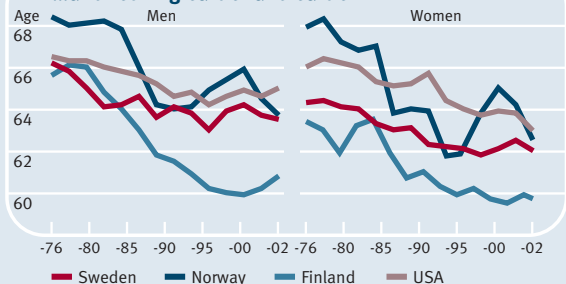
Public expenditure on old-age pensions



Fewer and fewer, but living longer and longer



...and retiring earlier and earlier



How much longer we are living

Year born	65 th birthday	Forecast annuitization divisor at 65	Effect of changed life expectancy on pension, %	Pensionable age to neutralise impact of changed life expectancy on pension	Life expectancy after 65, women and men
1940	2005	15.7	—	65 years	18 years 6 months
1945	2010	16.1	- 2	+4 months	+6 months
1950	2015	16.4	- 4	+7 months	+11 months
1955	2020	16.7	- 6	+10 months	+16 months
1960	2025	17.0	- 7	+13 months	+20 months
1965	2030	17.2	- 9	+16 months	+24 months
1970	2035	17.5	- 10	+18 months	+28 months
1975	2040	17.7	- 11	+21 months	+32 months
1980	2045	17.9	- 12	+23 months	+35 months
1985	2050	18.0	- 13	+25 months	+38 months

Sources: RFV, OECD and SEB.

advance is recouped in the system by indexing pensions by the growth in income, less 1.6 percent. Finally, there is “automatic balancing,” which ensures that the liabilities of the pension system can never exceed the total value of its future contribution revenue and the combined assets of the AP funds.

The forecast increase in pension disbursements, as shown in the diagram above, has been erroneously interpreted by some as evidence that the financial stability of the Swedish pension system has been overrated. This misunderstanding derives from the fact that in Sweden, unlike most other countries, the national pension system features a degree of funding – the assets managed by the AP funds. One advantage of these funds is that they enable the system to maintain both contribution rates and disbursements at fixed levels, regardless of demographic fluctuations like the post-war baby boom. To cope with these demographic variations, the funds must generate a return on invested assets at least equal in percent to the average growth in income. The average growth in income may be defined as the base rate of the pension system. If the return generated on fund assets exceeds this base rate, the funds may make it possible to maintain fixed contribution and pension levels even when the demographic trend is unfavourable.

The cost of Swedish stability

Statistics Sweden has forecast that our average life expectancy will increase by about 25 days per year, or by just over three years in all, up to the year 2050.

Based on that prediction, the annuitization divisor at age 65 will go up from 15.7 to 18.0 between 2005 and 2050. This increase means that the pension for persons born in 1985 will be calculated by dividing the accumulated pension credit by a number that is 13 percent higher than for those born in 1940. This means that those born in 1985 will receive a pension that is 13 percent lower than those born in 1940 – although both groups will receive the same pension over their lifetimes, since those born in 1985 will receive their lower pensions over a longer period. To compensate for the reduction in annual pension disbursements, the 1985 group will have to work 25 months longer than their predecessors born in 1940. If this change does occur the actual pensionable age 50 years from now will thus be 67.

In common with other countries, Sweden has had to face many problems that have resulted partly or entirely from unwise and ill-considered political decisions. By contrast, the reform of the Swedish national pension scheme was implemented only after thorough analysis of the short- and long-term consequences.

Economic trends 2003

Uncertainty about a recovery of the global economy during the first part of 2003 was transformed into growing optimism during the second half, fuelled by improved incoming economic data and the continuing low level of inflation. The recovery was also more geographically diversified, contributing to a more balanced risk profile in 2004, compared to the previous two years.

During the first half, the USA's GDP increased in line with potential growth, despite uncertainty concerning developments in Iraq during the first three months of the year. Japan also contributed to the global recovery, while the countries of the EMU noted growth below potential. During the summer and early autumn, market indicators suggested that the recovery would be more vigorous than previously anticipated. This resulted in a change of focus, from uncertainty about the timing of the recovery to uncertainty about how long the recovery might last.

After a very weak start to 2003, the financial markets noted an increasingly positive response to signs of imminent recovery, leading to a heightened appetite for higher-risk investments. Globally, equities noted much more vigorous growth than bonds.

Global economic recovery

The turnaround in the autumn gained additional help in the USA from extensive stimulation of the economy, in the form of lower tax and low interest rates. The need for extensive investment further fuelled the cyclical recovery. Positive economic signals were also noted in the countries

of the EMU, although the rate at which these hopes were realised was slower than in the USA and Great Britain. The global upswing helped catalyse the European economic recovery, as demand for European products rose. The breadth of this recovery was limited, however, due to continued weak domestic demand and its uneven distribution between different countries. In Japan, the economy developed better than expected, both during the second and third quarter, due mainly to increased investment activity.

The Swedish economy has remained fairly stable throughout 2003, despite warning signs of weaker public finances. The Swedish Central Bank cut the base rate on three separate occasions during the year, by a combined total of one percentage unit. The politicians have also placed more emphasis than earlier on the need to create better long-term economic growth. Much of the economic debate during the first nine months of the year was coloured by the impending Swedish referendum on the EMU. The result of the referendum appears not to have led to an immediately noticeable negative effect. The increasing strength of the Swedish krona, especially in relation to the US dollar, led some of Sweden's export industries to fore-



cast a decline in profits. Even so, in several cases the Swedish economy posted better results than many of the country's most important competitors on export markets.

As the prospects of a global recovery improved, so too did the assessments of international analysts during the year. At the start of 2003, analysts predicted that the US economy would grow some 2.5 percent, while the forecasts for the EMU were less than 1.5 percent, with Sweden at 2.0 percent. During the first six months of the year, these forecasts were adjusted downward for several countries, due to

Globally, equities noted much more vigorous growth than bonds.

uncertainty over the war in Iraq. With the conclusion of hostilities, the market regained its optimism and prospects improved. Expectations that the USA would spear a global recovery increased as the countries of the EMU continued to fall behind. One reason for this was the growing strength of the euro. The currency rose sharply in value against the US dollar, which was expected to have a particularly negative effect on the export sector.

Low level of inflation despite signs of increased economic activity

Admittedly, the current global downturn is both short and shallow when seen in a broader historical perspective, but almost three years of weak economic activity has built up considerable excess capacity in the major economies. The combination of continuing high growth in productivity in

the corporate sector with a fall in labour costs, especially in the USA, helped to keep inflation low, despite sharp increases in the prices of several raw materials.

This kept interest levels down, in relationship to historical trends as well as growth. Monetary policy has taken advantage of the continuing low level of inflation to keep current interest rates low, while at the same time avoiding the risk of creating major fluctuations on long-term interest rates.

Prospects for 2004

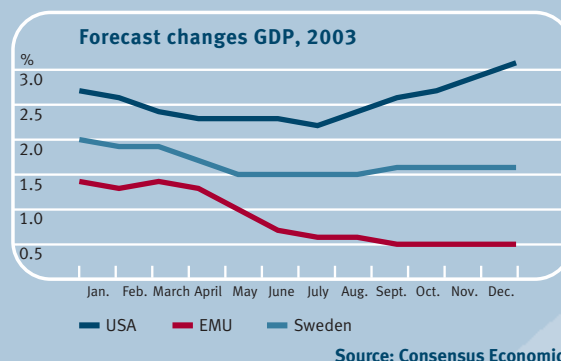
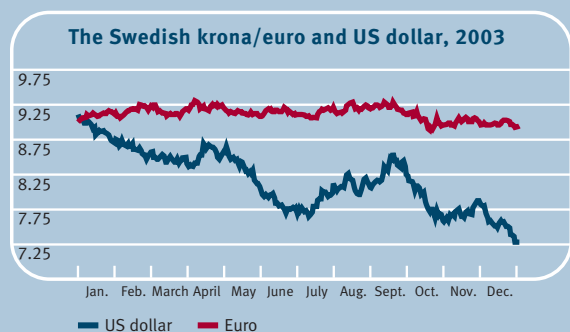
Although opportunities for further fiscal and monetary-policy measures to stimulate the US and European economies are now limited, the prospective risks appear to be better balanced in 2004 than has been the case for the past two years.

The global recovery continues to depend on the USA, which could be a reason for anxiety, given its substantial balance-of-payment and budget deficits. These deficits could trigger an unpleasantly rapid further decline in the value of the US dollar, combined with soaring interest rates.

In several countries, the vital role consumption has played in helping depressed economies has led to a sharp rise in property prices and increased household debt.

The belief in continued expansion in the USA is also connected with a clear move towards increased recruitment levels, in conjunction with the realisation of forecast profits in the corporate sector. If these expectations are not fulfilled, the result could be an accelerated slowdown in household consumption.

At the same time, most market analysts believe that the current upturn is developing at a more relaxed pace than previous recoveries, especially in the USA. This gives grounds for a certain degree of optimism.



Tactical asset allocation

The high volatility of the financial markets in 2003 created a favourable climate for active tactical asset allocation, i.e. small or slighter larger conscious deviations in the composition of the benchmark portfolio. The Second AP Fund has actively benefited from these favourable conditions, as well as initiating negotiations concerning the award of external mandates for tactical allocation.

In terms of the financial market, the year signalled a break in the sharp decline of the world's stock exchanges over the past three years. At the same time, the year 2003 reflected a typical post-recessionary period of recovery, where a plentiful inflow of liquidity and recovery of corporate profits created ideal conditions for the equities market.

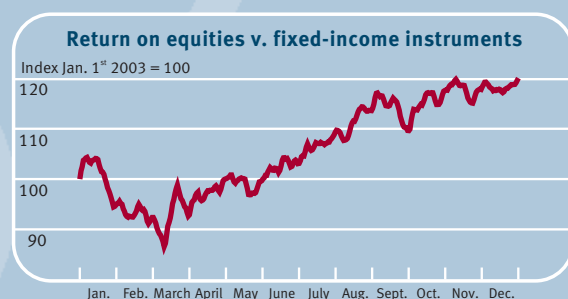
During the first quarter, share prices fell as the conflict in Iraq drew nearer, influenced by the geopolitical risks and widespread anxiety about a sharp slowdown in the global economy. These conditions supported reductions in bond yields. This decline in bond yields was accentuated by the central banks' continued reductions in policy rates, fuelled by fears of possible deflation. However, the unexpectedly rapid outcome of the Iraq conflict gradually increased the market's appetite for risk and, towards the end of March, the equities markets staged a recovery. Interim reports for the first quarter showed signs of an upturn in corporate earnings, coinciding with more favourable economic signals.

This transformed the equities market into something of a sweet spot, and share prices continued to climb in the late spring. During the summer, these highly favourable economic indicators contributed to expectations of continued recovery and higher corporate profits, which became an

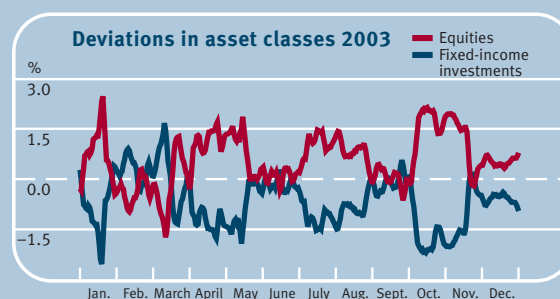
additional driving force on equities markets. The turbulence was transferred to the markets for fixed-income instruments, where US long-term interest rates in particular rose sharply, after bottoming-out in mid-June.

Economic recovery and corporate profits fuelled recovery on equities markets

During the autumn, the economic signals became more consistently favourable, and the outlines of a synchronised global economic recovery became increasingly distinct. Growing confidence of an early recovery in the corporate sector was especially important. During the third quarter, the companies were positively surprised to post unexpectedly large gains in profits. Corporate analysts and other market commentators found reason to up their profit forecasts for the remaining months of the year, as well as for 2004. Consequently, the downturn in September was somewhat parenthetical in an otherwise buoyant stock market during 2003. Even so, the favourable media coverage during the autumn had less of an impact on the financial markets than earlier in the year. Equity markets staged a gradual if rather jerky recovery, as interest rates rose slightly during the fourth quarter.



The diagram shows the Second AP Fund's benchmark index for equities v. the benchmark index for fixed-income investments. When the graph points up, equities generate a higher return than fixed-income investments and vice versa. In 2003, the return on the strategic portfolio for equities exceeded the corresponding benchmark portfolio return for fixed-income investments by about 20 percent.



The Second AP Fund's benchmark index comprises 60 percent equities and 40 percent fixed-income investments and Alternative Investments. The graph shows how actual asset allocations deviate from the benchmark allocations defined by the strategic portfolio.

During the latter part of 2003, market anxieties changed from fears of deflation to worries about the growing risk of inflation. The relatively sharp fluctuations noted by bond markets towards the close of the year reflected this tug-of-war between the need for higher base rates and worries about a new slowdown in the economy.

Krona firms in wake of falling dollar

The rise in the value of the Swedish krona that started in 2002 continued through 2003, although less vigorously. Due to the relatively high proportion of dollar-linked assets in the Second AP Fund's portfolio, the continued decline in the US exchange rate has had a particularly notable impact. The dollar continued to weaken against other currencies during the autumn, a trend that was further stimulated by exchange policy initiatives in September. This decline in the value of the US dollar derives from the American economy's huge deficits. The USA has been struggling with a significant balance-of-payments deficit for quite some time now, and more recently with a growing budget deficit. The country's monetary policy has continued to be highly expansive. In contrast, the Swedish economy has enjoyed relatively good stability, especially with respect to the balance of payments, while even the country's public finances are in better shape.

Second AP Fund's tactical allocation strategy

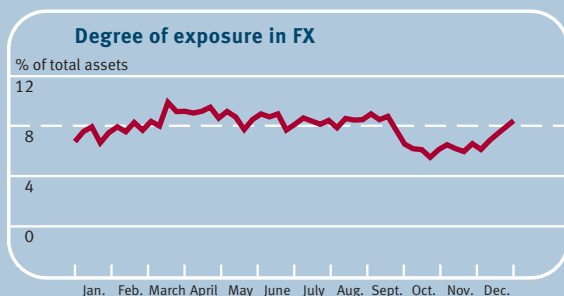
At the start of the year, the Fund was marginally over-weighted in equities, which had gradually been transformed into an under-weight by the end of January, start of February. The reduced weighting in equities created by the market decline was partially counteracted by the Fund's purchase of equities and sale of bonds during January and February. At the turnaround in the beginning of March, the Fund's portfolio of equities was rather under-weighted, being gradually built up to achieve an over-weight by the latter part of the month. This over-weight in equities was maintained throughout the greater part of May. By June, the Fund had achieved an almost neutral weighting in terms of its tactical asset allocation, with a marginal over-weight in

equities. A new over-weight in equities was built up at the start of July. This over-weight was retained until mid-August, when it was reduced. Equities were sold successively during this period, with a view to limiting the over-weight in equities. By the close of August, the portfolio's over-weight of equities was further reduced to achieve a neutral weighting. The goal of neutral weighting was subsequently maintained during the stock market decline in September. In the beginning of October, the Fund once again built up an over-weight in equities, which was sustained until mid-November, when the portfolio reverted to a neutral weighting. Yet another over-weight in equities was created at the start of December. Within the Second AP Fund, tactical deviations in the currency hedge is an active part of the tactical allocation mandate. In the beginning of the year the Fund was over-hedged. During the summer and prior to the Swedish referendum on the EMU, the Fund established a neutral weighting in its portfolio of assets. In September, a new over-hedge was created, which was reduced in December.

Apart from a few exceptions, the positions taken in the Fund's tactical allocation were small. Consequently, a periodically unfavourable rebalancing of the portfolio has dominated the result of this tactical allocation of assets, having a slight negative impact on the Fund's active return on investment from TAA.

External asset-management mandates

During the late autumn of 2003, the Second AP Fond initiated a search for external asset management mandates in the field of tactical asset allocation. The mandates shall generate an absolute return and shall not be measured against any benchmark index. The mandates will require no capital allocation, as the positions will be taken in a range of forward instruments. With this type of asset management mandate, a portion of the Fund's active risk budget is allocated for investment in areas where the Fund anticipates opportunities for a relatively high risk-adjusted return with a relatively low correlation to other parts of the total portfolio.



The diagram shows the Second AP Fund's FX exposure as a percentage of total portfolio assets. The strategic portfolio sets the degree of exposure in FX at eight percent. When the actual degree of exposure is less than eight percent, the Fund's tactical allocation ensures that it is positioned to gain additional benefit, should the Swedish krona appreciate in value.

NEW YORK

The Big Apple



New York Stock Exchange

The activities of the New York stock market date back to 1792, when the first formal contract for trading in stocks was signed.

Turnover 2003: SEK 69,739 billion.

The Second AP Fund's holdings on the New York Stock Exchange amount approximately to SEK 17.4 billion.

Equity management

Global equity markets have been characterised by a mood of optimism during the year. In line with its long-term investment strategy, AP2 has been a net seller of equities during the year. AP2 has continued to increase the share of foreign equities under active management and awarded a number of external mandates. The Fund's equity management made a major contribution to the growth of its capital assets in 2003.

Global stock markets fluctuated dramatically during 2003. The negative trend, which had persisted on global stock markets over the previous three years, continued during the first three months of 2003. However, this trend was broken at the beginning of March, heralding the start of a stable and enduring market upturn. This has been sustained through to the end of the year, in spite of the fact that profit-takings have led to temporary slowdowns. With only a few exceptions, the world's large stock markets have reflected the same trend. The happy combination of a strong general upturn on global stock markets during the last three quarters, in conjunction with the appreciation of the krona against the US dollar, has produced a substantial positive absolute return on investment at AP2.

This favourable trend has continued during the first months of 2004.

Second AP Fund equity management in 2003

As a consequence of the Fund's long-term investment strategy, in which equities account for some 60 percent of total portfolio assets, the Fund sold equities during the latter part of 2003. Even so, the Fund retained a tactical over-weight in equities during the greater part of the year.

The value of the portfolio of foreign equities amounted to SEK 56.7 billion by the close of 2003, SEK 44.8 billion of which was hedged and SEK 11.9 billion un-hedged. The return on invested assets was 22.5 percent. The Fund's benchmark index showed a return of 23.5 percent for the corresponding period. This may be attributed partly to the choice of securities, partly to the Fund's initially limited exposure to emerging markets.

The market value of the Swedish equity holdings increased by 34.4 percent during 2003. During the same period, the Fund's benchmark index increased by 36 percent. The Fund's original benchmark index for Swedish equities, the SIXRX index, posted an increase of 34.2 percent for the same period. The portfolio had an estimated market value of SEK 28.4 billion at the end of the year.

