



Andra AP-fonden
Second Swedish National Pension Fund - AP2

Annual Report 2005

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Unless otherwise stated, the portfolio assets referred to in this report are "allocated exposures". In addition to booked fair 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 their fair values.

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

This is the Second AP Fund

The capital assets invested in Sweden's publicly financed national pension system are managed by five "buffer funds", which invest these assets in the capital markets. The joint investment regulations, which are identical for the First to Fourth Swedish National Pension 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. Since then, it has progressively developed and implemented its strategies and infrastructure to become a modern and internationally focused portfolio 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 maximum long-term return at minimum risk, supported by efficient and professional portfolio 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".

2005 in brief

- The capital assets of the Second Swedish National Pension Fund/AP2* totalled SEK 190.6 billion as per December 31st 2005, an increase of SEK 32.5 billion compared with the preceding year. During the year, the Fund reported a net inflow of SEK 2.9 billion. Net profit for the year totalled SEK 29.6 billion.
- The Fund posted a return of 18.7 percent on the total portfolio, before commission fees and operating expenses. If these expenses are included, the portfolio generated a return of 18.5 percent.
- The Fund posted a positive relative return of 0.2 percent for market-listed assets, before commission fees and operating expenses, for 2005. This positive return is primarily attributable to the success of its tactical allocation during the year.
- The solid growth in Fund capital may be attributed primarily to the maintenance of a high allocation of equities, fully in line with long-term investment strategy.
- The level of exposure in foreign currency was 11 percent as per December 31st 2005. As a result of this limited degree of exposure, the weakness of the Swedish krona had a negative impact on Fund earnings.
- Restructuring of the Fund's portfolio management activities was completed in 2005, whereby mandates awarded were classified according to the level of risk accepted. Most equities were managed according to strategies based on low active risk. In addition to these, a number of more specialised mandates were awarded, involving higher levels of risk and offering higher potential returns. A large portion of the Fund's low-risk equity management has been taken over by its in-house quantitative management group, established in 2004.
- During the year, the Fund activated mandates in tactical asset allocation and the management of international bonds and credits.

*The Second AP Fund is officially translated as the Second Swedish National Pension Fund/AP2. In body text, for convenience, this is shortened to the Second AP Fund and, in some cases, AP2.

Three-year review	2003	2004	2005
Fund capital, SEK bn	140.4	158.1	190.6
Net inflows from RFV/Swedish Social Insurance Administration and liquidation/special funds, SEK bn	2.6	1.7	2.9
Net profit for the year, SEK bn	20.7	16.1	29.6
Return on total portfolio, excl. expenses, %	17.8	11.6	18.7
Relative return on market-listed assets, excl. operating expenses, %*	-0.5	-0.6	0.2
FX exposure, %	8	10	11
Under active, incl. enhanced, management, %	89	90	90
Under external management, incl. investments in private equity funds, %	45	37	28

* Relative return refers to the difference in return between portfolio and benchmark index.

The Second AP Fund: Mission, objectives and operations

The national pension system in brief

Sweden has a financially stable national pension system. Approximately 90 percent of future pensions are financed from contributions in the form of taxes and premiums levied based on the “pay-as-you-go” system, whereby the gainfully employed part of the population pays for the pensions of those who have retired on an ongoing basis. The remaining 10 percent is financed from investments managed by Sweden’s National Pension Funds. Each krona paid into the system earns one krona in pension entitlement. Should the system lack full financing, it features an inbuilt automated balancing function, or “brake”.

The Second AP Fund is one of the five “buffer funds” that comprise the Swedish pension system. The combined capital assets of these funds are designed to act as a buffer, smoothing out eventual periods of surplus and deficit experienced over the longer term.

Overall goal and result

The Second AP Fund’s overall goal is to generate a maximum long-term return on invested assets, with a view to minimising the impact should automatic balancing (of a deficit within the pension system) be required. Assets shall be managed with a low level of risk.

The Second AP Fund has established a target of 4.5 percent average real return on investment per year over the long term. The return on the total portfolio for 2005 was 18.7 percent.

As for relative return, the goal is to outperform the Fund’s benchmark index by 0.5 percentage points. The Fund did not attain this objective in 2005.



Investment strategy for value creation

The Second AP Fund implements a three-stage value creation strategy:

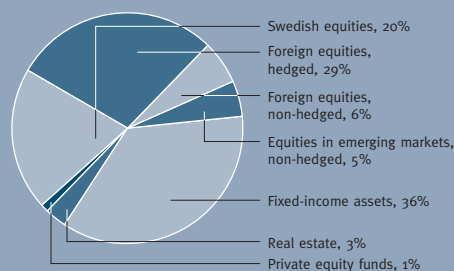
1. Selection of strategic portfolio
2. Selection of benchmark index
3. Active portfolio management

The strategic portfolio is determined with the aid of the Fund's own in-house "ALM model", enabling qualified prediction of anticipated development more than 30 years ahead. The model is an aid to determine the relative allocation of asset classes in the strategic portfolio and to finalise the Fund's foreign-exchange strategy. The strategic portfolio for 2006 comprises 60 percent equities, 36 percent fixed-income assets and 4 percent alternative investments.

Index selection is an integral part of the Second AP Fund's investment process.

The Fund's choice of index governs its active management strategy. Return on assets, under in-house and external management, shall exceed the indexes selected by the Fund.

New strategic portfolio 2006



Broad investment options

The Second AP Fund invests its assets in four different ways.

Tactical allocation

Tactical allocation enables the Fund to generate a higher return by deviating from its own strategic portfolio. In practice, this means that market perceptions are translated into decisions concerning under or over-weighting in foreign exchange or classes of asset.

Equities

The Second AP Fund is a global fund manager. The majority of the Second AP Fund's investments in Swedish and European equities are handled in-house, while external managers are primarily engaged for non-European and global investments.

Fixed-income and FX

The portfolio of fixed-income assets consists mainly of nominal and inflation-linked Swedish bonds, global government securities and corporate bonds. The Fund also trades in foreign currencies.

Alternative investments

To spread the investment risk and generate a higher return, the Fund invests in private equity funds and real estate.

Follow-up for future success

The Second AP Fund operates a sophisticated system to monitor and follow-up transactions. Investments already made are thoroughly analysed, to establish optimum conditions for future investment. This analytical process is conducted in close cooperation with the Fund's portfolio managers.

Business control

Control, administration and reconciliation of in-house and external portfolio management activities.

Yield analysis

Ongoing analysis of portfolio management performance.

Risk management

Ongoing analysis and control of risk utilisation.

Economic analysis

Analysis also of the Fund's unlisted holdings, based on acquisition value and ongoing assessment in line with EVCA* and similar principles.

*The European Private Equity and Venture Capital Association



Chairman's report: Best result to date



2005 was a good year for the Second AP Fund. Net profit for the full twelve months amounted to SEK 29.6 billion. The absolute return on investment was 18.7 percent and active management generated a positive return on investment. In-house efforts to implement the Fund's new equity management strategy have been intense.

The Second AP Fund has been operating in Gothenburg for the past five years. We have established a reputation as a modern, high-quality and professional fund manager. The Fund manages assets amounting to SEK 190.6 billion. Our goal is to manage the Fund's capital assets in a manner that will enable us to contribute to the financial security of current and future pensioners in their old age. The Fund can best do this by responsible management of pension assets with a view to generating a maximum return.

The Fund's new approach means that a much greater portion of pension assets are now under in-house management, which is only natural after a five-year building process.

The Second AP Fund's primary objective is to generate a high absolute long-term return on invested capital. This is the very essence of the Swedish National Pension Funds' mission.

We shall of course avoid incurring more risk than absolutely necessary. At the same time, the demands for a high return on investment are considerable. The Second AP Fund has established a target absolute real return of 4.5 percent per year.

The Second AP Fund's mission is very long

term, involving an investment horizon of 30 to 40 years. This said, we must also meet our targets in the shorter term, in the framework of a five-to-ten-year horizon.

Strong performance in 2005

Financially, 2005 was a good year. Return on investment was 18.7 percent, capital assets increased by SEK 32.5 billion and the Fund's net profit for the year was SEK 29.6 billion.

Since the Fund was established, its capital assets have increased by SEK 56.6 billion, including inflows of SEK 16.6 billion.

Implementation of new equities strategy

An ambitious programme to restructure the Fund's equity management organisation was initiated in 2004. It was decided to adopt a "core/satellite" strategy, where the majority of assets would be managed in line with low active-risk strategies under "core" mandates, while a sharply limited number of assets would be managed under "satellite" mandates. These "satellite" mandates would involve a higher level of risk, in the hope of a higher return. The Fund's new approach means that a much greater portion of pension assets are now under in-house management, which is only natural after a five-year building process. This has created cost-efficient portfolio management.

During 2004 and 2005, the Fund has terminated 21 equities mandates and eight hedge-fund mandates.

The Fund's core values – curiosity, flexibility and innovation – have played a key role in this change process, and I am proud of the professionalism and commitment demonstrated by our organisation.

Cost efficiency

In terms of media coverage, the main topic addressed during the year was the costs associated with Swedish National Pension Funds. Naturally, we shall do everything in our power to keep the cost of managing these pension assets to a minimum. But the end result, the bottom line, is still more important – at least for our principal and for Sweden's future pensioners. The Second AP Fund's trend of costs rose rapidly during the first few years of its establishment but, during 2005, costs as a percentage of total assets under management were reduced.

One key reason for the Fund's initially higher operating cost was its dependence on external fund managers, who are more expensive than in-house portfolio managers, during the build-up phase. Thanks to the Fund's new "core/satellite" strategy and the increasing degree of in-house portfolio management, costs in relation to the volume of assets managed are falling. However, two factors should be kept in mind when studying the operating cost of Sweden's National Pension Funds in absolute terms. First, many of our costs are linked to the amount of capital under management. Second, the cost of managing assets in partial markets, which are expected to generate a higher return, is often higher. This applies, for example, to investment in emerging markets and private equity funds – investment sectors where the Second AP Fund has posted solid returns in the past few years.

Corporate governance in focus

Recently, demands that the Second AP Fund play an active role in corporate governance have increased dramatically. The Fund's role in corporate governance issues is frequently addressed at board meetings. This is perfectly natural, given the fact that pension funds now control a significant proportion of the equities traded in Sweden and on global stock markets. It is also natural given the dramatic growth in popularity of another type of fund manager, the so-called "hedge funds". They often

play a key role in market dynamics, by exposing weaknesses and imperfections. However, a consequence of their short-term approach to value creation is that their activities sometimes clash with our own interests, which are based on a much longer investment horizon.

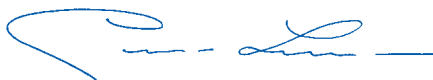
The Second AP Fund is determined to adopt an active role in corporate governance. We have established a corporate governance policy and a working and analytical approach to governance issues that derive from our mission: to generate the highest possible return. Our work with governance issues focuses on value creation, and although the strategy has been in place barely twelve months, our approach has already generated plenty of favourable reactions.

I am convinced that corporate governance issues will continue to be a subject of debate at international level, as well as in Sweden. The Second AP Fund will be only too pleased to act as a speaking partner in addressing these important issues.

Eva Halvarsson appointed new CEO

No organisation or business can ever be fully developed. The Second AP Fund is imbued with a constant need to seek new solutions and angles of approach, to stretch limits wherever possible and to dare to change whatever fails to satisfy. Lars Idermark, who has been the Fund's CEO since its foundation in 2000, has personified this spirit and has also achieved excellent results. Now that Lars has decided to accept a new challenge outside the Fund, it is pleasing to be able to present his successor, Eva Halvarsson, who takes over as CEO of the Second AP Fund in February 2006. She has unique experience in the administration of state-owned companies and knows what is required in combining the need for a competitive return on investment with the responsible administration of public assets. She stands for committed and dynamic leadership, and has a close association with Gothenburg.

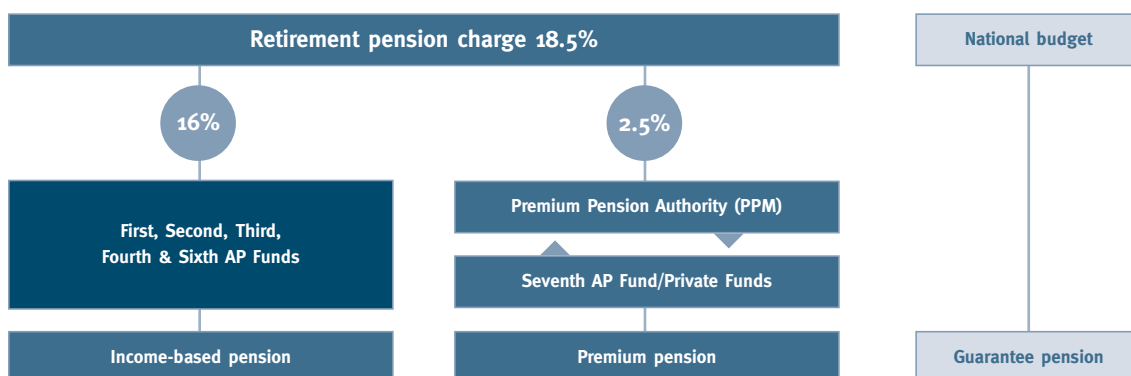
Gothenburg, February 2006.



Gunnar Larsson, Chairman

The Second AP Fund: An important part of the Swedish national pension system

The Second AP Fund is one of the Swedish national pension system's "buffer" funds. The Fund is tasked with achieving the highest possible return on assets under management and is also intended to act as a counterbalance at times when the national pension system is required to make major pension disbursements. When the baby-boomers of the 1940s and 1960s are due for retirement, the demands made on the pension system will be considerable.



The reformed income-based pension system is separate from and independent of the national budget. Future pension entitlement will be fundamentally determined by the individual's income, based on lifetime income.

The national retirement pension will consist of three elements

The national retirement pension to which individuals will be entitled will comprise three elements: an income-based pension, a premium pension and/or a guarantee pension.

The retirement pension is funded by an 18.5 percent charge levied on total income up to 7.5 times the income base amount (via social charges and taxes) on each wage/salary payment. Of this total charge, 16 percentage units are utilised to fund pension disbursements for the year (income-

based pension). The remaining 2.5 percentage units are saved and generate interest in an individual premium pension account.

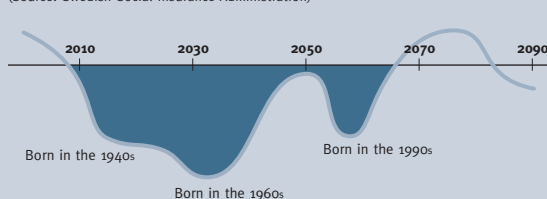
The guarantee pension provides a supplementary pension for those with low or no incomes. This guarantee pension is funded from the national budget.

The role of the buffer funds

Income-based pension contributions are transferred to the system's buffer funds: the First, Second, Third and Fourth AP (National Pension) Funds. Each fund contributes a quarter of the total charges levied and funds a quarter of total pension disbursements. The Sixth AP Fund is also considered to be a buffer fund, but differs from the others, partly the consequence of a different administrative directive. Monthly disbursements from the

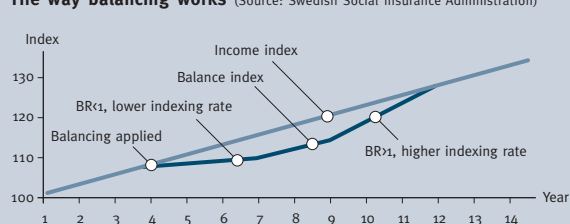
Impact of retirement peaks on pension system

(Source: Swedish Social Insurance Administration)



When baby-boomers retire, they create a demand for a buffer in the pension system. The system's disbursements will exceed contributions after 2010, when the large post-war generation of baby-boomers retire from gainful employment.

The way balancing works (Source: Swedish Social Insurance Administration)



The balance ratio (BR) represents the system's assets divided by combined pension liability. If the balance ratio is less than 1, balancing is applied. This means that pension liability and pensions are adjusted upwards only by wage growth multiplied by the balance ratio. This process continues until parity is reestablished.

income-based pension system are therefore made from the buffer funds.

In principle, contributions received during a given month are the same as the sums disbursed in the form of payments to pensions for the same period. This means that the income-based pension system generates almost no savings at the national level. For those covered by the system, however, the pension contribution may be seen as a form of saving.

Automatic balancing*

Seen in the broader context of the Swedish national budget, the pension system is highly robust and able to tolerate significant economic and demographic change. It features a number of special inbuilt control mechanisms.

Seen in the broader context of the Swedish national budget, the pension system is highly robust.

To counteract an actual decline in purchasing power, the total pension liability is adjusted on an ongoing basis, to reflect changes in the income index. Nevertheless, there are a number of exceptions where this basic principle is ignored.

In some cases, certain demographic and economic trends, when combined with a fixed level of contributions for funding income-based pensions, make it impossible to adjust the income-based pension at a pace commensurate with average growth in income, without jeopardising the system's long-term stability. In such a situation, instead of raising the pension contribution from

the current 16 percent of total income, it is possible to diverge from the income index, applying the "brake" to achieve an automatic balance.

Balancing ensures system stability

Pension assets are the sum of contributions to the system, and liabilities are the sum of disbursements due. Dividing the pension system's assets by the total pension liability returns a measure of its financial health. This is illustrated by a ratio known as the balance ratio. If the balance ratio exceeds one (1), the assets outweigh the liabilities. If the balance ratio is less than one, the system's liabilities outweigh its assets.

Balancing is applied when the balance ratio falls below one. When this automatic balancing process is activated, pension assets and pensions are indexed according to the change in balance index rather than income index. The rate at which pensions are adjusted upwards is modified until the system is in balance again (see chart below).

A mechanism for distributing a sustainable pension-system surplus is currently under consideration.

The pension system's balance sheet

In 2004, the national pension system had total assets amounting to approximately SEK 6 253 billion, of which the AP Funds accounted for SEK 646 billion. Pension liabilities amounted to SEK 6 244 billion, resulting in a balance ratio of 1.0014. The balance ratio represents total pension system assets divided by total pension liabilities. In 2004, this yielded an excess return of approximately SEK 9 billion (see chart below).

*The term "brake" is sometimes used to describe the automatic balancing system. When the "brake" is applied, pensions are revised upwards at a rate lower than income index.

Status of Swedish pension system as per December 31st 2004, SEK bn

ASSETS +	
Contributions	5 607
Buffer funds	646
	6 253
LIABILITIES -	
Pension disbursements due	6 244
Surplus	9
	6 253

Small surplus in pension system



Target, result and costs: Absolute return exceeds target for third year in succession

The Second AP Fund has exceeded its targeted absolute return for the third year running. The selected indexes have added value, and active management of Fund assets generated a favourable result in 2005.

The Second AP Fund's assets are managed with a view to generating a buffer for future pension disbursements as part of the reformed national pension system.

The Fund's operational activities started in 2001. The primary focus is to maximise return on investment, so as to minimise the consequences of automatic balancing within the pension system over the longer term. The Second AP Fund's specific risk is a weak return on the assets under management, especially if the pension system – or Sweden's economy – underperforms.

The Fund's activities are long term and are therefore judged over a long period. Rolling five-year periods are considered adequate for measuring performance.

Solid absolute return in 2005

To ensure attainment of the pension system's long-term overall objective, the Fund calculates a long-term target for absolute return on investment. If the Second AP Fund and its fellow buffer funds satisfy this long-term target, and if economic growth in Sweden develops in line with the Fund's forecast, it is likely that the pension system, at least the national pension system, will function smoothly.

The current target for real return on investment is 4.5 percent. The graph below presents absolute return in relation to the Fund's real target for return on investment for the years 2001–2005.

The Second AP Fund posted a 17.8-percent real return for 2005, exceeding target.

High weighting in equities key factor

The stock market recovery during the latter part of the autumn boosted market rates beyond the top levels noted during the first quarter. This also meant that, on balance, 2005 was a good year, with both fixed-income and equity portfolios generating solid returns.

The Fund met its target for real return on investment in 2003, 2004 and 2005, but not in 2001 and 2002. This may be attributed primarily to the overall portfolio's high weighting in equities, which had a negative impact on return due to the sharp decline of stock markets in 2001 and 2002. Since 2001, the Fund has averaged a nominal 5.0-percent annual return on investment.

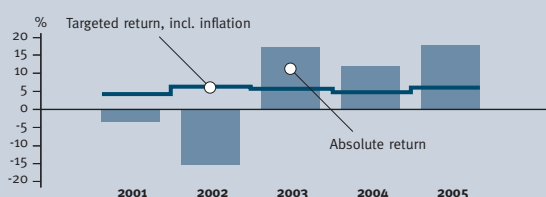
Choice of index has positive impact

As of July 1st 2005, the Fund has also reported the impact of its selection of benchmark index (more details on page 14). This has generated an excess return of 1.2 percent in 2005. The Fund has selected its own benchmark indexes since 2003, generating a total excess return of 3.7 percent.

Favourable relative return

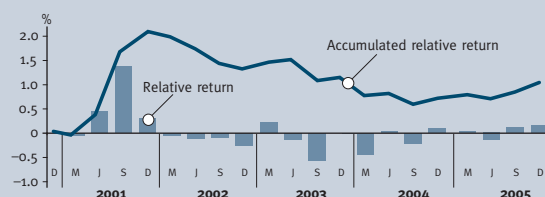
The Second AP Fund's targeted relative return on investment is 0.5 percent. This means that the Fund must outperform the benchmark portfolio

Five years' statistics on absolute return, 2001-2005



For the past three years, the Second AP Fund has exceeded its long-term target for real return on investment.

