

Corporate

GOVERNANCE REPORT

1 JULY 2006 – 30 JUNE 2007



Andra AP-fonden
Second Swedish National Pension Fund – AP2

Weak shareholders in US fuel Swedish CEOs' salary hikes

PAGE 10

Why women drop out on the way to the top

PAGE 15

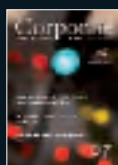
How the AP Fund's Joint Ethical Council functions

PAGE 22

07

CONTENTS

THIS IS THE SECOND SWEDISH NATIONAL PENSION FUND/AP2	2
INTERVIEW, CEO AND HEAD OF CORPORATE GOVERNANCE	3
SECOND AP FUND'S ENVIRONMENTAL & ETHICAL ANALYSIS	5
ASSA ABLOY – ONE EXAMPLE	8
WEAK SHAREHOLDERS IN US FUEL EXCESSIVE SALARY HIKES	10
FEWER OPTION SCHEMES – MORE PERSONAL INVESTMENT	12
SECOND AP FUND'S Q-INDEX	13
WHY EQUALITY PAYS	14
WHY WOMEN DROP OUT ON THE WAY TO THE TOP	15
RONALD FAGERFJÄLL ON WOMEN IN BUSINESS	17
FOUR SUCCESSFUL WOMEN ON EQUALITY IN BUSINESS	19
THE JOINT ETHICAL COUNCIL OF THE AP FUNDS	20
HOW MARRIOTT CLEANED UP ITS ACT	22
NEWS & VIEWS	23
ACTIVITIES IN 2006/2007	25
THE FUND'S CORPORATE GOVERNANCE ACTIVITIES IN BRIEF	27



COVER ILLUSTRATION:
The Second AP Fund
uses a simple traffic-light
system for its corporate
governance activities.

This is the Second Swedish National Pension Fund/AP2

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 (hereafter named as "the Second AP Fund"), located in Gothenburg, started operations on January 1st, 2001. Since then, it has progressively developed and implemented its objectives, strategies and infrastructure, and is today a globally oriented portfolio management organisation.

The Board of the Second AP Fund is appointed by the Swedish Government. Each director is appointed to further the Fund's management goals, according to his/her individual competence.

The Second AP Fund is determined to be a leading pension manager with regard to return on investment, staff, inventiveness, efficiency and the respect of its peers.

It will achieve this by means of efficient, professional and long-term portfolio management, featuring an effective utilisation of financial risk.

STRONG PERFORMANCE IN FIRST HALF 2007

The Second AP Fund's selection of strategic portfolio and its portfolio of Swedish equities, which outperformed index, have

been the key factors in its strong performance during the first half of 2007.

Additional measures have been taken to develop and further enhance the efficient management of assets.

The Fund's capital assets amounted to SEK 232.8 billion as per June 30th 2007, corresponding to an increase since January 1st of SEK 16 billion, including inflows. The result for the report period was SEK 15.1 billion.

The Fund's total portfolio, excluding expenses, showed a return of 7.0 percent for the six months ending June 30th 2007. The benchmark portfolio noted a corresponding return of 6.3 percent. Return on assets less commission costs and operating expenses amounted to 6.9 percent.

The level of currency exposure was 11 percent as per June 30th 2007.

The 0.5 percent relative return against index noted for the Fund's market-listed portfolio, excluding expenses, is mainly attributable to the performance of the Fund's Swedish OSX portfolio, the Volvo share performing especially well.

Three-year review

	June 30th 2007	2006	2005
Fund capital, SEK million	232 784	216 775	190 593
Inflows, SEK million	934	1 676	2 905
Share of asset management costs, excluding commission costs, over the year, %	0.06	0.06	0.07
Share of asset management costs, including commission costs, over the year, %	0.14	0.15	0.16
Net result for the period, SEK million	15 075	24 506	29 568
Return on total portfolio, excluding costs, %	7.0	13	18.7
Return on total portfolio, including costs, %	6.9	12.8	18.5
Relative return on listed assets, excluding costs, %	0.5	0.2	0.2
Currency exposure, %	11	12	11
Active risk, ex post, %	0.6	0.7	0.5
Share of active management (incl. enhanced), %	94	93	90
Share of external management (incl. investments in private equity funds), %	22	17	28

Active governance PAYS

Interview with Eva Halvarsson (EH), CEO of the Second AP Fund, and Carl Rosén (CR), head of Corporate Governance & Communications.

WHY SUCH AN AMBITIOUS CORPORATE GOVERNANCE REPORT?

CR: There is considerable interest in how a large public pension fund thinks and acts with respect to corporate governance issues. It is difficult to deal with complex arguments in the media – attention is often focused on disagreements and conflicts. In practice, many corporate decisions are made behind closed doors and, for commercial reasons, the full picture can never be revealed. For this reason, we wish to create a forum for broader discussion.

EH: I would say that interest in and pressure on us as investors is growing all the time. Our “customers” – Sweden’s future pensioners, our politicians, companies, the media, pressure groups and many others are extremely interested in what we do, and we have often been bad at explaining how our processes work and about our role as investors.

DOES CORPORATE GOVERNANCE PAY?

CR: It’s a difficult question. Academics would claim there’s no concrete evidence to support the claim. So far, however, we feel that it has proved profitable.

EH: In the past five years, our OSX portfolio, in which we take an active role with respect to corporate governance issues, has outperformed index by 18.7 percent, making a significant contribution to overall return on assets. We have gradually built up principles and working methods, and we feel we have now found an effective model that we can work with.

WHY NOT APPLY THIS METHOD TO MANAGEMENT OF THE ENTIRE PORTFOLIO?

CR: Not feasible, unfortunately. It would require too many resources. It would also involve adopting a higher risk profile.

However, applying it on this scale obviously works well.

YOUR APPROACH TO CORPORATE GOVERNANCE IS BASED ON TEN PRINCIPLES. CAN THEY BE RANKED BY IMPORTANCE?

CR: No – can’t be done. They differ in importance from one company to another. The list helps us pick up on certain issues at an early stage, such as the relative percentage of research and development invested in sustainable solutions, over the long term. In other words, the type of factors that have had a dramatic effect on long-term profitability and market worth. And these things vary, depending on the individual company.

EH: I agree. It’s certainly true that the capital structure and corporate structure can achieve rapid results, if that’s all you’re interested in. The problem with these types of changes is that they are often already added onto the share price. We are long-term investors by nature, and wish to assure ourselves that selected companies are going to continue to perform well for years ahead. This means we have to consider several variables.

HOW DIFFICULT IS IT TO INTRODUCE YOUR METHOD WITHIN A TRADITIONAL MANAGEMENT ORGANISATION?

CR: It’s really quite easy. Even so, I think many people are convinced that it’s going to be a problem, until they’ve tried it. It’s mainly about a change in

culture. The method involves asking companies a whole lot of questions, some of which are quite penetrating. Many are probably rather nervous about asking such searching questions, worried that it may spoil their relationship with the company’s management. Once they’ve seen what the method can achieve, however, earlier reservations tend to evaporate.

EH: The tendency of analysts and portfolio managers to be over-cautious in their relationships with company managements, from fear of being cold shouldered, is something >>

we are working hard to eradicate. We are shareholders. And – as shareholders – we have every right to question how the company is being run and to initiate a dialogue when things don't work as we think they should.

WHAT IS YOUR RESPONSE TO THOSE WHO SAY THAT CORPORATE GOVERNANCE STEALS TOO MUCH ENERGY AND RESOURCES FROM TRADITIONAL PORTFOLIO MANAGEMENT?

EH: That we make more money than they do.

WHAT IS THE MOST IMPORTANT THING THAT HAS HAPPENED IN THE CORPORATE GOVERNANCE SECTOR IN THE PAST FEW YEARS?

EH: The demands made on us as institutional shareholders have increased. It's no longer enough to vote with your feet. Especially since the introduction of the

new regulations and codes of conduct, which have made it easier for us to do our job. There has also been major stride forward on the gender issue. A process has now been put in place to promote women candidates to leading positions on nominating committees. The situation was quite different a few years ago.

CR: The work of these nominating committees has become far more professional. Those who fail to perform are voted off the board. It is precisely this explicit exercise of shareholder governance that is unique for Sweden. In global terms, we are something of a hothouse in the corporate governance sphere. In this respect, we are way ahead of the USA, where shareholders have considerably less power.

MANY ARE CRITICAL OF ADDITIONAL CODES OF CONDUCT AND REGULATIONS, CLAIMING THAT THEY ABSORB TOO MANY RESOURCES. DO YOU AGREE?

EH: I fail to understand such an attitude. If I come into contact with a company that has problems living up to the Swedish code of corporate conduct, I become suspicious. It can be symptomatic of another problem, which makes me wary of investing. When I read a company report, I want to see that they've been thinking about these issues.

WHAT ASPECT OF YOUR CORPORATE GOVERNANCE ACTIVITIES ARE YOU MOST PROUD OF?

EH: The fact that a UN report published earlier this year (see page 23) cited the Second AP Fund as one of the top fifteen funds in the world, in the corporate governance sphere, is a clear indication that we've done well.

CR: Another factor is the success of our investment strategy – the fact that so far we have outperformed index.

IS THERE ANY AREA WHERE YOU FEEL YOU COULD HAVE PROGRESSED FURTHER?

CR: We could have progressed further in every area. We still have a long way to go before we can feel entirely satisfied with our corporate governance process. Even so, we can be proud of what we have achieved so far. Such as the fact that we have been praised in a UN report, that we have established an Ethical Council, and our portfolio's solid performance.

EH: Private Equity is one of the areas we can develop in future. We are already pursuing a number of important issues, such as the idea that investment in Private Equity should be based on the UN's Global Compact initiative on sustainable investment. But we want to do much more, to be better at making our demands in this area really count as investors.

ENVIRONMENTAL ISSUES HEAD MANY AGENDAS RIGHT NOW. WHAT WILL EVERYONE BE TALKING ABOUT TEN YEARS FROM NOW?

CR: Sustainability issues will have developed and acquired still greater importance. Rather like all the hype over the Internet ten years ago. The past decade has seen the Internet become integral to every aspect of corporate activity: it will be the same with sustainability.

EH: One issue that I believe will gain increasing urgency is the need to get the economies of the poorest countries up and running. There are already signs that some big companies are introducing specially developed products for the poorest markets – useful products that have been adapted both in terms of functionality and cost. This encourages fair trade, instead of exploitation. Everyone gains in the long term.

WHAT IS THE GREATEST CHALLENGE FACING CORPORATE GOVERNANCE IN THE YEARS AHEAD?

CR: To ensure that shareholders' views are taken even more seriously. The extreme pay packages enjoyed by corporate managements, which have grown exponentially, clearly show that this is something that is really needed. Exaggerated differences in income, especially when apparently unjustified, can often lead to problems, as demonstrated by historical fact.

EH: Neither we nor our fellow fund managers can just bury our heads in the sand and hope the problems will go away. It's time to make a stand and propose ways to improve the situation. It enhances our credibility while offering a better long-term return on investment.

AP2's ten waypoints on the road to effective corporate governance

The way in which the Second AP Fund tackles governance issues has been modified in line with the Fund's new Corporate Governance Code, introduced on July 1st 2005. The Fund's Corporate Governance Policy forms the starting point for this task, based on ten principles of governance. These are listed below. By observing these principles, the Fund intends to contribute added value by exerting effective governance.