International developments

During the year, the global equity markets have reflected the expectation that the major economies are embarking on a new period of growth. This belief was enhanced by the rapid resolution of the Iraq conflict, even though the situation in the country remained unstable.

The upswing noted by the stock markets in the USA (Dow Jones), Great Britain (FTSE 100) and Japan (NIKKEI 225) amounted to between 15 and 25 percent in 2003. Nasdaq, America's technology dominated exchange, posted a 50-percent upswing, while several "emerging-market" exchanges also posted sharp rises during the year.

The Swedish equities market

One particular factor that had a major impact on the Swedish stock market's index growth was the positive re-rating of the IT, telecom and small-cap sectors. Stocks which declined substantially during previous years have risen sharply during 2003. Technology stocks in particular have enjoyed a strong recovery after several years of decline. This applies especially to Ericsson, which is without doubt the Swedish stock market's most traded share.

A number of major companies were able to post increased profits after personnel cutbacks and other cost-saving measures in spite of the weak economic environment. Industrial engineering companies such as Atlas Copco and SKF were able to report solid profit growth and saw their share prices appreciate.

The upswing noted by the Stockholm Stock Exchange was particularly notable in the energy and IT sectors. While the SBX index rose by 34.6 percent, the upturn in these sectors exceeded 75 percent. The opposite was true of companies in the power-generation sector, which reported a decline of about 3 percent in the year.

Equity management: focus and organisation

In strategic and organisational terms, the Second AP Fund's equity management activities involve a combination of in-

house management in selected sectors, and external management mandates.

These external mandates may be regional, such as North America, or may refer to specific industries, such as finance or pharmaceuticals. The external mandates may also be formulated in terms of a specific risk profile. As per December 31st 2003, 28 percent of the Fund's total equities portfolio was managed in-house, while 72 percent was managed externally.

In-house asset management activities, which focus on European as well as Swedish companies, are conducted in the following sectors: consumer products, IT/telecoms, finance, the pharmaceuticals industry and the engineering and raw materials sectors. These sectors are also handled by external fund managers. Other industries and regions are managed to closely reflect index or by external managers. This specialisation in particular sectors is based on the growing importance of individual asset managers' special competence in specific industries and in the internal logic of such industries, regardless of geographical borders, when assessing prospects for the creation of added long-term financial value.

For this reason, a large proportion of the Second AP Fund's equity portfolios are under external management. An important task for the in-house asset management team, apart from handling the Fund's own portfolios, is therefore to sustain a continual and informed evaluation of the performance of external asset managers. During 2003, the Fund has negotiated a number of additional external mandates. External managers contribute resources in regions where the Fund lacks in-house competence, and will also help to complement the Fund's in-house asset management activities. The intention, apart from generating a surplus return on invested assets, is to diversify risk in the Fund's active asset management activities.

Management of Swedish equities

Prior to 2003, the Second AP Fund changed its benchmark index for Swedish equities. From having previously used the SIXRX index, the Fund's management of Swedish equities

will be evaluated on a rolling five-year basis, employing a combination of three separate indexes. The composition of these three indexes is specified in the Financial review on page 42.

Management of foreign equities

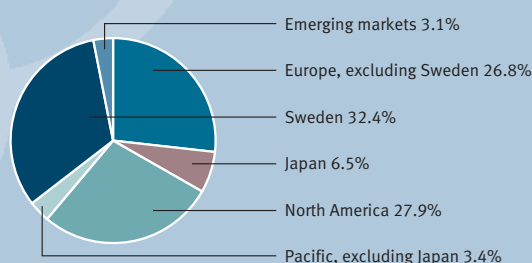
During the year, the Second AP Fund continued to increase the proportion of foreign equities under active management. Changes were introduced in three areas: North America, Europe and the Asia/Pacific Basin. The Fund's in-house management focuses on European equities while American and Asian equities are handled by external managers. In addition to this, the Fund has awarded a number of mandates to external managers for the administration of global equities.

The Second AP Fund's policy of diversification also includes new mandates for emerging markets, for which some SEK 600 million has been allocated for management by two current and one new unit trust, operated by Citigroup Asset Management. Other emerging markets mandates have been previously awarded to Foreign and Colonial, Deutsche Bank, State Street, Pictet and Genesis.

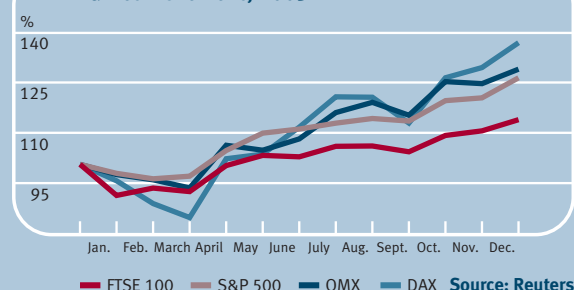
The first steps towards more active management of North American equities were taken during the spring. This involved the transfer of a number of passive portfolios to be managed externally in accordance with an "enhanced index mandate" (management at low risk with a targeted return of between 0.5 and 1.0 percent over the benchmark index). In May and August, a joint total of approximately SEK 9 billion was transferred to Barclays Global Investors to be managed under these terms.

In 2002, the Second AP Fund implemented a sector-based policy for the management of European equities handled in-house. In 2003, the Fund proceeded with this policy, awarding 13 new European sector-based mandates to external asset managers, covering consumer staples, consumer discretionary, telecom, finance, healthcare and IT. Mandates have been awarded to the following external managers: Citigroup, Goldman Sachs, BankInvest, Deutsche Asset Management and Credit Agricole Asset Management.

Exposure of equities-related securities by region, excluding liquidity



Market movement, 2003



This type of sector mandate offers several advantages. For one thing, it provides the asset manager with a clear sector focus. For another, it creates opportunities for rapid reallocation of assets to a sector that, in a given situation, may offer the potential for a higher return on invested assets than other sectors.

During the latter part of the year, four new mandates were awarded to manage assets in Asia. About SEK 2 billion

was invested in Asia, outside Japan, and about SEK 3 billion in Japanese equities. The asset managers selected for these assignments are Singer & Friedlander and BankInvest, for the Asia/Pacific mandate (excluding Japan), while Martin Currie and BankInvest were chosen to manage the Japanese mandates.

Regional equities mandates

	Mgmt. style	ROI, %	Negative/surplus return compared to index, %
Europe			
› In-house management	Active	14.8	0.4
› Barclays Global Investors	Passive	14.0	- 0.4
› Goldman Sachs Asset Management	Active		
Consumer Discretionary		- 2.9	- 4.4
Consumer Staples		5.7	2.9
IT		9.0	0.1
Telecom		- 5.5	1.0
› Citigroup Asset Management	Active		
Consumer Discretionary		- 0.4	- 1.9
Consumer Staples		2.7	- 0.1
Financials		3.0	- 1.5
Healthcare		2.9	- 0.4
IT		- 7.3	- 0.9
Telecom		11.4	2.6
› Crédit Agricole Asset Management	Active		
Financials		7.3*	- 0.4*
› Deutsche Asset Management	Active		
Healthcare		5.0*	- 0.2*
› BankInvest Asset Management	Active		
Healthcare		4.6*	- 0.6*
› Skandia small-cap fund	Active	19.9	9.9
North America			
› Barclays Global Investors	Passive	7.2	0.3
› Barclays Global Investors	Enhanced	7.4*	- 0.8*
Japan			
› Martin Currie Investment Management Limited	Active	2.1*	0.3*
› BankInvest Asset Management	Active	2.0*	0.2*
Asien/Pacific (excluding Japan)			
› Singer & Friedlander Investment Management Limited	Active	2.3*	0.7*
› BankInvest Asset Management	Active	0.6*	- 1.0*
Emerging Markets			
› DB Globalspectrum	Active	27.7	- 0.9
› F&C Global Emerging Markets	Active	28.0	- 0.7
› Genesis Emerging Markets	Active	32.7	4.0
› Pictet Emerging Markets	Active	39.3	10.6
› StateStreet Emerging Markets	Active	31.7	3.0
› Citigroup Emerging Markets	Active	6.9*	- 1.7*

Global equities mandates

	Mgmt. style	ROI, %	Negative/surplus return compared to index, %
MFS Institutional Advisors	Active	7.0	- 2.9
Merrill Lynch Investment Managers	Enhanced	10.3	0.4
State Street Global Advisors	Passive	10.1	0.2

Swedish OSX mandates

	Mgmt. style	ROI, %	Negative/surplus return compared to index, %
In-house management	Active	30.2	- 7.1
Carnegie capital management	Active	35.6	- 1.7
Carlson Investment Management	Active	32.6	- 4.6
SEB Asset Management	Active	35.8	- 1.4
E. Öhman J:or Capital management	Active	2.9*	- 0.8*
Fund portfolio:			
› Enter Sweden Fokus	Active	33.8	- 3.4
› RAM One	Active	- 8.3	- 45.6
› Eikos	Active	7.4	- 29.9
› Zenit	Active	- 3.5*	- 46.6*
› Nordic Absolute Return fund		1.2*	- 46.5*

Swedish SBX mandates

	Mgmt. style	ROI, %	Negative/surplus return compared to index, %
In-house management:			
› Portfolio 1	Active	33.6	- 1.0
› Portfolio 2	Active	47.7	11.7
SEB Asset Management	Active	35.0	0.4
Carlson Investment Management	Active	35.2	0.6
Svenska Handelsbanken AB	Enhanced	1.8*	0.0*

Swedish small-cap funds

	Mgmt. style	ROI, %	Negative/surplus return compared to index, %
SEB Sweden small-cap fund	Active	37.2	- 5.0
SEB Sweden small-cap fund opportunity/risk	Active	46.1	3.8
Carlson Sweden small-cap fund	Active	35.2	- 7.0
Lannebo small-cap fund	Active	43.9	1.7
Handelsbanken small-cap fund	Active	41.1	- 1.1
Robur small-cap fund	Active	48.6	6.4

*) ROI refers to part of the year.



The Hong Kong Stock Exchange



The Hong Kong Stock Exchange

The Hong Kong Stock Exchange was established in 1891 and is now the second largest stock exchange in Asia and the seventh largest in the world.

Turnover 2003: SEK 2,133 billion.

The Second AP Fund's holdings in the Hong Kong Stock Exchange amount to circa SEK 0.8 billion. Its holdings in other growth markets amount to circa SEK 2.6 billion.

Management of fixed-income portfolio and FX

The global fixed-income markets were affected during the year by uncertainty concerning the performance of the leading economies, while key interest rates set by central banks were historically low at the turn of the year. The currency market was influenced by a weakening US dollar and the growing strength of the Swedish krona. The Second AP Fund's management of its fixed-income assets shows a result in line with the Fund's benchmark index.

The main factor affecting the performance of global fixed-income markets has been the uncertainty surrounding the macroeconomic performance of the leading economies. At the start of the year, attention was focused on the uncertain geopolitical situation that led to a safe-haven bid in fixed income markets at the expense of equities. The resolution of the conflict in Iraq increased hopes of a rapid economic recovery, and bond yields rose.

As the year progressed, the continuous decline in core CPI led the market to fear the corrosive deflationary spiral experienced by Japan during the last decade. This triggered a sharp drop in interest rates, especially with the Federal Reserve giving hints of non-conventional methods that could be used in case deflation became apparent. In early summer, US bond yields reached their lowest levels since the end of the 1950s. As the summer progressed, the Fed moved away from their unconventional-methods hints, markets sold off massively as convexity hedging exaggerated the move, causing dramatic fluctuations on a highly volatile market. Encouraged by the increased activity of the major economies and bullish stock markets, the fixed-income market found itself trading in a recovery scenario. Fears that interest rates would prove too low in a period of vigorous economic growth have slowly but surely pushed interest rates higher. An economic recovery, with corporations concentrating on fixing their balance sheet, had an especially favourable impact on corporate bonds, and the interest gap between these and other fixed-income instruments narrowed dramatically during the year. The central banks' key interest rates continue to remain at historically low levels.

The central banks continue to stimulate growth

The year 2003 was also notable for a desire to stimulate economic growth by means of various financial and monetary policy measures. There has been plenty of liquidity around, and attention has focused mainly on avoiding deflation rather than worrying about potential inflationary risks.

Despite increased expectations of renewed growth after the cessation of hostilities in Iraq, the central banks con-

tinued to relax their monetary policy measures and lowered their key interest rates. Since March, both the American Federal Reserve and its European counterparts have lowered their key interest rates. The European Central Bank (ECB) has lowered the key interest rate on two occasions and the Swedish Central Bank (Riksbanken) on three, reducing the repo rate to 2.75 percent – i.e. an entire percentage unit lower than at the start of the year.

Since the summer, the markets have started to anticipate increases in short-term interest rates levels. So far, this has only been implemented in countries that are normally early in the interest cycle, such as Australia. The Bank of England also raised its key rate during the autumn, referring to its most recent cut in the interest rate as an insurance measure, now no longer required in view of the improved economic outlook.

Volatile bond markets

The year kicked off with falling bond yields. Apart from a period of uncertainty concerning the outcome of the conflict in Iraq, the trend seen in 2002 was maintained. During the early summer, this trend accelerated as fears that the USA might find itself in a deflationary spiral gained ground. The Federal Reserve clearly signalled its determination to utilise every available instrument in avoiding a deflationary scenario of this kind (including the purchase of bonds to maintain long interest rates). Ten-year yields fell to just over 3.1 percent in the USA, the lowest level for 40 years.

However, this extended trend of falling yields was broken during the summer. Ten-year yields rose by almost 1.5 percentage units in a brief space of time, resulting in extreme volatility and reduced market functionality. Fears about the threat of deflation, however, were gradually toned down and, with the normalisation of inflation and growth expectations, bonds started to look highly overvalued. During a brief period, American interest rates rose higher than those in Europe, although falling back by the end of the year to end lower than in Europe. Japan, which has had to live with interest rates at very low levels, also responded to the global

rise in interest rates and interest rates almost tripled in an extremely short time.

This trend slowed somewhat during the last few months of the year, producing greater stability in interest rates. Seen over the full twelve months, interest rates rose slightly, in line with the increasingly positive direction of the yields generated by expansive monetary policies.

Improved liquidity in corporate bond market

Past excesses in corporate investments and negative headlines from accounting scandals has put pressure on companies to rationalise and concentrate on strengthening their balance sheets. De-leveraging and better cash flow management has sharply reduced the perceived risk between government securities and corporate bonds, thereby reducing their interest-rate differential. During the year, bonds with the lowest credit ratings have tended to generate the highest returns.

Low nominal interest rates, a propensity to accept a higher level of risk and the need for higher returns have also increased investors' interest in corporate bonds. The market has also developed a high degree of functionality, with better liquidity, more structured products and effective trading in derivative instruments as a means of adjusting capital risk. A number of products for investment in the broad corporate bond index were also launched during the year. The American market for corporate bonds remains predominant, but the development of a joint bond market in the EMU favours the European corporate bond market.

Swedish fixed-income market keeps up with international market

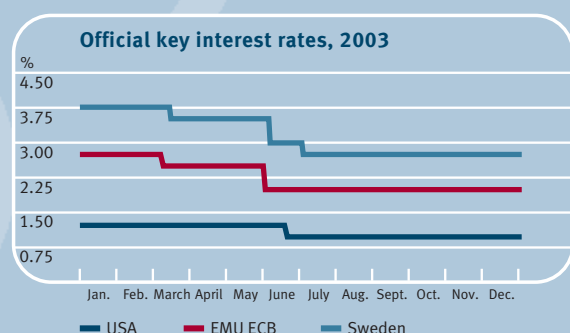
In broad terms, the performance of the Swedish fixed-income market paralleled that of the global market during the greater part of the year. The Swedish Central Bank (Riksbanken) acted somewhat more aggressively than its foreign colleagues by cutting the repo rate on three separate occasions, by a total of one percentage unit. In the summer, the market turned its attention to Sweden's immi-

grant referendum on membership of the EMU and the outcome's possible impact on market rates. At the start of the year, the market was convinced that the referendum would result in Swedish membership of the EMU, but as the referendum drew nearer, the opinion polls pointed in the opposite direction. Most analysts assumed that a "Yes" would produce a drop in market rates and a stronger krona, and vice versa with a "No". At the time of the referendum, the market's pricing had largely discounted a "No" and the reaction to the actual outcome resulted in relatively limited market movement. During the rest of the year, global developments dominated the direction of Swedish interest rates movements, although there was a steady increase in the amount of attention paid to the performance of Sweden's domestic economy and the viability of the country's public finances.

FX market reveals distinct patterns

The year may be summarised under two headings: "weaker dollar" and "stronger krona". The US dollar has declined sharply in value compared to most other major currencies during the year. The market has focused on imbalances in the American economy, which is burdened by substantial balance-of-trade and federal budget deficits. At the same time, scepticism about the present US administration's will to implement the "strong dollar policy" declared earlier helped further undermine the exchange rate.

At year-end 2003, the dollar fell below the initial launch level at the introduction of the euro. The dollar even declined sharply against the Japanese yen, which also had a negative impact on expectations of an export-led recovery of the Japanese economy.⁻³ The Swedish krona has risen sharply in value during the year. Apart from a period in conjunction with the referendum on Sweden's membership of the EMU, where a degree of uncertainty led to a brief weakening of the currency, the trend over the full twelve months was consistent strengthening of the currency. More favourable flows of capital and a belief in Swedish economic policy have both had a positive impact on the krona during the year.



Results of portfolio management in line with benchmark index

The Fund's management of the portfolio during the year has generated a result of 5.3 percent, which is almost in line with the fixed-income portfolio's benchmark index. The management of the Swedish fixed-income portfolio has made a positive contribution to overall assets, while management of the portfolio of foreign fixed-income instruments made a negative contribution to the relative return. The allocation of assets between the portfolios is generally consistent with the benchmark portfolio.

The portion of the fixed-income portfolio for which an absolute return was specified has performed very well during the year and made a favourable contribution to the total return on invested capital.

The favourable contribution generated by the assets managed in the Swedish portfolio may be largely attributed to long duration in relation to index during the spring, and a short position after the summer. The Fund had taken no position on the outcome of the EMU referendum, but the result has led to over-weighting in Swedish fixed-income investments compared to European investments.

The negative result of the assets managed in the foreign fixed-income portfolio derives mainly from a lower return on the Fund's credit management activities. The Fund has made a conscious decision not to become involved in the active management of corporate bonds, due to the complexity of the market and the consequent requirement for specialised analysts in this field. In accordance with current policy, responsibility for parts of the portfolio will be delegated to external managers in 2004. During 2003, the portfolio was under in-house passive management, whereby the

corporate component of the index was replicated using instruments whose return was likened to the return of specific credit market segments. During the year, the portfolio had an overweight position in higher rated credit instruments than the index, thereby underperforming as the lowest rated credit segments outperformed.