Relative return on Fund's listed assets, 2001-2005



The graph shows the Fund's accumulated relative return since its inauguration in 2001. The bars show relative return by period.

by 0.5 percentage units. This is a measure of the Fund's success in managing its assets to generate a value in excess of that generated by mere exposure to market trends. The Second AP Fund posted a relative return on investment of 0.2 percent in 2005. This is largely attributable to successful management of foreign equities and correct decisions concerning tactical asset allocation.

The Second AP Fund posted a relative return on investment of 0.2 percent in 2005.

Risk utilisation well within prescribed limits

Day-to-day management of the Fund's assets shall be conducted so that the anticipated active risk for the entire portfolio of listed assets shall not exceed three percent. In recent years, the financial markets have been characterised by low volatility. Rated as a standard deviation from ROI, volatility for the portfolio of market-listed equities was 4.8 percent. As for risk utilisation by asset class, active risk for Swedish equities was 1.6 percent, foreign equities 0.7 percent and fixed-income assets 0.4 percent. The Fund's modest overall level of risk utilisation in 2005 is partly attributable to application of the new "core/satellite" strategy to its portfolio management activities.

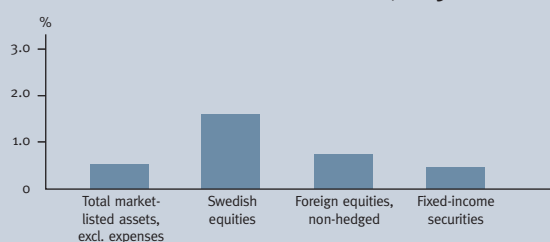
"Core/satellite" strategy promotes cost efficiency

The Second AP Fund has a target real return of 4.5 percent. The target is determined based on the anticipated growth of the Swedish National Pension System's assets and on what will therefore

be required of the Second AP Fund in meeting its commitments concerning the financing of future pensions. With current real interest at 1.5 to 2 percent, it is essential that the Fund locate asset classes that can generate a higher return with a balanced risk. Exposure in high-yield asset classes often incurs higher portfolio management costs. Private equity funds provide one example where, compared to other asset classes, the most successful fund managers have been able to generate high returns over a considerable period.

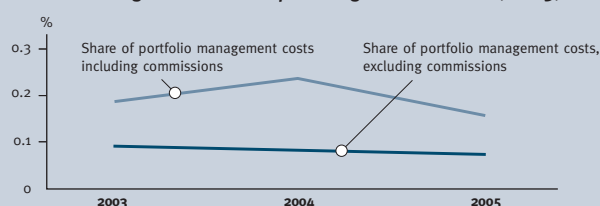
Conversion to a "core/satellite" strategy during 2004 and 2005 (see page 15) has improved the cost-efficiency of the Fund's portfolio management. One consequence is a reduction in the cost of portfolio management relative to the volume of assets managed in 2005.

Risk utilisation in the different asset classes, 2005



The modest level of risk utilisation during the year is attributable to low volatility and the adoption of a new strategy.

Portfolio management costs as percentage of total assets, 2003, 2004 and 2005



Following the build-up phase, costs have declined as a percentage of total assets.

Second AP Fund investment strategy: Well-balanced for long-term value

In several significant respects, the size of future pensions will be determined by factors which the Swedish National Pension Funds will be unable to influence through their investments. The most important conclusion to be drawn from the Second AP Fund's strategic analysis is that the overall objective is best served by investment in assets that offer a high expected return. The long investment horizon under which the AP funds operate makes them especially well positioned to incur the type of risk normally associated with higher returns on financial markets.

The Second AP Fund expects the future return on financial markets to be relatively low. Current interest rates are very low, especially in relation to the return that the AP funds' capital assets must generate to maintain the financial stability of the national pension system. Stock markets still offer the potential for higher returns in the longer term, although even these are expected to be lower than historical comparisons might suggest.

A major portion of equities is the first step towards a greater return on investment.

A major portion of equities is the first step towards a higher return on investment. In the case of the Second AP Fund, the room for increased risk – in terms of the traditional choice between broad investment in equities or bonds – has virtually been eliminated. At least 30 percent of the AP funds' capital assets must be placed in fixed-income securities, with high credit ratings and liquidity. Consequently, the work on long-term investment strategy is focused on allocations within the broad asset classes. Spread of risk in the portfolio and the choice of benchmark index play a growing role in

determining the composition of the strategic portfolio.

In 2006, to secure a higher future return relative to the level of risk incurred in the portfolio, the Second AP Fund will start to manage part of the equities portfolio with the assistance of modified indexes.

Changes in the strategic portfolio

At the start of the third quarter, an adjustment was made to the strategic portfolio whereby the portion allocated to hedge funds was reduced from one (1) percent to zero. This reduction was balanced by an increase in the global equities allocation of one percentage unit.

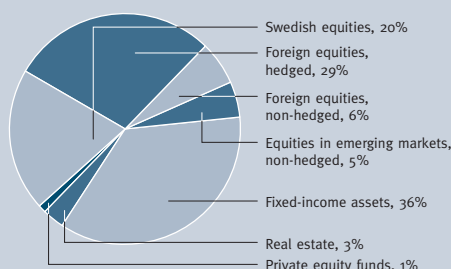
During 2005, analysis of the strategic portfolio, conducted within the framework of the Fund's ALM (Asset Liability Modelling) model, focused on changes within the broad asset classes. The essential purpose of this analysis is to ascertain the investment strategy most likely to secure a favourable development of future pensions. In practice, this involves determining investment strategies that are likely to generate a higher future return at a similar or lower level of risk than the portfolio as a whole.



The following adjustments were made to the strategic portfolio for 2006:

- Holdings in Swedish inflation-linked bonds were reduced by three percentage points (from five percent to two percent), while holdings in Swedish nominal government bonds were increased by three percentage points (from 16 percent to 19 percent). This reallocation of assets was designed to reduce the duration of the Swedish fixed-income portfolio, in the light of low interest rates and a flattening of the yield curve. This change in the strategic portfolio was made at year-end 2005.
- Equities in emerging markets were increased by two percentage points (from three percent to five percent), at the same time that asset class Foreign Equities in developed markets was reduced by two percentage points (from 37 percent to 35 percent). This re-weighting of the portfolio was designed to shift the emphasis of the Fund's combined portfolio of equities towards a higher expected return on investment. The relatively low correlation between equities in emerging markets and other portfolio assets is at the same time expected to improve overall portfolio risk. This change in the strategic portfolio was implemented at year-end.
- To raise the expected return and improve risk diversification in the portfolio, the Fund expanded its investment universe to include government bonds in emerging markets. A suitable opportunity for initiating these investments is being considered for 2006.
- The strategic portfolio's increased allocation of equities in emerging markets has increased the total degree of currency exposure from nine to eleven percent.

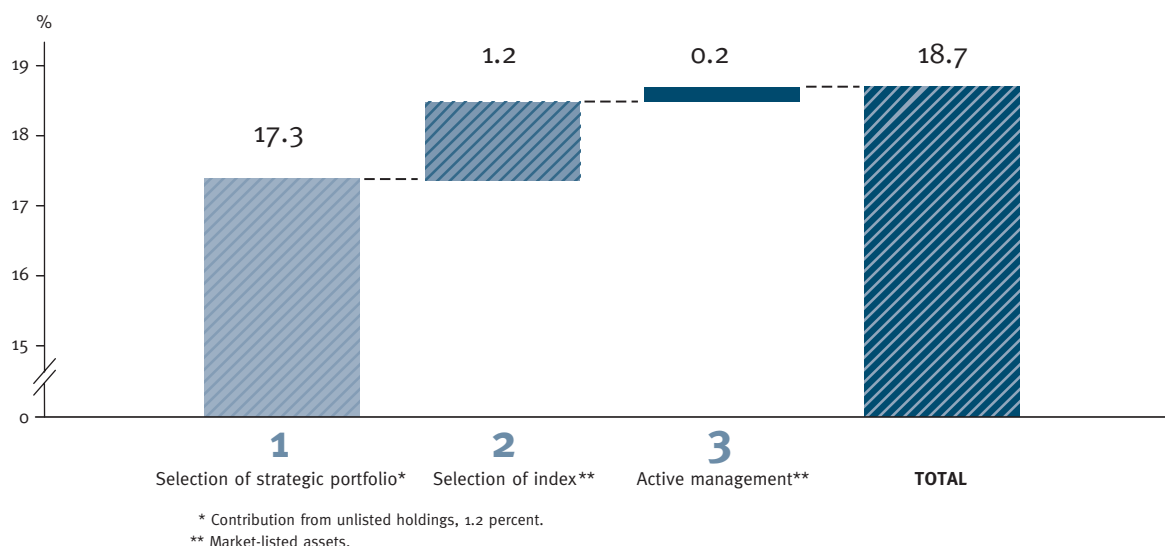
New strategic portfolio, 2006



The most notable changes in 2006 are a reduction in the percentage of Swedish inflation-linked bonds and an increase in the percentage of equities in emerging markets. During 2005, hedge funds were removed from the Fund's strategic portfolio.

Second AP Fund investment strategy: Three-stage value creation

All three stages of the Fund's value-creation process generated a positive return in 2005. The composition of the strategic portfolio is the most vital part.



In previous annual reports, the Second AP Fund only reported the absolute return on investment and “relative return” against its selected benchmark indexes. Dating from the six-month interim report for 2005, the Fund has adopted a three-stage approach in reporting value creation, with a view to providing a more comprehensive picture of the value of the active investment decisions made during the period: selection of strategic portfolio, selection of index and active portfolio management. The table on the facing page shows the Fund's performance in 2005, as well as since 2003, as per different elements. As of 2003, the strategic portfolio and indexes selected made a positive contribution to the Fund's performance. The negative return on assets under active management had an adverse impact on the result.

Value-creation stage 1.

Selection of strategic portfolio

The Second AP Fund's strategic portfolio is developed with the aid of an ALM (Asset Liability Modelling) model, developed in-house, designed to incorporate anticipated trends within the pension system based on a 30 to 40-year investment horizon. The model is used as an aid to create a

strategic portfolio that defines the relative allocation of asset classes, and FX strategy.

Value-creation stage 2. Selection of index

Selecting the index forms part of the Second AP Fund's investment process. In selecting the benchmark index, the Fund determines the levels of exposure that in-house and external asset managers should strive for in composing their portfolios. Rather than relying on traditional broad-based indexes, the Second AP Fund has chosen other specialised indexes in a range of different areas. This applies to fixed-income securities, for instance, where the Fund has excluded Japanese bonds listed in the global index. In the case of foreign equities, indexes have been chosen where exposure on the North American market has been reduced in favour of European and Japanese equities. In Sweden, the Fund complements its use of the SBX with its specially developed in-house OSX index – which is equally weighted, in contrast to traditional capital-weighted indexes – and CSX, a small-cap index.

The purpose of this selection of indexes is to enhance both in-house and external investment returns. For the full year 2005, the Fund's own

selection of indexes yielded a return that exceeded the broader indexes by 1.2 percent or SEK 2.2 billion. The corresponding return for the period 2003–2005 was 3.7 percent.

Value-creation stage 3. Active management

The Fund's selection of index determines its active management. In-house and external mandates shall outperform the Second AP Fund's selected indexes. In 2005, assets under active management generated a 0.2 percent return, equivalent to SEK 272 million. First and foremost, this derived from foreign equities and the tactical allocation mandates activated in 2005, which made a positive contribution to the operating result, while the Swedish portfolio of long-term equities underperformed against its benchmark index. This may be attributed to the portfolio's substantial holdings in Handelsbanken and SCA.

Calculated over the full period since its inauguration in 2001, the Fund has posted a positive relative return of 1.0 percent.

Value-creation over three years

%	2005	2004	2003	2003-2005
Total portfolio				
Strategic portfolio*	17.3	11.4	17.4	53.6
Choice of index**	1.2	0.7	0.9	3.7
Active management**	0.2	-0.6	-0.5	-1.3
Total	18.7	11.6	17.8	56.0
Swedish equities				
Strategic portfolio	36.3	20.8	34.2	120.8
Choice of index	3.2	-0.5	1.9	7.3
Active management	-2.9	-1.2	-1.7	-9.6
Total	36.6	19.0	34.4	118.5
Foreign equities, including currency hedging				
Strategic portfolio	20.0	10.6	22.6	62.7
Choice of index	0.9	1.3	0.9	4.3
Active management	2.0	-0.3	-1.0	0.9
Total	22.9	11.6	22.5	68.0
Fixed-income securities				
Strategic portfolio	3.8	6.8	4.9	16.3
Choice of index	0.6	0.8	0.5	2.1
Active management	0.0	-0.3	-0.1	-0.4
Total	4.3	7.3	5.3	17.9

* Including contributions from unlisted assets

** Market-listed assets

Portfolio management organised according to the “core/satellite” strategy

Traditionally, portfolio management strategy is organised in the form of a strategic portfolio, offering broad and long-term exposure in a range of asset classes on the financial markets, in combination with a set of active investment mandates that are designed to exploit short-term market trends within and between these asset classes.

Portfolio management can also be organised in relation to the degree of passive/active management. The strategic portfolio is managed passively while the active investment mandates are managed to incur more or less active risk. Some active mandates may be better suited to high-risk than others. One essential requirement when adopting an active high-risk strategy is good prospects of benefiting from changes in the relative return genera-

ted by different assets, either because substantial improvements in relative return may be expected and/or because the fund manager has an ability to predict future relative returns. Another important basic condition is that the active mandate should feature many different positions offering returns with a low correlation.

For some time now, mandates have been divided into core and satellite mandates, within the framework of the Second AP Fund's active risk budgeting. Passive mandates and mandates featuring a low active risk are classified as core mandates, while mandates involving high active risk are classified as satellite mandates.

Typical core mandates are “enhanced-mandates”, which are managed to closely reflect index with a low active risk driven by quantitative models.

Satellite mandates are found in the management of equities and fixed-income securities, and in global tactical asset allocation. In the equities management field, these mandates are global and therefore offer a broad investment universe that enhances the number of opportunities for active value creation. A broader selection of investment choices covering many national markets also increases the chance of locating undervalued investment opportunities. A number of the Fund's fixed-income global mandates have been activated during 2005, which similarly improves the prospects for generating a relative return. The GTAA global allocation mandate (see separate section), activated at the start of 2005, adopts the same logic.



Financial market trends in 2005:

Major regional differences

The capital worth of stock markets in Europe and Asia rose strongly, while growth on US stock markets was weaker. The Swedish krona weakened during the year.

In the wake of higher inflation, austere monetary policies and a tougher climate for corporate profits, the financial markets expected to be tested in 2005. Instead, the global equities market can look back on a bullish year, in which it showed a healthy appetite for risk, although with marked regional differences. The broader trends were occasionally fragmented by anxiety about the impact of rising energy prices and uncertainty concerning the general economic outlook. European indexes have performed significantly better than their North American equivalents, while the Swedish market rose in line with the rest of Europe.

Hungry for risk

High-risk markets have performed especially well, generating solid returns in sectors such as small-caps, growth markets and Asian indexes. Sharp upswings in the equities market have in many cases been reflected by strong gains in corporate profits. These have therefore been valued according to fixed price/earnings (P/E) ratios during the year. The extremely sharp growth in Japan was linked to expectations that the country was nearing the end of deflation, and that the opportunity for structural reform had increased as a result of political developments.

Global bond interest rates have either fluctuated within prescribed intervals or declined during the year. Compared to growth and inflation, bond interest rates still seem low.

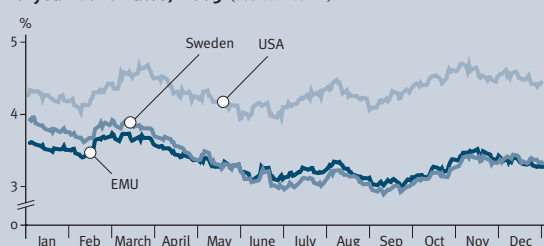
Rate hikes in the USA

Monetary policy provided the economy with on-going support, in spite of gradual rate hikes in the USA. Generally speaking, however, other central banks adopted a wait-and-see attitude, given the fact that inflation was under control and that the economic outlook was periodically subject to increased uncertainty. Swedish bond interest rates have been traded in harmony with European market rates, but fell below German rates in conjunction with the new investment guidelines proposed for life insurance companies ("the traffic-light system"). The FX market favoured currencies supported by high interest rates. The dominating factor was the ever-stronger US dollar, fuelled by more aggressively priced interest hikes. During the summer, however, the market responded to the fact that China's exchange-rate policy was cautiously redirected towards a strengthening of its currency. In contrast, the Swedish krona declined against the major currencies during the year, a consequence of Sweden's relaxed monetary policy compared to other countries, in spite of a strong economy and a balance-of-payments surplus.

Index growth in Swedish kronor and local currencies

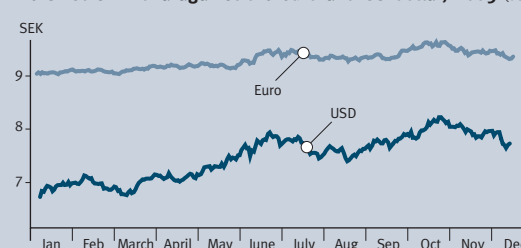
	SEK	Local currencies
Dow Jones	19	-1
Nasdaq	21	1
STOXX 50	26	21
Nikkei	46	40
OMX	29	29

10-year bond rates, 2005 (Source: EcoWin)



Compared to growth and inflation, bond interest rates still seem low.

The Swedish krona against the euro and US dollar, 2005 (Source: EcoWin)



The Swedish krona declined during the year, in spite of a strong economy and a balance-of-payments surplus.

Tactical asset allocation: Big changes, solid result

During 2005, major changes were introduced within the broad framework of tactical asset allocation. Two new external GTAA (Global Tactical Asset Allocation) mandates were implemented and the internal investment process for this sector was restructured to create a clearer “overlay mandate”. A quarter of the Fund’s active risk comes under GTAA, and the favourable result generated in 2005 accounts for a substantial proportion of the turnaround in the Fund’s relative return on invested capital last year.

Tactical asset allocation 2005	
	%
Contribution to relative return	0.3

In the middle of the 1970s, US institutional investors became interested in Tactical Asset Allocation (TAA) between equities and bonds, with a view to exploiting opportunities for “timing” the market. This was a reaction to the sharp decline posted by stock markets in 1973–1974. The growth of liquid futures markets for broad asset classes in the US further encouraged this development. Interest in the potential represented by tactical asset allocation grew, following the stock market crash of 1987, when many of those who had implemented TAA had been positioned for a market adjustment and had thereby limited the negative impact on their portfolios. During the 1990s, TAA was expanded into Global TAA, when a number of new markets and investment processes were added to what was essentially one-dimensional TAA. In conjunction with the stockmarket bubble at the close of the 1990s, many GTAA managers encountered problems in creating value, which led to a decline in interest among fund managers. In recent years, this interest has revived.

New multi-dimensional version

A “modern” TAA, or GTAA, differs significantly in several respects from older versions. Modern GTAA is based on an investment process where different positions driven by different investment themes form a well-diversified portfolio of tactical positions. Earlier versions of TAA were one-dimensional and driven mainly by a relative valuation of equities and bonds. If the tactical position failed, no other positions existed to protect the investor from losses.

In modern GTAA processes, positions are taken between different segments (mainly different countries or regions) of the global equities and bonds markets, and not just between equities and bonds. In the same way, modern GTAA mandates feature a considerable number of tactical positions on currency markets. This creates room for many smaller value-creation processes which, furthermore, feature a relatively low correlation.

Exploit “mispricing”

GTAA is based on the assumption that the market inefficiencies (or “mispricing”) to be exploited are mostly very small. These inefficiencies may be attributed to valuation anomalies made on different markets, periods of self-feeding price trends and a tendency towards sluggish price adjustment



Growth in value, GTAA mandates, 2005



in response to new information. Another form of inefficiency is linked to the fact that some dominant players are not driven by the profit motive, thereby counteracting a move towards market equilibrium. Central banks, that focus on currency and monetary-policy considerations when responding to foreign-exchange markets in particular, provide a typical example. A high degree of domestic-market dominance in many managers' portfolios can also serve to reduce inefficiencies in each separate equity market, although inefficiencies arising between different equity markets do not attract the same attention.

GTAA is based on the assumption that the market inefficiencies to be exploited are really very small.

Sharply reduced transaction costs

Thanks to increasingly well-developed and liquid futures and forward markets for equities, bonds and foreign exchange, transaction costs for GTAA have also been sharply reduced and it has been possible to expand the process to additional markets and positions. The ability to determine market impact from adopted positions, and to incorporate this as an important part of the investment process, plays an important role for the bottom line in GTAA.

Two new mandates activated in 2005

During 2003 and 2004, the Second AP Fund conducted a global search for external GTAA mandates. Five fund managers were approved subsequent to

an evaluation process conducted in 2004. At the start of 2005, the Second AP Fund decided to activate two fund managers, Goldman Sachs Asset Management and First Quadrant.

Informed Portfolio Management (IPM), based in Stockholm, manages First Quadrant's mandate. Both these external mandates are entirely and exclusively quantitative, and the investment decisions taken feature no subjective element.

In-house GTAA mandate

The Fund has been operating an in-house tactical allocation mandate for some time. Since 2005, this has followed the same GTAA format as external mandates.