The ten principles of corporate governance:

1. Capital structure
2. Corporate structure
3. Shareholder structure
4. Board of directors and nomination process
5. Executive management and executive remuneration
6. Auditors' role and audit
7. Information and its distribution
8. Investments, corporate acquisitions and divestments
9. Corporate culture
10. Ethics, environment and equality

More information about these ten principles can be found in the Second AP Fund's Corporate Governance Policy, which can be downloaded from our website at www.ap2.se, or which can be ordered direct from the Fund. Contact details are printed on the back cover of this Report.

A brief general description of how the Second AP Fund approaches its corporate governance responsibilities is given on page 27. Key documents with additional information are listed on the back cover.

THE METHOD IS ESTABLISHED

– the task of creating value by integrating ethics and environmental issues with corporate governance has already started.

The result of the Second AP Fund's management of its portfolio over the past three years demonstrates that active corporate governance has added true value. This success is largely attributable to the method applied by the Fund.

One challenge was how ethical and environmental issues could best be integrated into the corporate governance process. One of the thinkers behind the development of this approach is Christina Olivecrona – researcher and engineer, who claims that everything derives from four value-creation strategies and thorough field research.

Questions relating to ethics, the environment and sustainable development are all the rage right now – much more so than a mere ten years ago. But you don't have to go that far back to see the difference. "In just the two years since we started visiting companies, we have noted the growing strategic significance of these issues", says Christina Olivecrona, who is engaged in charting, analysing and conducting discussions with representatives from companies in which the Second AP Fund has holdings, and in which it practises active governance.

In practice, she and Carl Rosén, head of Corporate Governance at the Second AP Fund, form the nucleus of the team that conducts the Fund's corporate governance activities. They are backed up by all the analysts and portfolio managers, who also contribute indirectly through their analyses of (and contact with) the companies.

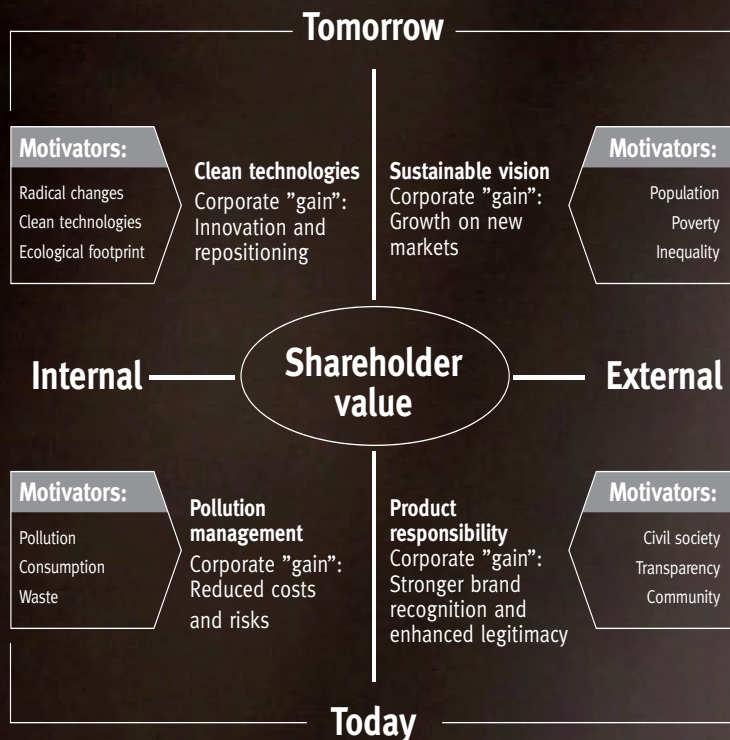
CORPORATE GOVERNANCE POLICY IS THE BASE

The corporate governance process is firmly grounded in the Corporate Governance Policy's ten key principles

(see preceding page). The Second AP Fund charts and analyses the extent to which Swedish companies observe the policy's principles and compiles the results in a so-called Corporate Governance Log, which is regularly updated.

Initially, considerable effort was invested in promoting in-house commitment to the Log process. "The first nine points cited in the Log involved factors with which analysts were already familiar. The final point, however – concerning the need to consider ethics, the environment and equality issues – was something new. »

How the Log and the four fields work



The Corporate Governance Log and the four-field chart are two of the instruments employed by the Second AP Fund in its governance of the approximately twenty Swedish companies in which it practises active governance.

Briefly, the Log is used to analyse corporate performance, based on the ten principles enshrined in the Corporate Governance Policy. Following such an analysis, the company is rated for its observance of each principle according to a three-colour "traffic light" system. The only exception is the tenth principle (ethics, environment and equality), where a coloured signal is given for each of the four fields.

- In principle, a red signal means the Fund should dispose of its holding.
- If it flashes yellow, it may be time for the Fund to act, with a view to changing the company's behaviour concerning a specific issue – and thereby create added value.
- A green signal means everything is as it should be.

This is why we were so particular about developing an instrument that was straightforward and robust, so as to be certain that everyone would quickly appreciate the value-creation benefits of sustainability", states Carl Rosén, head of Corporate Governance at the Second AP Fund.

THE PROJECT REALLY GOT UNDER WAY IN 2005

The job of incorporating ethics, the environment and equality issues into the Corporate Governance Log really started in earnest in 2005. At the same time, a dialogue was initiated with companies representing the Fund's largest holdings, including Volvo, TeliaSonera and AssaAbloy. "The dialogue with all these companies has proved highly positive and rewarding. When an investor like the Second AP Fund comes calling and wants to talk about ethics and the environment, it encourages these companies to continue

to address these types of issue", notes Christina Olivecrona.

Many companies have come a long way with their efforts. This is often attributable to an appreciation that improvements in these areas create value. Electrolux is one such example.

"It was clear that they recouped the cost of the investment in an environmental management system very rapidly, thanks to enhanced efficiency", says Carl Rosén.

FOUR-FIELD CLASSIFICATION OF COMPANIES

"Since value creation forms the commercial basis for corporate governance, we wanted an analytical model that addressed the business potential that is intrinsic to sustainability", says Christina Olivecrona.

This is why the Second AP Fund has adopted a four-field model. Briefly, this classifies the companies and their value-creation strategies in terms of sustainability.

And this is a four-dimensional model – today and tomorrow, internal and external – which results in an assessment that is then entered in the Log.

"Historically, most companies have found themselves at the bottom of the lower left frame, among those that have implemented internal measures. This is where environmental management systems belong, for example, which are limited to 'here and now'. This is fine, but it is not where the major results are achieved", says Christina Olivecrona.

More and more companies are taking the next step, however, though few may get all the way to the upper right field. One such company is Ericsson, which has developed a completely new model for base stations, powered by renewable energy. They are marketed in emerging nations, and contribute to these nations' overall development. They also generate a healthy return, which ensures long-term

The four-field model for value creation strategies is a complement to the Corporate Governance Log. It helps to classify the strategies adopted by different companies, seen in terms of sustainability and commercial viability.

Field 1 (lower left):

Here are companies that invest in systems that help reduce pollution, such as environmental management systems. Companies make money by using resources more efficiently, through reduced costs.

Field 2 (lower right):

This is where companies that put great emphasis on monitoring the supply chain, from raw material to end user, are placed. H&M, which has started using ecological cotton and which employs some 50 in-company auditors to monitor suppliers, is a typical example.

Field 3 (upper left):

This field features companies that are innovation intensive. Nibe, by virtue of its energy-saving innovations, is one. Volvo is another, thanks to the advances it has made in the past year.

“When we conducted the 2005 analysis, we were concerned about the unilateral focus on diesel technology. We felt that the company might face difficulties over the coming years if it failed to invest in hybrid technology and alternative fuels. Now, returning to evaluate the company in the spring of 2007, we discover that an enormous amount has happened in this field”, says Carl Rosén, head of Corporate Governance & Communications at the Second AP Fund.

SKE, a company that produces specially manufactured roller bearings for wind-power plants, a business unit currently enjoying dramatic growth, provides yet another example.

Field 4 (upper right):

This is where the companies that have developed radical business models for new markets are placed. These are business models that help reduce poverty, alienation and environmental problems – while also creating shareholder value. Ericsson is an example of one of the Second AP Fund’s major holdings that, thanks to its base stations, has gained a place in this field. Powered by renewable energy, these base stations have been developed specially for emerging nations. AstraZeneca is another example of a company that, in the past two years, has developed an interest in launching products specially manufactured for emerging nations.

sustainability”, says Christina Olivecrona.

MUCH STILL TO DO

Despite the fact that the Fund’s corporate governance process has progressed a long way in just a few years, there is still much to do.

“Yes. Although we now have a process that has started to acquire its own form, it will change. Rules and company attitudes both change fast. This means that we shall also change and refine our instruments”, says Christina Olivecrona.

TOO MUCH INFORMATION A PROBLEM

One of the problems is the sheer quantity of information that needs to be processed. There is so much that it is difficult to analyse it in depth. When they visit portfolio companies, the Fund’s representatives must be sure to do their homework. Prior to a company visit, preparations should include a thorough review of the annual report,

press clippings, and reports from various interest groups, to ensure that the questions asked are pertinent. This type of preparatory work takes time.

“For this reason, we must define certain limits. We monitor our 20 largest Swedish holdings very closely. This is a lot, but it works”, says Christina Olivecrona.

The Fund gets external support, too. This includes a battery of questions prepared by external consultants Sustainability Asset Management, SAM. This is a battery of more than 100 questions, which are used in regular surveys of large companies.

“We ask each company whether we may see its responses to the SAM questionnaire. In most cases, the company has no objection. This data is of tremendous value in our subsequent dialogue”, says Christina Olivecrona.

The men behind the four-field model

Researchers Stuart L Hart and Mark B Milstein from Cornell University are the men behind the four-field model used by the Second AP Fund. Both are considered to be at the forefront of research into sustainable development and, as well as the four-field model, have made a major contribution to developing ideas about “the base of the pyramid”, as a starting point for new business models that benefit the great number of poor in the world. This is one of the subjects addressed in Stuart L Hart’s notable book “Capitalism at the Crossroads”.



Stuart L Hart



Mark B Milstein

Assa Abloy steers the right course

Assa Abloy has enjoyed explosive growth in the past ten years. Sales have grown by a multiple of six and the company has achieved a world leading position in the field of locks and secure doors. To maintain this trend in the long term, however, the company needs to continue to advance its position on sustainability issues.

The Second AP Fund and Assa Abloy are in full agreement on this point.



The Second AP Fund is actively engaged in the governance of some twenty Swedish quoted companies. One of these is Assa Abloy. Contact was first made with the company in the spring of 2006. The idea was to initiate a dialogue as to how the company might best address sustainability issues – an area that the Fund considered important when evaluating the company. Karin Ekberg, responsible for sustainability issues at Assa Abloy, remembers her first meeting with the Fund's representatives, Carl Rosén and Christina Olivecrona.

“They were highly professional. Their questions showed that they had really done their homework – a basic requirement if the discussions are to go any deeper, and address specific areas that are important to us in the long term.”

A GOOD SPARRING PARTNER IS VITAL
“Their efforts have contributed a great deal. AP2 is a good sparring partner, and is able to put its finger on many key issues where we must take a stand. These are often associated with risks, such as

"It's good that these issues are raised on the agenda, so that we and others can implement improvements. Everyone gains."

those related to the work environment. The better we are at systematically reducing these risks, the more time we create for studying the opportunities presented by our business operations. Which is why it's so important", says Karin Ekberg.

Assa Abloy also conducts roundtable discussions with shareholders. Most recently, in May 2007, the company invited six major institutional shareholders, including the Second AP Fund, to participate in a discussion on sustainability issues from an Assa Abloy perspective. The company's first sustainability audit was used as the starting point for the discussion. The company's CEO, Johan Molin, also attended the meeting.