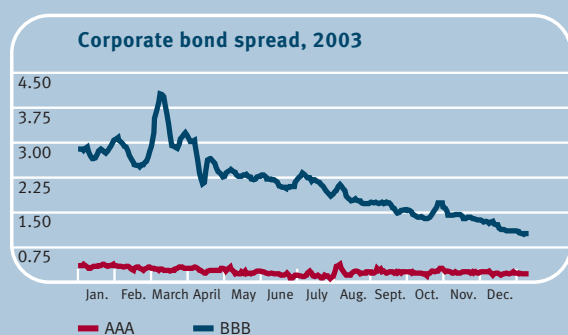
In 2003, management of the inflation-linked portfolio generated a return in line with the benchmark index: the management of the portfolio has followed index very closely.

The portion of the fixed-income portfolio for which an absolute return was specified has performed very well during the year and made a favourable contribution to the total return on invested capital. These investments consist of hedge funds and investments in fixed income investments in Sydsvenska Kemi.

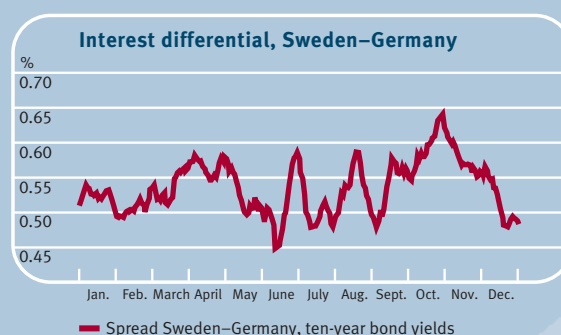
The Fund is currently engaged in a limited amount of FX trading except for currency hedging of the underlying equity and foreign fixed income portfolios. Some tactical and strategic positions are however taken in allocating the Fund's FX exposure and in rebalancing to achieve the desired weightings in equities and fixed-income investments. Until the referendum on Sweden's EMU membership, the Fund's FX exposure was in line with the benchmark portfolio. Since the referendum, however, the Fund has been positioned to benefit from a stronger krona, which has contributed favourably to the Fund's relative return on invested assets.

Looking ahead

The external mandate for the management of foreign fixed-income securities, in particular those that carry a credit risk, will be implemented in 2004. Increased attention will also be focused on the management of assets required to generate an absolute return, which will involve several new asset managers. Potential alternative sources for generating value, such as increased activity in currency markets, will also be evaluated.



Source: EcoWin



Source: EcoWin

Alternative investments

The Second AP Fund has concentrated its investment activities in private equity funds under asset class Alternative Investments. During the year, this asset class has undergone further development, towards a well-diversified portfolio of investments beyond as well as within the Nordic region. The Fund has received a large number of investment proposals, two of which have resulted in investments totalling almost one billion kronor.

The Second AP Fund's strategy for Alternative Investments in private equity funds is based on the following key principles:

- step-by-step implementation,
- diversification in several dimensions (geographical location, nature of industry, the portfolio company's maturity and estimated time to exit),
- careful individual assessment of each investment opportunity, as opposed to a rapid general allocation of funds to the asset class as a whole.

In the build-up phase, the portfolio's focus was restricted to funds with a geographical base in the Nordic countries. As a natural progression, and fully in line with the established strategy, the asset class is being developed towards a more balanced and well-diversified portfolio, with investments in funds that are based outside the Nordic countries. This will mainly be implemented indirectly, by means of "fund-of-fund" investments. Eventually, the Fund will also be able to make smaller complementary investments direct in individual funds.

Operations in 2003

During 2003, the Second AP Fund continued its active role on the Nordic market. Meetings were held with a large number of players, to extend the stable network established

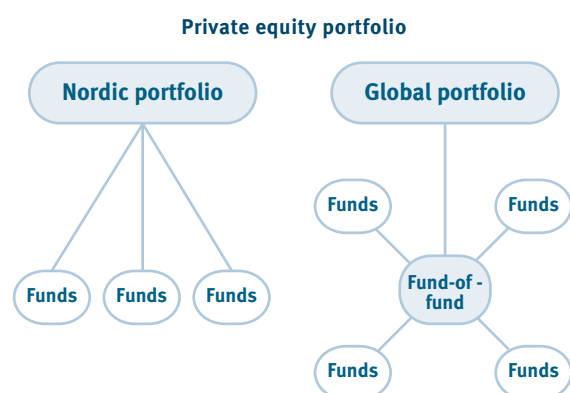
previously and to maintain an ongoing evaluation of earlier investments and new investment opportunities.

In the international arena, outside the Nordic countries, the Fund continued to establish a high quality network of contacts. Particular attention has been devoted to identifying an international "fund-of-fund". After conducting a selection process that has involved contact with more than 50 market players, the Second AP Fund is now engaged in final negotiations with an American fund manager in this field.

During the year, the Second AP Fund has received and evaluated a large number of investment proposals. These have resulted in undertakings to invest in two new funds during the period, EQT Mezzanine Fund and Amaranth Capital, amounting to a total investment of SEK 953 million. By year-end 2003, the Fund had committed a total of SEK 1,688 million, of which SEK 246 million had been invested (for further details, please refer to pp. 39 and 56 in the Financial Review).

Market review

At the start of 2003, Swedish and international players continued to adopt a "wait-and-see" policy, due to uncertainty about the global economy. The funds made relatively few new investments and focused on the companies in their existing portfolios. During the latter part of 2003, however, a growing feeling of optimism made itself felt. The global economy seems to have reached something of a turning point and, moreover, several interesting valuations present a number of attractive investment opportunities. There have even been repeated indications that some of the most eminent companies in the private equity fund portfolios have been approached by industrial buyers, who are interested in possible acquisition, something that has been far from common in recent years. To interpret these market indicators as hard evidence of a turnaround would be overreacting, but they are nevertheless a sign that we can look forward to increased activity in the M&A market. As in 2003, the level of interest for new stock market floatations in 2004 is thought to be very limited.



Real estate

The Second AP Fund's real estate-related holdings consist of shares in both listed and unlisted property companies. The listed holdings are managed within the framework of the Fund's ongoing equity management activities, i.e. with the assistance of both in-house and external managers. Unlisted real estate holdings, that comprise a 25-percent participation in AP Fastigheter and a 33-percent participation in Norrporten, are managed in-house by the Second AP Fund.

The Swedish real estate market revealed two quite different faces in 2003. The rental market has been weak, especially with regard to office space. This applies mainly to the Stockholm area, although other parts of the country have also been affected by the continuing recession. During the latter part of the year, however, the real estate market in Stockholm stabilised somewhat in terms of vacancy and rental levels in central locations, while the situation remained problematic in the suburbs. The market for residential property continues to be buoyant. New production levels for office space in Stockholm are not expected to increase over the next few years and, though one of the larger European cities, forecasts suggest that Stockholm will have the lowest production of new office space during 2003 and 2004. For this reason, analysts consider Stockholm to be one of the markets where rental increases could be implemented most rapidly in the wake of a clear economic upswing.

Both rental and new production levels are far more stable in other parts of the country and, in the Gothenburg and Malmö regions, the vacancy levels are significantly lower than in Stockholm.

Unlike the rental market for office space, the investment market has been strong in 2003. A number of major transactions involving large portfolios of real estate holdings were completed during the year. The degree of international interest in commercial real estate in the major urban centres, especially in Stockholm, is considerable. Several large foreign real estate funds have been active and acquired attractive portfolios in city locations.

In addition to the major transactions involving individual portfolios of real estate, investors have shown considerable interest in acquiring a number of exchange-listed real estate

companies. The Ratos/Lehman Brothers joint takeover bid for Tornet, the acquisition of Mandamus by Akelius and the bid from Norway's Eiendomsspar for Pandox, a hotel property company, were especially notable.

The Carnegie Real Estate Index has noted the same growth as the stock market in general, i.e. 34 percent.

The Second AP Fund's unlisted real estate holdings

The Second AP Fund's investments in real estate are designed to generate a solid direct return on investment and contribute to a satisfactory diversification of risk in the total portfolio.

The Fund's unlisted shareholdings in real estate consist of a 25-percent participation in AP Fastigheter AB, which is owned jointly by the four first AP funds, as well as a third of NS Holding AB (Fastighetsbolaget Norrporten AB). The Fund's holdings, including debenture loans, are valued at SEK 4.6 billion.

Norrporten, which has a portfolio of real estate holdings that consist mainly of centrally located office premises in regionally important urban centres, has continued its strategic expansion during the year, and invested in large portfolios of real estate in Helsingborg, Umeå, Linköping and Uppsala. The company reports vigorous earnings growth.

AP Fastigheter, with about 70 percent of its portfolio of real estate located in the Stockholm region, has had to face harsher market conditions. Even so, signs of a more stable earnings trend could be seen during the latter part of the year.

The Second AP Fund's investments in unlisted real estate holdings ensure a well-diversified level of risk, and the investments in AP Fastigheter and Norrporten are well balanced (see below).

Total return SFI (Svenskt Fastighetsindex)

	1997	1998	1999	2000	2001	2002
Stockholm, central locations	11.1	20.6	19.3	30	- 0.9	- 4.2
Large regional urban centres	9.9	9.6	12.8	15.2	7.3	4.8

The table shows total return as a percentage of real estate investments, incl. changes in the value of commercial properties in central Stockholm and large regional urban centres.



Scenic Sights of London



London Stock Exchange

Trading on the London Stock Exchange was formally established in March 1801, originating in the city's coffee-trading traditions, dating back to the 17th century.

Turnover 2003: SEK 26,076 billion.

The Second AP Fund's current holdings in the London Stock Exchange amount to about SEK 5.8 billion.

Second AP Fund as owner

In Sweden as well as on the global arena, the intense public debate about the way big companies are managed and controlled raged on in 2003. A number of financial scandals, in exchange listed as well as unlisted companies, helped stoke the debate. In the case of Swedish companies, attention has focused particularly on the bonus programmes operated by ABB and Skandia, which have been the subject of intense criticism, and the accusations of corruption and restrictive trade practices levelled against several companies, which have been given considerable coverage.

As part of the subsequent debate, there has been much discussion about the role of institutional shareholders, both in terms of monitoring and influencing the development of individual companies' true worth and of dealing with ethical and more general issues of corporate governance. This must be placed in the context of the fact that several surveys have revealed a sharp decline of public confidence in corporate leadership. In line with international praxis, the Swedish Government also appointed a "Credibility Commission" during the year, entrusted with the task of drafting proposals for measures that could re-establish public confidence in the long term.

This debate has raised countless questions about the roles and responsibilities of executive managements, boards of directors and majority shareholders. Particularly in view of the dramatic growth of institutional ownership in recent decades, both in Sweden and elsewhere, demands that institutional investors such as pension funds shall adopt a more active ownership role have grown dramatically. Many institutions now recognise an immediate business advantage in exercising their rights as majority shareholders more actively than before. Companies with distinct and demanding owners tend to be valued more highly than companies perceived as ownerless and dominated by their executives.

Given these conditions, corporate governance issues have gained increasing importance within the Second AP Fund, which has taken a firm stand on several issues. One of the most important has been the decision to encourage the recruitment of a higher proportion of women to the boards of companies in the Fund's portfolio. The Fund is convinced that a substantial increase in the number of women on the boards of Swedish companies will release significant potential. It seems only reasonable that an extension of the recruitment base will contribute to raising the quality of directors serving on the boards of Swedish companies.

In the past year, the Fund's representatives have also participated in a number of conferences and meetings where ownership issues have been on the agenda. The policy implications of ownership issues have also been addressed at meetings of the Fund's board of directors. During the year, the Fund has clarified and sharpened its corporate governance policy, while intensifying its efforts in this area.

AGMs during 2003

During 2003, the Second AP Fund participated in 38 Swedish annual general meetings (AGMs) and three extraordinary general meetings. The Fund also exercised its voting rights at the AGMs of its 50 largest foreign shareholdings, via "proxy voting".

The Second AP Fund has been directly represented in the nomination process for the boards of Pergo, Castellum and Getinge. The Fund has also been actively engaged in the preparatory work prior to many of these AGMs, cooperating with other institutional shareholders and board representatives in analysing and discussing the various proposals which the boards have planned for submission to their respective AGMs. During the year, the two most frequently asked questions at these AGMs concerned the Fund's attitude to numerous incentive programmes and the issue of board nominations.

Owner-related activities in 2003

In its contacts with companies in which it has an interest, the Fund normally adopts one of two approaches. This may be in the form of annual visits to a large number of companies, conducted by the Fund's portfolio managers and analysts, where attention is focused strictly on the company's investment potential. Or it may be in the form of a visit to a number of companies by the Fund's CEO and the head of corporate governance, to discuss ownership issues. In the latter case, the CEO or chairman of the company being visited acts as host.

A total of ten such corporate visits were made in 2003, focused specifically on ownership issues. The companies visited represent a selection of the Fund's largest Swedish holdings, in terms of capital investment or voting rights, as well as a number of smaller companies which the Fund was interested in visiting, for a number of different reasons. The purpose of these visits has been to present the newly started Second AP Fund's background and investment focus, to clarify the Fund's ownership policy and to listen to companies' expectations of the Fund in its role as owner. And the visits have contributed to an expansion of the Fund's network of contacts.

At the start of the year, the Second AP Fund published its own specially compiled index, updated after the AGM in 2003, to chart changes in the number of women directors on the boards of exchange-listed Swedish companies. This index, which reveals that the proportion of women on the

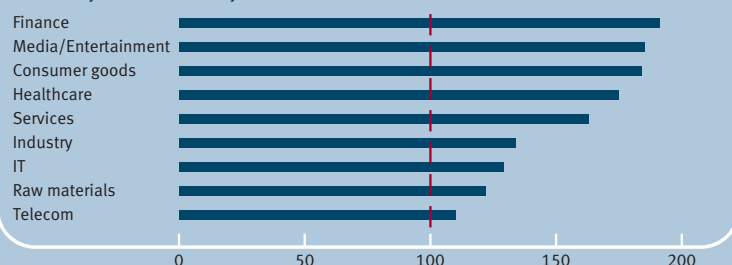
During the year, the Fund has clarified and sharpened its corporate governance policy, while intensifying its efforts in this area.

boards of listed Swedish companies had risen from seven to eleven percent, attracted considerable media attention. The statistical data on which these comparisons between industries and quoted companies are based is published on the Fund's website. The index will be updated after this year's AGMs have been completed.

Owner focus in 2004 – a glimpse of the future

Even though ownership issues may to some extent be said to be "event determined", the Second AP Fund is also committed to influencing the long-term development of companies in which it has interests, in line with its corporate governance policy. In its role as an institutional owner, the Fund will continue to focus on audit and accounting issues, incentive programmes and a range of measures to improve the quality of the work carried out by corporate boards. A specific issue to be addressed is the composition of boards and how the relative proportion of women on these boards can best be increased. During 2004, the Fund will continue to pursue a dialogue with companies which, in its opinion, fail to create shareholder value comparable to or better than that achieved by their immediate competitors.

Female representation on corporate boards by industrial sector, re. AP2 index, 2003



To chart progress concerning the number of female directors on the boards of quoted companies, the Second AP Fund created a special index, the Q index, in 2002. On this index, 100 corresponds to the average number of female directors on the boards of all the companies listed on the Stockholm Stock Exchange. This index is updated on an annual basis and is published on the Fund's website. The adjacent bar chart shows the considerable discrepancy between the number of female board members in different industries, based on data compiled after the AGMs held in 2003.

Integrated administration system for automated business processing

When operations started in January 2001, the Second AP Fund was confronted by an almost unique situation, demanding immediate and simultaneous decisions regarding the formulation of architecture, systems and processes for the Fund's IT support function. The fundamental idea was to optimise and automate business processes in line with the STP (Straight-Through Processing) concept.

The Second AP Fund has had the opportunity to build an in-house system for integration with the systems of a number of other external associates and suppliers. The system would also have to meet every demand that could be expected of a modern asset management organisation: daily follow-up and evaluation of huge numbers of trades, the processing of “corporate actions” (dividends, share issues etc), control of risk limits, and broad and thorough analyses of various forms of risk and performance measurement. For the Second AP Fund specifically, the system would also have to be accessible by those external partners to whom responsibility for a range of asset management mandates or custodial services would progressively be delegated, without burdening them with over-complex introductory processes. As well as meeting all these requirements, the system would also have to fulfil extremely stringent safety requirements.

Progressive development

After a thorough evaluation process, the system chosen was the SimCorp Dimension (SCD) administration system. Since the start of operations, this system has been progressively expanded and upgraded, with additional modules, to meet increasingly demanding performance specifications. Implementation of the capital management system started with an “empty shell”, which was progressively filled with

data over a period of more than twelve months, and adapted to meet a range of different user specifications. The system was designed to provide a high degree of automation and to optimise business processes, whether initiated by the Fund's in-house portfolio managers or by external managers. To satisfy these requirements, the system was complemented at an early stage with TradeseC, a web-based system for the import of external managers' trades.

The system registers all trades executed on the Fund's behalf on a day-to-day basis, whether implemented by in-house managers or by one of the Fund's 16 external managers. This provides unique opportunities for the continual follow-up, evaluation and analysis of the Fund's entire holdings, in terms of both risk and performance. The system allows Fund staff to maintain an excellent check on in-house and external holdings, whether in the form of equities, bonds or other instruments.

Fully integrated system

The Fund uses the SCD as a fully integrated Front/Middle/Back Office system for the entire investment process, from execution and matching of trades to settlement, reconciliation, follow-up and evaluation. The Fund checks, evaluates and analyses holdings on a daily basis.

All cash transactions (about 4,000 per month) involving the Fund's externally and in-house managed bank accounts are reconciled daily. Files are received electronically from the Fund's custodial bank, which are matched in a separate matching system (Adra) with the corresponding data from SCD. Positions are reconciled every week and at the end of every month, based on files from the custodial bank that are matched directly in SCD.

In evaluating and following up holdings, under both external and in-house management, the yields on different portfolios are valued at the market rate and measured against the appropriate benchmark index on a daily basis. Risk utilisation is also measured daily.

On average, some 1,200 trades a month are imported via TradeseC to SCD. In addition to the flow of trades from

every night, as are securities and counterparts from SCD to TradeseC. This enables external managers to register new trades and match the data sent to the Fund earlier against their own in-house systems.

At the close of every month, the data is finally transmitted from SCD to the Visma accounting system, which balances the monthly accounts.