The in-house mandate is currently based on a subjective investment process. During 2005, the in-house mandate was broken-out of the rebalancing process. A strict absolute-return mandate in an "overlay format" was created, increasing transparency both when taking positions and in performance attribution. In 2006, the in-house GTAA mandate will also feature a greater degree of quantitative investment processes.

Greatest contribution to value creation, 2005

In 2005, GTAA dominated overall value creation for assets under the Second AP Fund's active management. The return generated by GTAA mandates for the year was SEK 447 million.

Return and information ratio for GTAA mandates, 2005

	Return since start, SEK m	Information-ratio*
Goldman Sachs	235	0.86
IPM/First Quadrant	148	0.81
In-house GTAA mandate	64	0.53
	447	

* Information ratio for GTAA mandate calculated as return divided by absolute risk.

Second AP Fund equity management: Implementation of “core/satellite” strategy

Two important change processes were completed in 2005. The new “core/satellite” strategy was implemented and the in-house share of equity management increased by nine percentage points.

Equity management 2005		
	Swedish equities	Foreign equities
Share of equities in total portfolio, %	21.4	40.7
Absolute return, %	36.6	22.9
Relative return, %	-2.9	2.0
Share under in-house management, %	82.5	47.3
Share under active management, %	100	81.9

The Second AP Fund was established in 2001, since when there has been a steady build-up of competence on the equity side. In the start-up phase, it was perfectly natural that a large part of the portfolio was either indexed or placed under external management. The final stage of transformation to the present strategy, which to a great extent is based on in-house resources, was determined in 2004 and fully implemented by year-end 2005.

The Fund's equity organisation underwent major restructuring in 2005. 2005 saw the termination of two Swedish and nine foreign equities mandates. If mandates terminated in the preceding year are included, this brings the total to seven Swedish and fourteen foreign equities mandates. A greater proportion of the Fund's equity manage-

ment is now handled in-house. In consequence, more risk has been allocated to external global mandates, with subsequent expectations of higher returns.

The following presentation focuses on three important mandates on the equity side, two of which form part of the Fund's core strategy and one of which forms part of its satellite strategy (see page 15 for a more detailed description of this strategy). Quantitative management, described on page 23, is a crucial element of the new core strategy. The strategies described represent 60 per cent of the total equities portfolio. Other mandates are reported in the form of tables.

Core mandate: Swedish equities

During the year, the Fund has reorganised its Swedish portfolio activities. Having previously been sector-based, the broad Swedish portfolio is now composed to match the SBX. Furthermore, the Fund has built up an in-house portfolio of small-cap funds during the second half of the year. The year has been notable for development of the investment process and the build-up of the organisation. The portfolio comprises a total investment of SEK 21.4 billion, which is 52 per cent of the Fund's overall holdings in Swedish equities.

The Fund observes a strictly fundamental

Core mandate – Swedish equities

Capital under management (SEK bn)	21.4
Type (core/satellite)	Core
Investment style (active/enhanced/passive)	Active
Return, %	36.3
Excess return against index, %	-0.5*

* Applied to the full twelve months. Under the new organisation, the mandate has generated a return in line with the market.

Core mandate – European equities

Capital under management (SEK bn)	20.9
Type (core/satellite)	Core
Investment style (active/enhanced/passive)	Active
Return, %	31.3
Excess return against index, %	0.3*

* Applied to the full twelve months.

investment philosophy, based on the firm conviction that a higher return is achieved by conducting more thorough analyses than the market as a whole. We use our own analytical tool to identify investment opportunities. Under the new organisation, the Swedish equities mandate has generated a return in line with market performance (see table below).

Core mandate: European equities

By far the largest portion of the Fund's holdings in European equities, outside Sweden, is managed within the framework of an in-house mandate. At year-end 2005, the mandate comprised equities totalling an estimated market value of SEK 20.9 billion. During the year, the management of European equities has moved from a sector-based focus to one based on a broad index. The investment strategy adopted involves two parts: a tactical part, and a strategy involving selection of equities from a number of sectors. This strategy has generated a positive relative return of 0.3 percent (see table below).

Satellite mandate: Special holdings in Sweden

Special holdings are managed quite independent of considerations of index constituents. However, the appraisal is based on absolute return and the OSX. This is done to strengthen the investment strategy, which is absolute in nature, where the portfolio is focused on a number of major hol-

dings, including Skandia, Volvo, Electrolux, Handelsbanken, Meda and SCA. This investment strategy means a longer investment horizon (more than three years) and, in several instances, involves an extensive commitment in respect of corporate governance issues.

A greater proportion of the Fund's equity management is now handled in-house.

During the year, the portfolio has grown by 36.4 percent, underperforming the selected benchmark index by 9.1 percent, although 0.1 percent better than a broad index.

Over a period of three years, the portfolio has generated a return of 147 percent, outperforming both the specialised and the broad index (see table below).

Satellite mandate – Special holdings in Sweden		2005	3 years
Capital under management (SEK bn)		10.8	
Type (core/satellite)		Satellite	
Investment style (active/enhanced/passive)		Active	
Return against broad index*, %		0.1	25.7
Excess return against index**, %		-9.1	8.8

* Six RX

** OSX



The Second AP Fund's equity mandates

The table below shows all the Fund's equity mandates. Mandates named as "passive" or "enhanced" are attributable to the core equity-management mandate. Mandates featuring an active style of management belong primarily to the satellite portion of the Fund's equity management activities, where it is hoped that a more aggressive use of the Fund's risk options would generate an excess return in the long term. External mandates under active management are concentrated mainly on emerging markets, Swedish small-cap funds and global funds. In all cases, the Second AP Fund had no in-house expertise in 2005, which is why external fund managers were chosen. In the Swedish small-cap sector, the Fund built up its

own in-house competence during 2005 – although external fund managers will continue to be used for liquidity reasons. The only external fund manager to be awarded a European mandate is SAM, Sustainable Asset Management, with an investment philosophy where sustainable issues are an integral part of the investment model.

On the American market, management is passive and, therefore, index-driven. In 2006, enhanced mandates will also be implemented within this region. In our view it is more difficult to generate an excess return using fundamental stock analysis on a market that is considered the most exhaustively analysed in the world.

Regional equity mandates	Style	Return, %	Excess return against index, %
Europe			
In-house	Active	31.3	0.3
SAM Sustainable	Active	29.8	-1.2
In-house*	Passive	4.6	0.0
North America			
Barclays	Passive	28.2	0.8
In-house*	Enhanced	6.3	0.2
Japan			
Martin Currie	Active	53.9	3.6
In-house*	Passive	4.1	0.0
Emerging markets			
AIG Global	Active	69.4	8.9
Citigroup	Active	53.4	-7.1
Merrill Lynch*	Active	17.5	-0.8
Genesis	Active	65.1	4.6
Pictet	Active	62.0	1.5
State Street	Active	66.1	5.6
Global equity mandates			
MFS	Active	29.1	-2.0
Merrill Lynch	Enhanced	32.2	1.1
Carnegie*	Active	22.0	8.3
Franklin Templeton	Active	13.7	0.0
StateStreet	Passive	31.3	0.1

Regional equity mandates	Style	Return, %	Excess return against index, %
Pacific, excluding Japan			
In-house*	Passive	28.2	1.7
Swedish OSX mandates			
In-house,			
Special holdings	Active	36.4	-9.1
Enter Select Fokus	Active	38.8	-6.7
Swedish SBX mandates			
SEB	Active	33.8	-2.9
In-house			
quantitative portfolio	Enhanced	37.2	0.4
In-house	Active	36.3	-0.5
Swedish CSX mandates, small-cap funds			
In-house*	Active	18.2	0.0
SEB Sverige	Active	40.9	-3.2
SEB Sverige ChansRisk	Active	44.7	0.6
Carlsson Sverige	Active	51.4	7.3
Robur	Active	53.6	9.5
Lannebo	Active	43.6	-0.6
Handelsbanken	Active	45.9	1.7

* Has not been under management during the entire twelve months.

Quantitative management

A fifth of the Fund's portfolio of equities is managed according to quantitative models. Founded on tested strategies and risk and transaction-cost estimates, these offer excellent opportunities for generating excess return at low risk.

Quantitative management differs from "fundamental" management in that the entire investment process is expressed in terms of mathematical models and statistical relationships. By this means, the investment theme is based on actual market inefficiencies, located by observing quantifiable shifts in market rates or valuations. Quantitative management should be considered as a form of core management (see page 15).

One major benefit of this approach is that the strategies can be tested historically and are transferable between different markets.

The active strategies are based both on observed patterns relating to market valuation and on key ratios based on fundamental stock analysis.

The fact that the Second AP Fund already has well-developed quantitative management systems means lower costs, compared with external index-management. It also increases the flexibility of equity management as a whole, as when moving positions between regions.

At year-end 2005, quantitative management was organised under five separate mandates: Sweden, Europe, USA, Japan and the developed nations of Asia. In all, assets totalling SEK 21 billi-

on are being managed with the aid of quantitative analytical methods.

AP2 uses a quantitative model where techniques for replicating index are only implemented once models for risk and transaction costs have been developed. Active strategies are then developed, which means that there is an assumption that the portfolio will outperform its benchmark index. The active strategies are based both on observed patterns relating to market valuation and on key ratios based on fundamental stock analysis. Other quantifiable themes are also used.

The development of quantitative management has progressed furthest on the Swedish market. All elements have been implemented on this market, with satisfactory results. On other markets, only some elements have been implemented, but the aim is to introduce this strategy for all sub-mandates over the next few years.

Quantitative management	Sweden	Europe	North America	Japan	Rest of Asia	Total
Capital under management (SEK bn)	2.8	1.1	12.4	1.2	3.5	21.0
Type	Core	Core	Core	Core	Core	
Investment style	Enhanced	Passive	Passive	Passive	Passive	
Return, %	37.2	4.6	6.3	4.1	28.2	
Excess return against index, %	0.4	0.0	0.2	0.0	1.7	

Governance issues 2005:

Clearer link to portfolio management

The Second AP Fund's value-based governance strategy has been developed and implemented as part of its ongoing portfolio management activities. The Fund's efforts in connection with Old Mutual's bid for Skandia have focused attention on the relevance of a number of crucial governance issues.

Through its enhanced commitment to governance issues, the Second AP Fund improves the potential to maximise return on capital under management.

Good governance creates value

Most investors subscribe to the idea that well run companies also tend to be a good investment.

The hub around which the analysis of governance issues revolves is the Fund's in-house governance logbook. This records the appraisals of in-house portfolio managers and analysts, after which the potential of a specific change process can be determined. The corporate governance committee then uses this data in drafting a list of commitments relating to the four or five companies with the greatest potential. The committee develops a strategy for achieving the required change, and the work is coordinated by the Fund's corporate governance function. The Fund's respective in-house portfolio managers decide independently as to how governance issues should be addressed, with a view to adding value.

The hub around which the analysis of governance issues revolves is the Fund's in-house governance logbook.

Normally, the work involved in addressing individual governance issues is not official, but due to the attention generated by the Skandia issue, the

Second AP Fund decided to issue a special report concerning its commitments and deliberations.

AGMs and nomination committees

During 2005, the Second AP Fund participated in 49 Annual General Meetings (AGMs) and five extraordinary general meetings. The Fund also exercised its voting rights by proxy (Internet-based) at the AGMs of companies representing its 50 largest foreign holdings.

The Second AP Fund has been represented in the nomination process for the boards of a whole series of companies, which are listed in the Fund's governance report. Prior to the 2006 AGM season, the Second AP Fund is represented on the nomination committees of Artimplant, Capio, Electrolux, Handelsbanken, Karo Bio, Meda, Oriflame, Pergo, ProAct, Sardus, Skandia, VitroLife, Volvo and Wedins.

The Fund has also been actively engaged in preparatory work prior to several of these AGMs. This has involved analysing the various proposals that boards have planned for submission to their respective AGMs, discussing them with other institutional investors and representatives of the companies' boards. The issues most often raised during the year have centred on incentive systems, capital structure and the board nomination process.

Separate governance report

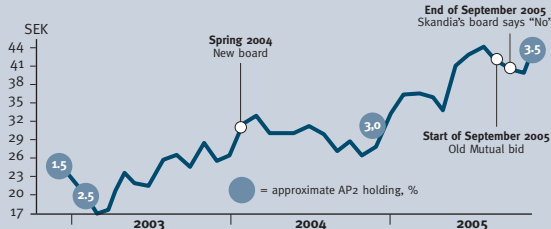
In conjunction with its six-month interim report, the Second AP Fund published a special gover-

The Second AP Fund's governance logbook

	Corporate structure	Capital-structure	Ownership structure
Company V	●	●	●
Company X	●	●	●
Company Y	●	●	●
Company Z	●	●	●

The potential of portfolio companies is identified with the help of the Fund's own in-house analytical model for governance issues. Red means "warning", yellow that there is a problem.

Performance of the Skandia share, 2003-2005



The Second AP Fund has been represented on the nomination committee since 2004.

nance report. This reviews the previous AGM season and reports on the positions adopted by the Fund on specific issues at respective AGMs, as well as on the Fund's use of its voting rights in foreign holdings. The report also describes positions taken by the Fund on certain matters, and its observations concerning key governance issues.

Female representation index

The Second AP Fund's index for charting female representation on the boards and executives of exchange-listed companies was presented for the fourth year in succession. Although there has been an increase in the number of women represented on the boards of quoted companies in recent years, the number of women represented in executive managements has remained more or less the same. Since 2002, female representation on the boards of quoted companies has more than doubled, from 6.1 to 15.9 percent. During the same period, the increase in the number of women on executive managements has been only marginal, from 11.1 to 11.6 percent.

SAM's valuation model has also been used in a dialogue with the Fund's ten largest Swedish holdings, concerning ethical and environmental issues.

Environmental and ethical issues are integrated in policy and analysis

Environmental and ethical issues form an integral part of the Second AP Fund's corporate governance policy. During the year, no companies have been excluded as targets for investment, although this might become appropriate where a company

transgresses the law or international conventions.

The Second AP Fund was one of the sponsors of the Gothenburg International Environmental Award 2005. The Award was presented to the Maraba Cooperative, Abahuzamugambi, in Rwanda, for its pioneer work in producing coffee based on socially, economically and ecologically sustainable methods.

Pursuing its commitment to positive selection based on sustainability criteria, the Second AP Fund invested in a fund managed by Swiss fund manager SAM (Sustainable Asset Management). This fund's investment strategy is based on a valuation model that judges a company's actions in terms of its performance with respect to a number of key sustainability issues. The companies that satisfy these criteria are those in which SAM can invest.

SAM's valuation model has also been used in a dialogue with the Fund's ten largest Swedish holdings, concerning ethical and environmental issues. This dialogue has formed the basis for developing the ethical and environmental appraisal recorded in the Fund's in-house governance logbook, for use by portfolio managers as a selection tool.

In the case of foreign holdings, work is currently in progress to create a more balanced picture of which companies, from an ethical and environmental standpoint, are most important to the Fund. During the year, 50 of the largest holdings have been judged according to environmental and ethical criteria.

The Second AP Fund has also participated in the Carbon Disclosure Project, where 143 institutional investors have challenged the world's 500 largest companies, as per market value, to declare their position on the climate issue.

Female representation on boards and executive managements, 2005



The Second AP Fund's index for female representation on boards and executive managements was published for the fourth year in succession.





Second AP Fund fixed-income portfolio and FX: External mandates activated during the year

The Fund is exposed to the US bonds and global credit bonds market through two new external mandates. The market was characterised by a strong US dollar, weaker krona and expectations of continued lower yields.

Management of fixed-income portfolio, 2005	
	%
Share of total portfolio	34.1
Absolute return	4.3
Relative return	0.0
Under in-house management	92
Under active management	93

Broad management of Swedish and global bonds is the foundation on which the Fund's fixed-income and FX management is based. In-house portfolio management shall focus on areas where the Fund can manage its assets close to index, at low cost, or on active management in areas where the Fund anticipates opportunities for generating a return that outperforms the Fund's benchmark index. To these are added external mandates with higher risk and return expectations, as well as specialised in-house mandates.

Three different mandates

Following the public procurement process in 2004, the Fund has approved managers for three different mandates; one for broad global bonds, one for US government and credit bonds and one for a portfolio of global credit bonds.

After thorough analysis, the following fund managers were chosen:

- For global broad mandates – Bridgewater, Rogge and Capital International.
- For US government and credit bonds – Blackrock, Singer & Friedlander/Denver LL and Wellington.
- For global credit bonds – Rogge, Franklin Templeton (Fiduciary Trust) and Payden & Rygel.

Rogge's and Franklin Templeton's (Fiduciary Trusts) mandates were activated in the late autumn of 2005. The intention is to activate a further two mandates in the spring of 2006.

Well positioned in the autumn

During most of the year, the Fund's broad bond portfolio was positioned to benefit from an up-swing in global bond yields. During the autumn, global bond yields rose and this improved relative return for the second half of the year. The Fund had taken no direct positions in individual corporate bonds in its in-house portfolio, but a slight negative weighting in allocation to credits and an exposure in bonds with higher credit ratings have generated a positive relative return on credit management activities.

In-house fixed-income management, Sweden

Capital under management	28.7
Investment style	Enhanced
Return, %	4.2
Excess return against index*, %	-0.3

* SHB All Bond

The Fund's external mandates contribute capacity and specialist competence to the management of corporate bonds. This helps expand opportunities for value creation, as in the choice of individual borrowers and securities, and in weightings between different sectors. Both portfolio managers have generated a positive relative return since the mandates were activated.

Trends in global management of fixed-income securities

Growth in the fixed-income markets has been subject primarily to two key factors: the impact of supply and demand on fixed-income instruments, and the impact of developments in new products and technologies. The two main factors affecting supply and demand with respect to fixed-income products have been the US balance of payments deficit and the consequent financing requirement, as well as the current regulation of life and pension funds.

To prevent large capital inflows from putting upward pressure on their domestic currencies, Russia, Japan and China have built up large currency reserves that have been invested in fixed-income securities, especially in the USA.

Consequently, both map and ground rules for managing global fixed-income securities are changing rapidly, while increasing demands are being made on investors.

Artificially low US interest rates

The result is that Russia, Japan and China have financed US consumption and helped force US

interest rates to levels well below those suggested by historical precedent and economic theory as appropriate for a country burdened by similar deficits. Another factor that has affected global interest levels is the current regulation of life and pension funds, where balancing of the liability and asset sides has attracted the spotlight. One effect of this regulatory process is increased demand for long maturity fixed-income investments, with a consequent drop in long-term yields. Taken as a whole, it is clear that factors other than macroeconomics and monetary policy are having a growing impact on the pricing of fixed-income securities.

New instruments launched at accelerating rate

In response to the new market situation, and in the light of the fact that general interest levels are low and are failing to meet investors' yield requirements, new instruments are being launched at an accelerating rate. Derivative instruments, for example, are being used to an increasing extent. Derivates are used both to create products and to secure the required exposure, as well as to balance the term between the liability and asset sides. A large number of structured products are also being created, often of complex design. The need to manage and understand the risks and opportunities presented by different types of derivative instrument and structured products place increasing demands

US dollar rate 2005 (Source: EcoWin)



The graph shows the US dollar rate against the currencies of G6 countries in 2005.

Swedish real rate of interest 2001-2005 (Source: EcoWin)



The graph shows real return on long inflation-hedged bonds since the Fund's start.

on the level of competence within investors' organisations.

Consequently, the environment for managing global fixed-income securities is changing rapidly.

FX markets affected by stronger US dollar

Going into 2005, the US dollar was weak. It gained strength during the early part of the year, partly due to an increased short interest differential, as well as tax relief for companies that brought money home to the USA.

The Swedish krona weakened against the US dollar and other currencies during the latter part of the year.

The Yen weakened during the year despite encouraging signs of increased growth.

One of the big questions has been the valuation of China's currency. A minor write-up was implemented during the summer, and further revaluation is expected.

The Swedish krona weakened against the US dollar and other currencies during the latter part of the year.

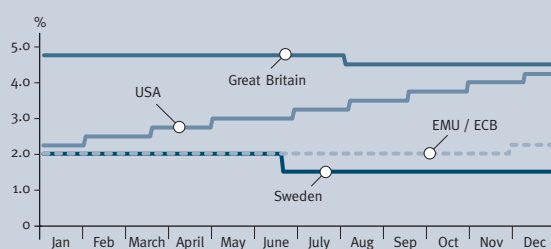
Tactical positions and active trading

During the year, the Fund has taken positions based on tactical deviations from the strategic hedging level adopted for the Fund's total portfolio. These positions are based mainly on macro-economic views with an investment horizon of one to three months.

A programme to actively generate value from currency market movements was launched in 2004. These positions are based strictly on technical analysis with the focus on short-term movements. From 2006, the trading mandate has also been allocated risk to a quantitative model.

Both tactical and trading positions have made a positive contribution to the Fund's return in 2005.

Official key rates 2005 (Source: EcoWin)



The graph shows changes in official key rates in 2005.



Alternative investments: Real-estate and private-equity funds perform well

Asset class “Alternative Investments” comprises the Fund’s combined investments in unlisted real-estate companies and private equity funds. Holdings in real estate represent three percent of the Fund’s total capital assets. Private equity funds currently account for approximately one percent of Fund investment, but will eventually increase to account for two to three percent of the total portfolio. The Fund’s holdings in hedge funds were divested during the year.

Alternative investments 2005	
	%
Share of total portfolio	3.8
Absolute return	30.1
Relative return	17.2

Asset class Alternative Investments posted a return of 30.1 percent for 2005. Real estate generated a return of 35.8 percent and private equity funds 24.3 percent.