A VISIT THAT REALLY PAID DIVIDENDS

That this type of issue has progressed up the corporate agenda and become established at executive management level is as yet by no means self-evident among quoted companies. But things are moving in the right direction. Karin Ekberg is convinced that several quoted companies could benefit from a visit from the Second AP Fund.

"Our experience is that it pays. In our dialogue with shareholders, critical issues are addressed and long-term solutions are analysed, in an informed manner."

Even so, there is still room for development regarding the Second AP Fund's approach.

"Yes, I'd like a training session in how the AP2 analytical model functions, to learn how the Fund actually carries out its analysis of us. It would make it easier for me to communicate these issues within the company, to executive management

and to the organisation as a whole, and enable me to provide a better answer as to why we are analysed in the way we are", says Karin Ekberg.

MORE STRINGENT DEMANDS ON SUPPLIERS

Assa Abloy, in common with many other companies with a large percentage of their production outside Sweden, has found itself under the microscope in recent years with respect to work environment issues. Organisations such as SwedWatch conduct regular surveys, which are often reported in the media. Companies and the organisations that monitor them do not always share the same view when it comes to the details.

"But it's good that these issues are raised on the agenda, so that we and others can implement improvements. Everyone gains", says Karin Ekberg.

Working for approved assurances that individual suppliers are actually observing the strictures placed upon them by the company, in areas such as the work environment, is one of the most important issues facing Assa Abloy. This is particularly the case where low-cost nations are involved.

"This is where the greatest risks lie. We must strive for consistent improvement, and monitor and refine procurement processes to ensure that they exceed the requirements contained in the code we have established for all our suppliers. This is crucially important to us", says Karin Ekberg.

ASSA ABLOY IN BRIEF

Assa Abloy is the world's leading manufacturer and supplier of locks and secure doors. The Group, with over 30,000 employees in 150 companies, established in more than 40 countries, has sales in excess of SEK 31 billion. In the rapidly growing electromechanical security sector, the Group has a leading position in fields such as access control, identification technology, automatic doors and hotel security.



ASSA ABLOYs
Sustainability Report 2005-2006

PAY SPIRAL – A COSTLY

US\$-IMPORT

The increased pay levels awarded to top Swedish management in recent years have ensured that the income gap between ordinary workers and top business executives has reached a record level. This worries many, especially institutional investors. Perhaps the most important factor fuelling this development is that shareholders lack enough power – in the USA. This is something several pension funds are trying to change.



Anne Simpson, President of ICGN, welcomes the Second AP Fund's efforts.

The pay spiral for top business management has acquired increasing momentum over the past 25 years. In 1980, the corresponding average salary for the heads of Sweden's 50 largest companies was only just ten times the average industrial wage. By 2005, this gap had increased to 40 times the average industrial wage, according to statistics released by the Swedish Trade Union Confederation.

This trend has its origins in the USA, where the difference is much greater. At the start of the new millennium, top executives in the largest US corporations – at a rough estimate – earned the equivalent of an industrial worker's annual income in a single day – largely thanks to the system's dependence on the "options programme hysteria" that ruled at the time. Since then, the gap has shrunk somewhat. The differences are still huge, however. In 2005, the average annu-

al remuneration paid to top executives was close to 180 times the annual income of a normal worker.

GAP THAT CAUSED A CREDIBILITY CRISIS

This leads to a crisis of credibility. A survey conducted on behalf of Bloomberg and the Los Angeles Times in 2006 revealed that four out of five Americans thought top managers were overpaid. Attitudes in Sweden are moving in the same direction. A survey of 1000 Swedes, conducted in 2007 by the Swedish Corporate Governance Board, indicates a low level of confidence in the way executive remuneration is determined.

This can have a negative impact, both in corporate and social terms. According to researchers Uslaner and Brown, anyway. In a report published in 2002, they note among other things how confidence in others, which forms the basis of efficient cooperation between colleagues, is negatively affected by growing discrepancies in income.

PARADOXICALLY LITTLE POWER

This discontent is even found in unexpected places. A survey of students at Harvard Business School reveals that two-thirds of those polled are critical to these levels of remuneration, according to business journal *The Economist*, which also points to the fact that

no less than 90 percent of institutional investors believe corporate managements to be grossly overpaid. This creates something of a paradox, since the majority of institutional investors, who express themselves so critically, in all probability have shareholdings in the companies led by these overpaid executives, and should therefore be cleaning up their own act before criticising others. The problem is, it can't be done. Shareholders in the USA lack any real power to change the situation. This may seem strange, when talking about the Promised Land of shareholder rights. Yet this is confirmed by Anne Simpson, President of International Corporate Governance Network (ICGN), in which the Second AP Fund is represented.

"Shareholders are in a weak position in the USA. Their options for action are more or less limited to 'sell or sue'."

ICGN is a significant power player on the international capital market. Its members manage capital assets in excess of USD 10 000 billion. The organisation is now focused on achieving change in the USA.

SWEDISH CHANGE MUST START IN THE USA

The logic is simple. As with so many other currents in the business world, this trend was also triggered by sharp rises in executive remuneration in the USA.

This trend eventually reached Sweden. To achieve a change, towards a more

balanced level of remuneration, requires a “counter-trend”. And, if it is to have a broad impact, this too must originate on the other side of the Atlantic – and prove tough enough to survive several counter attacks.

“The USA has a standardising effect on the rest of the world, largely due to its size – USD 10 000 billion can hardly be ignored on the global financial market”, states Anne Simpson.

FIRST REQUIREMENT IS A “SAY ON PAY” OPTION

One of the first points on the “to do” list for reducing the pace of the pay spiral is to ensure that shareholders are given a “say on pay” option. At present, shareholders cannot vote on remuneration principles at the AGMs of American companies – which they are free to do in countries such as Sweden and Great Britain.

A comprehensive initiative, sponsored by ICGN, was launched in 2007 to address this issue, in an attempt to influence political decision-makers in the USA. The

Second AP Fund assisted in the process of drafting the proposal for change that was eventually submitted to Congressman Barney Frank.

BOARDS NEED TO BE CONTROLLED TOO

Another important question that must be resolved urgently is the way boards are composed. The problem is that shareholders in American corporations basically lack any possibility of influencing the selection of board members. In recent years, more and more voices have been raised in a clamour for change. One proposal has suggested the introduction of “Proxy Access”. In principle, this means that long-term investors may include their own candidates to the board in the information material (management proxy) distributed by the company to all shareholders, prior to determining who is to be awarded a seat on the board. This is a right that, strangely, shareholders in American corporations currently lack.

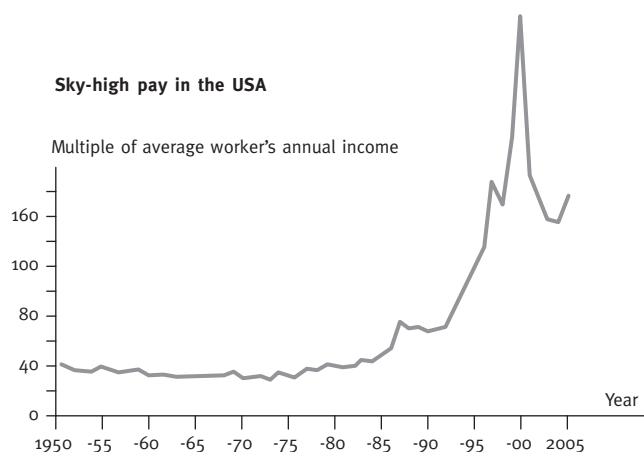
The Second AP Fund, with a number of other large European institutional investors,

has already taken action to change the situation in this respect, which has included lobbying political contacts in the USA. This is something that has been welcomed by ICGN.

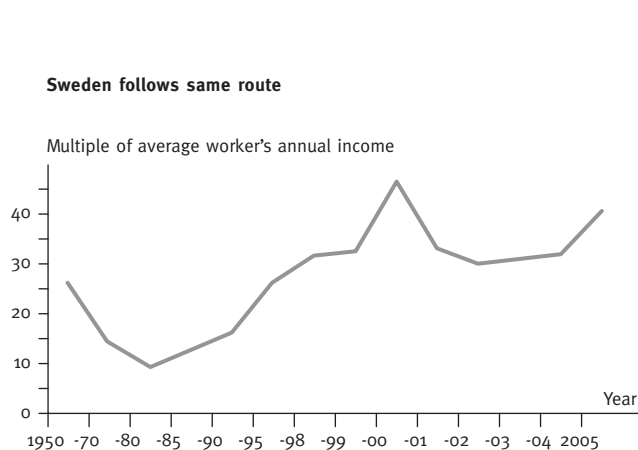
“We want the boards to be responsible to their shareholders. And we want the option to nominate candidates to sit on the board. We also want to see the introduction of voting by majority, so that shareholders can register a negative vote if a candidate turns up who they cannot support”, says Anne Simpson.

She feels that cross-border collaboration between major institutional investors, like that in which the Second AP Fund is currently involved, is going to be increasingly common.

Our members are long-term investors who wish to become involved in companies in which they invest, with a view to achieving positive change. They can achieve a lot by getting together and utilising their combined experience and resources.”



Average income for the three most highly paid CEOs in the 50 largest corporations listed on the S&P 500, as a multiple of a worker's average annual income in the USA. The figures include salary, bonuses and options programme (1950-2005). The peak noted at the start of the new millennium is largely attributable to the high number of options programmes generated at that time by the IT-bubble. Source: The Economist.



Average income for the CEOs of the 50 largest corporations in Sweden – as a multiple of a worker's average annual income (1950-2005). The IT bubble also affected Sweden, sending executive pay levels sky-high at the start of the new millennium. Source: LO (The Swedish Trade Union Confederation)

CEOs' pay in focus:

Fewer free options – demands for own investment increase

The days of free options seem numbered. This seems indicated by a recent survey of the most highly traded shares of major companies on the Stockholm Stock Exchange. One factor is the clear demands made by fund managers as investors.

Buffet

a tough advocate of Principal-Agent Approach

One of the foremost advocates of the principal-agent* approach is Warren Buffet who, with his partner Charlie Munger, constitutes the world's most successful investor duo. Anyone who had invested USD 10 000 in their investment company Berkshire Hathaway, in 1965, was able to take out USD 30 million in 2005. If the same sum had instead been invested in the S&P 500 index, the same investor would have found 'only' USD 500 000 in his account in 2005. Warren Buffet is himself good for more than USD 50 billion. One of his principles is that CEOs should invest their own money in the companies they lead. These investments should be in the form of shares bought on the stock exchange, not an options programme – and definitely not in combination with a large share repurchasing programme, which can lead to an increase in profit per share, although no 'actual' increase in profit is achieved.

*According to the principal-agent approach, a company benefits when senior management invests its own money in the company, since this guarantees that management will do everything to maximise the company's profits. This ensures that management's interests are fully in line with those of shareholders, who also keen to see the company generate the highest possible long-term return on investment.



Warren Buffet

"Yes. We and other institutions have advanced our positions on several fronts in recent years. One of our goals has been to deal with the 'free options' issue. Another has been to increase the demands we make on boards via nominating committees. It's gratifying that our efforts are having an effect", says Carl Rosén, head of Corporate Governance & Communications at the Second AP Fund.

The survey, which covered the 31 most traded shares on the Stockholm Stock Exchange's 'A' list during the period 2002–2006, suggests that it is still common to offer CEOs option programmes. One difference, though, is that these programmes are now smaller, in strict cash terms, consequently reducing dilution.