Control and security

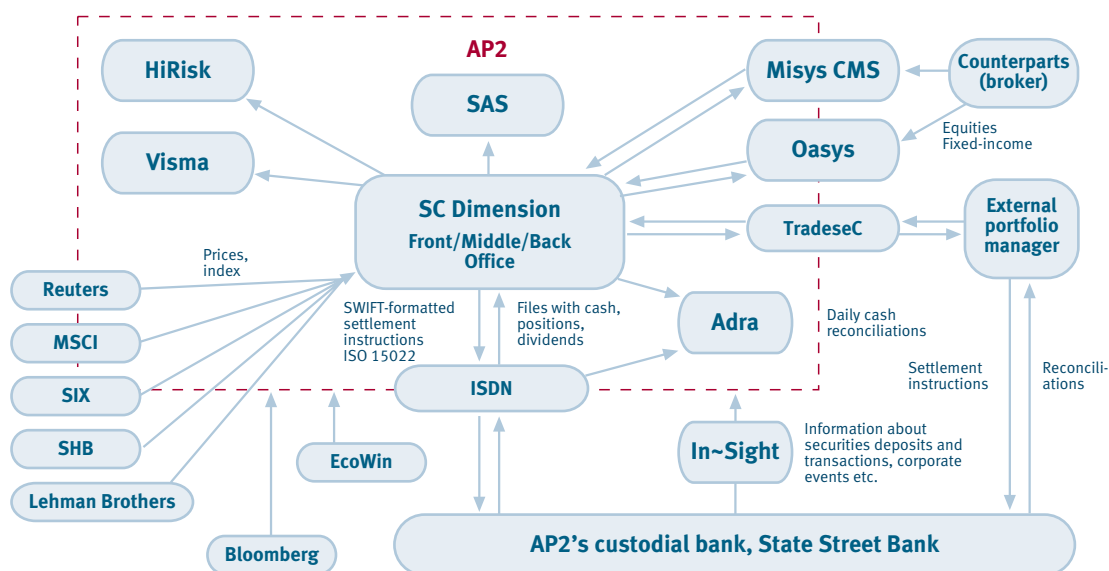
The fact that the administration system is used both by in-house and external staff, who communicate over the Internet, places extreme demands on effective security. Because of this, there are different levels of access to TradeseC and SCD, and each user is issued with individual and specially authorised access certificates. As well as individualised authorisation, the system features a number of automated control functions to determine that permitted limits and guidelines are not exceeded.

On a more general plane, the Fund's IT security efforts are dedicated to minimising the risk of downtime and ensuring continued operation even in the case of fire or some similar crisis. During 2003, work has focused on defining guidelines and developing continuity plans to maintain operations despite breakdowns or crisis situations. A data security management system was also implemented during the year.

The Fund checks, evaluates and analyses holdings on a daily basis.

external managers to the Fund, there is a simultaneous flow in the opposite direction, from the Fund via TradeseC to external partners. Positions and basic data are transferred

System overview, Second AP Fund



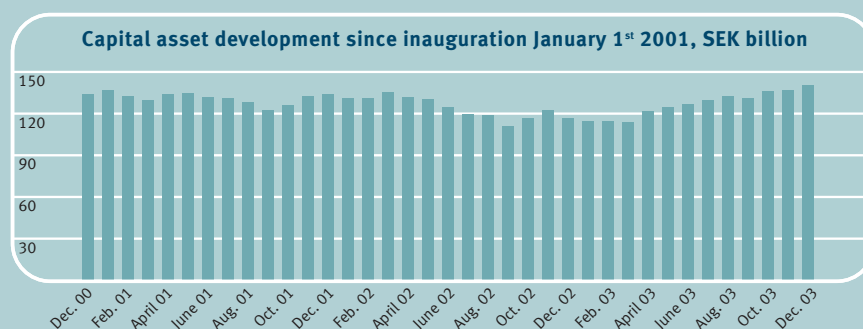
Financial review

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After three years of sharp decline, 2003 witnessed a strong recovery by Swedish and global stock markets. For the Second AP Fund, which had maintained a consistently high exposure in equity markets, 2003 led to

a substantial improvement in the reported net result.

The Second AP Fund reported capital assets amounting to SEK 140.4 billion at year-end 2003, an increase of SEK 23.3 billion since the start of the year.



Unless otherwise stated, the portfolio assets referred to in this report are “allocated exposures”. In addition to booked market values, these also refer to allocated (but not yet invested) liquidity for the specific class of asset, and the liquid funds held as collateral for positions already taken in derivative instruments. Classes of asset, derivative instruments and liquid funds are reported individually in the balance sheet at market values.

Second AP Fund in 2003

During the latter part of 2003, as a consequence of the Second AP Fund's long-term investment strategy, whereby some 60 percent of total assets are allocated to equities, the Fund became a net seller of equities. Even so, the Fund noted a relative over-weight of its exposure in equities during much of the year. The percentage of assets under active management was extended during 2003, as was the Fund's delegation of portfolio responsibilities to external asset managers. At year-end 2003, the Second AP Fund had achieved broad exposure in the global market and a well-diversified spread of risk.

At the close of the year, the Second AP Fund reported assets totalling SEK 140.4 billion, an increase of SEK 23.2 billion. The return on the Fund's invested assets was 17.7 percent, compared with the strategic portfolio's 18.5 percent.

Highlights of the year

A new ALM study was conducted during the second half of 2003, to generate decision data for the Board's approval of the strategic allocation of Fund assets in 2004. In broad terms, the new strategic portfolio retains the same distribution between equities and fixed-income instruments.

A new asset class, "Alternative Investments", which comprises the Fund's investments in private equity funds, hedge funds and real estate, has been assigned a clearly defined role in asset allocation. A number of smaller changes have been introduced in a number of asset classes, including a limited increase in the level of exposure tolerated on investment in emerging markets.

The Fund's portfolio management department completed negotiations concerning a number of external international mandates. These negotiations are integral to the development and implementation of the strategic decision to increase active management of the Fund's assets, and to transform it into a skilled "manager of managers".

During the year, the Fund has analysed and refined the management of its portfolios of fixed-income instruments. The planned negotiation of mandates for the external management of fixed-income instruments was postponed and will be implemented in 2004.

The process of building up asset class Alternative Investments has continued. During the year, the Fund considered a large number of investment proposals. This resulted in two concrete investment decisions, involving EQT Mezzanine Fund and Amaranth Capital. A thorough inventory and analysis of foreign "fund-of-fund" managers has been conducted, in line with the policy to promote increased internationalisation of the portfolio.

As a joint owner of AP-fastigheter, the Second Swedish National Pension Fund/AP2 has participated in the restructure of the company. The change is designed to adapt

the company's structure better to long-term and efficient investment by the AP funds. During the year, the Fund's role as an institutional shareholder has attracted increasing attention, in connection with current Swedish public debate concerning the state of ethics and morality in the business world. The Fund has clarified and sharpened its corporate governance policy during 2003, as well as increasing its efforts in this area.

Net result for the year

The Fund reports total assets of SEK 140.4 billion, including net flows, as per December 31st 2003. The Fund's return on invested assets for 2003, including unlisted assets and operating expenses, amounted to 17.7 percent. Excluding unlisted assets and operating expenses, the Fund thereby generated an ROI that was 0.5 percent under the benchmark index. The inflow of external liquid funds during the year totalled SEK 2.6 billion, of which SEK 2.1 billion in the form of net payments from RFV (The National Social Insurance Board). The remaining inflows pertain to dividends from the "Liquidation Fund" and "Special Fund", which are managed by the First Swedish National Pension Fund (Första AP Fonden) and Fourth Swedish National Pension Fund (Fjärde AP Fonden) respectively. The net result for the year amounted to SEK 20.7 billion. Dividends received amount to SEK 1.6 billion and the capital loss incurred on equities-related assets was SEK -1.6 billion. Net interest income totalled SEK 2.9 billion and the capital gain on fixed-income-related assets was SEK 0.4 billion.

The Fund's operating expenses amounted to SEK 234 million, personnel costs accounting for SEK 62 million, and the costs of external management (including fund management) accounting for SEK 110 million. Operating expenses in relation to average market value over the year, or "asset management cost quotient", corresponded to 0.18 percent. The asset management cost quotient for external management (external management costs in relation to average market value of the Fund's capital assets during the year) amounted to 0.09 percent. The Fund's operating expenses include provisions for VAT payments totalling SEK 8 million. All Fund investments have been written off.

Inflows

Amount (SEK million)	Dec. 31 st 2001	Dec. 31 st 2002	Dec. 31 st 2003
Net payments to the national pension system (RFV)	3,062	1,985	2,143
Transferred from Liquidation Fund and Special Fund	1,461	3,017	424
Total inflows	4,523	5,002	2,567

Key ratios

	2001	2002	2003
Average fund capital, SEK m	133,282	124,949	128,031
Asset management cost quotient, %	0.14	0.16	0.18
Net result, SEK m	- 5,005	- 21,405	20,693
Total return, %	- 3.7	- 15.3	17.7
Active return, %	1.7	0.4	- 0.8
Total return, excluding unlisted assets and operating expenses, %	—	- 16.0	18.6
Active return, excluding unlisted assets and operating expenses, %	—	0.6	- 0.5
FX exposure, %	10	7	8
Share of assets under active management, %	37	62	89
Share of assets under external management, %	82	38	45

The work of the board

The Second AP Fund's board of directors comprises nine members in all, appointed by the Swedish Government. Two members left the board in 2003 and one new member was appointed. Consequently, the board comprised a total of eight members at year-end 2003.

The Fund's CEO also attends board meetings, with any member of staff required in connection with a specific item on the agenda. Even others – such as the Fund's auditors or external partners – may also attend these meetings, as required.

The board has met on six occasions during 2003. The Fund's economic development and results have been presented and discussed at all these meetings. In addition to reviewing the Fund's day-to-day asset management activities, the board devoted a considerable amount of time to issues of strategic importance to the Fund. This work has included specific ratification of the Fund's strategic asset allocation. During the year, the board has ratified a revised operations plan that includes an updated corporate governance and risk policy. The board has also approved the half-year and year-end accounts, as well as a budget for the Fund's business operations. The Fund's auditors presented their report on the year's operations in conjunction with the board's approval of the year-end accounts. As well as the issues noted above, the board discussed and addressed several questions of principle arising from the Fund's operational activities. These included various rulings on ownership issues, as well as questions and decisions pertaining to investment proposals within the asset class Alternative Investments.

During the year, the work of the board has been appraised by an external consultant. This appraisal has comprised a

study of the minutes recorded at all board meetings, individual interviews with every member of the board, the presentation of a report on the consultant's findings and a plenary discussion of the various issues addressed.

The appraisal has been forwarded to the Swedish Ministry of Finance and will be subjected to continued deliberation by the board in the coming year.

Ministry of Finance appraisal of Second AP Fund

The Swedish Ministry of Finance supervises the activities of the AP funds by means of legislation and through the appointment of board members and auditors. The ongoing follow-up and control of the work carried out by the board and CEO, as well as monitoring of the Fund's net result and financial status, is conducted in the form of an audit, although this is complemented by a separate annual appraisal under the auspices of the Ministry of Finance.

During the year, the Ministry of Finance conducted its usual annual appraisal of the performance and business operations of the AP funds, for subsequent presentation to the Riksdag (Swedish Parliament). Among other topics, the appraisal notes that the combined losses incurred by the First to Fourth AP funds in 2002, as a consequence of rapidly expanded trading in equities, provides grounds for criticism. At the same time, the appraisal stresses that fact that this criticism could just as well be levelled at the capital market as a whole. The negative performance of the stock market at the start of 2001, when the long-term investment focus of each fund was finalised, derived from circumstances that defied simple prediction. Referring specifically to the Second AP Fund, the Ministry of Finance appraisal highlights the new model developed to determine the composition of the Swedish equities portfolio, praising it as "innovative". Work on the appraisal for 2003 started at the end of the year and is expected to be ready by the spring of 2004.

The auditors of the Second AP Fund, Anders Bäckström (KPMG) and Göran Jacobsson (PricewaterhouseCoopers) have been appointed by the Ministry of Finance for the period 2002–2004. Anders Bäckström is also responsible for coordinating the audits of all the AP funds. This year's audit comprises an examination of a number of areas common to all the AP funds, mainly related to issues such as mandates governing the external management of assets, as well as environmental and ethical issues. The auditors have also examined the procedures adopted by the Fund in preparing an ALM study, the way it exercises its corporate governance role, and its internal routines and control functions. Any observations made concerning the audit, or comments on the Fund's internal controls, are presented to the board of directors by the auditors in person.

Total portfolio

Distribution of Fund assets

The Fund's assets as at December 31st 2003 were distributed as follows: SEK 85.1 billion in listed equities, of which SEK 28.4 billion in Swedish equities and SEK 56.7 billion in foreign equities. Interest-bearing assets, including liquid funds, amounted to SEK 50.4 billion. Holdings in unlisted shares in real estate companies amounted to SEK 4.6 billion, including subordinated debenture loans, while holdings in Alternative Investments amounted to SEK 255 million. Some 45 percent of the Fund's assets are managed, both actively and passively, by external asset managers. These external asset managers have been chosen after a stringent process of analysis and evaluation, in accordance with the regulations governing the procurement of services by public authorities. Mandates have been awarded to a number of Swedish and international asset managers (see Note 4, page 53).

Changes of exposure in derivative instruments

In compliance with the guidelines approved in the business plan for 2003, the Fund has utilised derivative instruments to secure more effective management of assets, to reduce transaction costs and cut risk. Investments in the form of derivative instruments may not be executed if they incur stock market exposure in excess of total Fund capital. During 2003, derivative instruments have mainly been used in the following areas:

- Currency derivatives for handling FX exposure.
- Stock derivatives – especially standardised share futures – for effective rebalancing of the portfolio and when adopting positions in connection with tactical asset allocation.
- Index-linked derivatives – mainly in the form of standardised index-linked futures – for rebalancing, tactical asset allocation and management of the Fund's index-linked risk.

Exposure in derivative instruments is followed up and analysed on a current basis, as required for other investment instruments.

Risk utilisation 2003

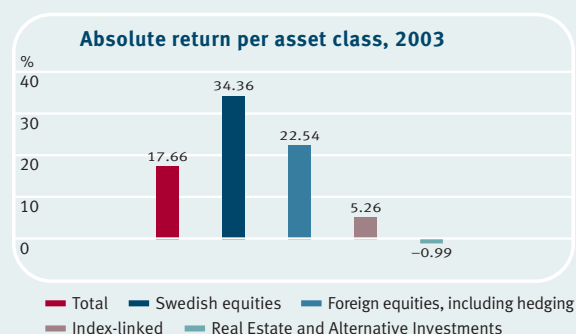
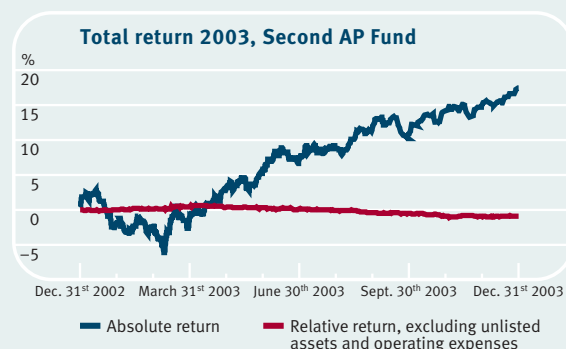
During the year, the Fund has progressively implemented a form of asset management that ensures a more equitable distribution of risk. Fund utilisation of active risk for the total portfolio, ex post, amounted to 1.0 percent at the start

of the year. By December 31st 2003, the Fund had reduced its active utilisation of risk to 0.7 percent.

The standard deviations for the Fund's total and benchmark portfolios declined during the year from 13.0 percent and 13.1 percent to 8.6 percent and 8.6 percent respectively. The Fund reported a negative information ratio for 2003.

ROI

The return on the Second AP Fund's total portfolio of assets amounted to 17.7 percent for the full year 2003, including unlisted assets and operating expenses, and 18.6 percent excluding unlisted assets and operating expenses. This substantial growth in capital assets may be attributed primarily to the Fund's maintenance of a high share of equities throughout 2003, which coincided with a sharp upturn on the world's leading stock markets. Low exposure in foreign currency, with active positions taken to benefit from a stronger krona, in conjunction with a relatively high degree of exposure on the Stockholm Stock Exchange, have further contributed to this strong return on invested assets.

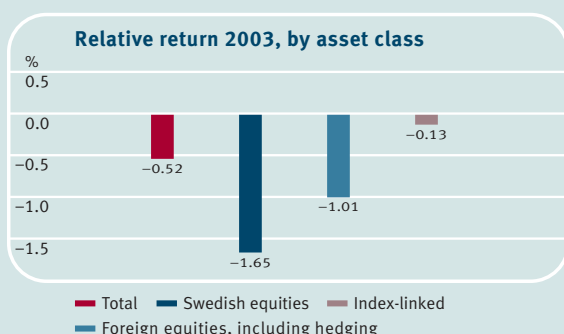


Risk adjusted return for total portfolio, valued by year

	AP2 2001, %	Strategic portfolio 2001, %	AP2 2002, %	Strategic portfolio 2002, %	AP2 2003, %	Strategic portfolio 2003, %
Return	- 3.7	- 5.4	- 15.3	- 15.7	17.7	18.5
Standard deviation	9.7	10.2	13.0	13.1	8.6	8.6
Active risk, ex post	1.7	—	1.0	—	0.7	—
Information ratio	1.0	—	0.5	—	neg	—
Sharpe ratio	neg	—	neg	—	1.7	—

Asset class development

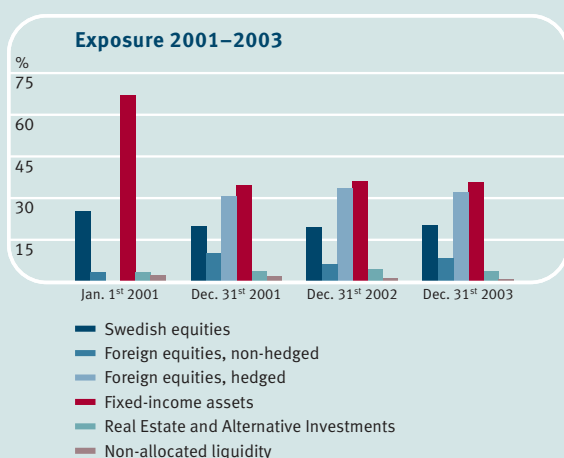
A description of the Fund's exposure, reported market value and ROI per asset class at year-end 2003 is given below.



The Fund's strategic portfolio generated a return of 18.5 percent, which resulted in a relative return of -0.8 percent for 2003. The Fund's relative return, excluding unlisted assets and operating expenses, amounted to -0.5 percent. This negative relative return may be attributed partly to the fact that hedge fund holdings are included under asset class Swedish Equities, partly to the choice of securities. The choice of securities has also had a negative impact on asset class Foreign Equities, in conjunction with an initial under-weighting in terms of exposure on emerging markets. A relative return on a level with index was posted for fixed-income assets.