Real estate – a long term investment

Investments in real estate have long been a common form of investment for institutional investors. Compared to exchange-listed assets, real estate has generated a stable return. Real estate holdings are relatively non-liquid and should therefore be viewed as extremely long-term investments. Nevertheless, real estate investments generate an ongoing return throughout the entire investment period, in the form of dividends, for example. Given the long-term nature of the Second AP Fund’s investment horizon, a certain proportion of real estate holdings is highly appropriate.

Rental market shows signs of turnaround

After some years of rising vacancy levels and falling rents, the rental market has staged a turnaround in 2005. This has applied mainly to the Stockholm market, although the trend has also been stable in most other areas.

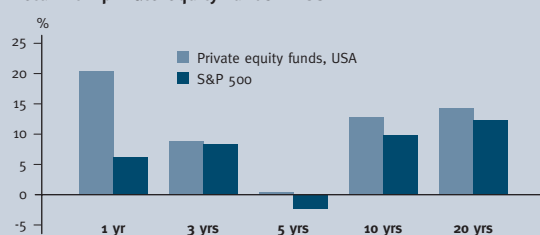
During the latter part of 2004, there were signs that the rental market had bottomed out and, in the most sought after areas, the level of vacancies declined slightly. There were also indications that rents were on the way up. This trend was maintained in 2005. According to the economic forecasting institutes, a rise in the level of employment, so essential to an improved rental market, is likely to be delayed yet again. In Stockholm’s inner city, vacancy levels for office space are at about 10 percent. In Gothenburg, the figure is around 12 percent and in Malmö about 15 percent.

International interest expected to continue

The investment market is still strong. In recent years, the liquidity offered by the Swedish real estate market has been among the highest in Europe. Foreign real estate funds (mainly German, British and American) have predominated. This keen international interest in Swedish real estate,



Return on private equity funds in USA



Return on all private equity funds in the USA compared with the return on listed equities as per June 30th 2005.

focused mainly on major commercial properties, is likely to continue, since the return on investment remains attractive to international investors.

In recent years, the liquidity offered by the Swedish real estate market has been among the highest in Europe.

Newly started Swedish real-estate funds, Swedish real-estate companies and other domestic investors have become increasingly active on the market. Prices have been dramatically affected, attributable in part to strong demand, and in part to low interest rates.

Solid profit growth

The Second AP Fund's investments in unlisted real estate consist of NS Holding AB (Fastighetsbolaget Norrporten) and AP Fastigheter Holding AB. The value of the Fund's holdings, including debenture loans, is estimated at SEK 5.8 billion.

Norrporten's business concept involves the acquisition, development and management of real estate, primarily for commercial use, in centrally located regional centres with high growth potential. During the year, the company has continued to develop its real estate portfolio in line with its defined business strategy. During 2005, Norrporten became established in Copenhagen. The company acquired real-estate holdings in Copenhagen and Uppsala, and divested its portfolio of properties in Karlstad.

At year-end 2005, the estimated market value of real estate holdings in Norrporten was SEK 14 billion. The company reports solid profit growth.

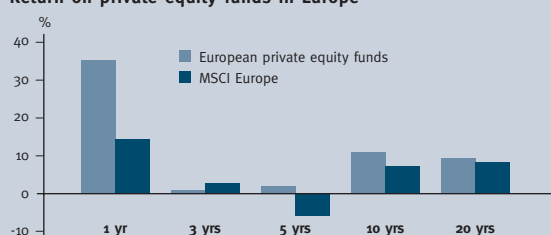
AP Fastigheter's real-estate holdings are concentrated mainly to the major urban centres of Stockholm, Uppsala and Gothenburg. The properties are attractive and well located. Having been weak for the past few years, the commercial rental market in Stockholm stabilised during 2005, and the first signs of a possible recovery could be discerned. The market value of AP Fastigheter's real-estate holdings amounted to SEK 32.2 billion at year-end. The company reports solid profit growth.

Private equity funds – good return and risk spread

In recent years, institutional investors such as insurance companies and pension funds have started increasingly to invest in unlisted equities (private equity). Investors cite the possibility of high returns and well-diversified risk as the main factors driving this increased activity. Furthermore, investments in unlisted companies offer private equity funds excellent opportunities to exercise active ownership and participate in the development of the individual companies.

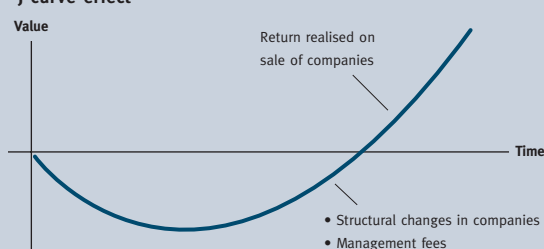
The investment regulations to which the First to Fourth AP Funds subscribe present the possibility of indirect investment in unlisted equities via private equity funds.

Return on private equity funds in Europe



Return on all private equity funds in Europe compared with the return on listed equities as per June 30th 2005.

"J-curve effect"



The normal curve depicting the return on investment in private equity funds is often likened to the letter "J".

Select choice of reputable funds

The Second AP Fund's strategy is based on the gradual build-up of a diversified portfolio of investments in unlisted equities, by investing in private equity funds. The goal, within the next four to five years, is to indirectly own unlisted equities corresponding to two to three percent of the Fund's total capital assets. The Fund believes a careful selection of quality funds with a well-documented ability for adding value to their portfolio companies will generate attractive levels of return on investment.

An intensive year for the private equity sector

The high level of activity noted by the private equity sector in 2004 continued in 2005. In both North America and Europe, activity in the sale and acquisition of companies was considerable. Private equity funds account for a significant percentage of completed transactions. In Europe, the number of IPOs continues to rise, while the reverse is true in the USA.

The credit market continued to enjoy a high degree of liquidity, making it easier to secure bank loans when acquiring mature businesses. However, a number of lenders have warned that the risk premium charged on this type of transaction is too low.

Building an international network

During 2005, the Second AP Fund continued its systematic build-up of an international network. Meetings have been held both on the Fund's initiative, and as a direct consequence of its "open door policy". Outside the Nordic countries, the Fund has focused on establishing contacts with reputable and

experienced market players in Europe and the USA.

The Second AP Fund has also been an active participant in meetings with the largest international institutional investors. This ensures that the Fund has access to extremely valuable sources of information, and that it is able to take part in industry-wide discussions that offer opportunities for influencing issues of common interest.

The Fund is the first non-North American investor to gain a seat on the board of the Institutional Limited Partner Association, which is the sole global organisation for institutional investors in private equity funds. The Association represents more than 150 investors, out of a global base that has invested approximately USD 350 billion in private equity funds.

The Fund believes a careful selection of quality funds with a well-documented ability for adding value to their portfolio companies will generate attractive levels of return on investment.

Commitments in 2005

During 2005, the Second AP Fund continued to develop its portfolio by investing in private equity funds.

During the year, the Fund made the following new commitments:

- Pathway, a fund-on-fund, which invests in funds on a global basis: USD 250 million.
- CVC, which invests in major businesses throughout Europe: EUR 35.5 million.

- Carlyle/Riverstone Renewable Energy Fund, which invests in energy production from renewable energy sources: USD 20 million.
- Carlyle/Riverstone Global Energy Fund, which invests in mature companies in the energy sector: USD 30 million.
- Nordic Capital, which invests in medium-size Nordic companies: EUR 50 million.

During 2005, actual investment in private equity funds totalled SEK 680 million, including commissions to fund managers. The Fund's total investment commitments amount to SEK 6.0 billion, distributed between 13 funds. Of these total commitments, SEK 1.3 billion has already been invested. The funds' long-term strategies for developing their portfolio companies are starting to generate visible results. During the period, the portfolio companies have developed well, and a number of sales were implemented. The net result of approximately SEK 400 million for the period includes the sales of Sirona and Dometic, which were owned by EQT.

Termination of investment in hedge funds

Asset class Hedge Funds was divested during the period. It was deemed that the Fund's new tactical allocation mandate (see page 18) is able to generate an absolute return in a more cost efficient manner. During the year, the asset class generated a return of 3.2 percent, which was 2.5 percent higher than the benchmark index.

Private Equity holdings	Style	Total investment commitments, SEK m
EQT Northern Europe KB (EQT III)	LBO	181
Swedestart Life Science KB	VC	25
Swedestart Tech KB	VC	25
Carnegie Fund BiotechBridge	VC	50
Cevian Capital L.P.	Active	681
CVC European Equity Partners IV L.P.	LBO	335
EQT Mezzanine L.P.	Mezz	272
Nordic Capital V, L.P.	LBO	454
Pathway Private Equity Fund IX, LLC	Fund-on-fund	1 118
Pathway Private Equity Fund IXB, LLC	Fund-on-fund	1 990
Carlyle/Riverstone Renewable Energy Infrastructure Fund I	LBO	159
Carlyle/Riverstone Global Energy Fund III	LBO	239
Nordic Capital VI, L.P.	LBO	469
Total		5 998

LBO = leveraged buyout: investment in large mature companies.

VC = venture capital: investment in small, young, development-driven companies.

Mezz = mezzanine fund: investment in acquisition credits.

Investments per fund are listed on page 50.

Second AP Fund Business Services

The Second AP Fund's Business Services organisation comprises six departments, responsible for business control, follow-up and analysis. The organisation has been formed to create a flexible unit where changes in investment strategy and focus can be implemented speedily and cost-efficiently within the existing structure, at the same low level of risk.



Detailed analysis of completed trades ensures optimal conditions for future investment. Backed by the Fund's systems support and efficient business processes and working methods, operations can concentrate on investment analysis and strategic and tactical choices. The analytical process, conducted in several stages, involves daily evaluation and rebalancing of Fund holdings.

1. Daily evaluation and rebalancing

The evaluation and rebalancing of portfolios is conducted on a daily basis against benchmark index, at fixed weights. Day-to-day knowledge of the degree of exposure per asset class and market is vital in determining the Fund's tactical allocation.

2. Analysis of trades executed

All trades executed under the Fund's mandate are updated daily. This enables detailed monitoring and analysis of the Fund's investments in both in-house and external mandates. Monitoring of direct and indirect transaction costs and turnover

rate for portfolio assets is conducted at regular intervals.

3. Analysis of positions taken

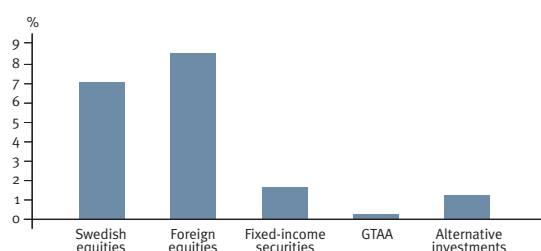
Risk and return are analysed and followed up daily in different dimensions and at different levels, such as sector and geographical area. The level of risk utilisation for the total portfolio, as well as per asset class and mandate, is monitored and matched against current risk limits. The Fund's absolute and relative risk and return is monitored and analysed. The preventive form of risk analysis features "stress tests", where alternative scenarios are tested on the current portfolio.

4. Attribution analysis

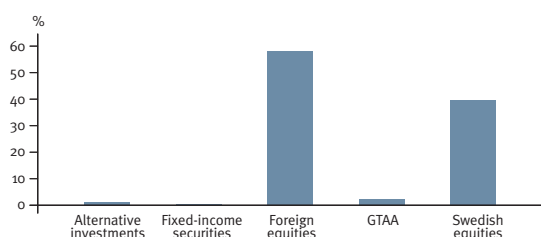
Attribution analysis determines the extent to which individual portfolios have contributed to the Fund's return and risk utilisation. The attribution is made on the basis of several criteria, such as choice of security, industry and geographical area.

During 2005, the Fund has focused on a num-

Attribution, total portfolio. Absolute return incl. alternative investments.



Attribution of risk, absolute risk



ber of large projects with a view to further improving and refining working approach, methods and systems utilisation. The aim is to create an environment that allows flexibility but that at the same time maintains a high quality and level of security. Innovative thinking and a holistic approach create consistent opportunities for improvement

and heightened efficiency. The Fund's Business Services organisation therefore studies trends and developments to find more efficient ways to increase the Fund's revenues and reduce its costs.

The projects described below are some of those that Business Services has worked on and implemented during the year.

Mapping of operative risks

The Fund is actively engaged in the development and improvement of processes, systems and routines to minimise operative risks, i.e. errors or stoppages in operations lead to losses, in economic terms or in terms of market confidence. As early as 2004, as part of this work, the Fund mapped potential risks affecting procedures or infrastructure, as well as legal and personnel risks. This mapping process,

which was conducted in association with external consultants from Atos Consulting AB, involved a review and appraisal of the Fund's operative level of risk. Potential risks are classified using a risk matrix, based on probability and consequence.

This mapping process revealed that the Fund's total level of risk was low and that awareness of risk-related issues within the organisation was high. The greatest potential for improvement lay in optimising the Fund's use of its SimCorp Dimension investment management system, and in the field of continuity and disruption planning, with the emphasis on IT security issues.

Risk matrix – operative risks

Consequence	High			
	Medium			
	Low			
		Low	Medium	High
		Probability		

"The Second AP Fund operates in a complex environment, subject to constant change. The organisation is characterised by the wish to excel and the will to strive for consistent improvement."

Elizabeth Kihlbom, Managing Director, Atos Consulting AB

Optimisation of systems utilisation

The Second AP Fund has used SimCorp Dimension, a fully integrated Front/Middle/Back Office system, from the very start. The system is used for the entire investment management process, from execution and matching of trades, to reconciliation, monitoring and daily evaluation. This working approach places considerable demands on the way the system is set up and requires ongoing development of the systems and methods used, to adapt to factors such new investment mandates, instruments and benchmark structures.

To ensure that the SimCorp Dimension system is used as efficiently as possible, the Fund has worked on an optimisation project known as the PIP (Profit Improvement Plan), in close association with the systems supplier, SimCorp. The project, implemented in 2005, has been designed to identify areas that can be improved, to achieve greater efficiency. The goal is to enhance STP (Straight Through Processing), reduce operational risks and, from a systems viewpoint, to establish the conditions necessary to operate a modern and

successful investment management system.

The project has involved systems users, mainly investment managers and representatives from the Business Services organisation. Analyses designed to help optimise systems utilisation have been carried out using a combination of interviews and project groups. These show that today's Second AP Fund possesses a very satisfactory level of systems know-how and enjoys a high degree of automation in terms of its business processes, and that the work is carried out efficiently. To further optimise system use, the Fund is evaluating proposals for additional functionality as well as greater integration of certain analyses and calculations in

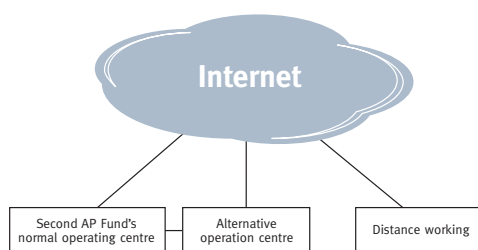
SimCorp Dimension. These changes derive from the fact that the system has been further developed in a number of areas. A newly designed portfolio structure, which among other things can simplify the maintenance of benchmarks, is currently under evaluation, and may eventually be implemented.

"By virtue of its competence and pro-active approach, the Second AP Fund, as a major and demanding customer, is actively contributing to the further development of the SimCorp Dimension system."

Mikkel Mördrup, Vice President, SimCorp Sverige AB

Strategic IT security

Right from the start of the formation of the Second AP Fund, it was decided that IT security was an area of strategic importance. During 2005, security has been further developed and strengthened in the field of continuity and disruption planning. Much of this work has focused on securing the Fund's most business-critical systems in the event of a crisis or catastrophe.



A fixed connection links the Second AP Fund's normal operating centre to the back-up centre. Two separate connections permit external access (from home or hotel) to both centres.

The technology is designed to ensure that the most critical systems can be brought on line immediately, as soon as the Fund has decided to activate them. The goal has been to make these reserve systems as accessible as possible, without compromising the Fund's current high security standards. Another element of this strategy to prevent disruptions to operations has been the implementation of monitoring systems for selected

aspects of the IT environment. This round-the-clock monitoring system is managed from a separate control centre.

Sustaining a high degree of system accessibility and IT security demands continuous maintenance and development of the Fund's various system solutions, a task that is handled by several functions within the organisation. Systems managers, responsible for accessibility, authorisation, functionality and quality, have been appointed for all business-critical systems. The Fund contracts external expertise to handle control, development and optimisation in specific areas.

The coordination and integration of strategy, operations and development are handled in the form of frequent meetings and special IT "advisory councils", when all systems managers get together to discuss priority issues. At regular intervals, the Fund's entire staff gathers for information about and training in topical information security issues, to enhance awareness and knowledge of these issues.

"As a state agency entrusted with considerable responsibility, the Second AP Fund, through the implementation of its strategic security programme, has established a highly effective system for continuity and disruption planning."

Thomas Hagström, Managing Director, Svensk Krisledning AB

Focus on efficiency continues

The Second AP Fund strives for and conducts cost-efficient fund management that has been analysed and authenticated by internationally respected firms of market analysts. During the year, a comprehensive analysis of the Fund's asset management was carried out by the Canadian firm, Cost Effectiveness Measurement Inc. (CEM). The purpose of this analysis was to develop relevant comparative data to assess the Fund's asset management performance, taking into account the volume of capital under management, its allocation by asset class and degree of active management, as well as the portfolio's geographic spread. This analysis, which is based on the years 2001–2004, was presented in the autumn and confirms that the Second AP Fund's costs are normal and that its asset management is cost efficient.

During the year, the Fund reduced the number of mandates under external management, which has reduced costs and improved the return on assets under active management. The Fund continues to strive for greater efficiency: implementation of the “operative alfa” concept represents one more stage of this ongoing process. The principle in this case is to exploit alternative sources of revenue that, while not increasing the Fund's exposure to market fluctuation, nevertheless make a positive contribution to its active return on investment. Examples of “operative alfa” include measures for reducing the Fund's transaction costs and the negative effects of foreign currency trades. In 2006, a number of key ratios will be established to enable long-term measurement and control of in-house and external development.

To complement current analytical tools, the Fund will in future add a new dimension in the form of a more detailed picture of costs for both asset managers and markets. The Fund has initiated cooperation with an international company to provide analytical results that will enable the Fund

to compare and analyse its own operations in terms of a global perspective. It is hoped that these more powerful analytical tools will promote transparency and know-how, thereby increasing opportunities to respond more efficiently.

The Second AP Fund intends to conduct an objective annual analysis of operations, along the lines of the CEM analysis. The idea is to increase value creation by means of the cost-efficient active management of assets, with limited active risk. The graph below illustrates the relationship between level of costs, based on activity and exposure, and the return generated by the Fund matched against a reference group of similar fund managers. The graph is one example of how the Fund monitors and analyses performance and results. The arrow indicates level of ambition.

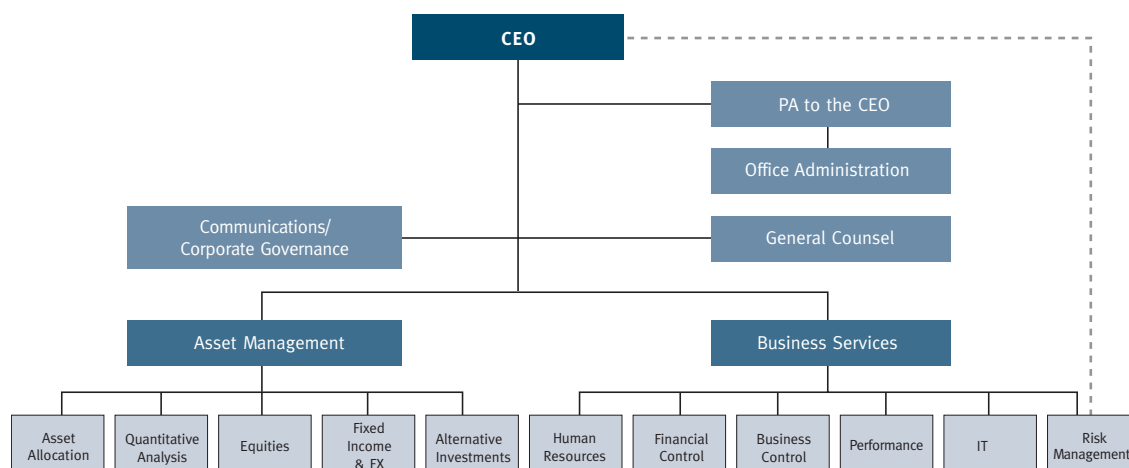
Example of analysis for monitoring costs and return compared to a reference group of similar fund managers.



Structure and staff:

Personal development good business for the Fund

The Second AP Fund is a knowledge-based organisation. The specialist expertise, professional skills and networking abilities of its staff are decisive to success.



As specialist and manager in a professional work environment with an international focus, the potential for career development is good. The Fund's HR strategy aims to enhance the efficiency of the organisation and further develop its determination to be a modern and attractive employer. A number of programmes and processes derive from this personnel strategy. The strategy comprises three main elements: "the HR value proposition", leadership development and staffing.

The "value proposition" is a document that describes the Second AP Fund's proposition to current and prospective employees, while also describing the demands and expectations placed on the individual.

One important HR programme established in 2005 focused on support and development of the Fund's departmental managers.