LESS DILUTION AMONG LARGE COMPANIES
Dilution is what occurs when the number of shares is increased in connection with an options programme. For existing shareholders, this means a slight reduction in the value of their old shares. Between 2002 and 2006, the dilution of outstanding programmes among the companies covered by the survey was reduced from 2.4 percent to 1.8 percent of total market value. These figures may seem small, but for a major investor, calculated on the basis of these companies total market value, it can involve considerable sums of money.

During the period measured, the portion of CEOs' remuneration comprised of options fell from almost 18 percent to just over 3 percent. This may largely be attributable to increases in their "ordinary" pay, but also to reductions in options programmes.

USUALLY IN THE SAME BOAT

Options programmes have not only been reduced in size. In almost half of the com-

panies (14 out of 31), requirements for own investment have now been linked to outstanding options programmes. Furthermore, the number of performance-linked programmes has increased by more than 300 percent, from 3 to 13 companies, between 2002 and 2006.

The thinking behind this scheme is known as the "flight school" approach. It is based on the principle that the CEO should be sitting in the same seat as the company's shareholders – in terms of risks as well as rewards. This approach is popular with an increasing number of shareholders. It is even popular among CEOs. Hexagon's CEO Ola Rollén is a typical example.

"I believe in our company, and I believe it is extremely important for CEOs and key personnel to own shares in their own company. I am convinced that the dynamic this creates is underrated," he said, when interviewed by business daily Dagens Industri on April 28th this year.

He has little good to say about "free options", the term used to describe options that enable senior management to own shares in a company, without having to pay or risk anything.

"Free options are often treated as additional salary, which is not at all the same thing as investing your hard-earned savings. If things go badly, it should hurt. What do you take most care of? Your own car or one you rent?"

His approach is fully compatible with Second AP Fund thinking. "No studies of the Swedish market exist that demonstrate a distinct link between free options and increased share value. Which is why we should instead focus primarily on other proven and more effective ways of motivating senior management to do their very best", says Carl Rosén.



Second AP Fund's Q-index 2007

Board representation up – lower levels lag behind

The Second AP Fund conducts an annual survey to determine the number of women represented on the boards of 256 Swedish quoted companies. This year's survey indicates continuing male overrepresentation in senior management positions. This in spite of the fact that the recruitment base is substantial, given the number of women who possess the appropriate qualifications.

The dropout rate for women between completion of university studies and appointment to a management position, and between a middle-management and an executive position, in quoted companies, is considerable. This year's survey is more comprehensive than its predecessors. This is due to the Fund's determination to study the recruitment base more closely, by which is meant the percentage of women with a university qualification, who either hold middle-management or executive positions in quoted companies. The result is very clear. The percentage of women with university qualifications in disciplines that have provided the traditional recruitment base for business careers has doubled in the past 20 years – from less than 20 percent to more than 40 percent.

MIDDLE-MANAGEMENT LAGS BEHIND

At middle-management level, however, development has been slower. Figures

released by the Swedish Central Bureau of Statistics show a level of about 20 percent. The pace of change at executive level is even slower, women filling a mere 12 percent of the top posts.

At board level, which has long been bottom of the league, there has been a dramatic improvement over the six years during which the surveys have been conducted: from 6.1 to 19.3 percent. This corresponds to an annual increase of 21 percent and a total increase of 211 percent – even if from a very low level. It is worth noting, however, that the pace of improvements recorded in 2002–2004 has slowed in the past three years.

WHERE TO LOOK

– IF YOU PLAN TO RECRUIT WOMEN

Those seeking qualified women for their boards should focus on companies in the following business sectors: Services, Consumer Goods, Media and Entertainment. And bigger companies employ a significantly larger percentage of women. Companies with the lowest levels of female representation are found in classic male-dominated industries such as Telecom, Raw Materials and IT. This said, it should be noted that the percentage of women is on the rise in all main business sectors.

DROPOUT RATE A BIG PROBLEM

One problem is the high dropout rate between the different career levels on the way up, towards executive and board level

appointments. The greatest dropout occurs on the way to middle-management positions in private-sector companies.

According to fundamental mathematical principles, the difference between the percentage of women with the “right” qualifications (at just over 40 percent) and the percentage of women at executive level in the private sector (at just over 20 percent) is about 20 percentage units. And the rate of female dropout from executive positions to the boardroom of a quoted company is also considerable, at about 10 percentage units (for more on the possible reasons for this dropout rate, turn to the interview with psychologist Professor Barbro Dahlbom-Hall, on the following page).

Wish to contribute to an objective debate

Historically, no instruments have been available for measuring the percentage of women on corporate boards and in executive positions, at industry and corporate level. It is hoped that the Second AP Fund's Q-Index will contribute to an objective debate on how the percentage of female representation on the boards of Swedish companies may be increased. The reason is simple: a broader recruitment base creates better boards and executive managements, which inevitably helps create better companies. And this enhances shareholder value.

* Study conducted by Nordic Investor Services

Why equality pays

There are at least six good reasons for increasing the percentage of women in leading positions in the Swedish business world. All contribute to the same end result: increased profitability. And – if you accept the research conclusions presented here – the way to achieve this is via more contented employees and more (and more loyal) customers

1. MORE WOMEN EXECUTIVES BOOST PROFITABILITY

In 2004, New York-based Catalyst conducted a survey of 353 Fortune 500 companies, covering the period 1996–2000. The results showed that the companies with the highest proportions of female representation at senior management level posted a return on investment 35.1 percent higher than companies with the lowest level of female representation. Furthermore, total return for shareholders, i.e. market rate plus dividend, was 34 percent higher during the same period.

The study demonstrated that this pattern was repeated all the way down to sector level. In all five sectors analysed, it was revealed that companies with the highest percentage of female representation in senior positions showed a higher return on invested equity than those with a lower percentage. A study by Professor Roy Adler, presented in the November 2001 issue of Harvard Business Review and other publications, notes the same correlation. His study, which covered the period 1980 to 1998, showed that the 25 Fortune 500 companies with the highest percentage of female representation in senior positions generated a return on investment that was between 18 and 69 percent higher than the average reported for the respective companies' industries. The study employs three ways of gauging ROI: return in relation to turnover, return on assets and return on equity. Correlation was high in all instances.

2. COMPANIES WITH A HIGHER PERCENTAGE OF WOMEN DIRECTORS EXPRESS GREATER INTEREST IN CORPORATE GOVERNANCE WHICH LINKS DIRECTLY TO VALUE CREATION

A study conducted by the Conference Board of Canada in 2002 has revealed a distinct link between the percentage of women on company boards and the degree of commitment to issues related to corporate governance and credibility. This study, which traced developments between 1995 and 2001, showed for example that 94 percent of boards with three or more female directors expressly evaluated

implementation of the company's strategy, as compared to 66 percent for boards made up of men alone. And 86 percent of boards with three or more female directors ensured that a code of conduct had been established for the organisation, as against 66 percent for boards with only male directors.

3. INCREASED COMPETITION FOR LEADING POSITIONS ENSURES HIGHER MANAGEMENT QUALITY

The percentage of women taking degrees in disciplines that have traditionally functioned as door-openers for future executive careers (economics, engineering and law) has been slightly in excess of 40 percent in Sweden in recent years. This has significantly expanded the pool of suitably qualified candidates available to fill future positions in senior management. This has sharpened the competition, creating excellent prospects for improved executive quality and increased profitability.

4. MORE WOMEN IN SENIOR MANAGEMENT INCREASE UNDERSTANDING OF HOUSEHOLD CONSUMPTION

A number of studies conducted by the US Census Bureau in 2005 indicate that women control more than 80 percent of household consumption. Increasing the number of women in senior management will contribute additional competence for attracting this customer base. The fact that there is a clear connection between increased gender equality and access to new customer groups has also been highlighted in Glashuset, a 2005 report from the Office of the Equal Opportunities Ombudsman, in which 22 employers are interviewed about equal-opportunity recruitment.

5. MORE WOMEN IN SENIOR MANAGEMENT INCREASE UNDERSTANDING OF CORPORATE CUSTOMERS

The number of female entrepreneurs is growing. Even though Sweden may be in the bottom division when it comes to female entrepreneurship, the percentage is growing. One in every three new start-

ups is owned by a woman, according to a report from the Swedish Institute for Growth Policy Studies (ITPS). And in the USA, the Center for Women's Business Research notes that the rate of growth has been higher for companies owned by women than for the business community in general in recent years. These new companies form a potentially high-growth customer sector for companies focused on "business to business". Women in senior positions will present these companies with increased opportunities to attract this growth market.

6. MORE WOMEN IN SENIOR MANAGEMENT CREATE A BETTER WORK ENVIRONMENT – AND GREATER PROFITABILITY

Greater numbers of women in senior positions have a positive impact on the corporate work environment. For example, the 1988 study conducted by the American not-for-profit research organization, Families & Work Institute, shows that 82 percent of companies where women comprised half or more of senior management offered flexible working hours, compared with 56 percent in companies without any women in senior management positions. Well considered policies for creating a good work environment, including flexible working hours, establish favourable conditions that reduce personnel turnover, among both men and women, as well as attracting new talent. One example of this may be found in the result of a study conducted by the Conference Board of Canada. It shows that employees who feel that management creates opportunities for combining work and family life give their companies top ratings in employee-satisfaction surveys. This promotes increased profitability. The Harvard Business Review OnPoint 2000 study presented research results that established a clear link between employee satisfaction and enhanced customer loyalty, which has a significant impact on profitability. The result showed that a 5 percent gain in customer loyalty could generate a significant percent increase in profitability.



Foto: Jacob Forsell

Why women drop out on the way to the top

More women than men drop out on their way to senior positions in Swedish business. One reason is that many male managers still lack understanding of the obstacles that women must confront, but men avoid. And as long as they fail to understand, they cannot hope to change. So says Professor Barbro Dahlbom-Hall, one of Sweden's foremost experts in executive development.

The Second AP Fund's 2007 Q-Index indicates that there is a large recruitment base of well-qualified women, who are prepared to embark on a career and to step into leading positions in the business world. In the disciplines that have formed the traditional recruitment base for corporate managements and directorships on boards, the percentage of women has increased from less than 20 percent to more than 40 percent in just over 20 years. Even so, statistics show that far more women than men drop out of the picture as they climb the career ladder to the top, where only one in ten is a woman.

INCREASING NUMBERS OF WOMEN WANT A CAREER

The claim that one reason women fail to go all the way to the top is that they are less interested than men in pursuing a career is just not true. This is clearly shown by statistics published by the Women's Business Research Institute. A study of 1 250 male and female middle managers in the private sector confirms that 27 percent of women are keen to have a career. The percentage of men who were interested in pursuing a career was lower – at 26 percent.

The study also shows that men and women have different views concerning the possible obstacles to a career. About half the women interviewed felt that there were several obstacles along the way. One in three women answered that the main obstacle was the resistance encountered in working life. This included outdated attitudes to gender, where women were not expected to attain managerial positions, as well as the persistence of a macho culture, that features male social networks from which women are excluded.

FEW MEN SEE OBSTACLES TO CAREER PROSPECTS

Of the men, a clear majority (seven of ten) saw no obstacles to career prospects. Barbro Dahlbom-Hall feels that this difference illustrates an essential part of the problem.

"Many men are still oblivious to the fact that men and women are treated differently – and that many women are hindered from pursuing a career, even though they are normally more ambitious than their male counterparts," says Barbro Dahlbom-Hall.

Her observations are supported by a fresh report published by Sweden's Institute for Future Studies. One of the findings is that women are normally more highly qualified than the job actually requires – and that among those who are underqualified, men account for the greatest percentage, seen in terms of what is typical for respective professions.