Exposure

The Fund's market exposure has undergone significant changes since its inauguration on Jan 1st 2001. The share of fixed-income assets has declined from 67 percent to 36 percent, and exposure in foreign hedged equities has increased from 0 percent till 32 percent. In 2001, the Fund instigated an extensive rebalancing of the assets in its portfolio, from fixed-income to equities-related assets, in line with its strategic portfolio. During the following year, this exposure was further extended and refined to include new regions and asset classes. This diversification and internationalisation of the portfolio, in terms of both fixed-income and equities-related assets, has continued during 2003. Here follows a description of the Fund's market exposure, declared market value and return per asset class, as at year-end 2003.



Swedish equities

In 2002, the Second AP Fund adjusted its benchmark index for Swedish equities. Modification of the Swedish equities portfolio was implemented in full during 2003. From having previously used the SIXRX index, equity management is now subject to a rolling five-year appraisal based on a combination of three separate parts, each with its individual benchmark index. Each part features assets under both in-house and external management. The portfolio consists of a part that is capital-weighted (70 percent) and benchmarked against the SBX index; a part that is equally weighted (20 percent) and benchmarked against the OSX index, and a part that comprises small-cap funds (10 percent), benchmarked against the CSX index (for further details, refer to the section "Strategic portfolio 2003" on page 41).

The upswing noted by the Stockholm Stock Exchange has been especially marked in the energy and IT sectors. While the SBX index as a whole has climbed by 34.6 percent, the upswing in these sectors has exceeded 75 percent. The reverse is true of companies in the power supply sector, which have noted a stock market decline of about -3 percent. The market value of the Swedish equities portfolio totalled 28.4 billion, featuring a well-diversified spread of holdings in a number of large exchange-listed companies. The entire portfolio has been under active management throughout the year, with limited relative risk. As per Dec 31st 2003, 56 percent of the Fund's holdings in Swedish equities were under external management. The portfolio of Swedish equities generated a 34.4 percent return against the benchmark index (weighted) of 36 percent. During the same period, the SIXRX noted a 34.2 percent return.

Largest Swedish holdings

The Fund's five single largest Swedish holdings by worth were Ericsson (2.7 percent), SHB (2.3 percent), AstraZeneca (2.2 percent), Volvo (1.9 percent), and Nordea (1.7 percent).

Swedish equities

	2001	2002	2003
Exposed value, SEK billion	26.2	22.8	28.4
Absolute return, %	-15.6	-36.7	34.4
Relative return, %	-0.8	-0.9	-1.6
SIXRX, %	—	—	34.2
Active management, %	75	100	100
External management, %	100	50	56

Foreign equities

During the year, the Second AP Fund continued to increase the share of foreign equities under active management. Changes have been implemented in three areas: North America, Europe and Asia/Pacific. The Fund's in-house management has focused on European equities, adopting a sector-based approach to the management of these assets. Exposure on other markets has been delegated to a number of external managers. As part of the Fund's policy of diversification, new mandates have also been issued concerning the management of investments in emerging markets, for which approximately SEK 600 million was allocated during the year. In a move to increase the degree of active management, the Fund has implemented a gradual transition from passive management against index to "enhanced" management, with a particular focus on its holdings in the North American market.

The market value of the foreign equities portfolio amounted to SEK 56.7 billion at year-end 2003. During the year, the degree of market exposure in the USA was reduced in favour of European, Japanese and Pacific stocks, as well as emerging markets. Investments were also made in emerging markets. The portfolio of foreign equities has yielded a return of 22.5 percent compared with a regionally adjusted MSCI World index, which generated a return of 23.5 percent for the same period. As per December 31st 2003, 82 percent of assets held in foreign equities were under external management.

Largest foreign holdings

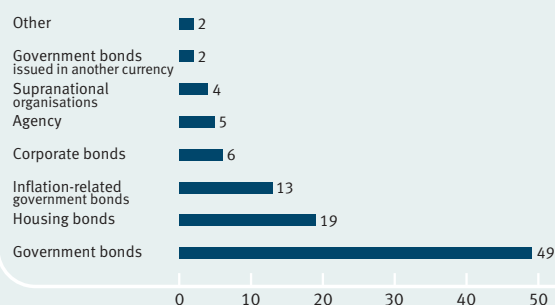
At the end of the year, the five single largest foreign holdings were Citigroup (0.7 percent), Pfizer Inc. (0.7 percent),

General Electric (0.7 percent), BP (0.7 percent) and Vodafone (0.7 percent).

Fixed-income & FX

During the year, the composition of the fixed-income portfolio was reallocated to secure a higher share of active management and achieve a global spread of assets. The majority of the assets in this portfolio have been under in-house management. The management of Swedish fixed-income assets has contributed positively to the relative return, while the management of investments in foreign fixed-income instruments has resulted in a negative return. This negative result from the management of foreign fixed-income instruments is mainly attributable to a poorer return on the Fund's credit management activities.

Distribution by type of security, %



The Fund had taken no active position prior to the EMU referendum. During the latter part of 2003, the Fund's Swedish fixed-income portfolio was over-weighted while the corresponding portfolio of European fixed-income instruments was underweighted.

Management of the inflation-linked portfolio during the year has yielded a return in line with the benchmark index, and management of the portfolio has been close to index. The portion of the portfolio for which an absolute return has been specified, consisting of hedge funds and investments in bond loans, has yielded an excellent return over the year and made a positive contribution to total return on invested capital.

Foreign equities

	2001	2002	2003
Exposed value, SEK billion	53.8	46.1	56.7
Absolute return, %	- 7.7	- 24.9	22.5
Relative return, %	1.0	0.3	- 1.0
MSCI World, %	—	—	21.8
Active management, %	11	37	78
External management, %	100	64	82

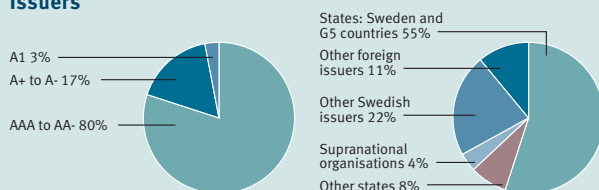
Composition of strategic portfolio, exposure and return as per Dec. 31st 2003

Asset class	Strategic portfolio, %	Exposure, %	Exposed value, SEK billion	Market value, SEK billion	Return AP2, %	Return benchmark index, %
Swedish equities	20	20.2	28.4	29.8	34.4	36.0
Foreign equities	40	40.4	56.7	47.5	22.5	23.5
Fixed-income assets, including liquidity and accumulated interest	37	35.9	50.4	57.3	5.3	5.4
Real estate	3	3.3	4.6	3.8	- 0.7	- 0.2
Alternative Investments		0.2	0.3	0.3	- 8.0	- 0.2
Total	100	100	140.4¹⁾	138.7¹⁾	17.7	18.5

1) The difference between total market value and exposure consists mainly of derivative instruments.

At the start of the year, the duration of the portfolio amounted to 5.3 years, which remained unchanged at the close of the full twelve months. National issuers accounted for 63 percent of the fixed-income portfolio. As per Dec 31st 2003, 80 percent of the portfolio was placed in fixed-income securities, rated from AA- to triple A (AAA).

Issuers



At year-end 2003, government bonds accounted for 64 percent of the total value of the fixed-income portfolio.

At present, the Fund is engaged in no active trading in FX. Tactical and strategic positions are taken in allocating the Fund's currency exposure, and when rebalancing to achieve the desired weighting in equities and fixed-income instruments. After the EMU referendum, the Fund has been positioned to benefit from a stronger krona, which has made a positive contribution to the relative return.

The market worth of the Fund's fixed-income instruments, excluding liquidity, amounted to SEK 50.1 billion on December 31st 2003, compared to SEK 42.2 billion at year-end 2002. The fixed-income portfolio generated a return of 5.3 percent on investment. The fixed income portfolio consists mainly of nominal and inflation-linked Swedish bonds, as well as internationally traded government securities and corporate bonds. The yield on the portfolio of fixed-income securities was 5.3 percent, which was in line with the benchmark index. In addition to its fixed income securities, the Fund reported liquid funds amounting to SEK 0.3 billion at year-end 2003.

Fixed-income assets

	2001	2002	2003
Exposed value including liquidity, SEK billion	50.3	43.4	50.4
Absolute return, %	3.7	8.9	5.3
Relative return, %	- 0.1	0.0	- 0.1
Active management, %	12	88	98
External management, %	57	9	10

Alternative investments

The Second AP Fund's investments in unlisted equities must, by law, be made indirectly via private equity companies, mutual funds or similar institutions. In asset class Alternative Investments, resources have been focused on investments in funds for unlisted and listed equities with an absolute yield requirement.

During 2003, the Second AP Fund has remained active on the Nordic market. In the international arena, outside the Nordic countries, the Fund has continued the process of establishing a high-quality network of professional associates. Special emphasis has been placed on the task of identifying a "fund-of-fund" manager. After a comprehensive inventory and evaluation of some fifty market players, the Second AP Fund is currently engaged in final discussions concerning an agreement with an American manager in this "fund-of-fund" sector.

During 2003, the Fund signed undertakings with two new funds, EQT Mezzanine and Amaranth Capital, to a combined value of SEK 953 million. This brought the total worth of new undertakings at year-end 2003 to SEK 1,688 billion. Of this sum, SEK 246 million has already been invested. Management fees paid to these external counterparts, which are written off on a current basis, amounted to SEK 24 million in 2003. This means that

Investments and undertakings, unlisted stocks

Fund	2001		2002		2003		Total	
	Investment	Undertaking	Investment	Undertaking	Investment	Undertaking	Investment	Undertaking
EQT Northern Europe KB	52	181	59	—	- 1 ¹⁾	—	110	181
Swedestart Life Science KB	2	25	2	—	2	—	6	25
Swedestart Tech KB	3	25	2	—	2	—	7	25
Carnegie Fund II Biotech Bridge	—	—	49	50	—	—	49	50
Nordic Capital V	—	—	—	454	1	—	1	454
EQT Mezzanine Fund	—	—	—	—	22	272	22	272
Amaranth Capital	—	—	—	—	51	681	51	681
Total	57	231	112	504	77	953	246	1,688
Market value, total							255	

1) Refers to expense of asset management fees incurred.

a total of SEK 32 million has been paid in fees for the external management of the Fund's investments in unlisted funds since the Fund started operations. These fees are calculated on total undertakings and will be deducted from subsequent profits in venture capital funds and refunded prior to profit sharing.

Real estate

The Second AP Fund's real estate-related holdings consist of shares in both listed and unlisted property companies. The listed holdings are managed within the framework of the Fund's ongoing equities management activities, i.e. with the assistance of both in-house and external managers. Unlisted real estate holdings, that comprise a 25-percent participation in AP-fastigheter and a 33-percent participation in NS Holding AB (Norrporten), are managed in-house by the Second AP Fund. The Second AP Fund's investments in real estate are designed to generate a solid direct return on investment and contribute to a satisfactory diversification of risk in the total portfolio.

AP-fastigheter AB is owned jointly by the four first AP funds. In December 2003, as a consequence of restructuring, this holding has been replaced by holdings in a newly established parent company, AP-fastigheter Holding AB.

This has had no impact on the reported value or net result of the AP-funds. AP-fastigheter has a concentrated and attractively located portfolio of real estate holdings in the Stockholm, Gothenburg and Uppsala areas. The company owns and manages some 300 properties, totalling 2.4 million square metres of floor space, at a combined estimated market value of SEK 32 billion.

Norrporten continued its strategic expansion during the year, and has invested in a number of substantial properties in Helsingborg, Umeå, Linköping and Uppsala. Norrporten owns and manages some 240 properties, totalling approximately 1.4 million square metres of floor space. These properties have a combined estimated market value of SEK 12 billion. The company reports solid earnings growth.

The holdings in NS Holding AB have noted favourable development, generating a SEK 53 million increase in market value and interest income on debenture loans amounting to SEK 83 million. The Second AP Fund's holdings in AP-fastigheter note a decline of SEK 333 million in market value. During the year, AP-fastigheter rendered a dividend of SEK 175 million to the Second AP Fund. The market values of AP-fastigheter and Norrporten were reported at SEK 3,221 million and SEK 1,399 million respectively, including debenture loans.

Unlisted real estate holdings Dec. 31st 2003

AP Fastigheter Holding AB, amounts in SEKm

Equities

Acquisition value	3,660
Valuation	- 439
(of which affecting the operating result 2003: - 333)	

Market value Dec. 31st 2003 **3,221**

Total dividend 2001-2003 **375**
(of which in 2003: 175)

Norrporten, amounts in SEKm

Equities

Acquisition value	372
(of which invested 2003: 79)	
Valuation/appreciation	169
(of which appreciation 2003: 53)	

Market value Dec. 31st 2003 **541**

Debenture loans

Debenture loans incl. accrued interest per Dec. 31st 2003	858
(of which invested 2003: 154)	

Total interest income 2001-2003 **192**
(of which in 2003: 83)

Strategic asset allocation

The Second AP Fund's board of directors conducts an annual internal evaluation of the focus chosen for the Fund's portfolio management policy. This process includes an ongoing review of the latest ALM (Asset Liability Modelling) study, which forms the basis of the board of directors' decision concerning the composition of the Fund's strategic portfolio.

In 2001, during its first six months of operation, the Fund conducted a comprehensive reallocation of assets, involving the divestment of fixed-income instruments and purchase of foreign equities. In the late autumn of the same year, the Fund achieved parity between the composition of the actual portfolio and that of the benchmark portfolio approved by the board of directors. By the close of 2001, in the simplest terms, the portfolio was comprised approximately of 60 percent equities and 40 percent fixed-income instruments and real estate.

In 2002, on completion of the ALM study, and despite the market situation, the Fund's board of directors decided to maintain a high proportion of equities in the strategic portfolio throughout 2003 as well. The new strategic portfolio represents a refinement in terms of asset class distribution on different markets and choice of portfolio management style. The sharp upswing noted by the world's stock markets during the year has favourably affected the management result. Essentially, this has been the decisive factor behind the Fund's SEK 21 billion growth in market value in 2003.

The ALM study reviewed during 2003, which focused on the strategic allocation of assets in 2004, involves only small changes in the portfolio's composition. A key feature of this strategy is the commitment to increase the share of invested assets under active management and for which an absolute yield is specified.

Strategic portfolio 2003

During the year, the Fund has progressively implemented a management style that better serves the aims of the modified strategic portfolio for 2003. This has resulted in a more diversified risk and active management, while ensuring that the portfolio meets the Fund's long-term yield require-

ments. The percentage of assets managed against an absolute return requirement has grown.

The management of the Fund's fixed-income portfolio has also developed, with the completion of an international diversification of the bond portfolio and an increased allocation in corporate bonds.

Major changes have been introduced in managing the portfolio of Swedish equities, which has been divided into three parts:

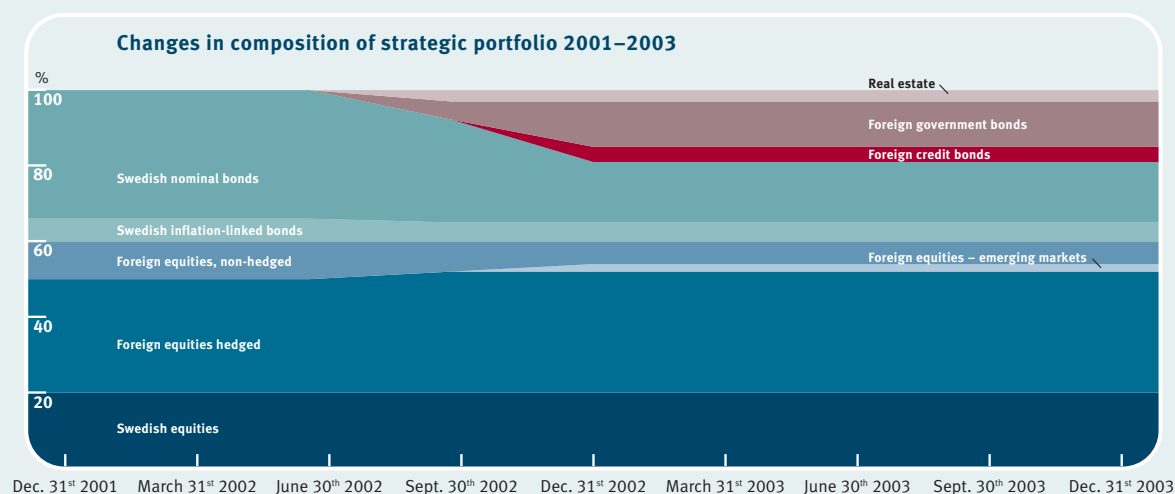
A capital-weighted part. A substantial part of the portfolio (70 percent), it is matched against a "capital-weighted" index (SBX) that features just over 80 equities and corresponds to about 90 percent of the SIXRX. This part of the portfolio is managed in a more conventional manner, with a low level of active risk. The target is a surplus yield against index of more than one percent.

An equally-weighted part. A completely new index (OSX) was created in 2002, which accounts for 20% of the Swedish equities portfolio and comprises the 50 largest companies on the Stockholm Stock Exchange. All companies have the same weighting in the index, which reduces dependence on the large companies. Great emphasis has also been placed on the need for a positive absolute return on invested assets. An important aspect of the OSX portfolio is that it should function as a counterweight in a falling stock market, which is why the style of portfolio management adopted is expected to differ significantly from index.

A small-cap fund part. The third part (10 percent) of the Swedish equities portfolio involves the management of holdings in small Swedish businesses, where the Second AP Fund investments are in the form of shares in unit trusts. The performance of this part of the portfolio is matched against Carnegie's small-cap index (CSX). The objective here is to exceed index by two to four percent in the long term.

The regional composition of the portfolio of foreign equities has changed, reducing exposure in US stocks in favour of European and Japanese equity markets.

Furthermore, two new asset classes have been defined, in the form Emerging Markets and Real Estate (unlisted holdings).