Well-developed cooperation with universities

The Fund has developed a programme for its on-going staffing requirements, based on the principle of recruiting first and foremost from within the Fund itself, although external recruitment may be considered for certain functions. The Second AP Fund has extensive contact with Gothenburg University's School of Economics and Chalmers University of Technology. This cooperation allows the Fund to offer students assignments for their graduation theses, opportunities for temporary employment on individual projects, trainee positions and vacation jobs. This also creates an excellent recruiting base for new members of staff, offering the opportunity for gradual adaptation to a new role.

Solid basis for responsible action

One of the crucial elements of this HR strategy has been to discuss and implement the special code of conduct that must apply to the activities of a national pension fund. This is based on the assumption that all employees are willing and able to accept individual responsibility for data and results, and are prepared to use their initiative and inquiring minds in addressing issues and seeking the best solutions. This makes special demands in terms of morality, responsibility and ethics.

Another important aspect of this strategy is further development of clearly defined models for performance evaluation and remuneration, adapted to the nature of the Fund's operations. The HR strategy now in place provides excellent support to the Fund's current operations and future development.

Programme to raise percentage of female employees

The number of female applicants for positions as portfolio managers has been low, which has led to the initiation of a programme to increase the number of female applicants in the long term. Six female students from Gothenburg University's School of Economics and Chalmers University of Technology are now working for the Second AP Fund, parallel to their university studies. After an induction course, they have completed a number of special projects within asset management. The programme will be evaluated in the spring of 2006.

Continued commitment to this HR strategy is designed to create a still more efficient organisation, and to further develop the Fund's determination to be a modern and attractive employer. The organisation functions well: thanks to a programme of continuous improvement, cooperation

between the different units has developed very satisfactorily. The focus now is on leadership issues, where areas for development have been identified and work is already in progress.

Creating networks a priority

Many Fund employees are specialists, and as such are members of broad networks of Swedish and international experts in their fields of expertise. It is important to adopt a systematic approach in building up these contacts, partly through participation in seminars and conferences, partly by establishing personal contacts. These contacts can provide new insights into the Fund's activities and can lead to new and more effective solutions. Members of the Fund's staff have attended a number of panel discussions during the year, and been invited to speak at some ten conferences.

Few sick days

Physical exercise and good health continue to form an important element of the Fund's corporate culture, and are among the goals established for personal development plans.

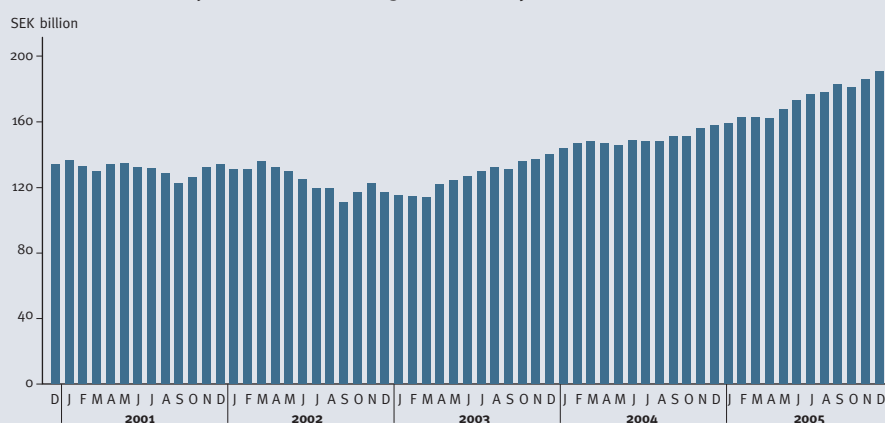
Second AP Fund staff members exert considerable influence over their own working conditions, with personal responsibility for achieving a balance between work and family life. Absence due to illness is minimal.



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Performance of capital assets since inauguration January 1st 2001, SEK billion



The Second AP Fund posted an excellent result for 2005. A bullish year on stock markets and relatively high exposure on the Swedish equities market, in conjunction with the Fund's active selection of indexes, have jointly contributed to the high return of 18.7 percent. The Fund has also generated a positive relative return on invested assets, amounting to 0.2 percent.

The Fund reported total capital assets, including inflows, of SEK 190.6 billion – an increase of SEK 32.5 billion since the start of the year. The net result of SEK 29.6 billion is the best since the Fund's inauguration.

Unless otherwise stated, the portfolio assets referred to in this report are "allocated exposures". In addition to booked actual 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 their actual values.

The Second AP Fund in 2005

The Second AP Fund's reported assets at year-end totalled SEK 190.6 billion, an increase of SEK 32.5 billion on 2004. The Fund's return on the total portfolio, excluding commission costs and operating expenses, amounted to 18.7 percent.

As per December 31st 2005, the Second AP Fund's capital assets were allocated as follows: approximately 62 percent equities, 34 percent fixed income assets and four percent alternative investments. The Fund's portfolio was thereby somewhat over-weighted in equities-related holdings compared with the strategic portfolio. At year-end 2005, the Fund's portfolio assets were broadly exposed on the global market, featuring a well-diversified risk.

Key events of the year

Management of the Fund's equities has been consolidated during the year and adapted to a management strategy with clearly defined mandates concerning active risk utilisation – the “core/satellite” strategy. Two new external global active mandates were activated during the year. The share of the total portfolio under in-house management increased during the second half of the year, rising to 72 percent by year-end. It is based largely on the Fund's own quantitative model, developed in-house.

Within the fixed-income management sphere, negotiations were completed concerning the award of a number of external global management mandates, two of which were activated during the autumn: one for global credit bonds and one for global government bonds and credit bonds.

Two new external GTAA (Global Tactical Asset Allocation) mandates were implemented within the framework of the Fund's tactical allocation during the year.

The Fund continues the process of creating a geographically well-diversified portfolio within asset group private equity funds. During the year, the Fund reached decisions concerning a large number of investment proposals, global as well as Swedish. New investment commitments have been made in four foreign funds, as well as one Swedish fund.

During 2005, the Canadian company Cost Effectiveness Measurement Inc. was commissioned to conduct an analysis to compare the Fund's level of costs and efficiency with similar companies and organisations of the same size. The analysis has confirmed that the Fund's level of costs is normal in relation to volume of capital under management, geographic spread and degree of activity.

The Fund's new strategic portfolio for 2006 takes into account both the liability and assets side, and illuminates different scenarios concerning the future development of the Swedish pension system. Broadly speaking, the portfolio has retained the same balance between equities and fixed-income instruments. Even so, there has been a slight increase in FX exposure, due to increased exposure to equities on emerging markets. Furthermore, the duration of fixed-income portfolios has been reduced, due to a reduced allocation of inflation-linked bonds. The target for the new strategic portfolio is a long-term real return in excess of 4.5 percent per annum.

The Fund's role as an institutional investor has gained increasing importance, not least in connection with developments involving a number of its larger holdings, such as Skandia and Meda. During the year, the Fund increased its involvement in nomination committees and topical corporate governance issues, in line with its declared governance policy.

Five-year review	01-12-31	02-12-31	03-12-31	04-12-31	05-12-31
Fund capital, SEK m	133 493	117 090	140 350	158 120	190 593
Net inflows from RFV/Swedish Social Insurance Administration and liquidation/special funds, SEK m	4 523	5 002	2 567	1 651	2 905
Net profit for the year, SEK m	-5 005	-21 405	20 693	16 119	29 568
Return on total portfolio per annum, before commission costs and operating expenses, %	-3.2	-15.3	17.8	11.6	18.7
Return on total portfolio per annum, after commission costs and operating expenses, %	-3.4	-15.4	17.7	11.4	18.5
Relative return per annum on listed assets before commission costs and operating expenses, %*	2.1	-0.4	-0.5	-0.6	0.2
Active risk ex post	1.7	1.0	0.6	0.5	0.5
FX exposure, %	10	7	8	10	11
Under active, incl. enhanced, management, %	37	62	89	90	90
Under external management, incl. investments in private equity companies, %	82	38	45	37	28
Expense ratio, incl. commission costs, %	0.14	0.16	0.18	0.22	0.16
Expense ratio, excl. commission costs, %	0.11	0.11	0.09	0.08	0.07

An adjustment for the change in accounting principle for performance-based fees has been made in the 2004 figures for the income statement, although not for historical key ratios.

* Relative return refers to the difference in return between a portfolio and its benchmark index.

Net result for the year

The Fund reported total assets of SEK 190.6 billion, including net flows, as per December 31st 2005. The Fund's return on total portfolio, excluding total costs (commission costs and operating expenses), amounted to 18.7 percent. The relative return on market-listed assets, excluding combined costs, amounted to 0.2 percent, thereby over-performing against the Fund's benchmark portfolio.

Inflows for the year amounted to SEK 2.9 billion, of which SEK 2.3 billion in net payments from Swedish Social Insurance Administration. The remaining inflows pertain to dividends from the "Liquidation Fund" and "Special Fund", which are managed by the First Swedish National Pension Fund and Fourth Swedish National Pension Fund respectively. The net result for the year, comprising operating income less commission costs and operating expenses, amounted to SEK 29.6 billion.

Operating income comprises dividends, net interest income, net return on all assets, exchange gains/losses and commission costs. Dividends received exceed the previous year's levels as a consequence of changes in dividend policy, in Swedish and foreign companies.

The Fund's commission costs include fixed external portfolio-management fees and custodial expenses, amounting to SEK 160 million. Performance-based charges for externally managed portfolios are included in the net result reported for each asset class.

The Fund's operating expenses amount to SEK 123 million, including personnel and other administration expenses. Total expenses include provisions for VAT payments totalling SEK 4 million.

Total expenses in relation to the Fund's average total capital assets for the year, or expenses ratio, amounted to 0.16 percent. The expenses ratio for funds under external management, including custodial expenses, in relation to the average actual value of Fund capital during the year, was 0.09 percent.

The work of the board

The Second AP Fund's board of directors comprises nine members in all, appointed by the Swedish Government. One new member was appointed to the board in 2005. The Fund's CEO, Lars Idermark, resigned his post on October 31st 2005, to be succeeded in February 2006 by Eva Halvarsson. The Fund's Chairman, Gunnar Larsson, has filled in as acting CEO during the interim period.

The board met on ten occasions in 2005, one of which was a long meeting on strategy. The Fund's economic development and results were presented and discussed at all these meetings. As well as considering 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. During the year, the board approved a new operations plan for 2006, the half-year and year-end accounts and a budget for the Fund's business activities. 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.

The Fund's CEO also participates in board meetings, as well as other members of staff, as required. Other persons may also be asked to attend meetings, as needed, such as the Fund's auditors or external partners.

Ministry of Finance appraisal of Second AP Fund

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 AP Funds have posted good results in 2004, due to a generally bullish stock market. The appraisal notes that the AP Funds' return on invested assets revealed only minor deviations from their respective benchmark portfolios, indicating a low degree of active risk. The Government also noted that there should be greater diversification of risk between the four AP funds. The appraisal also addresses the importance of index selection in value creation.

Under the auspices of the Ministry of Finance, KPMG conducted an analysis of the Swedish National Pension System's cost level. This analysis was based on data from 2004. In conducting the analysis, KPMG used reference data from active national and international pension funds, as well as private fund managers of varying sizes and fields of interest. The report criticised the Swedish National Pension System for its high cost level.

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 2005 to year-end 2007. 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 com-

mon to all Sweden's AP funds, dealing mainly with questions concerning the evaluation of security measures relating to business-critical IT systems. The auditors have also examined in-house routines and control functions. Any observations made concerning the audit are presented to the board of directors by the auditors in person.

The Fund's total portfolio

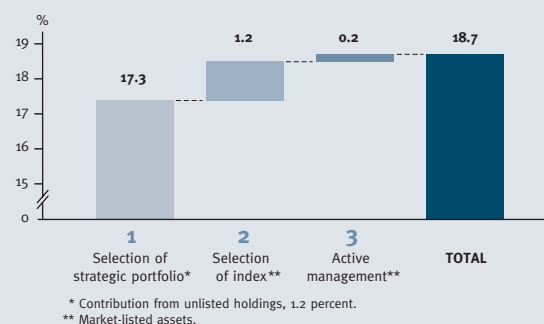
Distribution of Fund assets

The Fund's total assets of SEK 190.6 billion, as per December 31st 2005, were distributed as follows:

- listed equities totalling SEK 118.3 billion, of which SEK 40.8 billion in Swedish equities and SEK 77.5 billion in foreign equities
- fixed-income securities, including liquidity, totalling SEK 65.1 billion
- holdings in unlisted real-estate equities, including subordinated debenture loans, totalling SEK 5.8 billion
- holdings in private-equity funds totalling SEK 1.4 billion (outstanding investment commitments of SEK 4.7 billion).

During the year, an average of 34 percent of the Fund's assets were 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 3, page 63).

Three-stage value creation



To provide a more comprehensive picture of the Fund's value-creation strategy, the "three-stage value creation" concept was introduced in conjunction with the publication of the six-month interim report for 2005. The three stages involve the following: selection of strategic portfolio, selection of benchmark-index and active asset management. The Fund considers the selection of index an integral part of the investment process, whereby an investment universe is defined for in-house and external management of its assets. Rather than rely on more conventional broad-based indexes, the Second AP Fund has selected specialised indexes for its fixed-income securities from which, for example, Japanese bonds are excluded, and for its portfolio management where, among other things, regional weightings have been adjusted. In the case of the Fund itself, the selection of strategic portfolio and benchmark index has made a positive contribution to the Fund's result since the active selection of indexes was introduced in 2003. The Fund's relative return has also made a positive contribution to the result since its introduction.

Risk-adjusted return for total portfolio, valued by year

	2001		2002		2003		2004		2005	
	AP2	Strategic portfolio	AP2	Strategic portfolio	AP2	Strategic portfolio	AP2	Strategic portfolio	AP2	Strategic portfolio
Return, %	-3.2	-5.4	-15.3	-15.7	17.8	18.5	11.6	12.0	18.7	17.8
Standard deviation, %	9.7	10.2	13.0	13.1	8.6	8.6	5.8	5.7	4.8	4.7
Active risk ex post, %	1.7	-	1.0	-	0.6*	-	0.5*	-	0.5*	-
Information ratio	1.0	-	0.5	-	neg	-	neg	-	0.3	-
Sharpe ratio	neg	-	neg	-	1.7	-	1.6	-	3.4	-

* Total market-listed portfolio, excluding commission costs and operating expenses.

Risk utilisation 2005

In 2005, the Fund's relative utilisation of risk underwent a lateral shift. The level of active risk (ex post) for the Fund's market-listed assets was 0.5 percent at year-end, excluding combined expenses, corresponding to the level for the previous year. In the case of Swedish and foreign equities, however, active risk rose to 1.6 and 0.7 percent respectively.

Volatility for the Fund's total and strategic portfolios, expressed in terms of standard deviation, declined during the year, from 5.8 and 5.7 percent to 4.8 and 4.7 percent. The Fund reported a Sharpe ratio of 3.4 and a positive information ratio of 0.3 for 2005.

ROI

The substantial growth in the Fund's capital assets in 2005 was primarily attributable to the retention of a high share of equities in the portfolio, at a time when the Swedish stock market, like leading stock markets in other parts of the world, were reporting sharp upswings. However, the Fund's relatively limited exposure in foreign currency, in conjunction with a weakening of the

Swedish krona during the year, has had a negative effect on the net result. A relatively high degree of exposure on the Stockholm Stock Exchange has made a positive contribution to the Fund's pleasing performance.

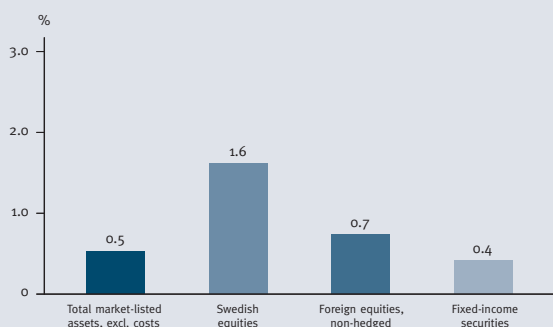
The Second AP Fund's return on the total portfolio amounted to 18.7 percent for 2005, excluding commission costs and operating expenses. This ROI includes the performance-based element of management costs. These costs arise in connection with the discretionary external management of listed assets. The Fund's return derives from the total portfolio, i.e. its portfolio of both listed and unlisted holdings. The Fund reports a relative return on market-listed assets, excluding expenses, of 0.2 percent for 2005.

The Fund's positive relative return is mainly the result of contributions from external GTAA mandates and the management of global equities.

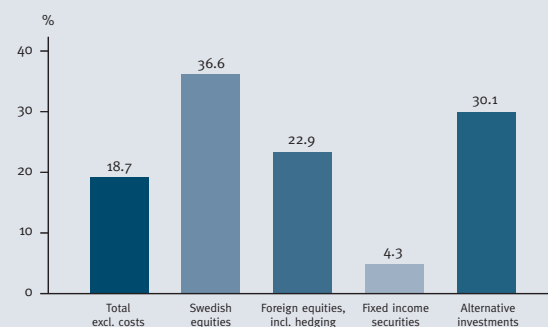
Changes of exposure in derivative instruments

In compliance with the guidelines approved in the business plan for 2005, the Fund has utilised derivative instruments to secure more effective management of

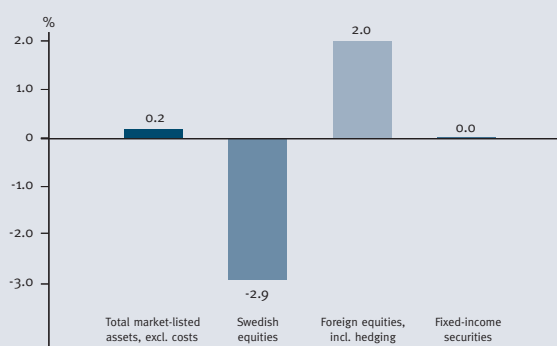
Active risk by asset class, 2005



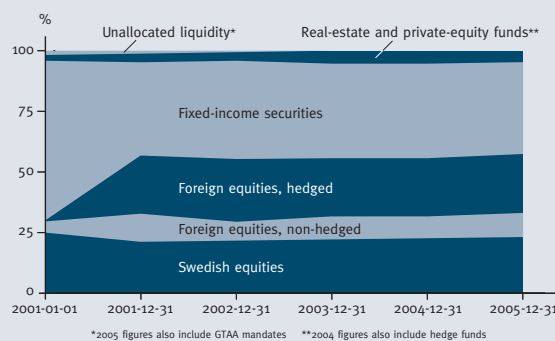
Absolute return by asset class, 2005



Relative return by asset class, 2005



Exposure 2001-2005



*2005 figures also include GTAA mandates **2004 figures also include hedge funds

assets, to reduce transaction costs and cut risk. During 2005, 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.
- Interest rate derivatives – mainly in the form of standardised bond futures – for rebalancing, tactical asset allocation and management of the Fund's interest rate risk.
- Within the framework of the Fund's GTAA (Global Tactical Asset Allocation) mandates, positions have been adopted with the aid of derivative instruments. The mandates are allowed to act with the help of short and long positions in permitted asset classes. However, the mandates may not adopt a net long position.

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

Listed and unlisted assets

The Fund's portfolio features assets of varying liquidity. The greater part of the Fund's assets are appraised and quoted daily, and are therefore considered to be liquid. Liquid assets comprise equities, bonds, derivative instruments and FX. Non-liquid assets are valued at longer periodicity and consist of real-estate and private-equity funds. To ensure that the ongoing monitoring and an-

alysis of return and risk provides a true and accurate picture, all assets should be valued on the same occasions and at the same periodicity, which at present is not possible. The Fund's reported return shall thereby always consist of the return generated on both parts of the portfolio. Relative return, however, is measured against the performance of the market-quoted portfolio. The Fund's variable costs for external portfolio management – commonly referred to as performance-based fees – are included in both instances. The Fund's commission costs and operating expenses for the current year are excluded, as per the appraisal model used by the Ministry of Finance.

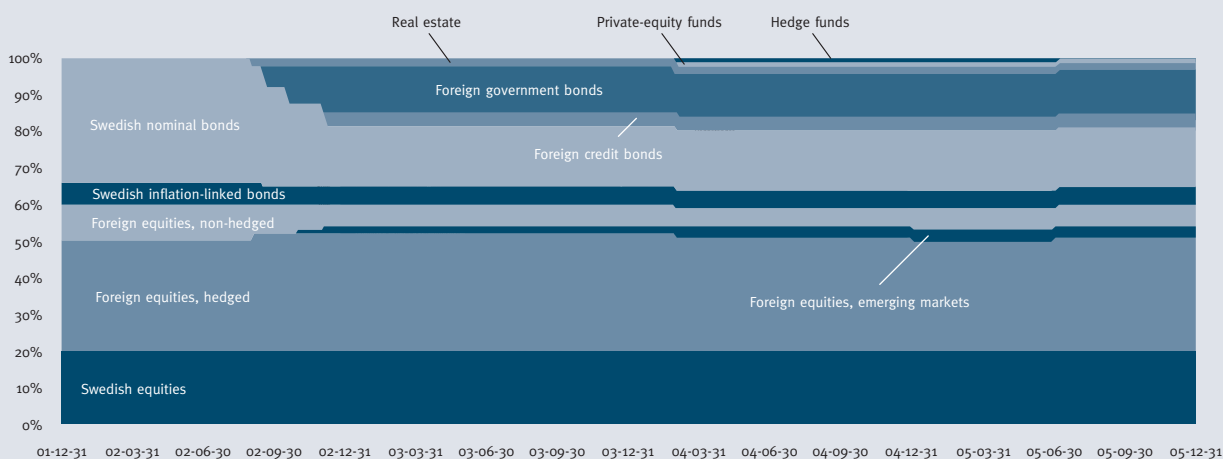
Tactical allocation

Significant changes were implemented within the framework of the Fund's tactical allocation in 2005. The in-house mandate has been complemented by two external mandates, which account for a substantial amount of the Fund's utilisation of active risk. The Fund's GTAA mandates are based on an investment process where several positions, driven by different investment themes, are used to form a well-diversified portfolio of tactical positions.