THE GREATEST "OBSTACLE" LURKS JUST BELOW SENIOR MANAGEMENT

The greatest "obstacle" that may be encountered on the way to the "right" job, as defined by qualifications and experience, is not encountered at the very highest level, but just below.

"Greater demands must be placed on line managers to ensure that they give more women the opportunity to advance. But this is by no means easy. Line managers are under pressure both from above and below. It is often easier just to let things roll on as before."

"Managers need help to appreciate the consequences of their value judgments and behaviour. This is particularly important when it involves men who identify closely with their jobs", says Barbro Dahlbom-Hall.

According to Professor Dahlbom-Hall, this is an identity that such men are

subconsciously afraid of losing, when they find themselves competing with competent women.

"Many men are surprised to discover that good leadership and the creation of greater equality of opportunity is so much a case of understanding and gaining increased insight into oneself."

QUESTIONS THAT RAISE ISSUES

Any simple tips for a male manager who seeks greater self-awareness?

"Yes. To start with, he can try to imagine what his working life would be like if he was a woman, with the same qualifications or better. After a time, most men realise they would fail to get as far – not because they were less competent, but because they would be treated differently. This type of mental exercise can be a good starting point for increased awareness", says Barbro Dahlbom-Hall.

For women, she has a different tip to help stimulate this mental process.

"Do nothing for a whole day. Stop trying to 'overperform' all the time, and stop spoiling your male colleagues. Just thinking like this can generate a whole range of useful insights about attitudes to sex roles and the workplace," says Barbro Dahlbom-Hall.

Acclaimed teacher in the school of leadership



Barbro Dahlbom-Hall has been engaged in leadership development and management training since the 1970s, in Sweden and abroad. Her clients include organisations such as the UN and SIDA, as well as multinational companies.

She is the author of several books that address equal opportunity issues in business and the public sector, including "Teaching men to lead women" and the prize-winning "Teaching women to lead men".

Her new book, "Teaching men to live – with the dilemma of leadership", is scheduled for publication in autumn 2007. Barbro Dahlbom-Hall has been awarded an Honorary Doctorate by Uppsala University and HM the King's Medal of the 8th Grade with the Blue Ribbon of the Order of the Seraphim, for her achievements in management education.

“We need all the help we can get, even from the politicians”

“Many economists claim that the market is efficient, that it is programmed to absorb the most profitable ideas. But in that case, why hasn’t the market created greater equality of opportunity? After all, research shows that it’s a profitable idea.”

The Second AP Fund turned to Ronald Fagerfjäll, journalist, author and one of the country’s most knowledgeable corporate historians, for an answer to this and a number of other questions.



INTERNATIONAL RESEARCH HAS APPEARED IN RECENT YEARS THAT SHOWS THAT A HIGH PERCENTAGE OF WOMEN IN SENIOR MANAGEMENT LEADS TO INCREASED PROFITABILITY. WHAT DO YOU THINK OF THIS RESEARCH AND ITS CONCLUSIONS?

“I’m not sure that you can be too categorical about such a thing, and suspect that the period of time over which this research was conducted is too limited. Intuitively though, I think most things support the idea that gender equality

improves profitability. This is because the pool of talent expands, our understanding of the complexity of the market is enhanced and the work of the organisation becomes more creative when traditional strictures can be relaxed.”

IF THE MARKET IS SO EFFICIENT, WHY DON’T WE ALREADY ENJOY EQUALITY?

“Equality of opportunity is a new concept when seen from a historical perspective, being inextricably linked with economic and technical evolution. Before the age of machines and electricity, physical strength constituted the primary driving force in the economy. This benefited men, who could either carry out the demanding physical labour themselves or force others to do it for them.”

WHAT’S SLOWING DOWN THE DEVELOPMENT?

“The pace of sociological evolution and adaptation to change is slower than that of technology. There are actually plenty of people, even in countries like Sweden, who think that the roles of men and women can still be determined by documents that date back thousands of years. In spite of this, the number of women in executive positions has risen by 10–15

percent per year in recent decades.”

WHO WILL PUSH FOR CHANGE, AND EMBRACE ECONOMIC ARGUMENTS TO MOTIVATE THEIR ALTERED ATTITUDE? WILL IT BE ENTERPRISING BUSINESSES OR CIVIL SERVANTS?

“It’ll be a mixture. Gradually, more and more people will realise what perhaps a third of the population is already fully aware of – that women and men are more or less equally capable of handling any profession and any type of work that doesn’t demand extreme muscle power. The problem is that not even all women have yet fully understood the new conditions. Businessmen and entrepreneurs are definitely ahead of politicians and civil servants in this respect, since it is in their own interests to optimise their personnel resources. Yet even they continue to subscribe to a number of outdated assumptions.”

“For politicians, the primary motivation is to attract women’s votes. Sadly, women in many countries, after long exclusion from participation in the democratic process, register their protest by voting against the Left and in favour of a planned economy. There is a strong tendency in politics to confuse equality with similarity.

The point of equality is not that men and women are exactly the same but that, while different, are of equal value. Nor does equality assume that all women are alike or shall have similar salaries. The point is that women should be able to enjoy the same broad choice of career and salary level as already enjoyed by their male counterparts.”

HOW LONG DO YOU THINK IT WILL TAKE BEFORE WE REACH THIS GOAL?

“We need all the help we can get, even from the politicians. During the latest quadrupling of the global economy, dating from 1970, the percentage of women in executive positions has risen from almost zero to between 20 and 40 percent in the industrialised countries. I believe it will take us another thirty years to get there. It may take even longer for women to reach the most elevated executive positions and gain power in the boardroom, since it will depend on the number of women available for promotion from the levels immediately below. One major problem is that the pipeline’, i.e. the channel leading to the corridors of power, is leaking. Women, after starting a career, leave it more often than their male counterparts. It’s probably about role divisions in the family. This also needs to change, as part of the social development process.”

WILL WE NEED LEGISLATION, AS IN NORWAY, IF THIS DEVELOPMENT IS HALTED?

“Establish goals focused on executive positions, not seats on the board, which is something totally different. Use the threat of legislation if development in this area stagnates over a number of years. The

important thing is to adopt a dynamic approach to the situation. The number of women in executive positions should increase exponentially, as opposed to the huge ‘leaps’ that are so popular with Leftist politicians.”

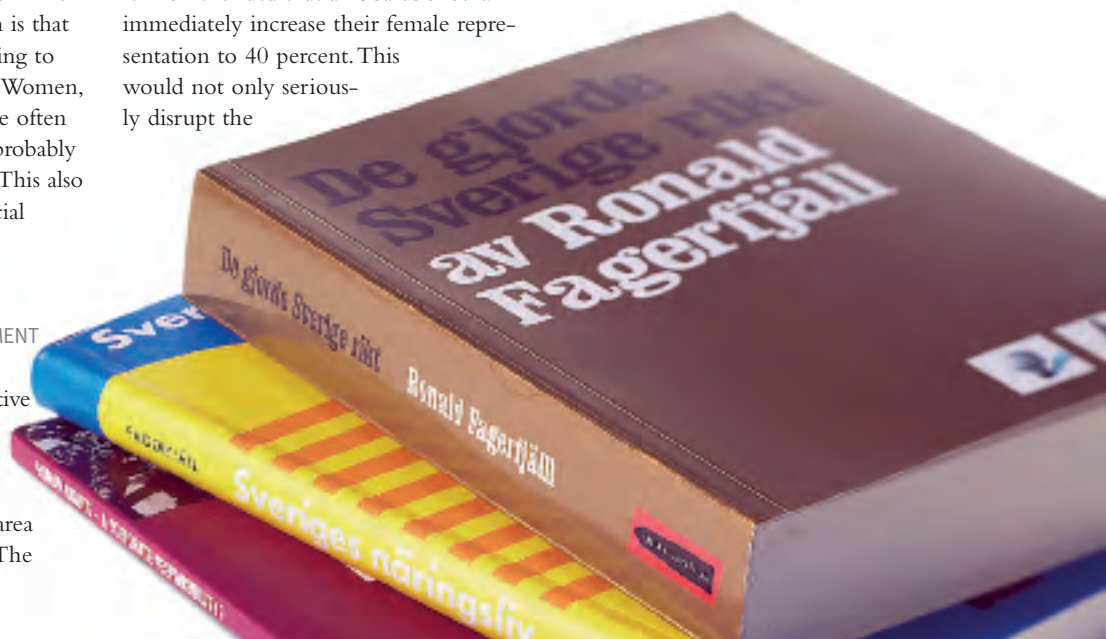
BROADLY SPEAKING, OPINION IS DIVIDED INTO TWO CAMPS ON THIS ISSUE. THERE ARE THOSE WHO ADVOCATE QUOTAS, AND THOSE WHO BELIEVE MARKET FORCES CAN BE LEFT TO SOLVE THE SITUATION WITHOUT EXTERNAL MEDDLING. DO WE KNOW WHICH IS THE MOST EFFECTIVE WAY TO DEAL WITH THIS TYPE OF ISSUE?

“Quotas can certainly be used, preferably slightly in advance of any ‘organic development’, as a form of encouragement. The problem here is that many politicians simply don’t care about the evolution process itself. One regularly mooted proposal is that a quota system be applied to ensure that women are appointed to the boards of Swedish companies, based – for example – on the idea that all boards should immediately increase their female representation to 40 percent. This would not only seriously disrupt the

work of these boards: it would block subsequent opportunities for future competent women to attain such positions on a continuing basis.”

“And, as already noted, the power of the board is a pseudo issue. In practice, the board’s role is to appoint a company’s executive management and monitor its performance: it is this executive that is of central importance. Each board should contain a majority of directors who have themselves led companies. This is actually more important than whether they are men or women.”

If, as a symbolic gesture, politicians decided to introduce legislation that required that 20–25 percent of the seats on Swedish boards be filled by women, I wouldn’t think it especially problematic. However, I believe this excessive focus on boards is because politicians equate democratically elected boards with the corporate boards of a market economy, which are not the same thing at all.”



Nicolin prize-winner knows his corporate history

Ronald Fagerfjäll is both author and a leader-writer for Swedish business daily Dagens Industri. He was earlier editor-in-chief of business magazine Affärsvärlden. Ronald Fagerfjäll was awarded the 2007 Nicolin Prize for his achievements in chronicling Swedish corporate history –

including the trilogy entitled *Företagsledarnas århundrade* (*The Century of the CEO*) and the anthology *De gjorde Sverige rikt: 1900-talets entreprenörer, företagsledare och riskkapitalister* (*They made Sweden rich: the twentieth-century's entrepreneurs, corporate moguls and*

venture capitalists). Ronald Fagerfjäll is also the author of *Så spricker vi glastaket!*, a manual on how the private sector could recruit and develop 3000 new top women executives. This manual provides advice and establishes guidelines on how company managements can

become more dynamic, creative and multifaceted. It features a historical review and an analysis of the current situation, and discusses ways in which the recruitment and development of women candidates for top executive positions can become a natural part of company activities.

The Second AP Fund asked four successful women to answer two questions related to gender equality in quoted Swedish companies:
 1) When do you think we can achieve equality at executive and board level in quoted Swedish companies?
 2) What will it take to achieve this? See below for their answers.



Peggy Bruzelius
Director of numerous boards

One of Sweden's most experienced board directors, with an extensive career in finance. Member of several boards, including Electrolux and Scania. Also partner in and chairman of Lancelot Asset Management, a significant yet low-profile player in Swedish asset management.

1. Many years, if ever. The critical selection is made at middle management level, i.e. when the individuals in question are about 30–40 years old and often engaged in building a family.