Benchmark index for strategic portfolio 2003

Part-portfolio	Index
Equities	
Sweden	70% SBX "Stockholm Stock Exchange Benchmark Index" 20% OSX "Unweighted Sweden Index" 10% CSX "Carnegie Small Cap Index"
Europe	MSCI Europe
North America	MSCI North America
Japan	MSCI Japan
Asia excl. Japan	MSCI Pacific excl. Japan
Emerging markets	MSCI Emerging Markets
Real estate + Alternative Investments	SFIX Svenskt Fastighetsindex
Fixed-income assets	
Swedish nominal fixed-income securities	SHB Swedish All Bond
Inflation-linked bonds	SHB Index Linked
Foreign government bonds	Lehman Brothers Govt 1000 x Asia
Foreign credit bonds	Lehman Brothers Cred 1000 x Asia

Investment regulations for Swedish National Pension Funds

- Investments may be made in all types of listed and negotiable instruments on the capital market.
- No more than 5% of the assets in each fund shall be invested in unlisted securities. Such investments shall only be made indirectly, via venture capital companies, mutual funds or by similar means.
- At least 30% of each fund's assets shall be invested in interest-bearing securities with low credit and liquidity risk.
- Each fund's holding in listed Swedish companies shall not exceed the equivalent of 2% of the total market value.
- Each fund may own no more than 10% of the votes in a single listed company. The corresponding limit for unlisted private equity companies is 30%.
- The Funds may not invest in warrants, forward contracts or other financial instruments based on commodities as collateral.
- After a gradual increase of five percentage points per year, from 15 percent in 2001, no more than 40% of a fund's assets shall be exposed to currency risk.
- No more than 10% of a fund's assets shall be exposed to one issuer or one group of issuers.
- At least 10% of the assets of each fund shall be managed by outside managers.

New strategic portfolio 2004

The changes in the strategic asset allocation for 2004 are relatively minor. The differences between the strategic portfolios for 2003 and 2004 include the formation of Alternative Investments as a new asset class comprising asset groups Real Estate, Private Equity Funds and Hedge Funds. In addition to this, the Fund's assets will be divided into two separate parts, liquid and non-liquid. The idea is to simplify and clarify an ongoing evaluation of the Fund's portfolio management performance.

Asset class Alternative Investments will comprise five percent of the Fund's strategic portfolio. This asset class consists of Real Estate (three percent), Private Equity Funds (one percent) and Hedge Funds (one percent). These are not new assets, having earlier formed part of the Fund's portfolio, but they have now been gathered to form a joint asset class. Consequently, asset classes Equities and Fixed Income Securities will shrink by one percent each.

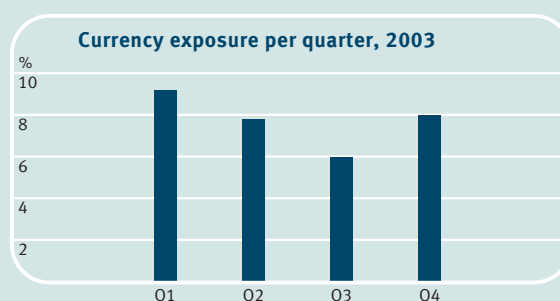
Liquid and non-liquid asset

The Fund's portfolio contains assets of varying liquidity. The liquid assets consist of equities, bonds and foreign exchange while the non-liquid assets consist of real estate and venture capital funds. To ensure that the ongoing monitoring of yield and risk is true and accurate, all assets are valued on the same occasions and at the same intervals, which until now has not been possible. The Fund's reported total return shall always consist of the yield generated by both parts of the portfolio. However, the active return on invested assets shall be matched against the performance of the liquid portfolio.



FX exposure

At year-end 2003, approximately 8 percent of the Fund's assets were exposed in foreign currency, which was in line with the strategic portfolio. The remaining assets exposed in foreign currency have been hedged by means of forward exchange contracts. The Fund's total exposure in FX is distributed as shown in the table below. This exposure derives mainly from assets held in the foreign equities portfolio.



Currency exposure

Dec. 31 st 2003, equivalent in millions	USD	GBP	EUR	JPY	Other	Total
Equities and participations	21,823	6,209	8,978	5,028	5,601	47,639
Bonds and other fixed-income securities	7,443	1,478	13,208	1	637	22,767
Other assets and liabilities, net	424	160	607	33	254	1,478
Derivative instruments excluding FX derivatives	80	34	51	15	16	196
FX derivatives	- 24,402	- 6,718	- 19,924	- 4,110	- 5,416	- 60,570
Currency exposure, net	5,368	1,163	2,920	967	1,092	11,510

Currency exposure reported as per the Fund's true management of FX risk, which means that it is based on local currency at the trading location, and not the currency pertaining at the company's registered office.

External portfolio management

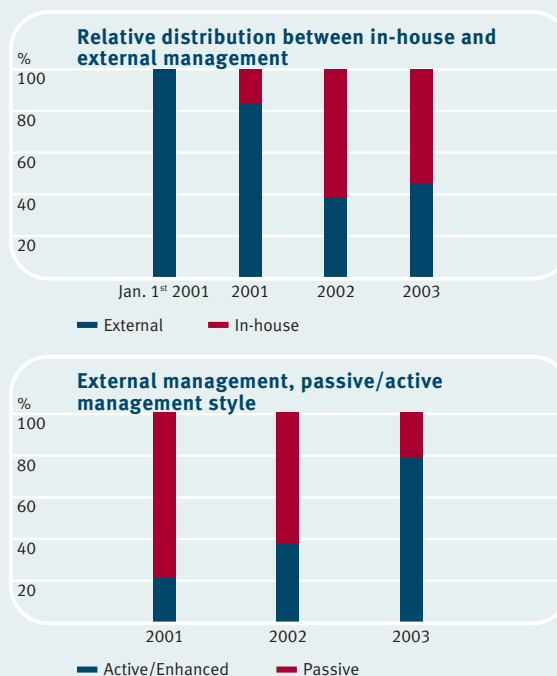
The Second AP Fund manages a significant proportion of its total portfolio, about 45 percent, with the assistance of external managers. At the start of 2003, 38 percent of the Fund's exchange-listed external management mandates were under active management. During the year, the share of assets under active external management, featuring both relative and absolute yield requirements, was increased to 78 percent. The Fund has cooperated with more than 35 external managers in 2003, mainly in the management of equities and private equity. These external managers contribute specialist expertise in the management of assets outside Europe. As required, opportunities are provided for rapid and flexible redistribution of assets under management.

Strategy and concept

The strategy and focus of the Second AP Fund's portfolio management policy, which is committed to an increasing degree of active management, especially on markets outside Europe, assumes access to a growing amount of specialist expertise. External fund managers shall be utilised where it can be demonstrated that they generate a higher return, or function as a useful complement to the Fund's in-house investment activities. Even on markets where the Second AP Fund is well qualified to conduct the successful management of its assets, external fund managers may still be able to contribute additional experience, as when a need arises to diversify the portfolio. Using external fund managers makes it easier to switch investment style or change risk profile, with the added benefit that the Fund's organisation is less vulnerable to changes in personnel.

Contract negotiation and selection criteria

Since the formation of the Second AP Fund, three series of contract negotiations have been conducted to determine the award of external mandates for the management of Fund assets. The first series of negotiations, which was initiated in November 2000, concerned mandates for the management of Swedish fixed-income securities and Swedish and foreign equities. During the period June 2002 to January 2003, a further series of contract negotiations were held concerning the management of European and North American Equities, as well as mandates for stock portfolios in Asia and Japan. Negotiations concerning the award of mandates for Swedish equities were completed in 2003.



The Fund's selection process involves a number of pre-determined selection criteria, such as investment style, analytical quality, organisational structure, staffing and yield history. Qualitative and quantitative factors are subjected to thorough analysis, both during the negotiations and, if selected, during ongoing portfolio management.

Cost of external management

In all, 45 percent of the Fund's total assets are under external management, of which 78 percent under active management. Active management incurs higher costs for managed investments, as a result of which external management costs have risen from SEK 46 million to SEK 110 million, including management fees paid to unlisted venture capital funds during the year. These costs corresponded to 0.2 percent of the average fund capital placed under external management in 2003.

In connection with the implementation of external fixed-income and allocation mandates, combined with the focus on an absolute yield requirement, management costs are expected to rise yet again in 2004. Despite the costs incurred by such a high degree of external management, the benefits – in the form of flexibility, diversification of the potential active management risk and an expected surplus yield against index – are thought to outweigh any disadvantages.

External management, costs for active/passive management

Year	Active management share of total external management, %	Passive management share of total external management, %	Externally managed capital Dec. 31 st , SEK billion	External management costs, SEK million
2001	21	79	110.1	39
2002	38	62	44.6	46
2003	78	22	62.7	110

Follow-up, analysis and control

As a large and internationally active asset manager, with several asset management assignments delegated to external fund managers, the Second AP Fund is subject to stringent demands in terms of its ability to analyse, follow up and monitor portfolio performance. This applies as much to individual mandates as to the portfolio as a whole. To satisfy these demands, the Fund has invested in an advanced IT platform that combines high reliability with flexibility. The Fund monitors, evaluates and analyses holdings on a daily basis, whether the assets are managed externally or in-house. Complete balance sheets and income statements are prepared on a monthly basis, together with whole range of relevant economic analyses.

Systems environment

After a thorough evaluation process, the Second AP Fund selected the Simcorp Dimension (SCD) asset management system – a fully integrated Front/Middle/Back Office system – as its basic computerised administrative system. Since its implementation, this system has been progressively expanded and upgraded, with additional modules, to meet the increasingly demanding and constantly changing performance requirements. The system has been designed to provide a high degree of automation and to optimise business processes, whether initiated by the Fund's in-house portfolio managers or by external managers. To satisfy the additional requirements deriving from cooperation with external managers, the system was complemented at an early stage with TradeseC, a web-based system for the import of external managers' trades.

The system registers all trades executed by the Fund's discretionary external managers on a day-to-day basis, via TradeseC to SCD. The number of mandated external managers has increased in the past year, requiring clear and secure routines and continual review and follow-up of the flow of data. The Fund's systems architecture provides excellent opportunities for continual follow-up, evaluation and analysis of its entire holdings, as well as full and direct access to the status of portfolios managed under external mandates, in terms of risk and performance too. The system

allows Fund staff to maintain an excellent check on in-house and external holdings, whether in the form of equities, bonds or other instruments.

External managers are responsible for the entire business process within the parameters of their respective mandates, from execution to settlement and reporting via TradeseC. The portfolio manager is issued with separate reporting and control authorisation codes to access TradeseC. This method has proved highly successful and has provided the Fund with some flexible and effective tools, which are decisive in meeting the demands imposed by active management and a capital asset allocation that is divided between several portfolios, asset classes and fund managers.

Risk management

Follow-up of investment regulations, limits and financial risks is handled on a daily basis. The Fund's level of risk utilisation is within the specified parameters. Follow-up and analysis are conducted for both absolute and relative levels, as well as ex ante and ex post for the total portfolio, per asset class and per mandate. Operative management is to be conducted so that the anticipated active risk for the entire exchange-listed portfolio should not exceed three percent. This risk limit has been complemented with a target that defines the preferred level for the Fund's risk utilisation. The target set for active risk for the Fund's total portfolio is two percent. In the same way, individual limits for anticipated active risk are set for each asset class.

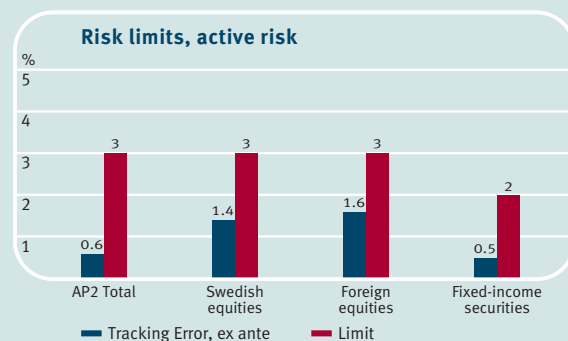
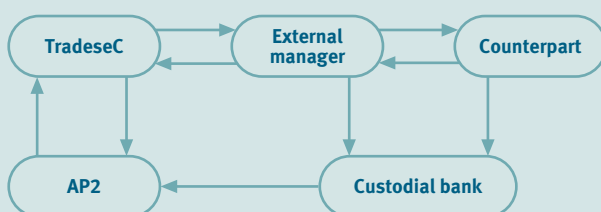
The HiRisk system

The implementation of the HiRisk risk management system was completed in March 2003. The system permits analysis and follow-up of the Fund's combined market and credit risks. The system conducts deep analysis of risk utilisation, at both asset class and mandate level.

Measure of total risk for the Second AP Fund

The Fund's risk exposure is analysed and followed up on a daily basis.

Flow chart for externally managed trades



During 2003, the Sharpe ratio noted an upswing and had risen to 1.7 percent by year-end. The twelve-month rolling information ratio shows a negative value.



Attribution analyses

Yield attribution

Yield attribution is employed to clarify the differences in yield between the Fund’s portfolio of exposed assets and the strategic portfolio. The analytical process is conducted at several levels, for the total portfolio, between asset class, within each asset class and at the portfolio level.

As far as possible, the Fund applies the same rates to underlying securities in respective indexes as used by the official indexes in determining the benchmark index. To

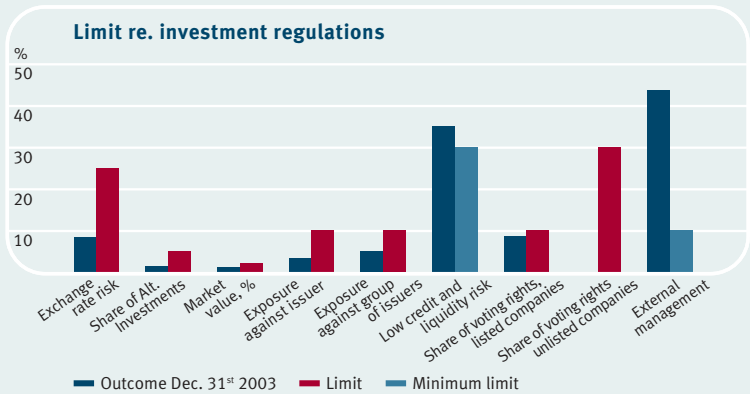
ensure that “corporate actions” are treated consistently in both portfolio and index, daily controls are implemented at the securities level to match respective portfolios against their benchmark indexes. In conjunction with these control functions, yields and weightings per security are down-loaded to a separate attribution database, permitting rapid and flexible complementary analysis at the securities level.

The Second AP Fund observes the principle that indexes that depend on underlying market data shall be calculated by independent, external suppliers. Co-weighting of indexes to create a top index is carried out daily, supported by the SCD asset management system.

Reporting of exposure, yield and portfolio results is conducted on a daily, weekly and monthly basis. The ROI is measured arithmetically and time-weighted. The Second AP Fund plans to conduct an evaluation of the yield attribution system in 2004.

Risk attribution

Risk follow-up routines have been expanded during the year and now also comprise risk attribution. Risk attribution defines which marginal factors contribute most to relative and absolute risk. Attribution is implemented for a range of factors such as allocation, choice of securities, sectors, countries, ratings, duration and assets. The Fund implements both ex ante and ex post risk attributions.



Commission

In connection with the purchase of equities and participations, the commission is capitalised in accordance with generally accepted auditing standards and thereby included in the acquisition value. Total commission received in 2003 amounted to SEK 86 million. Of this total commission expense, 67 percent is attributable to the Fund's in-house management and the remaining 33 percent to external managers. This corresponded to an expense amounting to 0.05 percent of the total volume of shares traded during the period.

The following five counterparts (in alphabetical order) have received commissions corresponding to 63 percent of commission payments: ABN Amro Bank, Carnegie, Citigroup, Goldman Sachs and Morgan Stanley.

Taxation

In its capacity as a government agency, the Second AP Fund is exempt from tax. Nor is the Fund subject to VAT.

Structure and staff

A new HR (Human Resources) strategy will be implemented in 2004. This new strategy comprises long-term guidelines for leadership, recruitment, skills-development and communication. The strategy is designed to contribute to a more efficient organisation and to help realise the Fund's ambition of becoming a modern and attractive employer.

At year-end 2003, the Fund had a total of 45 employees, of whom 39 were employed full time. Of these, 13 were women. The average age of Fund employees is 39, with a median age of 38.9 years and an age spread from 25 to 58. Members of staff, who have an average working experience of 15 years, represent five different nationalities.

The Fund has a low rate of personnel turnover. During 2003, two employees left and five new employees joined the Fund. The level of absence due to ill health during the year was also low: 0.62 percent.

Corporate governance

In its contacts with companies in which it has an interest, the Fund normally adopts one of two approaches. This may be in the form of annual visits to a large number of companies, conducted by the Fund's portfolio managers and

analysts, where attention is focused strictly on the company's investment potential. Or it may be in the form of a visit to a number of companies by the Fund's CEO and the head of corporate governance, to discuss ownership issues. In the latter case, the CEO or chairman of the company being visited acts as host. A total of ten such corporate visits were made in 2003, focused specifically on ownership issues. The companies visited represent a selection of the Fund's largest Swedish holdings, in terms of capital investment or voting rights, as well as a number of smaller companies which the Fund was interested in visiting, for a number of different reasons. The purpose of these visits has been to present the newly started Second AP Fund and its investment focus, to clarify the Fund's ownership policy and to listen to companies' expectations of the Fund in its role as owner.

Owner-related activities in 2003

During 2003, the Second AP Fund participated in 38 Swedish annual general meetings (AGMs) and three extraordinary general meetings. The Fund also exercised its voting rights at the AGMs of its 50 largest foreign shareholdings, via "proxy voting". The Second AP Fund has also been represented in the nomination process for the boards of Pergo, Castellum and Getinge and, together with other major investors, has been actively engaged in the preparatory work prior to many of these AGMs.

Over the past year, the Fund has defined and adopted a more stringent attitude to a number of owner-related issues. These are stated in the Fund's corporate governance policy. The owner-related issues on which the Fund has placed special emphasis during the year concern the need to increase the percentage of women on corporate boards, and to disseminate the Fund's views on incentive programmes and the importance of better auditing.

Owner focus 2004 – a glimpse of the future

Even though ownership issues may to some extent be said to be "event determined", the Second AP Fund is also committed to influencing the long-term development of companies in which it has interests, in line with its corporate governance policy. In its role as an institutional owner, the Fund will continue to focus on audit and accounting issues, incentive programmes and a range of measures to improve the quality of the work carried out by corporate boards. A specific issue to be addressed is the composition of boards and how the relative proportion of women on these boards can best be increased. During 2004, the Fund will continue to pursue a dialogue with companies which, in its opinion, fail to create shareholder value comparable to or better than that achieved by their immediate competitors.

Income statement

Amounts in SEK million	Note	Jan–Dec 2003	Jan–Dec 2002
Operating income			
Dividends received		1,639	1,578
Net interest income	1	2,915	3,193
Capital gain/loss, net	2	– 1,666	– 12,602
Exchange gain/loss, net		– 2,621	– 835
Unrealised changes in value	3	20,660	– 12,542
Total operating income		20,927	– 21,208
Operating expenses			
External asset management expenses	4	– 110	– 46
Personnel expenses	5	– 62	– 61
Other asset management expenses	6	– 62	– 90
Total operating expenses		– 234	– 197
Net result for the year		20,693	– 21,405

Comments to the income statement

Operating income

The Second AP Fund's net result for 2003 amounted to SEK 20,693 million (–21,405) and comprised a return on managed assets of SEK 20,927 million (–21,208), less operating expenses of SEK 234 million (197).