Positions are taken between different national and regional segments on the global equities and bond markets. In the same way, large numbers of tactical positions are taken on global FX markets.

The tactical allocation made a major contribution to the Fund's relative return during the year. Both the in-house and the two external mandates have performed well.

Changes in composition of strategic portfolio 2001-2005



Strategic asset allocation

The Second AP Fund's board of directors conducts an annual in-house evaluation of the focus chosen for the Fund's portfolio management policy. This process includes a 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, the first year of operation, the Fund conducted a comprehensive re-allocation of assets, involving the divestment of fixed-income instruments and purchase of foreign equities.

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 strategic portfolio for 2003 represented a refinement in terms of asset class distribution on different markets and changes in portfolio management style. The changes in the strategic asset allocation for 2004 were relatively minor. Alternative Investments became a new asset class comprising asset groups Real Estate, Private Equity Funds and Hedge Funds, and was expanded to comprise five percent of the Fund's total assets. Consequently, asset classes Equities and Fixed Income Securities shrank by one percent each.

The strategic portfolio for 2005 retained the same relative overall distribution of assets as for the preceding year, namely 59 percent equities, 36 percent fixed-income instruments and 5 percent alternative investments. Changes involved an increase in the degree of currency exposure (8 to 9 percent) and the adaptation of the Fund's hedging strategy to individual currencies. At the

end of the first six months of the year, the strategic portfolio was adjusted, the allocation to hedge funds being cut from one percent to zero. At the same time, the allocation to global equities was increased by one percent.

The new model for Asset Liability Modelling (ALM), developed in association with Fraunhofer Chalmers Research Centre for Industrial Mathematics, increases the Fund's opportunities for developing its strategic portfolio and asset allocation. One concrete result of this new ALM activity was to raise the Fund's target for real return on investment, as of 2005, from 3.5 to 4.5 percent.

New strategic portfolio 2006

In December 2005, the Board of Directors of the Second Swedish National Pension Fund/AP2 approved a somewhat altered strategic portfolio for 2006, with the intention of enhancing the anticipated return by marginal changes in risk, both in individual asset classes and in the portfolio as a whole. The distribution of assets within the strategic portfolio for 2006 is 60 percent equities, 36 percent fixed-income securities and four percent alternative investments.

In the Fund's strategic portfolio for 2006, the following changes have been made to asset class fixed-income securities:

- Swedish inflation-linked bonds two percent, a three-percent reduction.
- Swedish nominal government bonds 19 percent, a three-percent increase.

Benchmark index for strategic portfolio, 2005

Part-portfolio	Index
Equities	
Sweden	67% SBX "Stockholm Stock Exchange Benchmark Index" 23% OSX "Unweighted Sweden Index" 10% CSRX "Carnegie Small Cap Return 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	SFIX Svenskt Fastighetssindex
Private-equity funds	11% per annum
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

These changes are intended to shorten duration in the Swedish fixed-income portfolio, given the fact that today's fixed-income market offers no reasonable compensation for duration risk. The Fund's new strategic portfolio also offers opportunities to invest in government bonds on emerging markets.

The following changes are being introduced for equities-related asset classes:

- Equities in emerging markets five percent, a two-percent increase
- Foreign equities 35 percent, a two-percent reduction.

The increased investment in emerging markets is partly in anticipation of a higher return, partly to spread risk.

Asset class development

There were significant changes in portfolio management focus towards the end of 2004 and throughout 2005. The majority of external mandates have been terminated and 72 percent of the Fund's assets are now under in-house management.

A "core/satellite" strategy has been introduced for portfolio management, where a greater proportion of active risk is allocated to the global external mandates. The in-house mandates are increasingly managed according to the core strategy with the support of quantitative analysis. This is known as "enhanced management", where maximum risk may not exceed two percent. The Fund's in-house active management of Swedish and foreign equities has focused on a limited number of portfolios with clearly-defined risk mandates.

Swedish equities

During the year, management of Swedish equities has been fully adapted to the Fund's new asset management strategy. Most of the active risk is limited to the "special holdings" portfolio, into which holdings of a more long-term and strategic nature have been gathered. The equities portfolio is subject to long-term appraisal based on a combination of three separate elements, each assigned its own benchmark index. The portfolio comprises a capital-weighted element (67 percent), benchmarked against the SBX index; an equally-weighted element (23 percent), benchmarked against the OSX index, and a capital-weighted small cap element (10 percent), benchmarked against the CSX.

The Stockholm Stock Exchange saw its market worth rise by 32.6 percent in 2005, a bullishness that was particularly marked in the energy sector. On the other hand, according to the MSCI index, companies in the telecom sector noted a rise of only 7.6 percent.

The market value of the Swedish equities portfolio amounted to SEK 40.8 billion. Holdings were well diversified among large exchange-listed companies.

The greater part of the portfolio has been under active/enhanced management throughout the year, with limited active risk. The active level of risk assigned these Swedish holdings was 1.6 percent. As per December 31st 2005, 18 percent of the Swedish equities portfolio was under external management. Averaged over the year as a whole, some 21 percent of the portfolio was under external management. The Fund's Swedish equities holdings have performed well in 2005, rising to 36.6 percent against the benchmark's 39.5 percent. During the same period, the broad-based SIXRX index generated a return of 36.3 percent.

Largest Swedish holdings

The Fund's five single largest Swedish holdings by worth, in the total equities portfolio, were Ericsson (4.0

Swedish equities

	2001	2002	2003	2004	2005
Exposed value, SEK billion	26.2	22.8	28.4	32.8	40.8
Absolute return, %	-15.6	-36.7	34.4	19.0	36.6
Relative return, %	-0.8	-0.9	-1.6	-1.2	-2.9
SIXRX, %	-	-	34.2	20.8	36.3
Active management, %	75	100	100	94	100
External management, %	100	50	56	27	18

Foreign equities

	2001	2002	2003	2004	2005
Exposed value, SEK billion	53.8	46.1	56.7	63.8	77.5
Absolute return, %	-7.7	-24.9	22.5	11.5	22.9
Relative return, %	1.0	0.3	-1.0	-0.3	2.0
MSCI AC World, %	-	-	22.6	10.6	20.0
Active management, %	11	37	78	80	82
External management, %	100	64	82	77	53

percent), SHB (2.6 percent), Volvo (2.6 percent), Nordea (2.0 percent) and Electrolux (1.9 percent).

Foreign equities

82 percent of the Fund's holdings in foreign equities are under active management, distributed according to the geographical regions North America, Europe and Asia/Pacific, as well as in emerging markets and via global mandates. During the year, consolidation of the Fund's external asset management activities continued. A limited number of new specialised mandates were implemented in 2005, accounting for the majority of the Fund's active risk utilisation. Global equities totalling SEK 34.7 billion are now under in-house management, equivalent to 47 percent of the total portfolio, part of which are managed passively, part under enhanced management, in line with the core strategy. The intention is to introduce the core strategy as soon as possible for all in-house portfolio management, apart from the European portfolio, which is managed under an active risk mandate. The level of active risk for the Fund's foreign holdings is 0.7 percent. Fund investments in emerging markets amount to SEK 7.5 billion and have made a major contribution to the return on foreign equities. In 2005, implementation of the core/satellite strategy was also initiated for investments in emerging markets.

The market value of the foreign equities portfolio amounted to SEK 77.5 billion at year-end. In line with the Fund's strategic asset allocation policy, the degree of market exposure in the USA was reduced in favour of European, Japanese and Pacific stocks, as well as emerging markets. The portfolio of foreign equities has yielded a return of 22.9 percent compared with an MSCI World index, hedged and regionally adjusted by

the Fund, which generated a return of 20.9 percent for the same period. For the same period, the broad-based MSCI World index posted a return of 20.0 percent. As per December 31st 2005, 53 percent of assets held in foreign equities were under external management. The average over the full twelve months was 70 percent.

Largest foreign holdings

At the end of the year, the five single largest foreign holdings in the Second AP Fund's total portfolio were BP (0.8 percent), General Electric (0.6 percent), Exxon Mobil (0.6 percent), Nestlé (0.6 percent) and HSBC (0.5 percent).

Fixed-income and FX

During the latter part of the year, the Fund activated two external fixed-income mandates that have performed well. In line with its recently adopted core/satellite strategy, the Fund plans to locate fund managers with special competence to complement that of its in-house portfolio managers. The process of establishing quantitative asset management models for Swedish and foreign bonds has already been initiated, and their implementation is scheduled sometime during 2006. Parts of the inflation-linked portfolio were divested during the year. Portfolio performance, which is in line with index, was adversely affected during the first half of the year, when the Fund was positioned for gains in long interest rates. The performance of these assets improved during the second half, however, thanks to rising interest rates.

As per December 31st 2005, the duration of the portfolio amounted to 5.1 years, unchanged compared to the preceding year. National issuers accounted for 59.8 percent of the fixed-income portfolio. As per December 31st 2005, 81 percent of the portfolio was

Composition of strategic portfolio, exposure and return, as per Dec 31 2005

Asset class	Strategic portfolio, %	Exposure, %	Exposed value, SEK billion	Return AP2, %	Return on benchmark portfolio, %	Active risk ex post*, %
Swedish equities	20	21.4	40.8	36.6	39.5	1.6
Foreign equities	40	40.7	77.5	22.9	20.9	0.7
Fixed-income assets, including liquidity and accumulated interest	36	34.1	65.1	4.3	4.3	0.4
Total listed assets, excluding commissions and operating expenses				18.1	17.9	0.5
Alternative investments	4	3.8	7.2	30.1	12.9	
Total Fund capital, excluding commissions and operating expenses	100.0	100.0	190.6	18.7	17.8	

* Historic outcome, 12 months rolling

placed in fixed-income securities, rated from AA- to triple A (AAA). At year-end 2005, nominal and inflation-linked government bonds accounted for 60 percent of the total value of the fixed-income portfolio.

The Fund has been engaged to only a limited degree in active foreign exchange trading. An active FX mandate was nevertheless initiated in 2004, to generate value from foreign exchange market volatility. Under this mandate, positions are taken to benefit from anticipated movement in the intrinsic values of foreign currencies. The management of these assets had a favourable impact on the Fund's overall return.

The market worth of the Fund's fixed-income instruments as per December 31st 2005, including liquidity, amounted to SEK 65.1 billion. The fixed income portfolio consists mainly of nominal and inflation-

linked Swedish bonds, as well as internationally traded government securities and corporate bonds. Foreign fixed-income holdings totalled SEK 32.3 billion. The return on the portfolio of fixed-income securities was 4.3 percent, in line with the benchmark index.

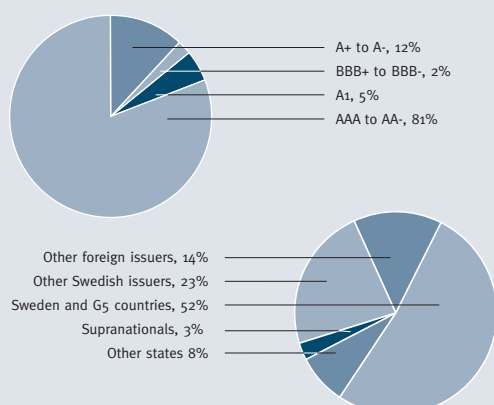
Alternative investments

The Fund has gathered its investments in asset groups real estate and private equity funds, which account for 3.8 percent of the Fund's total capital, under asset class Alternative Investments. Hedge funds, previously included in this asset class, were divested during the year. Real estate, corresponding to 3.1 percent of the Fund's total capital assets, accounts for the largest share of Alternative Investments: private equity funds account for approximately 0.7 percent of the Fund's investments.

Private-equity funds

The law requires that Swedish AP funds may only invest in unlisted equities indirectly, via private equity funds,

Issuers



Fixed-income assets

	2001	2002	2003	2004	2005
Exposed value including liquidity, SEK billion	50.3	43.4	50.4	54.6	65.1
Absolute return, %	3.7	8.9	5.3	7.3	4.3
Relative return, %	-0.1	0.0	-0.1	-0.3	0.0
Active management, %	12	88	98	94	93
External management, %	57	9	10	8	8

Investments and commitments, private equity funds, SEK million

Fund	2001-2004		2005			Total		
	Investment*	Commitment	Investment*	Exit**	Commitment	Investment*	Exit**	Commitment
EQT Northern Europe KB (EQT III)	118	181	42	31		160	31	181
Swedestart Life Science KB	11	25	2	1		13	1	25
Swedestart Tech KB	11	25	2	3		13	3	25
Carnegie Biotech Bridge Fund	47	50				47		50
Nordic Capital V L.P.	145	454	214	3		359	3	454
EQT Mezzanine L.P.	43	272	84			127		272
Cevian Capital L.P.	176	681	110	12		286	12	681
Pathway Private Equity Fund IX, LLC	32	1 118	152	4		184	4	1 118
CVC European Equity Partners IV, L.P.			32		335	32		335
Carlyle Riverstone Renewable Energy Infrastructure Fund I					159			159
Carlyle Riverstone Global Energy Fund III					239			239
Pathway Private Equity Fund IXB					1 990			1 990
Nordic Capital VI L.P.					469			469
Total	583	2 806	638	54	3 192	1 221	54	5 998
Fair value, total						1 392		

* Investment, excluding commission for unlisted assets

** Acquisition value of underlying portfolio companies sold

mutual funds or their equivalent. The strategy adopted by the Second Swedish National Pension Fund/AP2 is to create a geographically well-diversified portfolio of private equity funds. A step in this direction was taken in 2004, when the Fund embarked on its first major undertaking outside the Nordic region. This took the form of a USD 150 million investment in a “fund-on-fund”, managed by Pathway Capital. During 2005, the Fund increased its investment commitments with additional investments in CVC European Equity IV, Pathway Private Equity Fund IXB, Carlyle Riverstone Renewable Energy Fund I, Carlyle Riverstone Global Energy Fund III and Nordic Capital VI. In conjunction with the undertakings made in the preceding year, this brought the Fund’s total investment commitment to SEK 6.0 billion. Actual investments to date total SEK 1 329 million, including management expenses, of which SEK 680 million in 2005. This corresponded to a fair value of SEK 1 392 million.

During the year, the AP funds brought their accounting principles more in line with international standards. Management fees for unlisted assets, where reimbursement is permitted prior to profit sharing and is deemed likely, are reported as a receivable below other assets in

the balance sheet. See also the Fund’s accounting and valuation principles, page 60.

Since the Fund’s inauguration, a total of SEK 108 million has been paid out in the form of management fees for Fund investments in private-equity funds. Of this sum, SEK 66 million has been accounted for as costs as per previously applied principles.

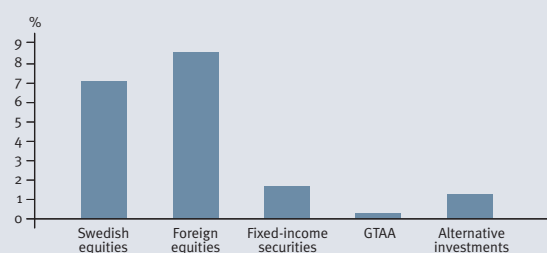
The probable repayment capacity of private-equity funds is judged annually, to determine an appropriate level for the capitalisation of management fees. In cases where this capacity is deemed low, paid and capitalised management fees are written off as a commission cost. Management fees paid to private-equity funds where the contract precludes repayment are reported as commission costs.

In 2005, payment of management fees totalling SEK 18 million net have been reported as other receivables.

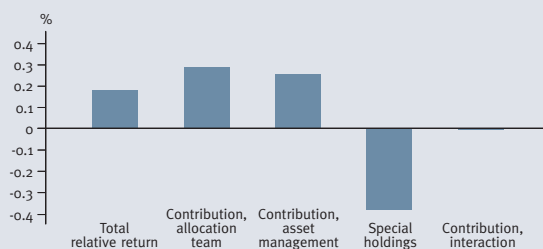
Real estate

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

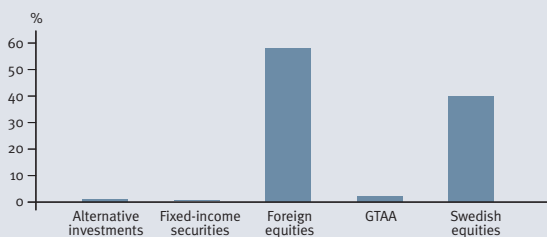
Attribution total portfolio, absolute return including alternative investments



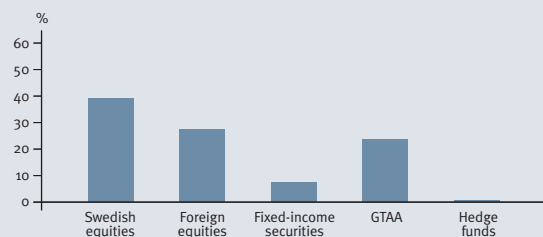
Attribution relative return, listed assets



Risk attribution, absolute risk



Risk attribution – tracking error



external managers. Unlisted real-estate holdings, comprising 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.

Unlisted real-estate holdings Dec 31st 2005

AP Fastigheter Holding AB, amounts in SEK m

Equities	
Acquisition value	721
Valuation	940
(of which affecting operating result 2005: 728)	
Fair value as per Dec 31st 2005	1 661
Total dividend 2001-2005 (of which in 2005: 342)	717

Promissory note loan, incl. accrued interest

Promissory note loan,	
incl. accrued interest per Dec 31st 2005	2 180
Total interest income 2001-2005 (of which in 2005: 181)	339

NS Holding AB, amounts in SEK m

Equities	
Acquisition value	372
Valuation	606
(of which affecting operating result in 2005: 282)	
Fair value as per Dec 31st 2005	978

Subordinated debenture loans incl. accrued interest

Subordinated debenture loans incl. accrued interest	
as per Dec 31st 2005	1 010
Total interest income 2001-2005 (of which in 2005: 107)	398

AP Fastigheter is owned jointly by the First to Fourth Swedish National Pension Funds and has a concentrated and attractively located portfolio of real-estate holdings in the Stockholm, Gothenburg and Uppsala areas. The company owns and manages some 200 properties, totalling two million square metres of floor space, at a combined estimated market value of SEK 32 billion.

Norrporten is owned jointly by the Second AP Fund, the Sixth AP Fund and Vasakronan, all of which hold a one-third interest in the company. The company continued its strategic expansion during the year and has invested in a number of substantial properties in Uppsala and Copenhagen. Norrporten owns and manages some 180 properties, totalling approximately 1.2 million square metres of floor space. These properties have a combined estimated market value of SEK 14 billion.

The holdings in Norrporten have noted favourable development, generating a SEK 282 million increase in market value and interest income on debenture loans amounting to SEK 107 million. Return on investment was 24 percent. The Fund's holdings in AP Fastigheter have also noted an increase in market value, of SEK 728 million, with interest income on debenture loans amounting to SEK 181 million. Return on investment was 48 percent. This high return is partly attributable to the application of changed valuation principles in AP Fastigheter's accounts. The market values of the Second AP Fund's portfolios of real estate in AP Fastigheter and Norrporten, including debenture loans, were reported as SEK 3 841 million and SEK 1 988 million respectively.

Currency exposure

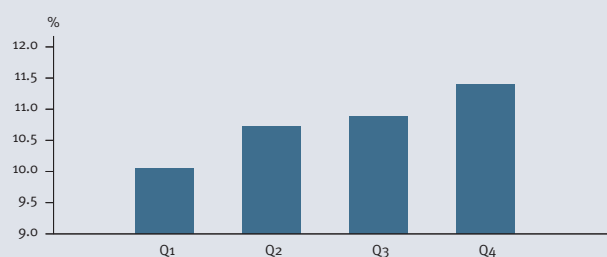
Dec 31st 2005, equivalent in SEK million	USD	GBP	EUR	JPY	Other	Total
Equities and participations	33 473	10 166	16 795	7 252	9 944	77 630
Bonds and other fixed-income securities	9 487	1 505	11 298	0	2 236	24 526
Other assets and liabilities, net	514	67	765	187	341	1 874
Derivative instruments, excl. FX derivatives	11	-41	1	21	-13	-21
FX derivatives	-32 947	-9 511	-23 627	-6 965	-9 172	-82 222
Currency exposure, net	10 538	2 186	5 232	495	3 336	21 787

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.

FX exposure

At year-end 2005, 11.4 percent of the Fund's assets were exposed in foreign currency, a slightly higher figure compared with the strategic portfolio. Assets exposed in foreign currency, found mainly in the foreign fixed-income and equities portfolios, have been hedged by means of forward exchange contracts. The Fund's total exposure in FX is distributed as shown in the table below.

Currency exposure per quarter, 2005



External portfolio management

The Second AP Fund manages a certain proportion of its total portfolio assets with the assistance of external managers. During the year, the Fund's external portfolio management has been concentrated to a few fund managers with an active style of asset management, in line with the Fund's new investment strategy. As per December 31st 2005, 28 percent of the Fund's assets were under external management. Some 76 percent of

all assets under external mandates were managed actively. During 2005, a number of new mandates were activated within the GTAA sphere, as well as in global equities and fixed-income securities.