2. A society with more highly developed support services, in which it is possible to purchase household help legally and at reasonable cost. The Swedish Government's introduction of tax benefits for household help is probably the greatest advance in gender equality since women were granted the right to vote. There is also a need for a change in social attitudes, so that the purchase of such services is perceived as natural and productive.



Gunilla Herlitz
Editor-in-Chief and Managing Director, Dagens Industri

Manages what is perhaps Sweden's most influential media group from her office on Torsgatan 21, Stockholm.

1. I believe it will take so long that it is hardly foreseeable, if it ever happens at all. I doubt my sons and daughters will ever experience a business world of true equality. On the other hand, it's good news that many quoted companies take this issue seriously.

2. What is required is increased awareness, transformed attitudes and a genuine commitment by the business world to utilise all available competence.



Marianne Dicander Alexandersson
Managing Director, Apoteket Privatkund

Formerly Managing Director of Kronans Droghandel and recipient of the Ruter Dam award "Most significant female executive appointment" in 2003. As MD of Apoteket Privatkund, she is responsible for more than 900 state pharmacies, with sales in excess of SEK 28 billion.

1. I think we still have many years to go – but when things start to change, they are likely to change fast.

2. I think two things will be needed. For one thing, those of us with executive responsibility, both men and women, must see to it that we recruit women to line management positions in our companies. And social attitudes must change. When it comes to the younger generation, attitudes have already changed to some extent, but scepticism about women in executive positions is still too common. Especially in the media. For example, when reporter Stina Dabrowski interviewed two of Sweden's foremost female role models on Swedish TV, she seemed most interested in hinting that they had too little time for their children. Another important aspect is that women must be keen to make the effort.



Caroline Sundewall
Director of numerous boards

After a long and successful career as a business journalist, Caroline Sundewall has now stepped into the boardroom. A member of several boards, including Telia and Electrolux.

1. The question we must ask is: how should equality be defined? In which sectors should we strive for just the right balance of young and old, native Swedes and immigrants, and so on? This continuing fixation on equality is not going to sharpen a company's ability to compete. Rather, it will be determined by its openness to the way customers and markets develop over the years ahead, and its ability to attract the most relevant skills. Competition for appropriately qualified staff will become still fiercer, requiring attractive workplaces with potential for personal and career development.

2. Senior managers who are highly motivating, enthusiastic and open to new ways of leading companies in an increasingly globalised and fast-changing world, in terms both of customer and staff behaviour. There has been a dramatic increase in tempo, inside and outside companies, increasing the pressure on all staff, including executives and members of the board.

2 questions 8 answers

Joint Ethical Council: united, we can make a difference.

Four Swedish National Pension (AP) Funds, acting jointly, have more influence than four funds acting separately. That's the way it works when dealing with corporate governance issues in the global arena. Which is why the decision to collaborate was welcomed by all, with the possible exception of some of the companies that risk a visit.

Nadine Viel Lamare is chairman of the Joint Ethical Council, which comprises the First, Second, Third and Fourth AP Funds. She is also responsible for information, ethical and environmental issues at the First Swedish National Pension Fund (AP1), which has achieved considerable success in its corporate governance activities in recent years, including the case of Marriott Hotels (see next spread).

The idea of forming a Joint Ethical Council was originally mooted in the summer of 2006, when the four AP Funds (1-4) were engaged in the joint procurement of consulting services to conduct analyses of portfolio companies. The Funds reached common agreement that it would be more efficient to work together concerning the governance of foreign portfolio companies.

"This is a highly resource intensive job, and four funds can handle much more than one. Another benefit is that we command much greater respect when we act in concert, as a group of funds. We've already noticed a difference, compared to the reception we used to get as a single fund", says Nadine Viel Lamare, chairman of the Joint Ethical Council and head of information, ethics and environmental issues at the First AP Fund.

THE DOORS ARE OPEN FOR SHAREHOLDER VALUE

It is all very well that doors have now

been opened to the Joint Ethical Council. The question is if, and in such cases how, the Joint Ethical Council can create value in its asset management activities by entering these doors.

"Shareholder value is generated by many different factors. This is one. Historically, we have seen several examples where scandals have caused the price to dive in the blink of an eye. We have also seen initiatives, where companies claim that they are going to take appropriate measures, where the price rises. If we can persuade companies to act when confronted by troublesome issues, this will enhance their long term market value. And we are long-term investors."

One example that demonstrates this relationship can be found in the hotel industry. The hotel chains that have removed pornographic films from the TV broadcast in their rooms have increased their bookings compared to the rest. This boosts profits.

"We should also remember that scan-

dals are also costly in a less direct sense. A company's executive management and internal organisation must expend considerable energy in dousing the fire, drawing attention from strategically important issues. This can have far-reaching consequences."

ANALYSIS POINTED TOWARDS COLLABORATION

The whole idea of having four national pension funds instead of one is to stimulate competition, intended to promote a higher combined return on investment in relation to risk. Furthermore, the AP Funds suggest that active governance leads to an increased return. In this case, doesn't collaboration on corporate governance seriously undermine the whole idea of competition on which the Funds have been founded?

"We carried out a thorough analysis and reached the conclusion that the creation of a Joint Ethical Council in this form would pose no problem. Quite the opposite: it's highly beneficial. The Joint

Ethical Council only concerns itself with foreign companies and, given the approach adopted by the AP Funds in managing foreign equities, this yields greater efficiency and offers increased opportunities for living up to the demands made on us as responsible investors”, says Nadine Viel Lamare.

The Government’s evaluation anticipated no obstacles to forming such a Council either.

“We should also remember that the Joint Ethical Council merely offers recommendations as to how the Funds should act. It has no right of determination.”

IT HAS INVOLVED A LOT OF WORK

This has involved quite a lot of work so far this year, such as all the follow-ups and the maintenance of regular contact with GES, which provides analyses of the portfolio companies. The Council also holds regular meetings. By June this year, it had already met five times.

“This is because we are still in the launch phase. Once we are up to speed, we plan to meet every second month”, says Nadine Viel Lamare.

A number of cases that the Council plans to take up were addressed at the most recent meeting, including Yahoo, and how the company is dealing with the problems encountered concerning free-

dom of speech in China, related to its search engines and other services.

Nadine Viel Lamare is used to success in the corporate governance field, from her previous activities at the First AP Fund. The case that perhaps attracted the most attention concerned Marriott Hotels (see next spread).

“We conducted this campaign entirely on our own, from the First AP Fund. If we hadn’t taken up the issue, nothing would have been done”, says Nadine Viel Lamare.

KETCHUP EFFECT IN 2005-2006

Together with other representatives for major shareholders, she has been engaged in dialogues with some 25 companies.

“We started this process in 2003. The first two years were tough. Later, in 2005 and 2006, things really took off, and no fewer than 15 companies implemented improvements in line with our wishes.”

Of course, there have been disappointments as well, although not that many.

“Wal-Mart has been the greatest disappointment, without doubt. We wanted to initiate a dialogue with the company concerning its infringements in the field of labour law. Some years ago, they totally ignored us. Things have got a little better, but there’s still a huge amount to do.”

That companies finally respond is usu-

ally the result of persistent and patient effort. There is also the lurking anxiety that they may be exposed in the media – which tends to increase their willingness to change.

“This was definitely so with the Marriott case. Even so, it’s important to choose the right moment to embark on a public debate. In some cases, it can be a good idea. In others, not, because it can lead to a period of stalemate”, says Nadine Viel Lamare, who started working with governance issues at the First AP Fund in 2002.

Prior to this, she was engaged in follow-up and assessment of investment activities. She sees clear differences in these two jobs.

“In this job, we get to see an immediate result. Either we succeed in getting a company to change, or we don’t. It’s not quite the same when working in a support function as part of an investment organisation. And in our work here, we have an opportunity to influence the really big players on issues that may not only generate a higher return, but that have considerable significance for the future of society in general”, says Nadine Viel Lamare.

The Joint Ethical Council in brief

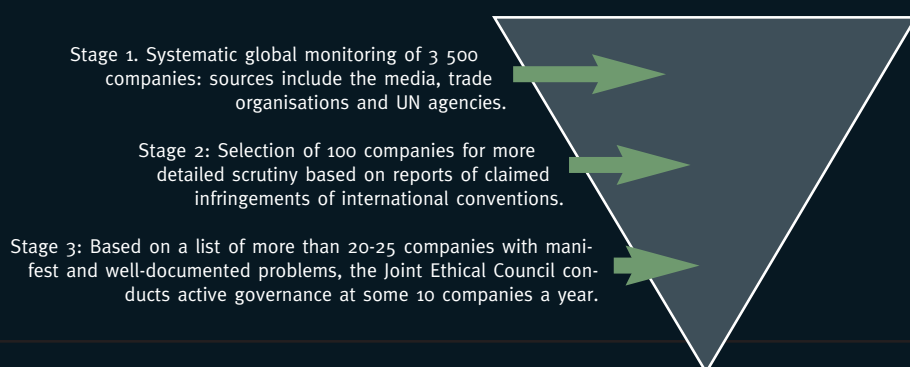
The Joint Ethical Council is a joint project between the First, Second, Third and Fourth AP Funds. In all, the four AP Funds represent assets valued at around SEK 800 billion. Each Fund has a representative on the Council. Its purpose is to jointly promote a positive change in foreign companies associated with infringements of international environmental and human rights conventions, such as the International Labour Organisation (ILO) core conventions and the UN Declaration on Human Rights.

Five-step working process

1. The Joint Ethical Council learns of an incident that has occurred at one of the portfolio companies.
2. A serious incident triggers more intense monitoring of the company.
3. The Joint Ethical Council initiates a direct dialogue with the company.
4. Additional measures are taken to influence the company. This includes collaboration with other investors as well as the proposal of motions for consideration by the AGM and exercise of voting rights at same.
5. Should steps 1-4 fail to yield the hoped-for result, each Fund makes an individual decision concerning the possible sale of its interest, based on a recommendation of the Joint Ethical Council.

The funnel – how 3 500 companies become 10

According to their directive, the AP funds that constitute the four members of the Joint Ethical Council can invest in thousands of international companies. Clearly, the Joint Ethical Council lacks the resources to conduct active governance of so many shareholdings. For this reason, the Council employs a model, to speedily identify the holdings that can benefit most from active governance and that offer a good spread of the problems encountered and types of holding – to avoid focusing too narrowly on the same industrial sector or the same type of problem. The process can be broken down roughly into three stages.



How Marriott Hotels cleaned up its act

It all started in 2002, following a conviction related to a case of child prostitution in Costa Rica. The offence occurred in a hotel owned by the exchange-quoted Marriott Hotels chain. Some months later, Nadine Viel Lamare, head of ethics and environmental issues at the First AP Fund, heard about what had happened. This signalled the start of a lobbying process by a single Swedish pension fund against this powerful US hotel chain – a process that was to take several years.

Of Sweden's four first national pension (AP) funds, the First AP Fund has worked longest with shareholder governance of international portfolio companies. "Project Marriott Hotels" is one of the Fund's better-known cases. It clearly illustrates the type of case now handled within the parameters established for the Joint Ethical Council, of which all four Funds are members.

"The Marriott-case is unique, in the sense that we found ourselves in the driving seat. If we had done nothing, this child prostitution would probably have continued. But it was tough. It took longer than I expected, and many times we celebrated our success, only to be disappointed a short time later", says Nadine Viel Lamare.

COOL WELCOME

The Fund's first attempts at contact got nowhere at all. Marriott Hotels seemed

fairly indifferent to pressure from a "little" fund in a faraway country. The first letter was met by total silence, the second by a number of tired standard clichés.