Net return on managed assets

The net of interest, totalling SEK 2,915 million (3,193), consists mainly of interest income from bonds and other interest-bearing securities amounting to a net of SEK 2,154 million, and interest income deriving from fixed forward exchange rates amounting to a net of SEK 741 million.

The net of capital gains/losses was SEK –1,666 million at year-end (–12,602). Of these realised changes in value, listed equities (including derivative instruments) accounted for a net capital loss of SEK 1,609 million, and fixed-income investments (including derivative instruments) for a net capital gain of SEK 382 million.

The net of exchange gains/losses comprised unrealised and realised exchange gains/losses on the Fund's foreign currency exposure. This resulted in a net deficit of SEK 2,621 million (–835). The majority of the Second AP Fund's currency exposure at year-end was in USD (corresponding to SEK 5,368 million) and in euros (corresponding to SEK 2,920 million). The Fund's total currency exposure amounted to SEK 11,510 million, corresponding to about eight percent of Fund capital (seven percent). In accordance with the guidelines governing the Fund's investment activities, no more than 20 percent of the portfolio's total market value could be invested in foreign equities and securities without hedging in 2003.

The net of unrealised changes in value amounted to SEK 20,660 million (–12,542). This profit is in all essential respects attributable to a net gain of SEK 20,644 million on equities and derivative instruments, and is explained by the upswing noted by global stock markets during the year.

Fixed-income securities and fixed-income derivatives incurred an unrealised deficit of SEK 152 million.

Unlisted equities and participations generated an unrealised net gain of SEK 168 million, attributable to the Fund's holdings in unlisted real estate companies and unlisted funds. During the year, the Second AP Fund received a dividend of SEK 175 million from AP-fastigheter.

Operating expenses

The Fund's operating expenses amounted to SEK 234 million (197), the cost of asset management corresponding to 0.18 percent of the Fund's average total investment capital during the year. Personnel costs accounted for SEK 62 million of this sum (61), other management costs accounting for a further SEK 62 million (90). The cost of external asset management services, including management fees in listed funds, amounted to SEK 110 million (46). The level of costs for external asset management services is primarily dependent on the extent and nature of such services (active or passive management). As at December 31st 2003, the Second AP Fund had awarded external mandates covering both the active and passive management of portfolio assets. At year-end 2003, approximately SEK 63 billion was under external management. Of this total, 78 percent was under active management (see Note 4).

Balance sheet

Amounts in SEK million	Note	Dec. 31 st 2003	Dec. 31 st 2002
ASSETS			
Investment assets			
Equities and participations			
Listed	7	77,263	56,906
Unlisted	8	4,016	4,131
Bonds and other fixed income assets	9	54,718	51,361
Derivatives	10	2,717	1,750
Total investment assets		138,714	114,148
Receivables and other assets			
Cash and bank balances	11	1,562	2,253
Other assets		16	240
Prepaid expenses and accrued income	12	1,257	1,534
Total receivables and other assets		2,835	4,027
TOTAL ASSETS		141,549	118,175
FUND CAPITAL AND LIABILITIES			
Fund capital			
Fund capital at beginning of year	13	117,090	133,493
Net contributions within the national pension system		2,143	1,985
Transferred from special funds and liquidation fund		424	3,017
Net profit for the year		20,693	– 21,405
Total fund capital		140,350	117,090
Liabilities			
Derivatives	10	1,018	928
Other liabilities		86	28
Accrued expenses and deferred income	14	95	129
Total liabilities		1,199	1,085
TOTAL FUND CAPITAL AND LIABILITIES		141,549	118,175
Memorandum items			
Assets pledged for forward transactions	11	679	1,094
Obligations	15	1,411	563

Comments to the balance sheet

Investment assets

At year-end 2003, the market value of "Listed equities" amounted to SEK 77.3 billion (56.9). The Fund's equities portfolio comprised Swedish equities with a market value of SEK 25.6 billion and foreign equities with a market value of SEK 45.0 billion. During 2003, the Second AP Fund continued to invest in a number of external Swedish and foreign unit trusts, focused on specific sectors of the equities market, such as small-cap funds and emerging markets. The market value of these funds totalled SEK 6.7 billion by year-end.

At the close of 2003, the Fund's unlisted real estate holdings consisted of its two associated companies, AP Fastigheter Holding AB and NS Holding AB. During the year, a capital contribution was made to NS Holding AB in an amount of SEK 0.1 billion. The two companies reported market values of SEK 3.3 billion (3.6) and SEK 0.5 billion (0.4) respectively. The Fund also owns a convertible debenture in NS Holding AB, the amount of the loan being increased during the year by SEK 154 million. At year-end, the market value totalled SEK 843 million (631).

Investment in funds for unlisted equities have continued during the year, with new investments totalling SEK 74 million in EQT Mezzanine Fund, Nordic Capital V and Amaranth Capital. Minor supplementary investments have also been made in previously capitalised commitments. Remaining investment commitments in funds for unlisted equities totalled SEK 1,411 million at year-end.

The total market value of unlisted equities amounted to SEK 4,016 million (4,131).

Derivative instruments

In the balance sheet, the market values of all outstanding derivatives are declared gross, regardless of type. Derivatives with a positive market value amounted to SEK 2,717 million (1,750), while those with a negative value amounted to SEK 1,018 million (928).

To achieve the required level of currency exposure, the Second AP Fund has a considerable trading volume in currency derivatives. These derivatives are traded with some

ten or more counterparts and, at year-end 2003, the volume of currency forwards traded totalled SEK 93.6 billion (68.5).

In the case of the equities and fixed income portfolios, share-index and interest-rate futures are mainly used as an effective means of achieving the required exposure at relatively low cost, assuming that the investment decision concerning underlying instruments has already been made. These transactions are cleared through one and the same clearing institute, Goldman Sachs in London, and outstanding volume at year-end amounted to SEK 3.9 billion (3.8) in interest-rate futures and SEK 9.1 billion (21.4) in share-index futures.

Derivative positions have never resulted in higher exposure to the equities and fixed-income market than the pension assets under management: i.e. they exert no leverage on the balance sheet.

Trading in stock and interest rate options has been limited in 2003. At year-end 2003, the Fund's portfolio of assets contained no options.

Fund capital

Fund capital totalled SEK 140,350 million (117,090).

The change is attributable to the return on investments (performance result), external capital flows and operating expenses for the year.

The performance result was a gain of SEK 20,927 million (–21,208), with operating expenses of SEK 234 million (197).

External capital flows consist mainly of the current pension contributions paid into the Fund and the current pension disbursements made by the Fund. The net of these capital flows amounted to SEK 2,143 million (1,985) in 2003. In addition to these capital flows, transfers were made to the Fund from the assets of the former national pension system, currently under liquidation, and held in the form of Special Funds and a Liquidation Fund, administered by the First and Fourth AP Funds. Transfers made from these funds during the year amount to SEK 394 million (3,017) and SEK 30 million (–) respectively.

Accounting and valuation principles

The annual report shall be prepared in accordance with the “Act concerning National Pension Funds (2000:192)” and implemented in line with generally accepted accounting principles. In conformity with the current regulations applying to comparable financial companies and institutions, the buffer funds have drafted and implemented joint accounting and valuation principles.

Transaction-date accounting

Transactions on the money and bond market, equities market and currency market are reported in the balance sheet on the transaction date, which is to say the date on which the significant rights and thereby risks are transferred between parties. The claim on or debt to the other party, between transaction date and settlement day, is reported gross under “Other assets” or “Other liabilities”.

Foreign exchange

Assets and liabilities in foreign currency are reported at the closing day rate. Changes in the value of assets and liabilities in foreign currency are separated into that part attributable to the change in value of the asset or liability, and that part attributable to the change in the exchange rate. Both realised and unrealised changes in value arising from changes in exchange rates are reported under “Exchange gain/loss, net”.

Equities and participations

Equities and participations are calculated at their true value. In the case of equities listed on an authorised exchange, this normally means the latest price paid in local currency on the final trading day of the year: otherwise, the latest bid rate. Equities are reported under the market where they were acquired. Unlisted holdings, apart from unlisted Swedish shares in property companies, are valued in accordance with EVCA principles. These principles state that holdings shall normally be valued at acquisition cost during the first twelve months, after which they shall be valued at a conservatively estimated true market value (net realisable value). This true value shall first and foremost be based on transactions with a third party, although in certain instances other methods of valuation may be employed. The valuation of holdings in unlisted Swedish shares in property companies is based on a market valuation of the company's real estate portfolio at year-end.

In calculating capital gains and losses, the average exchange rate method has been applied.

Bonds and other fixed-income securities

Bonds and other fixed-income assets are calculated at their true value. The market worth of fixed-income securities is

normally determined by the latest bid rate on the final trading day of the year: otherwise, the bid rate for the preceding day.

Net capital gains/losses and unrealised changes in value derive from the difference between the average accrued acquisition value and the market value/true value. The accrued acquisition value is the net present value of future payments, where the discount rate is the compound interest at the time of acquisition. This means that acquired premiums or discounts are accrual accounted over the security's remaining term, or until the next adjustment in the interest rate. Changes in the accrued acquisition value are reported as interest income.

Buy-backs

In a true buy-back transaction, also known as a repurchase agreement (repa), the asset is still reported in the balance sheet and the payment received is reported as a liability. The sold security is reported as a pledged asset among memorandum items in the balance sheet. The difference between spot payment and forward rate is accrual accounted over the term and reported as interest.

Derivative instruments

Derivative instruments are calculated at their true value. Derivative transactions with a positive market value on the balance sheet date are reported as investment assets, while transactions with a negative market value are reported as liabilities.

Equity lending

Equity lent is reported in the balance sheet, and disclosed as assets pledged under “Memorandum items”. Premiums received and accrued are reported as interest income.

Equipment

Investments in equipment, with in-house developed and externally-purchased software, are booked on current account.

Items entered directly against Fund capital

Contributions to and disbursements from the pension system, as well as transfers from the Special Funds and Liquidation Fund, owned jointly by the four buffer funds, are entered directly against Fund capital.

Income tax

The AP Funds are exempt from all income tax on investments in Sweden. Tax liability on investments outside Sweden varies from country to country.

Notes to the income statement and balance sheet

Note 1 Net interest income/expense

Amounts in SEK million	Jan-Dec 2003	Jan-Dec 2002
Interest income		
Bonds and other fixed income securities	2,154	2,130
Derivative instruments	921	1,420
Other interest income	45	279
Total interest income	3,120	3,829
Interest expenses		
Derivative instruments	- 180	- 607
Other interest expenses	- 25	- 29
Total interest expenses	- 205	- 636
Net interest income/expense	2,915	3,193

Note 2 Capital gains/losses, net

Amounts in SEK million	Jan-Dec 2003	Jan-Dec 2002
Equities and participations		
Listed	- 3,580	- 9,565
Unlisted	- 439	-
Bonds and other fixed income securities	455	10
Derivatives	1,898	- 3,047
Total capital gains/losses, net	- 1,666	- 12,602

Note 3 Unrealised changes in value

Amounts in SEK million	Jan-Dec 2003	Jan-Dec 2002
Equities and participations		
Listed	20,310	- 13,992
Unlisted	168	- 119
Bonds and other fixed income securities	- 163	1,795
Derivatives	345	- 226
Unrealised changes in value, net	20,660	- 12,542

Note 4 External asset management expenses

“External asset management expenses” refers to fees paid to external asset managers entrusted with confidential assignments pertaining to the management of listed and unlisted assets, and to management fees pertaining to listed unit trusts. External asset management expenses, distributed by active and passive mandate, and management fees to funds, are presented in the following table.

Distribution of Fund assets between external mandates and in-house asset management as at Dec. 31st 2003 (SEK m)

	Benchmark index	Market value, Dec. 31 st 2003 ¹⁾	Share of Fund capital, %	Asset manage- ment expense
External management mandate				
Equities mandate				
<i>Active management</i>				
SHB	Swedish equities	SBX	1,567	
SEB	Swedish equities	SBX	2,253	
SEB	Swedish equities – equally weighted	OSX	968	
Carlson	Swedish equities	SBX	4,903	
Carlson	Swedish equities – equally weighted	OSX	940	
Carnegie	Swedish equities – equally weighted	OSX	980	
Öhman	Swedish equities – equally weighted	OSX	925	
MFS Institutional Advisors	Global equities	MSCI World	3,685	
Citigroup	European equities – sector mandates	MSCI Europe – sector index	1,377	
Goldman Sachs	European equities – sector mandates	MSCI Europe – sector index	734	
Crédit Agricole	European equities – sector mandates	MSCI Europe – sector index	711	
Bankinvest	European equities – sector mandate/regional mandate	MSCI Europe – sector index/regional index	2,683	
Deutsche Asset Management	European equities – sector mandates	MSCI Europe – sector index	249	
Barclays	North America – Equities	MSCI North America	9,326	
Singer & Friedlander	Asia excl. Japan – Equities	MSCI Pacific excl. Japan	1,449	
Merill Lynch	Global equities	MSCI World	2,303	
Martin Currie	Japan – Equities	MSCI Japan	2,600	
Total		37,653	27	51
<i>Passive management</i>				
State Street	Global equities	MSCI World	2,531	
Barclays	Europe/North America – Equities	MSCI Europe/North America	10,263	
Total		12,794	9	6
Fixed income mandate		—	—	—
Total external management mandate		50,447	36	57
Investments in listed external funds				
Unit trusts	as per respective fund	6,665		
Fixed income funds	as per respective fund	5,374		
Total investments in listed external funds		12,039	9	29
Investments in Alternative Investments				
Unlisted equities and participations in Alternative Investments		255		
		255	0	24
Total external capital assets under management, and management expenses		62,741	45	110
In-house management mandates				
Listed equities and participations	SBX, OSX, MSCI	21,920		
Fixed income mandate, Swedish	SHB	28,595		
Fixed income mandate, foreign	Lehman	18,506		
Cash and bank balances, incl. deposits and accrued interest		4,076		
Unlisted equities in associated companies, incl. subordinated debentures		4,620		
Total capital assets managed in-house		77,717	55	
Other assets and liabilities		– 108	0	
Total Fund capital		140,350	100	

1) Market value including liquidity allocated for external mandates, and market value including derivative instruments and interest accrued for in-house asset management.

Note 5 Personnel costs

Amounts in SEK k	Jan–Dec 2003		Jan–Dec 2002	
	Men	Women	Men	Women
Average no. of employees	29	17	23	15
No. of employees, Dec. 31¹⁾	26	13	23	15
No. of persons in Executive Management Group, Dec. 31¹⁾	3	2	4	2
Salaries and remuneration				
Chairman of the Board		100		100
CEO		2,747		2,620
Board of Directors, excl. Chairman		400		425
Executive Management Group, excl. CEO		7,070		7,052
Other employees		24,257		24,216
Salaries and remuneration, total		34,574		34,413
Variable remuneration				
CEO		—		—
Executive Management Group, excl. CEO		—		—
Other employees		—		—
Variable remuneration, total		—		—
Remuneration to Members of the Board, in addition to directors' fees		—		—
Pension costs (incl. special employer's contribution)				
CEO		1,444		4,384
Executive Management Group, excl. CEO		1,929		1,522
Other employees		7,979		5,590
Pension costs, total		11,352		11,496
Payroll overhead				
Chairman		33		33
CEO		967		878
Board of Directors, excl. Chairman		131		139
Executive Management Group, excl. CEO		2,529		2,373
Other employees		7,786		7,981
Total payroll overhead		11,446		11,404
Other personnel costs		4,682		3,897
Total personnel costs		62,054		61,210

1) At the close of 2003, the Fund had a staff of 45, of whom 39 were full-time employees.

Pensions

The CEO is guaranteed retirement pension benefits in line with the retirement benefit agreement between BAO (The Employers' Organisation of the Swedish Banking Institutions) and Finansförbundet (The Union of Financial Sector Employees), known as the bank plan – but with the following supplementary clauses. The Fund and the CEO may both exercise the right to give notice with a retirement pension, as of the start of the month in which the CEO reaches the age of 60 years. The pension benefit shall in this instance correspond to 70 percent of the salary received at the time of retirement, and shall be paid until age 65.

New terms as of January 2004

As of January 2004, an individual retirement pension insurance policy has been taken out, to apply from a pensionable age of 65 years, with an annual premium corresponding to 34 percent of the agreed salary set each year (i.e. a pension benefit with an agreed premium). If employment is terminated as a result of dismissal by the Fund, the CEO is entitled to receive pension benefits from the Fund from age 60 until he reaches 65. In accordance with the agreement, the size of this pension corresponds to the number of years employed by the Second AP Fund.

The retirement benefit agreement between BAO (The Employers' Organisation of the Swedish Banking Institutions) and Finansförbundet (The Union of Financial Sector Employees) also applies to other senior executives.

cont. **Note 5 Personnel costs**

Severance-pay agreement

Where the contract of employment is terminated by the Fund, the CEO is entitled to a severance payment equivalent to eighteen months' salary, in addition to salary paid during the six-month period of notice, less income from an eventual new appointment. Other senior executives are not entitled to any severance pay.

Drafting and decision process

Directors' fees are determined by the Swedish Government, and the CEO's salary is determined by the Chairman and Deputy Chairman of the Board. The Second AP Fund has not appointed a remunerations committee.

Other directorships held by Members of the Board

See page 62.

Absence due to illness

In 2003, absence due to illness at the Second AP Fund amounted to 0.62 percent, calculated as a percentage of total days lost to illness against total normal working hours for all employees. No Fund employee has been absent due to illness for more than 60 days. Absence due to illness amounted to 0.35 percent for male employees and 1.17 percent for female employees.

Note 6 Other administrative expenses

Amounts in SEK million	Jan–Dec 2003	Jan–Dec 2002
Rental expenses	4	3
Custodial expenses	10	11
IT and computer expenses	22	37
Purchased services	12	22
Other expenses	14	17
Total other administrative expenses	62	90
"Purchased services" includes fees to auditors amounting to SEK 3 million (SEK 8 million).		
Audit assignments		
KPMG	1.87	1.76
PricewaterhouseCoopers	0.56	0.38
Other assignments		
KPMG	0.15	5.19
PricewaterhouseCoopers	—	1.15
Total	2.58	8.48

Note 7 Listed equities and participations¹⁾

Amounts in SEK million	Dec. 31 st 2003		Dec. 31 st 2002	
	Market value	Acquisition value	Market value	Acquisition value
Swedish equities	25,643	27,278	19,575	29,515
Foreign equities	44,956	52,776	33,040	47,187
Participations in Swedish funds	4,040	3,019	2,765	2,673
Participations in foreign funds	2,624	2,198	1,526	1,602
Total listed equities and participations	77,263	85,271	56,906	80,977

1) The 20 largest Swedish and foreign shareholdings, by value, are listed on page 60.
A complete list of Swedish holdings may be found on the Fund's website at www.ap2.se.