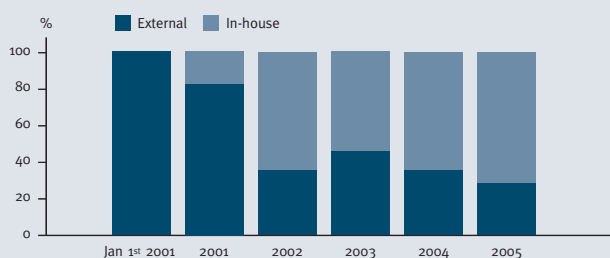
Contract negotiation and selection criteria

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.

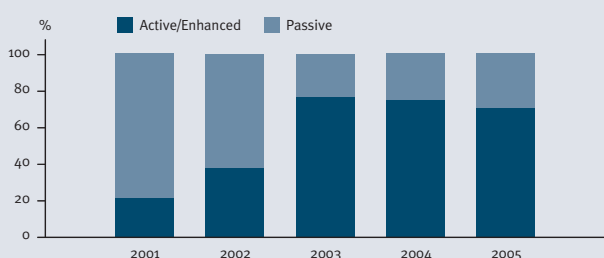
Cost of external management

On average, about 34 percent of the Fund's assets were under external management in 2005. The amount of assets under active external management amounted on average to 77 percent. The degree of active risk accepted, and selection of market, to a great extent determine the cost of managing assets. The Fund's external management mandates, excluding alternative investments, have been focused on increasing the level of active risk in 2005. The cost of placing market-listed assets under external management is partly fixed and partly performance-based. In 2005, the fixed cost was SEK 138 million and the variable performance-based element totalled SEK 90 million. If management fees for alternative investments are included, this brings the Fund's combined fixed costs for external management to SEK 145 million. This is equivalent to 0.25 percent of the average capital assets under external management during 2005. The Fund compares the cost for external management of capital assets with those for similar market players.

Relative distribution between in-house and external management



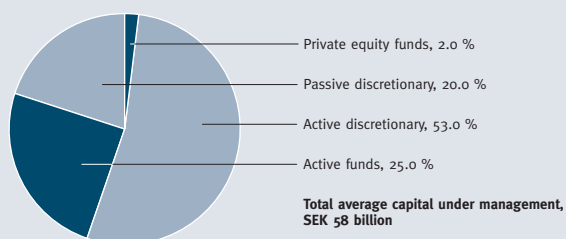
External management, passive/active management style



A fair and just comparison must take into account the volume of assets under management, the degree of in-house management and the style of management chosen

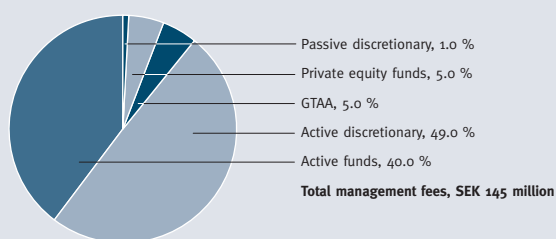
in terms of active versus passive, equities versus fixed-income securities and varying amounts of unlisted asset classes.

Capital assets under management, by management style



GTAA mandates have no allocated capital, since exposure is in the form of derivative instruments.

Management fees, by management style



Income and expenses, external management, listed assets, SEK million

	Active and enhanced mandates	Passive mandates	Total listed assets
Income, gross	14 021	2 938	16 959
Deduction, performance-based fees	-90		-90
Net	13 931	2 938	16 869
Fixed management fees	-137	-1	-138
Net contribution	13 794	2 937	16 731
Capital assets under management as per Dec. 31st 2005, excluding overlay mandates			
	39 166	13 071	52 237

Income and expenses, external management, unlisted assets, SEK million

	Unlisted assets
Income, gross	272
Repayment of management fees in conjunction with profitable exit	17
Management fees reported as commission cost	-7
Net contribution	282
Receivables in form of management fees, unlisted assets	18
Capital assets under management, as per Dec. 31st 2005:	
Invested, fair value	1 392
Original commitment	5 998

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. The Fund monitors, evaluates and analyses holdings on a daily basis, whether the assets are managed externally or in-house.

Reports on exposure, yields and risk utilisation are generated on a daily, weekly and monthly basis. Complete balance sheets and income statements are prepared on a monthly basis, together with whole range of relevant economic analyses.

Risk management

The Fund's level of risk utilisation for 2005 was within the specified parameters. Follow-up of investment regulations, limits and financial risks is handled on a daily basis. Operative management is conducted so that the anticipated active risk for the entire exchange-listed portfolio shall not exceed three percent. In the same way, individual limits for anticipated active risk are set for each asset class.

The Fund's absolute and relative risk is monitored and analysed, for the total portfolio, per asset class and per mandate. Absolute risk is monitored with the help of the Sharpe ratio and volatility measurements. Relative risk is measured in terms of anticipated active risk and information ratio.

During 2005, the Sharpe ratio (twelve-month rolling) was positive and noted 3.4 at year-end. The market-listed portfolio's volatility declined during the year from 5.8 to 4.8 percent, while the twelve-month rolling information ratio was 0.3.

The Fund uses an external risk system as a complement to enable both historic and forward analysis and

monitoring of the Fund's combined market and credit risk. These risk calculations are based on Value at Risk (VaR). The system permits advanced simulation for calculating alternative risk outcomes by means of stress tests and scenario analyses. Preparations with a view to procuring risk management systems in 2006 were initiated in 2005.

Attribution analyses

One way the Fund assesses portfolio performance is by conducting attribution analyses. These analyses are conducted in several dimensions, for both absolute and relative return, as well as for the level of risk utilisation. The analysis defines the extent to which the portfolio has contributed to return and risk utilisation.

Return attribution is employed partly to clarify the differences in return between the Fund's portfolio of assets and the strategic benchmark portfolio, and partly to explain the contribution to absolute return on investment. The analytical process is conducted at several levels: for the total portfolio, between and within each asset class and at the portfolio level. The contribution made, in terms of individual securities as well as sectors, regions and currencies, is analysed at each level. In 2005, the GTAA mandates and portfolio of foreign equities were the largest positive contributors to relative return. In the case of foreign equities, the greater part of this contribution derives from the North American mandates. The Fund's special mandate within the framework of the Swedish equities portfolio, Special Holdings, is the single largest negative contributor.

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.

Attribution analysis of relative return, %

Relative return	0.2
Allocation team including rebalancing, over/under cash-backing and GTAA mandates	0.3
Swedish equities including securities selection and allocation between sub-indexes	0.0
Foreign equities including securities selection by region and emerging market allocation	0.3
Fixed income portfolio including securities selection, cash management and allocation between sub-indexes	0.0
FX including allocated degree of hedging, FX-trading and securities selection of FX-hedge	0.0
Hedge funds	0.0
Special holdings	-0.4
Interaction	0.0

Systems environment

Right from the start, the Second AP Fund invested in an advanced IT platform and in a fully integrated Front/Middle/Back Office portfolio management system. Since its implementation, this system has been progressively expanded and upgraded with additional functions, 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 basic system was complemented with a web-based system for the import of external managers' trades. External managers are responsible for the entire business process within the parameters of their respective mandates, from execution to settlement and reporting.

During 2005, the Fund has worked on a systems optimisation project known as the PIP (Profit Improvement Plan), in close association with the systems supplier. This project is intended to improve and enhance efficient systems utilisation, as well as to promote a greater degree of STP (Straight Through Processing). Analyses indicate that today's Second AP Fund possesses a very satisfactory level of systems know-how and enjoys a high degree of automation in terms of its business processes, and that the work is carried out efficiently. To further optimise system use, the Fund is evaluating proposals for additional functionality and possible changes in portfolio structure.

Strategic IT security

IT security is one of the Fund's priority sectors. During 2005, the security programme has been further developed, in areas such as continuity and disruption planning. Much of this work has focused on securing the Fund's most business-critical systems in the event of crisis or catastrophe. The technical solution has concentrated on ensuring that the most business-critical systems can be

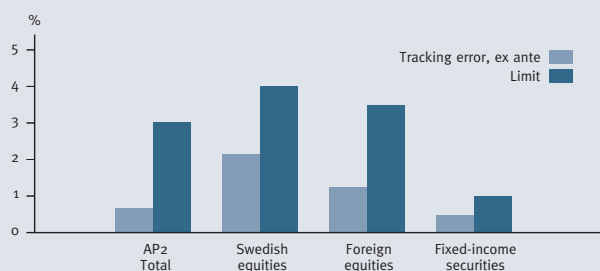
brought back on line as soon as the Fund's executive management has reached a decision. The system's present functionality has therefore been complemented to provide external access (a reserve site), offering full redundancy for the Fund's central IT system. This back-up system can be accessed without compromising the Fund's current stringent data security standards.

Focus on efficiency continues

The Second AP Fund strives for and conducts cost-efficient fund management that has been analysed and authenticated by internationally respected firms of market analysts. During the year, a comprehensive analysis of the Fund's asset management was carried out by the Canadian firm, Cost Effectiveness Measurement Inc. (CEM). The purpose of this analysis was to develop relevant comparative data to assess the Fund's asset management performance, taking into account the volume of capital under management, its allocation by asset class and degree of active management, as well as the portfolio's geographic spread. This analysis, which is based on the years 2001–2004, was presented in the autumn and confirms that the Second AP Fund's costs are normal and that its asset management is cost efficient.

The Fund continues to strive for greater efficiency: implementation of the "operative alfa" concept represents one more stage of this ongoing process. The principle in this case is to exploit alternative sources of reve-

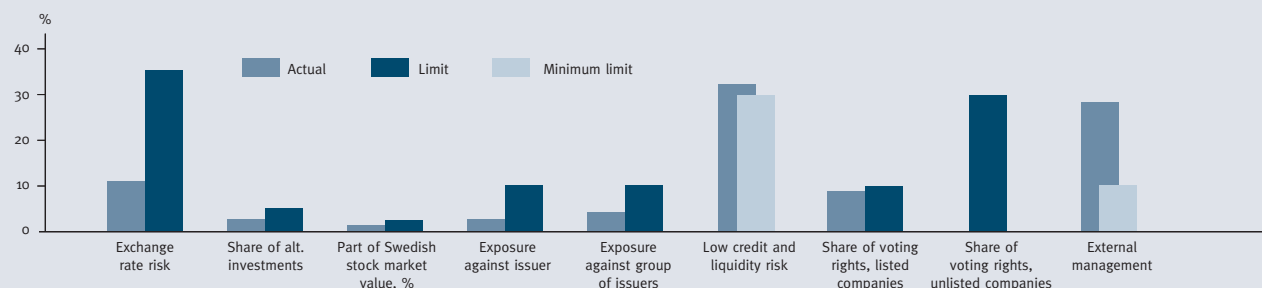
Risk limits, active risk



Sharpe ratio



Limit as per investment regulations



nue that, while not increasing the Fund's exposure to market fluctuation, nevertheless make a positive contribution to its active return on investment. Examples of "operative alfa" include measures for reducing the Fund's transaction costs and the negative effects of foreign currency trades.

To complement current analytical tools, the Fund will in future add a new dimension in the form of a more detailed picture of costs for both asset managers and markets. The Fund has initiated cooperation with an international company to provide analytical results that will enable the Fund to compare and analyse its own operations in terms of a global perspective. It is hoped that these more powerful analytical tools will promote transparency and know-how, thereby increasing opportunities to respond more efficiently.

Brokerage commission

In connection with the purchase of equities and participations, commission is capitalised in accordance with generally accepted auditing standards and thereby included in the acquisition value. Total commission paid in 2005 amounted to SEK 109 million. Transactions implemented during the year in connection with adjustment to the Fund's new core/satellite strategy have contributed to an increase in commission expense. Of the total commission expense, 49 percent is attributable to external management of Fund assets and the remainder to in-house portfolio management. This corresponded to an expense amounting to 0.02 percent of the total volume of shares traded during the period.

The following five counterparts have received commissions corresponding to 50 percent of commission payments (in alphabetical order): Carnegie, Citigroup, Goldman Sachs, SEB and Svenska Handelsbanken.

Tax

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

During the year, provisions for VAT amounting to SEK 5 million were resolved.

Structure and staff

In 2005, the Second AP Fund implemented a new HR strategy, featuring three main elements: "the HR value proposition", leadership development and staffing. The new strategy focuses on long-term guidelines for leadership, recruitment, competence 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 2005, the Fund numbered 46 full-time staff (of which 17 women), with three additional staff on a project basis. The average age of Fund employees is 38.5 years, with a median age of 39 years and an age spread from 26 to 60.

Members of staff, with an average work experience of 16 years, represent five different nationalities.

The Fund has a low rate of personnel turnover. During 2005, three employees left and four new employees joined the Fund. The level of absence due to illness during the year was low: 0.8 percent.

Corporate governance

Owner-related activities in 2005

A new corporate governance code was presented in 2004. As a consequence of the new code, the Second AP Fund's board of directors adopted a new corporate governance policy at the start of 2005, which clarifies the Fund's position on a number of governance issues. During the year, the Fund initiated a project designed to integrate corporate governance issues more clearly into the Fund's day-to-day management activities. This involves an internal analysis of corporate governance issues, with a view to subsequently incorporating conclusions as part of the investment process.

During 2005, the Second AP Fund was represented at 49 Swedish annual general meetings (AGMs) and exercised its voting rights at the AGMs of its 50 largest foreign shareholdings. The Second AP Fund has also participated in nomination committees for the boards of Artimplant, Capio, Castellum, Electrolux, Feelgood, Handelsbanken, Karo Bio, Pergo, ProAct, Sardus, Skandia, Vitrolife, Volvo, Wedins and WM-data.

Income statement

Amounts in SEK million	Note	January-December 2005	January-December 2004
Operating income			
Net interest income	1	1 696	2 632
Dividends received		2 696	1 903
Net result, listed equities and participations	3	22 421	10 399
Net result, unlisted equities and participations	2	1 249	414
Net result, fixed-income assets		532	1 641
Net result, derivative instruments		-565	808
Net result, exchange gain/loss		1 822	-1 370
Commission costs	3	-160	-189
Total operating income		29 691	16 238
Operating expenses			
Personnel costs	4	-70	-64
Other administration expenses	5	-53	-55
Total operating expenses		-123	-119
NET RESULT FOR THE YEAR		29 568	16 119

Balance sheet

Amounts in SEK million	Note	Dec. 31 2005	Dec. 31 2004
ASSETS			
Equities and participations			
Listed	6	120 591	88 844
Unlisted	7	4 012	2 267
Bonds and other fixed income assets	8	62 230	63 223
Derivative instruments	9	1 247	2 278
Cash and bank balances		2 141	1 193
Other assets	10	188	103
Prepaid expenses and accrued income	11	1 470	1 289
TOTAL ASSETS		191 879	159 197
FUND CAPITAL AND LIABILITIES			
Liabilities			
Derivative instruments	9	821	741
Other liabilities	12	84	214
Accrued expenses and deferred income	13	381	122
Total liabilities		1 286	1 077
Fund capital			
	14		
Opening fund capital		158 120	140 350
Net inflow to the national pension system		2 312	1 397
Transferred from special funds and liquidation fund		593	254
Net result for the year		29 568	16 119
Total fund capital		190 593	158 120
TOTAL FUND CAPITAL AND LIABILITIES		191 879	159 197
Memorandum items			
Other assets pledged	15	1 942	818
Investment commitments	16	4 669	2 157

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.

Changed accounting principles

As of 2005, the First – Fourth AP Funds have adapted the principle applied in reporting fees paid with respect to the external management of unlisted assets, together with the format of the income statement, to that applied by comparable organisations in Sweden and internationally. The new principle for reporting fees paid with respect to the external management of unlisted assets is applied with effect from January 1st 2005. Comparative figures have thus not been adjusted. However, comparative figures have been adjusted to correspond with the new format adopted for the income statement.

The performance-based fee, which is only paid out if the portfolio manager attains a return on investment in excess of the agreed level, is reported under net result per asset class in the income statement.

Fees paid for the external management of unlisted assets, where reimbursement is permitted prior to profit sharing and is deemed likely, are reported as a receivable below other assets in the balance sheet. Other fixed fees paid to external portfolio managers, as well as custodial fees, are reported under commission costs in the income statement.

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 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 "Net result, exchange gain/loss".

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.

Unlisted holdings are valued in accordance with EVCA or equivalent principles. Generally speaking, holdings shall be assigned a fair value, based on a conservative and consistent estimate.

Bonds and other fixed-income securities

Bonds and other fixed-income assets are calculated at their net realisable value. The net realisable value 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. 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, 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. The difference arising between the forward rate and the spot rate on exchange forwards is straight-line accounted over the term of the forward contract, and is reported as interest.

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 and software

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.

Commission costs

Commission costs are reported in the income statement as a deduction under operating income. These comprise direct transaction expenses such as custodial fees and fixed fees to external portfolio managers.

Accounting principles for performance-based fees and management fees for unlisted assets are reported under “Changed accounting principles”.

Operating expenses

All expenses incurred, excluding brokerage commission, performance-based fees to external portfolio managers and commission costs, are reported under operating expenses.

Due to the fact that the Second AP Fund is exempt from VAT, not being considered a commercial operation, it lacks the right to recover VAT payments made. VAT paid and for which provision has been made in the accounts is reported together with the respective cost item.

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

Amounts in SEK million	January-December 2005	January-December 2004
Interest income		
Bonds and other fixed-income assets	2 486	2 418
Derivative instruments	541	576
Other interest income	41	19
Total interest income	3 068	3 013
Interest expenses		
Derivative instruments	-1 301	-330
Other interest expenses	-71	-51
Total interest expenses	-1 372	-381
Net interest income	1 696	2 632

NOTE 2 Net result, unlisted equities and participations

Amounts in SEK million	January-December 2005	January-December 2004
Capital losses, net	-2	-
Unrealised changes in value	1 251	414
Net result, unlisted equities and participations	1 249	414

NOTE 3 Commission costs

Amounts in SEK million	January-December 2005	January-December 2004
External portfolio management fees, listed assets	138	142
External portfolio management fees, unlisted assets	7	34
Other commission costs, including custodial expenses	15	13
Total commission costs	160	189

Commission costs do not include performance-based expenses. During the year, performance-based expenses amounted to SEK 90 million (SEK 22 million) and reduce the net gain for the asset under management. External portfolio management fees for unlisted assets are reported under commission costs in so far as the contracts do not permit repayment prior to profit sharing in conjunction with future profitable exits. During 2005, a total of SEK 42 million (SEK 34 million) has been paid in management fees for unlisted assets. Of these, a sum of SEK 35 million is deemed likely to be repaid in conjunction with future profitable exits, and has therefore been reported in the balance sheet under "Other assets". During the year, a sum totalling SEK 17 million has been repaid in conjunction with profitable exits.

External portfolio management expenses comprise fees paid to external managers assigned to manage discretionary portfolios of listed and unlisted assets, as well as fees pertaining to the management of listed mutual funds. External asset management expenses, classified according to active and passive mandates, and management fees paid to funds, are shown in the table on the next page.

Distribution of Fund capital between external mandates and in-house portfolio management as per Dec. 31st 2005, (SEK m)

Mandate		Benchmark index	Average capital under management 2005	Market- value per Dec. 31 2005*	% of fund capital	External management expense
External discretionary mandates						
Equities mandates						
Active management						
SHB	Swedish equities, terminated	SBX	655	0		
SEB	Swedish equities	SBX	3 117	3 616		
Öhman	Swedish equities -equally-weighted, terminated	OSX	455	0		
Carnegie	Global equities	MSCI World	678	1 260		
Franklin Templeton	Global equities	MSCI World	1 754	3 199		
MFS	Global equities	MSCI World	4 694	5 279		
Merrill Lynch	Global equities	MSCI World	2 855	3 237		
Bankinvest	European equities -sector mandate, terminated	MSCI Europe – sector index	8	0		
Deutsche Asset Management	European equities -sector mandate, terminated	MSCI Europe – sector index	94	0		
Barclays Global Investors Ltd	European equities, terminated	MSCI Europe	4 118	0		
Barclays Global Investors Ltd	North America -Equities, terminated	MSCI North America	6 199	0		
Bankinvest	Asia excl. Japan -Equities, terminated	MSCI Pacific ex Japan	535	0		
Bankinvest	Japan - Equities, terminated	MSCI Japan	1 711	0		
Martin Currie	Japan - Equities	MSCI Japan	3 287	4 267		
Total			30 160	20 858	11	70
Passive management						
State Street Global Advisor UK Ltd	Global equities	MSCI World	3 106	3 521		
Barclays Global Investors Ltd	North America - Equities	MSCI North America	8 583	9 550		
Total			11 689	13 071	7	1
Fixed-income mandates						
Active management						
Franklin Templeton	Global credit mandate	Lehman Credit, ex Asia	265	1 587		
Rogge	Global aggregated fixed-income mandate	Lehman Global, ex Asia	662	3 959		
Total			927	5 546	3	2
GTAA mandates						
Active management						
IPM/First Quadrant and Goldman Sachs						7
Total external discretionary management mandates			42 776	39 475	21	80
Investments in listed external funds						
Unit trusts		as per respective fund	11 553	12 604		
Fixed-income funds		as per respective fund	2 678	158		
Total investments in listed external funds			14 231	12 762	6	58
Investments in private-equity funds						
Unlisted equities and participations in private-equity funds	Private Equity		1 062	1 370		
Total investments in private-equity funds			1 062	1 370	1	7
TOTAL EXTERNAL CAPITAL ASSETS UNDER MANAGEMENT, AND MANAGEMENT EXPENSES			58 069	53 607	28	145
In-house management mandates						
Listed equities and participations	Equity	SBX, OSX, CSX, MSCI World		68 220		
Fixed-income mandates, Swedish	Fixed Income	SHB		32 101		
Fixed-income mandates, foreign		Lehman		30 843		
Cash and bank balances, incl. deposits and accrued interest				104		
Unlisted equities in associated companies, incl. subordinated debentures				5 829		
Total capital assets managed in-house				137 097	72	
Other assets and liabilities				-111		
TOTAL FUND CAPITAL				190 593	100	

* Market value including allocated liquidity, derivative instruments and accrued interest.