But when the First AP Fund demonstrated that it was prepared to really stir things up, there was a reaction.

"I remember when the turnaround came. It was when we tabled a resolution at the AGM, in October 2005, when they asked us to withdraw our resolution, if they agreed to set up a committee to address these issues. This showed that they were anxious about what we had started", says Nadine Viel Lamare.

"ABSOLUTELY CERTAIN" IN SEPTEMBER 2006

Perhaps the main cause of this response was that information about what had occurred would become public knowledge

the moment the resolution was tabled. Up until then, the whole affair had virtually escaped everyone's attention. However, it soon became clear that far from all the obstacles to change had been removed. It was not until a meeting held in September 2006 that real change was implemented, in the form of a new policy to define how the company should act when dealing with this type of issue.

"It was really only at this point that I felt absolutely certain. If I learned anything from the Marriott case, it was the need for patience, not to lose heart when nothing happens, after promises have been made to address the problem. You just have to keep up the pressure, until they finally give in", says Nadine Viel Lamare.

Five years from start to finish

The case with the huge Marriott Hotels chain took time to complete and featured both successes and disappointments along the way, until the autumn of 2006, when success was achieved.

2002: Conviction against a private individual in Costa Rica. Child prostitution on hotel premises. Personnel fail to report the offence.

May 2003: The First AP Fund hears of the offence and initiates an inquiry.

Autumn 2003: The Fund writes the first letter to the company. The letter states that the Fund has noted the case and, in its role as a major shareholder, would like to know how the company plans to address such issues in future. A dialogue is proposed.

Spring 2004: The Fund has received no reply. A new letter is therefore sent.

August 2004: Marriott Hotels responds for the first time. The response is inadequate.

2004–2005: The Fund searches for new ways to initiate a dialogue with the company. Eventually, the Fund dispatches a letter making clear demands for improvement. The letter is accompanied by an initial draft of the resolution the Fund proposes to submit at the Marriott Hotels AGM.

October 2005: This is where the turnaround begins. It starts when the Fund registers its resolution prior to the Marriott Hotels AGM, in the spring of 2006. Other fund managers, including DnB and Boston Common Asset Management subscribe to the resolution.

November 2005: This is when Marriott Hotels really starts to jump. The company appoints a working committee of leading executives to address the issue and to conduct a dialogue with the investor group, in return for withdrawal of the resolution. The expressed intention is to resolve the case during 2006.

November 2006: During the year, three meetings are held between the investor group and Marriott Hotels. The definitive breakthrough comes in November, when the company adopts a new human rights policy that clearly addresses the child prostitution issue. After this, the company initiates a staff training scheme. Marriott Hotels has also taken a leading position in International Business Leaders Forum, which among other things is developing an industry initiative to combat child-related sex tourism.

2002

2003

2004

2005

2006

UN looked for good examples – ended up in Gothenburg

The UN mission was straightforward: check out the world's pension funds, and find 15 role models that are working with "sustainable investment". The result was a report in which the established global stars of the investment firmament rub shoulders with each other – and with the Second AP Fund – from Gothenburg.

"It is gratifying that the UN has noticed our efforts and that our method for integrating sustainability issues into asset management works", says Carl Rosén, head of corporate governance and information at the Second AP Fund, the only Swedish fund of those selected.

The report presents the 15 funds and their work in the form of concrete strategies. The intention is to give other fund managers ideas about how sustainability issues can be made an integral part of the investment process. The initiative has been sponsored by the UN agency for environmental issues within the financial sector, UNEPFI (The United Nations Environment Programme Finance Initiative), and UKSIF (The United Kingdom Social Investment Forum).

AMONG THE GIANTS

In the initial screening process, more than 25 funds were evaluated. Of these, 15 were selected for inclusion in the pub-

lished report. These range from giants such as the California Public Employees Retirement System Fund, better known as "Calpers", to Norska Statens Pensionsfond (The Norwegian State Pension Fund), which is the largest pension fund in Europe. As per March 31st 2007, these funds' assets totalled SEK 2 160 billion. This is equivalent to four-fifths of Sweden's entire GNP in 2005.

The Second AP Fund, after only six years and with SEK 232 billion under management, is both relatively young and relatively small in this context.

"Yes. Our organisation is young, which offers several advantages. There's less of the 'that's-the-way-we've-always-done-it' mentality, which I believe can be a key benefit when it comes to this type of issue", says Carl Rosén.

SIGNIFICANT ISSUES

The report stresses the important role played by the big funds as major sharehol-

ders in the sustainability sphere. It also notes that this type of issue can be integrated as part of the investment process so as to increase shareholder value. Furthermore, "sustainable investments" also generate social benefits. These may be matched against the risks that may arise from failure to change. Nicholas Stern, for example, former Chief Economist at the World Bank, in a report published in 2006, notes that the global warming that follows in the wake of climate change could cause the global economy to shrink by as much as 20 percent.

Those interested in reading the report in its entirety may download it from the following address:
www.unepfi.org/fileadmin/documents/infocus.pdf



The first PRI annual meeting was held in Geneva on July 3rd and 4th 2007.

Ethical investment is popular

It is increasingly common to do what the Second AP Fund does – observe the UN's Principles for Responsible Investment (PRI). Within the twelve months since the launch of PRI, 215 organisations from 28 countries have chosen to underwrite these principles.

The Second AP Fund's international investments are made in compliance with the UN's Global Compact and the OECD's Guidelines on Corporate Governance. This means, among other things, that the Fund may not invest in companies that breach certain principles.

The Principles for Responsible

Investment (PRI), which are based on the UN's Global Compact and which were an initiative of the former General Secretary of the UN, Kofi Annan, were launched in the spring of 2006. In brief, these PRI comprise a number of principles for governing companies' actions in areas such as human rights, labour law, environmental issues and problems associated with corruption. The Second AP Fund, which is one of the founding signatories, signed the Principles in 2006, in common with a number of the world's other major institutional investors.

Carbon Disclosure Project:

Trillions of reasons why multinationals should listen

The Carbon Disclosure Project (CDP) links 284 institutional investors worldwide. Including the Second AP Fund. These investors have combined total assets of more than SEK 280 trillion under management. The goal is to establish a dialogue with the world's largest companies, to gain a better understanding of the risks involved in climate change – and how to manage them.

On February 1st this year, the members of the Carbon Disclosure Project (CDP) sent a letter to 2 400 of the world's largest, quoted corporations. In this letter, the signatory investors invited each corporation to supply relevant data on the risks faced and opportunities anticipated due to climate change. The questions addressed topics such as the intensity of companies' greenhouse gas (GHG) emissions, their gas emission management activities, innovations for managing climate impact, and energy costs.

The result of this questionnaire is scheduled for publication in September 2007. Publishing the data is intended to

act as a catalyst. If influencers of public opinion such as journalists, analysts, politicians and consultants are given free access to the data, it can be disseminated more widely and strike sparks in other sectors of society.

IT ALL STARTED AT 10 DOWNING STREET CDP has turned the blowlamp on the world's largest companies since December 2000, when the Project was launched at 10 Downing Street, in London. The first letter to be dispatched was signed by 35 institutional investors. Since then, this has grown to almost seven times the original number. And over the years, the CDP has

become the "gold standard" in how emissions data should be managed. The CDP website comprises the world's largest database on the greenhouse gas (GHG) emissions generated by the world's corporations.

Right from the start, the companies expressed a fairly keen interest in participating. No less than 71 percent answered the letter, 45 percent of whom filled in the entire questionnaire. In the 2006 questionnaire, the number of responses had risen to 91 percent and the number that filled in the entire questionnaire was an impressive 72 percent.

The car won them the award

The Gothenburg International Environmental Award, of which the Second AP Fund is a sponsor, has been presented annually since the year 2000. The list of recipients features both known and unknown environmental heroes and heroines. The most recent recipients were three technology boffins who invested all they had to develop the hybrid car known as the Toyota Prius.

The engineers who created the Toyota Prius are Takeshi Uchiyamada, Takehisa Yaegashi and Yuichi Fujii. Cooperating with Toyota's management, they were determined to create an effective hybrid car. And they created a worldwide bestseller. By the end of 2006, more than half a million examples of the Prius had been sold – in Europe alone!

To top it all, the trio also received the Gothenburg International Environmental Award, worth a million kronor, presented at an award ceremony held at Gothenburg's Municipal Theatre in autumn 2006.

SUPPORT FROM THE TOP

The three engineers were part of a project team, backed by Toyota's top management,

which as early as 1993 had made the daring decision to develop and manufacture a car of the future that would consume half the fuel of contemporary models and generate considerably fewer emissions than was thought possible at the time. And they succeeded.

The Prius has already set the style for all other hybrid-based cars, buses and trucks.

SPONSORED BY THE SECOND AP FUND

The Gothenburg International Environmental Award is sponsored by the City of Gothenburg and ten corporations, including the Second AP Fund. The board comprises Göran Johansson, Helene Odenjung, Kia Andreasson and Carl Bennet.

Those who plan to become Award recipients have to achieve something truly exceptional. The Award is given to those who create a product, service or systems technology that provides a solution to a specific problem area, that can lead to a technical breakthrough or "system change" both in Gothenburg and in the international arena, as well as contributing to the development of greater global justice.

Recipients of the Gothenburg International Environmental Award 2006:

Takeshi Uchiyamada, Takehisa Yaegashi and Yuichi Fujii, Japan

AP2 raises its voice

VOTING AT SWEDISH AGMS 2006/2007

During the period July 1st 2006 to June 30th 2007, the Second AP Fund has exercised its voting right at 49 AGMs in Swedish quoted companies. In three instances, the Fund voted against board proposals at an AGM. In the case of Lundin Petroleum, the Fund voted against a proposal concerning a new share issue. At the Securitas AGM, the Fund voted against the proposed spin-off of a subsidiary, where shareholders were to be issued shares as per voting right rather than true economic worth. The Fund's reasoning was the same as in the earlier case of the Husqvarna spin-off. At the Swedish Match AGM, the Second AP Fund voted against proposals concerning a radical increase in the fees paid to members of the board, the adoption of new principles concerning directors' remuneration and a new incentive scheme for executive management. At Mandator's extraordinary AGM, the Second AP Fund voted in favour of a proposal for an alternative board, which failed to gain majority support. The list of AGMs at which the Fund was represented is given on the following page.

SECOND AP FUND PARTICIPATION IN NOMINATING COMMITTEES 2006-2007

The Fund has been represented on nominating committees in seven companies: Artimplant (chairman), Elanders, Haldex, Meda, SCA, Oriflame and Volvo (coopted). In companies where the Second AP Fund was represented on the nominating committee, the number of female members was 24.3 percent, as compared with 23.6 percent in 2006. The average for quoted companies in Sweden is 19.9 percent.

VOTING AT NON-SWEDISH AGMS 2007

During 2007, the Second AP Fund voted at 36 AGMs in non-Swedish companies. The selection was made based on the size of the holding, work carried out by the AP Funds' Joint Ethical Council or in collaboration with networks of investors outside Sweden.

FEW INITIATIVES FOR PROXY VOTING

The new Swedish Companies Act permits

proxy voting. There is consensus among major investors that Sweden should make it easier for foreign investors to exercise their votes at AGMs. At present, the Swedish system for voting by proxy is extremely unwieldy and complicated, when compared to other countries.

Even so, there is considerable anxiety that poorly informed foreign investors with limited knowledge of Swedish corporate law will continue to vote against items such as granting the board discharge from liability. Approval of this item is necessary for Swedish limited liability companies, but can appear strange when seen from an American judicial perspective. There is an urgent requirement to inform foreign investors about the Swedish system, and the Swedish Corporate Governance Board has taken such an initiative.