Note 8 Unlisted equities and participations

Amounts in SEK million		No. of equities	Dec. 31 ^a 2003		Acquisition value
			Participation right Capital	Votes	
Associated companies		Corp. reg.			
AP Fastigheter Holding AB	556650-4196	1,000,000	25%	25%	3,221
NS Holding AB	556594-3999	1,213,256	33%	33%	372
Total associated companies					3,593
Other unlisted holdings					
Swedish equities and participations		Corp. reg.			
Swedestart Life Science KB	969675-2337		5%		6
Swedestart Tech KB	969674-7725		3%		7
EQT Northern Europe KB	969670-3405		1%		110
Foreign equities and participations					
Carnegie Fund II Biotech Bridge			29%		49
Nordic Capital V, L.P.			3%		1
EQT Mezzanine L.P.			19%		22
Amaranth Capital L.P.			28%		51
Total other unlisted holdings					246
Total unlisted equities and participations					3,839
Total market value					4,016

Note 9 Bonds and other fixed income securities

Amounts in SEK million	Dec. 31 ^a 2003		Dec. 31 ^a 2002	
	Market value	Acquisition value	Market value	Acquisition value
Swedish State	18,363	17,718	16,434	15,789
Swedish municipalities	—	—	2	2
Swedish housing finance institutes	8,704	8,611	5,664	5,572
Other Swedish issuers				
Finance companies	546	525	343	333
Non-finance companies ¹⁾	1,679	1,514	1,669	1,652
Foreign states	12,059	12,715	11,743	11,757
Other foreign issuers	10,467	11,244	10,837	10,887
Demand loans	2,900	2,902	4,669	4,672
Total	54,718	55,229	51,361	50,664
Inflation-linked bonds	6,666	6,129	5,909	5,432
Other bonds	38,912	39,777	34,747	34,512
Treasury bills	—	—	—	—
Certificates	23	23	—	—
Participations in Swedish index-linked funds	104	100	—	—
Participations in foreign index-linked funds	5,270	5,587	5,405	5,417
Other instruments ¹⁾	843	711	631	631
Demand loans	2,900	2,902	4,669	4,672
Total	54,718	55,229	51,361	50,664

1) Including convertible debenture loans to associated companies totalling SEK 843 million (631).

Note 10 Derivatives

Amounts in SEK million	Dec. 31 st 2003		
	Face value ¹⁾	Derivative instruments with positive true value	Derivative instruments with negative true value
Currency-related instruments			
Forward contracts	93,644	2,550	– 1,018
Total	93,644	2,550	– 1,018
of which cleared	—		
Equities-related instruments			
Forward contracts	9,130	164	—
Total	9,130	164	—
of which cleared	9,130		
Fixed income instruments			
Forward contracts	3,897	3	0
Total	3,897	3	0
of which cleared	3,897		
Total derivatives		2,717	– 1,018

1) Face value refers to the number of contracts multiplied by the contract amount for the derivative instruments' absolute amount. The amount thereby includes both forward contracts purchased and sold, gross. Refer to page 36 for a description of the types of derivative instrument employed and the risks that can be managed with derivatives.

Note 11 Cash and bank balances

Amounts in SEK million	Dec. 31 st 2003	Dec. 31 st 2002
Cash and bank balances	883	1,159
Guarantees provided for forward trading	679	1,094
Total	1,562	2,253

Note 12 Prepaid expenses and accrued income

Amounts in SEK million	Dec. 31 st 2003	Dec. 31 st 2002
Income accrued	1,145	1,396
Refunds	38	87
Dividends accrued	56	44
Other prepaid expenses and accrued income	18	7
Total	1,257	1,534

Note 13 Fund capital

Amounts in SEK million	Dec. 31 st 2003	Dec. 31 st 2002
Opening fund capital as per approved balance sheet	117,090	133,493
Net payments to the national pension system		
Payments from RFV of pension contributions received	41,481	40,187
Payments to RFV for disbursement of supplementary pension benefits ¹⁾	– 39,338	– 38,202
Surplus	2,143	1,985
Transferred from Special Funds		
From First AP Fund's liquidation fund	394	3,017
From Fourth AP Fund's liquidation fund	30	–
Total	424	3,017
Net result for the year	20,693	– 21,405
Total	140,350	117,090

1) Including remuneration for administration expenses amounting to SEK 281 million (263).

On Dec. 31st 2003, the capital carried forward in the accounts of the First AP Fund's Liquidation Fund and the Fourth AP Fund's Special Fund amounted, respectively, to SEK 5,214 million (6,511) and SEK 1,291 million (1,377). For information about these Special Funds, please refer to the First AP Fund's website at www.ap1.se, or to the Fourth AP Fund, to order a copy of the annual report.

Note 14 Accrued expenses and deferred income

Amounts in SEK million	Dec. 31 st 2003	Dec. 31 st 2002
Management fees	41	15
Accrued interest expenses on currency forwards	35	98
Other accrued expenses	19	16
Total	95	129

Note 15 Obligations

Amounts in SEK million	Dec. 31 st 2003	Dec. 31 st 2002
Obligations concerning future payments		
Investment obligations, unlisted holdings	1,411	563
Total	1,411	563

Gothenburg, February 5th, 2004

Kurth Augustson

Gunnar Larsson
Chairman

Bo Dockered

Märtha Josefsson

Clas Nykvist

Roland Svensson

Lilian Ringsand

Ylva Thörn

Lars Idermark
CEO

Auditors' report

Auditors' report for the Second AP Fund
(Corp. reg.: 857209-0606)

We have examined the annual report, the accounting records and the administration of the Second AP Fund by the Board of Directors for the financial year 2003. The Board is responsible for the accounting records and administration. Our duty is to state our opinion with respect to the annual report and the administration, based on the results of our audit.

Our examination has been conducted in accordance with generally accepted auditing standards in Sweden. This means that we have planned and conducted the audit in such a manner as to satisfy ourselves, beyond reasonable doubt, that the annual report contains no significant errors. An audit comprises the examination of selected supporting documentation for the figures and other information presented in the accounting records. An audit further comprises an evaluation of the accounting principles and of the application of these same principles by the Board, as well as evaluating the data accumulated in the annual report.

The annual report has been prepared in accordance with the Swedish Act on National Pension Funds, and therefore provides a true and fair picture of the Second AP Fund's net result and financial position in accordance with generally accepted auditing standards in Sweden.

Our audit has given no reason to qualify our approval of the annual report, of the enclosed income statements and balance sheets, of the accounting or inventory of the Fund's assets or any other aspect of its administration.

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

Gothenburg, February 5th, 2004

Anders Bäckström
*Authorised Public Accountant
Appointed by
the Swedish Government*

Göran Jacobsson
*Authorised Public Accountant
Appointed by
the Swedish Government*

Shares, participations and fixed-income securities

Second AP Fund's 20 largest Swedish shareholdings¹⁾

Name of company	Share of capital, %	No. of equities	Market value, SEK	Share of voting rights, %	Sector
Ericsson B	1.09	177,203,116	2,285,920,196	0.02	Information Technology
Swedish Handelsbanken A	1.84	13,156,836	1,934,054,892	2.00	Financials
Swedish Handelsbanken B	0.02	158,238	22,548,915	0.00	Financials
AstraZeneca PLC	0.01	10,749,010	1,878,837,248	0.01	Healthcare
Volvo A	1.21	5,410,255	1,141,563,805	3.20	Industrials
Volvo B	0.52	2,257,608	496,673,760	0.13	Industrials
Nordea	0.96	28,148,866	1,520,038,764	0.96	Financials
Hennes & Mauritz B	1.01	8,481,262	1,450,295,802	0.51	Consumer Discretionary
TeliaSonera	0.63	29,618,964	1,113,673,046	0.63	Telecommunication Services
Föreningssparbanken A	1.36	7,262,888	1,027,698,652	1.36	Financials
Sandvik	1.40	3,626,291	899,320,168	1.40	Industrials
SCA B	1.28	3,003,785	883,112,790	0.50	Raw Materials
Skandinaviska Enskilda Banken A	1.12	7,879,862	835,265,372	1.16	Financials
Skandinaviska Enskilda Banken C	0.02	139,841	13,494,657	0.00	Financials
Tele2 B	1.40	2,066,406	793,499,904	0.61	Telecommunication Services
Electrolux B	1.35	4,414,431	697,480,098	1.07	Consumer Discretionary
SKF B	1.60	1,827,495	508,043,610	0.61	Industrials
SKF A	0.21	240,105	66,989,295	0.78	Industrials
Skandia	1.75	17,787,552	466,033,862	1.75	Financials
Atlas Copco A	0.82	1,745,337	449,424,278	1.18	Industrials
Atlas Copco B	0.52	1,082,014	253,732,283	0.07	Industrials
Investor B	0.79	5,970,602	414,956,839	0.16	Financials
Investor A	0.28	2,151,955	148,484,895	0.60	Financials
Assa Abloy B	1.29	4,728,486	404,285,553	0.88	Industrials
Castellum	5.10	2,193,086	372,824,620	5.10	Financials

Second AP Fund's 20 largest foreign shareholdings¹⁾

Name of company	No. of equities	Market value, SEK	Sector
Citigroup INC	1,951,853	645,611,266	Financials
Pfizer Inc.	2,439,924	620,252,956	Healthcare
General Electric Co	2,686,503	598,849,442	Industrials
Bp Amoco Plc	10,233,322	597,108,720	Energy
Vodafone Group PLC	32,369,739	594,389,200	Telecommunication Services
Skyworth Digital Holdings Ltd	19,456,251	570,753,475	Financials
Nokia	4,411,671	549,112,513	Information Technology
Exxon Mobil Corp	1,713,342	502,387,484	Energy
Intel Corporation	2,136,689	495,046,611	Information Technology
Total SA	335,376	448,656,733	Energy
Microsoft Corporation	2,179,414	431,869,544	Information Technology
Novartis	1,295,327	423,151,058	Healthcare
GlaxoSmithKline Plc	2,489,479	410,446,927	Healthcare
IBM Corporation	602,708	401,922,100	Information Technology
Royal Dutch Petroleum	997,957	378,593,223	Energy
Bank of America Corp	612,409	354,412,099	Financials
Nestle SA -R-	196,525	353,299,104	Consumer Staples
Johnson & Johnson	936,204	347,995,638	Healthcare
Royal Bank of Scotland Group	1,625,047	344,535,779	Financials
Honda Motor Co Ltd	1,048,900	335,209,781	Consumer Discretionary

1) The above table of Second AP Fund shareholdings lists the 30 largest Swedish holdings and 20 largest foreign holdings, by worth. "Swedish shareholdings" even includes companies that have changed their legal domicile after merging with a foreign company, as with AstraZeneca and StoraEnso. Share of capital and voting rights for shareholdings listed principally on foreign exchanges in no case exceeds 0.3% and is therefore not reported.

A complete list of the Second AP Fund's Swedish holdings may be found on the Fund's website at www.ap2.se. A complete list of foreign holdings may be ordered from the Second AP Fund.

Second AP Fund holdings in unit trusts and fixed income funds

	No. of equities, participations	Market value, SEK m
Unit trusts, foreign		
F&C Global emerging markets portfolio	8,685,263	662
StateStreet, emerging markets	200,929	567
Genesis emerging markets	3,915,883	406
Pictet Funds, emerging markets	191,062	359
CitiEquity emerging markets fund	268,673	330
Deutsche Bank Global emerging markets fund	2,372,620	227
Skandia småbolag (small-cap) Europe	952,469	72
	No. of equities, participations	Market value, SEK m
Fixed income funds, foreign		
BGI Euro Liquidity	418,374,189	3,804
Ishare Investop Corp	1,745,510	1,389
Nektar ¹⁾	52,629	105
The Finch Neutral Fund ¹⁾	82,043	77

1) Hedge funds.

	No. of equities, participations	Market value, SEK m
Unit trusts, Swedish		
Carlson Sverige Småbolagsfond (small-cap fund)	1,516,985	1,022
SEB Sverige Småbolag (small-cap fund)	92,654,653	989
SHB Småbolagsfond (small-cap fund)	2,062,441	534
Lannebo Småbolagsfond (small-cap fund)	21,711,522	305
Robur Småbolagsfond (small-cap fund)	14,459,404	293
Enter Sverige Focus	306,115	268
Eikos ¹⁾	943	163
Zenit ¹⁾	3,802	145
RAM One ¹⁾	151,992	137
SEB Sverige Småbolag Chans/Risk (small-cap fund)	3,263,480	136
Nordic Absolute Return Fund ¹⁾	500,000	51

1) Hedge funds.

Bonds and other fixed income securities

Swedish inflation-linked bond portfolio, five largest holdings

Bond	Market value, SEK m
Sgb 3105	2,003
Sgb 3104	1,516
Sgb 3102	1,377
Sgb 3101	1,377
Sgb 3001	393

Swedish nominal bonds, five largest holdings

Bond	Market value, SEK m
Sgb 1041	1,980
Sgb 1037	1,589
Sgb 1035	1,343
Sgb 1044	1,334
Sgb 1046	1,252

Global government bond portfolio, five largest holdings

Bond	Market value, SEK m
Ger Bund 07/04/2007	694
Ger Bund 07/04/2012	471
France Btan 10/25/2006	447
Sgb 1044	441
Us Tsy 08/15/2023	410

Global credit portfolio, five largest holdings

Bond	Market value, SEK m
DB Iboxx Linked Note	502
KFW 04/18/2005	149
EIB 07/06/2021	133
Ontario Province 10/01/2008	117
KFW 08/17/2007	114

Detailed information about the Second AP Fund's holdings in fixed income securities is available on request from the Fund.

Board of Directors and Executive Management



Upper row, from left:

Gunnar Larsson

CHAIRMAN

Chairman of The Swedish Sports Confederation. Chairman of the boards of Tholin & Larsson-Gruppen AB and GöteborgsOperan. Directorships on several boards, including Castellum AB and Samhall AB. Former authorised public accountant and Municipal Commissioner for Gothenburg. Born 1940.

Bo Dockered

VICE CHAIRMAN

Chairman of the boards of AB Trav and Galopp, Sveaskog AB and The Swedish University of Agricultural Sciences. Honorary Doctor of Agronomy (Dr.h.c. Agronomy) and farmer. Born 1941.

Ylva Thörn

President, Swedish Municipal Workers' Union. Chairman of The Public Services International. Directorships on several boards, including LO (The Swedish Trade Union Confederation) and Riksbyggen. Assistant nurse. Born 1954.

Clas Nykvist

Financial director, Swedish Building Workers' Union. Directorships on several boards, including Folksam Spar AB. Born 1948.

Kurth Augustson

Former president of SCA Mölnlycke AB and AB Marabou. Directorships on several boards, including BRIO AB, Pergo AB, Orrefors Kosta Boda AB and Oy Paulig. M.Sc (Econ). Born 1944.

Lower row, from left:

Märtha Josefsson

Independent investment consultant. Former Investment Director at DnB Asset Management and Carlson Investment Management AB. Chairman of Carlson Lärarfonder. Directorships on several boards, including Drott, Song Network, Luxonen and Skandia Funds. B.A. Born 1947.

Roland Svensson

Former President and CEO of Coop Norden AB and KF Group. Chairman of the Swedish National Museum of Art. LL.B., Uppsala University. Born 1941.

Lilian Ringsand

Senior Deputy Chairman of SIF (Swedish Union of Clerical and Technical Employees in Industry) and TCO (Swedish Confederation of Professional Employees). Directorships on the board of the Authority for Advanced Industrial Training. Research engineer at Boliden Mineral. Born 1942.

Lars Idermark

CHIEF EXECUTIVE OFFICER

Directorships on several boards, including AP Fastigheter AB, Södra Skogsägarna and Swedish Meats. Born 1957.



Executive Management

Fund management, Second AP Fund

Above, from left:

Margaretha Veres, Personal Assistant to the CEO, born 1945

Lena Smeby-Udesen, CFO, born 1961

Lars Idermark, CEO, born 1957

Martin Jonasson, General Counsel, born 1964

Petter Odhnoff, CIO, born 1956

Auditors

Anders Bäckström

Authorised Public Accountant

KPMG

Göran Jacobsson

Authorised Public Accountant

PricewaterhouseCoopers

Definitions

Absolute/relative return on investment

The return generated on a portfolio or portfolios of assets, measured in kronor or percent, of the original invested amount.

Active return (also relative return)

The difference in return between a portfolio and its benchmark index.

Total return

Calculated arithmetically and time-weighted.

Active/passive management

Active: Management where the portfolio may deviate from the benchmark portfolio, to generate an active return.

Passive: Management where the portfolio is identical with the benchmark portfolio.

ALM study

Asset Liability Modelling. An analytical model used to determine the Fund's benchmark portfolio. The study, which is revised on a continual basis, is designed to determine the optimal composition for the different classes of asset under Fund management, to ensure that it satisfies the Fund's long-term commitment to the collective requirements of the Swedish national pension system. The judgements based on this analysis shall take into account demographic change as well general economic trends.

Strategic portfolio

The Second AP Fund's strategic portfolio is determined annually by the Board of Directors and confirms the Fund's decision on strategic asset allocation. It also serves as the benchmark portfolio in the day-to-day management of the Fund's capital assets.

DEFINITIONS OF RISK

Market risk

The market risks most relevant to the Second AP Fund are share-price risk, interest-rate risk and currency risk.

Credit risk and counterpart risk

"Credit risk" refers to the risk that an issuer may become insolvent or be awarded a lower credit rating. "Counterpart risk" refers to the risk that the other party may be unable to meet its business obligations.

Operational risk

"Operational risk" refers to the risk that an error or stoppage in operations could lead to economic loss or reduced credibility.

Liquidity risk

"Liquidity risk" refers to the risk that securities cannot be converted into cash, because of reduced access to or demand from the market, which either precludes the purchase or sale of such securities, or would require their sale at a loss.

Absolute return on investment

Return on portfolio = R_p

Absolute risk

Volatility = standard deviation for return on portfolio

Risk-adjusted absolute return

Sharpe ratio = $\frac{R_p - R_f}{\sigma_p}$

Where R_f = risk-free interest and
 σ_p = standard deviation for return on portfolio

Relative return

Surplus return = $R_p - R_i$

Where R_i = return against index

Tracking Error (active risk)

Standard deviation relative to return = $\sigma_p - i$

Risk-adjusted relative return

Information ratio = $\frac{R_p - R_i}{\sigma_p - i}$

Solberg

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