NOTE 4 Personnel costs

Amounts in SEK k	January-December 2005		January-December 2004	
	Men	Women	Men	Women
Average no. of employees	33	18	33	17
No. of employees, Dec. 31*	29	17	28	16
No. of persons in Executive Management Group, Dec. 31	3	2	4	2
Salaries and remuneration				
Chairman of the Board		100		100
CEO		2 342		2 657
Board of Directors, excl. Chairman		425		415
Executive Management Group, excl. CEO		8 005		6 948
Other employees		30 678		29 054
Salaries and remuneration, total		41 550		39 174
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		624		-430**
Executive Management Group, excl. CEO		2 065		1 799
Other employees		8 748		7 483
Pension costs, total		11 437		8 852
Payroll overhead				
Chairman		32		33
CEO		779		895
Board of Directors, excl. Chairman		138		145
Executive Management Group, excl. CEO		2 673		2 351
Other employees		10 087		9 657
Total payroll overhead		13 709		13 081
Other personnel costs		3 576		2 962
Total personnel costs		70 272		64 069

* At the close of 2005, the Fund had a staff of 49, of whom 46 were full-time employees.

** With respect to 2004, the conversion from a benefit-based to premium-based pension policy has resulted in a liquidation of the provisions made in previous years. Consequently, the pension cost for 2004 appears as income.

In the above table, salary and remuneration to the CEO consists of salary paid to the previous CEO, Lars Idermark, up to and including October 2005. Pension costs and payroll overhead for Lars Idermark refer to the same period.

Pensions

An individual retirement pension insurance policy was taken out for Lars Idermark, starting January 2004, 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 was terminated as a result of dismissal by the Fund, the CEO was entitled to receive pension benefits from the Fund from age 60 until he reached 65. In accordance with the agreement, the size of this pension corresponded 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.

Severance-pay agreement

Lars Idermark withdrew from the post of CEO at his own request during the year. If the contract of employment had been terminated by the Fund, CEO Lars Idermark would have been 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. The Presiding Committee, which serves as the Fund's remuneration committee, determines the CEO's salary and discusses remuneration for the Fund's executive management.

Other directorships held by Members of the Board

See page 72.

Absence due to illness

In 2005, absence attributable to illness at the Second AP Fund was 0.77 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 was 0.74 percent for male employees and 0.82 percent for female employees.

NOTE 5 Other administrative expenses

Amounts in SEK million	January-December 2005	January-December 2004
Rental expenses	4	6
IT and computer expenses	26	26
Purchased services	7	10
Other expenses	16	13
Total other administrative expenses	53	55

"Purchased services" includes fees to auditors amounting to SEK 2 million (SEK 1 million)

Audit assignments

KPMG	1.48	0.93
PricewaterhouseCoopers	0.32	0.24
Other assignments		
KPMG	0.32	0.19
PricewaterhouseCoopers	0.02	0.07
Total	2.14	1.43

NOTE 6 Listed equities and participations ¹⁾

Amounts in SEK million	Dec. 31st 2005		Dec. 31st 2004	
	Fair value	Acquisition value	Fair value	Acquisition value
Swedish equities	40 150	29 696	31 273	29 471
Foreign equities	67 837	61 228	48 527	53 398
Participations in Swedish funds	4 165	1 943	3 728	2 527
Participations in foreign funds	8 439	4 976	5 316	4 492
Total listed equities and participations	120 591	97 843	88 844	89 888

¹⁾ The 20 largest Swedish and foreign shareholdings, by value, are listed on page 70.

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

NOTE 7 Unlisted equities and participations

Amounts in SEK million	Corp. reg.	Dec. 31st 2005		Acquisition value
		No. of equities	Participation right, capital Participation right, votes	
Swedish equities and participations			% %	
AP Fastigheter Holding AB	556650-4196	1 000 000	25	721
NS Holding AB	556594-3999	1 213 256	33	372
EQT Northern Europe KB	969670-3405		1	41
Swedestart Life Science KB	969675-2337		5	12
Swedestart Tech KB	969674-7725		3	7
Foreign equities and participations				
Carnegie Fund II BiotechBridge			29	46
Cevian Capital L.P.			22	275
CVC European Equity IV © LP			1	32
EQT Mezzanine L.P.			16	127
Nordic Capital V, L.P.			3	317
Pathway Private Equity Fund IX, LLC			99	174
Total unlisted equities and participations				2 124
Total fair value				4 012

Fees paid for the external management of unlisted assets, where reimbursement is permitted prior to profit sharing and is deemed likely amounted to SEK 18 million and are reported below "Other assets".

NOTE 8 Bonds and other fixed income assets

Amounts in SEK million	Dec. 31st 2005		Dec. 31st 2004	
	Fair value	Acquisition value	Fair value	Acquisition value
Swedish state	20 951	19 346	19 773	18 309
Swedish housing finance institutes	12 632	12 535	9 857	9 617
Other Swedish issuers				
Finance companies	156	147	82	78
Non-finance companies	3 606	3 309	4 170	3 934
Foreign states	14 172	13 662	12 801	13 350
Other foreign issuers	10 713	10 448	10 241	10 991
Demand loans	-	-	6 299	6 290
Total	62 230	59 447	63 223	62 569
Inflation-linked bonds	6 634	5 587	8 111	7 104
Other bonds	52 314	50 894	40 904	41 051
Treasury bills	130	129	-	-
Unlisted promissory notes	2 000	2 000	2 000	2 000
Unlisted convertible subordinated debentures	994	711	914	711
Participations in Swedish index-linked funds	33	25	530	520
Participations in foreign index-linked funds	125	101	4 465	4 893
Demand loans	-	-	6 299	6 290
Total	62 230	59 447	63 223	62 569

NOTE 9 Derivative instruments

Amounts in SEK million	Face value*	Dec. 31st 2005 Derivative instruments with positive fair value	Derivative instruments with negative fair value
Currency-related instruments			
Forward contracts	136 542	1 100	565
Total	136 542	1 100	565
of which cleared	-		
Equities-related instruments			
Forward contracts	10	82	142
Total	10	82	142
of which cleared	10		
Fixed-income instruments			
Forward contracts	11 760	58	107
Total	11 760	58	107
of which cleared	11 760		

* 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 45 for a description of the types of derivative instrument employed and the risks that can be managed with derivatives.

NOTE 10 Other assets

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Incoming payments, unsettled transactions	168	99
Receivables, repayment of management fees	18	-
Other receivables	2	4
Total	188	103

NOTE 11 Prepaid expenses and accrued income

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Interest income accrued	1 353	1 159
Receivables from foreign tax authorities	11	40
Dividends accrued	81	66
Other prepaid expenses and accrued income	25	24
Total	1 470	1 289

NOTE 12 Other liabilities

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Outgoing payments, unsettled transactions	78	201
Accounts payable	4	11
Other liabilities	2	2
Total	84	214

NOTE 13 Accrued expenses and deferred income

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Accrued management fees	130	68
Accrued interest expenses on currency forwards	231	34
Other accrued expenses	20	20
Total	381	122

NOTE 14 Fund capital

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Opening fund capital	158 120	140 350
Net inflow to the national pension system		
Incoming pension contributions	44 883	42 904
Transfer of pension entitlements from EU	-	-
Outgoing pension disbursements	-42 268	-40 696
Transfer of pension entitlements to EU	-14	-95
Adjustment of pension entitlements	5	-4
Non-recurring adjustment for period 1999-2002	-	-400
Outgoing administrative contribution to the Social Insurance Administration	-294	-312
Total net inflow to the national pension system	2 312	1 397
Transferred from First AP Fund's liquidation fund	363	129
Transferred from Fourth AP Fund's special fund	230	125
Total transferred from liquidation fund/special fund	593	254
Net result for the year	29 568	16 119
Closing fund capital	190 593	158 120
Capital assets under management of First AP Fund's liquidation fund	3 688	4 924
Capital assets under management of Fourth AP Fund's special fund	472	806

Copies of the annual reports of the Liquidation Fund and Special Fund are available on request from the First and Fourth AP Funds respectively.

NOTE 15 Other pledged assets

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Collateral for futures	601	507
Securities on loan for which guarantees have been secured*		
Securities on loan	1 341	311
Total	1 942	818

* Guarantees secured for securities on loan 1 404 (327).

NOTE 16 Commitments

Amounts in SEK million	Dec. 31st 2005	Dec. 31st 2004
Commitments regarding future payments		
Investment commitments, unlisted holdings	4 669	2 157
Total	4 669	2 157

The administration report, income statement, balance sheet and notes for 2005 have been approved
by the Board of Directors.

Gothenburg, February 9th 2006

Anders Jansson

Gunnar Larsson
Chairman

Bo Dockered

Märtha Josefsson

Clas Nykvist

Roland Svensson

Eva Persson

Eva Fernvall-Markstedt

Ylva Thörn

Auditors' report

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

We have audited the annual accounts, the accounting records and the administration of the board of directors of the Second AP Fund for the financial year 2005. These accounts and the administration of the Fund and the application of the Swedish National Pensions Act are the responsibility of the board of directors. Our responsibility is to express an opinion on the annual accounts and the administration based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Sweden. Those standards require that we plan and perform the audit to obtain reasonable assurance that the annual accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and their application by the board of directors, as well as evaluating the overall presentation of information in the annual accounts. We believe that our audit provides a reasonable basis for our opinion set out below.

The annual accounts have been prepared in accordance with the Swedish National Pensions Act and, thereby, give a true and fair view of the company's financial position and results of operations in accordance with generally accepted accounting principles in Sweden. The statutory administration report is consistent with the other parts of the annual accounts.

In performing this audit, we have found no reason for qualifications regarding the annual accounts, the income statements and balance sheets included therein, the accounting records or the inventory of assets, or otherwise regarding the Fund's management by the board of directors.

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

Gothenburg, February 9th 2006.

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

The Second AP Fund's 20 largest Swedish shareholdings¹⁾

Name of company	Share of equity, %	No. of equities	Fair value, SEK m	Share of voting rights, %	Sector
Ericsson B	1.06	170 646 901	4 659	0.61	Information Technology
Ericsson A	0.01	1 367 271	38	0.05	Information Technology
Svenska Handelsbanken A	2.33	15 626 335	3 078	2.40	Financials
Volvo A	1.74	7 407 034	2 700	4.50	Industrials
Volvo B	0.22	944 801	354	0.06	Industrials
Nordea	1.08	29 216 457	2 410	1.08	Financials
Electrolux B	3.58	11 062 212	2 284	2.80	Consumer Discretionary
Astra Zeneca Plc	0.23	4 474 219	1 738	0.23	Healthcare
Skandia	3.53	36 142 971	1 720	3.53	Financials
Hennes & Mauritz B	0.76	6 305 215	1 702	0.37	Consumer Discretionary
SCA B	1.75	4 112 113	1 221	0.71	Raw Materials
SCA A	0.24	564 237	168	0.97	Raw Materials
TeliaSonera	0.60	28 106 264	1 200	0.60	Telecommunication Services
Föreningssparbanken	0.91	4 832 343	1 046	0.91	Financials
Atlas Copco B	0.68	4 270 793	677	0.10	Industrials
Atlas Copco A	0.33	2 049 249	363	0.47	Industrials
Meda AB	8.30	9 497 567	1 026	8.30	Healthcare
Sandvik	1.17	2 769 246	1 025	1.17	Industrials
Skandinaviska Enskilda Banken A	0.90	6 166 530	1 008	0.93	Financials
Investor B	0.73	5 578 848	775	0.16	Financials
Investor A	0.16	1 227 058	170	0.34	Financials
Assa Abloy B	1.75	6 418 026	802	1.19	Industrials
Skanska B	1.33	5 721 265	692	0.76	Industrials
Securitas B	1.36	4 969 143	656	0.96	Industrials
Capio	4.98	4 206 465	595	4.98	Healthcare

The Second AP Fund's 20 largest foreign shareholdings¹⁾

Name of company	No. of equities	Fair value, SEK m	Sector
BP Amoco Plc	10 599 883	896	Energy
General Electric Co	2 739 794	764	Industrials
Exxon Mobil Corp	1 644 752	735	Energy
Nestle	296 191	703	Consumer Staples
HSBC Holdings	5 076 746	647	Financials
Total SA	319 648	637	Energy
GlaxoSmithKline Plc	2 982 412	599	Healthcare
Citigroup Inc	1 412 541	546	Financials
Roche	451 882	538	Healthcare
UBS AG	703 268	531	Financials
Microsoft Corp	2 541 718	529	Information Technology
Vodafone Group	30 253 053	519	Telecommunication Services
Johnson & Johnson	1 009 069	483	Healthcare
Procter & Gamble co	1 037 727	478	Consumer Staples
Novartis	1 124 548	469	Healthcare
Sanofi-Aventis	663 404	461	Healthcare
Royal Dutch Shell	1 866 869	452	Energy
E. ON	518 375	425	Utilities
Bank of America Corp	1 108 516	407	Financials
Intel Corp	1 937 392	385	Information Technology

1) The above table of Second AP Fund shareholdings lists the 20 largest Swedish holdings and 20 largest foreign holdings, by worth. "Swedish shareholdings" also includes companies that have changed their legal domicile after merging with a foreign company, as with AstraZeneca. 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 hedge funds

Unit trusts, foreign	No. of equities, participations	Fair value, SEK m
Genesis Emerging Markets	7 725 431	1 605
Pictet Emerging Markets	437 063	1 514
StateStreet Emerging Markets	237 687	1 249
Merrill Lynch Emerging Markets	12 493 781	1 153
Citigroup Emerging Markets	511 879	1 089
Sustainable Asset Management Fund	764 858	928
AIG Global Emerging Markets	369 354	839

Unit trusts, Swedish	No. of equities, participations	Fair value, SEK m
Carlson Sverige Småbolagsfond	889 397	982
SHB Småbolagsfond	1 445 992	600
SEB Sverige Småbolag	32 617 752	590
Robur Småbolagsfond	15 262 705	557
Lannebo Småbolagsfond	22 682 764	527
Enter Select Fokus	297 179	451
SEB Sverige Småbolag Chans/Risk	3 406 328	265

Hedge funds	No. of equities, participations	Fair value, SEK m
Eikos	1 031	196
Amplus	250 000	33

The Second AP Fund's holdings in bonds and other fixed-income securities

Global credit portfolio, five largest holdings

Bond	Fair value, SEK m
DB Iboxx Linked Note	580
IBRD 7 2023-01-19	200
Federal Republic of Germany 3.875 2010-06-01	182
EIB 5.375 2021-06-07	172
EIB 4.625 2015-10-20	159

Global government bond portfolio, five largest holdings

Bond	Fair value, SEK m
Germany 4.75 2008-07-04	702
US Treasury 3.75 2007-03-31	494
France 4 2014-10-25	489
US Treasury 6.25 2006-11-15	440
France 4.25 2019-04-25	399

Swedish nominal bond portfolio, five largest holdings

Bond	Fair value, SEK m
Swedish Government 1041	2 209
Swedish Government 1043	1 762
Swedish Government 1045	1 724
Swedish Government 1037	1 638
Spintab 172 5% 2007-06-20	1 495

Swedish inflation-linked bond portfolio, five largest holdings

Bond	Fair value, SEK m
Swedish Government 3105	1 839
Swedish Government 3104	1 633
Swedish Government 3102	1 344
Swedish Government 3101	1 146
Swedish Government 3001	431

Detailed information about the Second AP Fund's fixed-income securities may be ordered from the Fund.

Board of Directors



The Board of Directors of the Second AP Fund, December 31st 2005. Members of the Board are appointed by the Swedish Government. They are appointed on the basis of their competence to promote the Fund's management of its portfolio.

Upper row, from left:

Gunnar Larsson

Chairman since 2000 and acting CEO from November 2005. Chairman of the boards of GöteborgsOperan and Tholin & Larsson-Gruppen AB. Directorship on the board of Norrporten AB. Former authorised public accountant and Municipal Commissioner for Gothenburg. Born 1940.

Bo Dockered

Vice Chairman since 2000. Chairman of the boards of AB Trav and Galopp and Sveaskog AB. Honorary Doctor of Agronomy (Dr.h.c. Agronomy) and farmer. Born 1941.

Ylva Thörn

Member of the Board since 2000. President, Swedish Municipal Workers' Union. Chairman of The Public Services International. Directorships on several boards, including LO (The Swedish Trade Union Confederation) and Riksborgen. Assistant nurse. Born 1954.

Clas Nykvist

Member of the Board since 2000. Controller, Swedish Building Workers' Union. Directorships on several boards, including Folksam Spar AB. Born 1948.

Märtha Josefsson

Member of the Board since 2003. Independent investment consultant. Former Investment Director at DnB Asset Management and Carlson Investment Management AB. Directorships on several boards, including Anoto, Faberge, Ledstjärnan, Luxonen, Skandia Funds and Uppsala Nya Tidning. B.A. Born 1947.

Lower row, from left:

Eva Persson

Member of the Volvo Group executive committee, with responsibility for legal, tax and security matters, and Secretary to the board of AB Volvo. Directorship on the board of Handelsbanken Region Väst. Member of the Swedish Industry and Commerce Stock Exchange Committee. LL.M. Born 1953.

Roland Svensson

Member of the Board since 2000. Former President and CEO of Coop Norden AB and KF Ekonomisk förening. Chairman of the Swedish National Museum of Art. LL.B. Born 1941.

Anders Jansson

Member of the Board since 2005. President and CEO of Stena Metall AB. Formerly president of Volvo Car Finance, head of Global Trading at Handelsbanken Markets, and president of Volvo Group Finance. Born 1957.

Eva Fernvall-Markstedt

Member of the Board since 2004. Marketing Director of Apoteket AB. Chairman of the Donation Council and the Institute for Health and Medical Economy. Former Chairman of the Swedish Federation of Salaried Employees in the Hospital and Public Health Services, and chairman of the 24/7 Agency Delegation. Born 1953.

Executive management and auditors



Management

Fund management, Second AP Fund

Back row, from left:

Martin Jonasson, General Counsel, born 1964

Margaretha Veres, Personal Assistant to the CEO, born 1945

Front row, from left:

Carl Rosén, Head of Corporate Governance and Communications, born 1959

Lena Smeby-Udesen, CFO, born 1961

Petter Odhnoff, CIO, born 1956

Lars Idermark (not in picture)

was CEO until the end of October 2005



Eva Halvarsson

New CEO, effective February 14th 2006.

Eva Halvarsson joins the Fund from a position as Head of the Unit for State-Owned Companies at the Swedish Ministry for Industry, Employment and Communications. Member of the board of AB Swedcarrier. M.Sc (Econ). Born 1962.

Auditors

Anders Bäckström,
Authorised Public Accountant,
KPMG

Göran Jacobsson,
Authorised Public Accountant,
PricewaterhouseCoopers

Definitions

Absolute return on investment

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

Absolute risk

Variation in absolute return. Measured as a standard deviation on absolute return. Also known as “volatility”.

Active/passive management

Active: Where portfolio management may deviate from the benchmark portfolio, to generate an active return.

Passive: Where portfolio management exactly matches 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 requirements of the Swedish national pension system. The judgements based on this analysis shall take into account demographic change as well general economic trends.

Benchmark index

Index based on the Second AP Fund's strategic portfolio, against which the Fund's management performance is measured.

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.

Discretionary mandate

A mandate that is limited and specific to a single portfolio manager. The alternative to discretionary management is management in a fund, where several managers invest jointly in the same mandate.

Enhanced index mandate

Management of assets at low risk, with the support of quantitative analysis.

Fair value

Fair value is defined as the amount for which an asset may be transferred or a debt settled, between parties who are mutually independent and who have a vested interest in completing the transaction. Normally speaking, this means that listed assets are valued at the buying-rate (market value) and that the fair value of unlisted assets is estimated with the help of generally accepted valuation models.

Information ratio

A gauge of risk-adjusted relative return. Measured as relative return, divided by tracking error/active risk.

Interaction

Interaction is a consequence of the interplay between a strict allocation of assets and a strict choice of securities.

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.

Market risk

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

Operational risk

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

Overlay mandate

An active asset management mandate that is separated from the underlying portfolios. In an overlay mandate, forward contracts or other derivative instruments are used instead of underlying equities and bonds. Overlay mandates are normally “long-short” mandates, which do not affect the size of the total portfolio of investments under management. The Fund's GTAA mandates are typical examples of an overlay mandate.

Quantitative management

Portfolio management that focuses on exposing incorrect market pricing with the help of a mathematical model.

Relative return

The difference in return generated by a portfolio and its benchmark index.

Sharpe ratio

A gauge of risk-adjusted return. Measured as the portfolio's absolute return less risk-free interest, divided by the standard deviation on absolute return.

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.

Tracking error/Active risk

The variation in relative return. Often measured as standard deviation on the relative return.



Andra AP-fonden
Second Swedish National Pension Fund - AP2

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