So far, Nordea, TeliaSonera, Swedish Match and Eniro are the only companies to have altered their articles of association to permit proxy voting.

SAFEGUARDING SHAREHOLDER RIGHTS

The Second AP Fund collaborates with a network of other investors to safeguard the rights of minority shareholders. The Fund has been engaged in a number of initiatives over the year.

SWEDISH CONSOLIDATION RULES

In recent years, "creative" advisors, partly thanks to changed tax regulations, have been able to circumvent the so-called 90-percent rule governing compulsory acquisition in connection with corporate acquisitions. This has been made possible by exploiting consolidation rules that require no more than a two-third majority. During 2006, bidders for Capio, Gambro, Semcon and Cybercom, for example, indicated their willingness to adopt this method – probably as a way to reduce bid premiums. In these instances, the Swedish Securities Council has expressed no objections in principle, although legislation to prevent circumvention of the 90-percent rule has been on the cards.

After considerable effort by major

Swedish institutional investors, including lively correspondence with the Swedish Securities Council, joint responses to the issue and the publication of a leading article, legislation to plug this loophole was finally introduced in early 2007.

ACTIVE GOVERNANCE IN HUSQVARNA YIELDS RESULTS

The Second AP Fund tabled its own proposal in connection with Electrolux' distribution of shares in its Husqvarna subsidiary. This proposal derived from the economic value attached to shares distributed to investors in a company, given the fact that the Swedish Companies Act states that all shareholders share equal rights to a company's economic worth. According to the Second AP Fund, Husqvarna departed from the equal treatment principle by issuing Class A and Class B shares. There have been a number of similar cases, where Class A shareholders have received significant premiums (as much as 30 percent) in connection with bids for the company. This issue is therefore important to protecting the rights of Class B shareholders.

The Second AP Fund's proposal involved a single series of shares, as opposed to two. The Board was unconvinced by the Fund's contention that all shareholders have equal rights to the economic worth of the company. On the other hand, Investor made a voluntary proposal to reform the way voting rights were structured in Husqvarna. According to this new structure, the number of Class A shares in Husqvarna were to be raised from 3 to 25 percent, by awarding Class B shares the right to convert to Class A shares. This proposal from Investor was approved at Husqvarna's AGM in 2007.

This means, in practice, that Class B shareholders' rights have been strengthened within the company. The reform of voting rights at Husqvarna has considerably enhanced the economic worth of Class B shareholders' investments.

ABLE TO NOMINATE BOARD MEMBERS IN USA

Traditionally, shareholders' rights in the USA have been weak, compared with

many other countries. For one thing, shareholders have in practice lacked any possibility of nominating their own representatives on the board. Many feel that this is one explanation for the inflated pay levels enjoyed by top executives in American companies, something that has spread to non-American companies too. In autumn 2006, Norska Statens Pensionsfond (Norwegian State Pension Fund), Britain's Hermes, Holland's ABP and PGGM (all of which are among Europe's largest pension funds) decided to pen a joint letter to America's SEC, requesting that these rules be revised, to grant shareholders the right to nominate their own candidates to company boards. Sweden's Second and Third AP Funds have sent similar letters.

ABLE TO VOTE ON REMUNERATION SYSTEM IN USA

In Great Britain, Holland, Australia and Sweden, shareholders are able to vote at the AGM concerning the principles applied to executive remuneration. The International Corporate Governance Network (ICGN), which organises the world's major pension and mutual funds, has been lobbying for the introduction of this right in the USA, in a move to restrain the explosive increase in executive pay levels. The Second AP Fund assisted in preparing the proposal submitted by ICGN, which was presented to Barney Frank, Chairman of the United States Senate Committee on Finance.

INITIATIVE

In 2006, the Second AP Fund and some 30 major fund managers became founding signatories of the PRI (Principles for Responsible Investment), principles established by the UN. A follow-up of compliance with these principles has been conducted in 2007 and published on the PRI website. The Joint Ethical Council of the AP Funds has also utilised the PRI's information forum.

The Second AP Fund has participated in the Carbon Disclosure Project too, an initiative in which some 100 major fund managers require the world's largest quoted companies to state their position on a number of issues related to the greenhouse effect. The Carbon Disclosure Project has opened a Scandinavian office, and plans to publish its first report in autumn 2007.

The Second AP Fund is also a member of the European Corporate Governance Institute in Brussels, which published a number of notable academic studies in the field of corporate governance, and of the Swedish organisation SNS Corporate Governance Network.

The Second AP Fund is even one of the sponsors of the major Gothenburg International Environmental Award, which in 2006 was presented to the engineers who developed the Toyota Prius hybrid-powered car.

EXCLUDED COMPANIES

Wal-Mart and Singapore Technologies are the only companies to have been excluded

from the Second AP Fund's investment universe. Singapore Technologies could potentially manufacture landmines, which contravenes the conventions relating to landmines to which Sweden has subscribed.

The Second AP Fund has stated its position about claims concerning Wal-Mart's offences against human rights in the work environment. Wal-Mart is the world's largest retailer, with sales of USD 285 billion in 2005.

Since 2003, the Second AP Fund has written letters, voted at AGMs and participated in an investor group in an effort to influence the company, but the company has failed to communicate any intention of changing its attitude to employee rights.

The Norwegian Council on Ethics, which advises the Norwegian Government Pension Fund (formerly the Government Petroleum Fund), has compiled comprehensive documentation that demonstrates how Wal-Mart severely and systematically breaches internationally recognized ethical norms.

Wal-Mart has been reported so often in connection with incidents concerning breaches of ethical standards, both within its own operations and in the supply chain, that it is beyond reasonable doubt that the company systematically pursues a labour policy that, in the Second AP Fund's view, is unethical. Consequently, in 2006, the board of the Second AP Fund decided to exclude the company from its investment portfolio.

Gothenburg, August 22nd 2007

Swedish AGMs at which the Second AP Fund exercised its voting rights:

ABB (proxy)	Electrolux	Intrum Justitia	Sandvik	Swedbank
Alfa Laval	Eniro	Investor	SCA	Swedish Match (extra)
Astra Zeneca (proxy)	Ericsson	Kinnevik	Scania	Swedol
Atlas Copco	Ericsson (extra)	Lundin Petroleum	SEB	Tele2
Axfood	Getinge	Mandator	Securitas	TeliaSonera
Balder	Gunnebo AB	Mandator (extra)	Securitas (extra)	TeliaSonera (extra)
Biotage	H&M	Meda	SHB	Trelleborg
Broströms	Haldex	MTG	Skanska	Volvo
Castellum	Husqvarna	Nordea	SKF	ÅF
Elanders	Industrivärden	Oriflame (proxy)	SSAB	

The Fund's governance activities in brief

The Second AP Fund shall through its actions actively promote sound practice in the areas of ethics, the environment and asset management, with the ultimate aim of enhancing the long-term value of the Fund's capital assets. The Fund adopts a number of different approaches in addressing governance issues, based on an in-house analysis of portfolio companies from an investor perspective. A description of the instruments employed in corporate governance is given below. A more comprehensive description may be found in the Second AP Fund's Corporate Governance Policy, which may be downloaded from www.ap2.se.

ANSWERS TO TEN QUESTIONS DETERMINE FUND'S ACTIONS

The Fund's actions are determined by ten key principles, each of which is subjected to thorough analysis. The process involves an analysis of structural issues (corporate structure, capital structure and shareholder structure); governance (board of directors, nomination process, executive management and executive remuneration); transparency (information, corporate communication, audits); investments (corporate acquisitions, divestments and investments); corporate culture and ethical, environmental and gender equality issues.

THE SECOND AP FUND

... gets in touch with companies directly if necessary

In companies where the Fund identifies a need for change concerning one or more of the ten principles, it attempts to establish contact at an early stage. This may even involve collaboration with other investors. The Second AP Fund believes that an ongoing dialogue with companies is invaluable in contributing to change that creates increased shareholder value, without thereby placing the Fund in an insider position.

... focuses on companies in which it can exert a major governance role

In Sweden, the Second AP Fund mainly becomes engaged in governance issues in companies in which it is one of the largest stakeholders or in which it has invested most. In cases where matters of principle are concerned, even where other portfolio companies are involved, the Fund may consider it important to make a stand.

The Second AP Fund believes that a clear majority interest is inappropriate due, for one thing, to the danger that a

high degree of active involvement in portfolio companies on the part of Fund personnel can have a limiting effect that risks undermining efficient portfolio management. The Second AP Fund shall not hold shares in an individual quoted company, Swedish or foreign, that correspond to more than ten percent of the voting rights. Outside Sweden, the Fund exercises its voting right at the AGMs of its 50 largest holdings.

As regard its holdings through mutual funds, private equity funds and share-index forwards, the Fund has neither the intention nor the possibility of adopting an active role as a shareholder. In cases where the Fund is informed of governance-related problems in such companies, any action will be taken will be determined by the nature of the case in question.

...excludes the portfolio company where the dialogue fails to produce the desired result
Should a suspicion arise that one of the companies in which the Second AP Fund has invested has been in breach of sound ethics, ignored important environmental considerations or has deviated in some serious respect from the desired governance principles, the actual state of affairs must be ascertained immediately. Should this suspicion be confirmed, the company shall be asked to provide immediate clarification and submit a plan of action to remedy the situation. In evaluating the situation, the Fund shall consider the nature of the event and any corrective measures that may have been taken, or are to be taken, to ensure that the problem does not recur. If the response is unsatisfactory, if corrective action is not implemented and if the nature of the event is sufficiently serious, the Second AP Fund shall divest itself of the holding as quickly as possible.

... participates in nominating committees and votes at AGMs

The Second AP Fund makes it a principle to participate in nominating committees in companies where it is one of the largest shareholders. When not represented on the nominating committee, the Fund submits its views via the chairman of the nominating committee. To avoid complicating the Fund's role as an active portfolio manager, Fund employees shall in principle not serve on the boards of quoted companies.

The Annual General Meeting of a company is its highest executive organ, and the Fund assumes that important decisions are well prepared prior to the AGM. The Second AP Fund shall participate in, exercise its voting rights at and, in some cases, also act at the AGMs of companies in which it has a significant interest.

... places the same high demands on holdings owned via external managers

When an external mandate is awarded for the active management of Fund assets, the Second AP Fund shall inform the selected manager about its current Corporate Governance Policy. If necessary, an ongoing dialogue shall be conducted with the portfolio manager concerning governance issues. The Second AP Fund always retains responsibility for governance matters, regardless of whether the corporate holdings form part of an in-house or externally managed portfolio.

SOURCES OF ADDITIONAL INFORMATION

- The Second AP Fund's Corporate Governance Policy,
www.ap2.se
- The Second AP Fund's 2006 Annual Report, parts 1 and 2,
www.ap2.se
- Presentation of the AP Fund's Joint Ethical Council,
www.ap2.se/upload/Presentation_ethical_council.pdf
- Orange Report, Swedish Pension System's Annual Report 2006,
www.forsakringskassan.se/filer/publikationer/pdf/paro6-e.pdf
- UN report "Responsible Investment in Focus:
How leading public pension funds are meeting the challenge",
in which the work of the Second AP Fund is presented,
www.unepfi.org/fileadmin/documents/infocus.pdf
- Presentation of the Principles for Responsible Investment,
www.unpri.org/files/pri.pdf
- Presentation of the Global Compact,
www.globalcompact.org/docs/about_the_gc/gc_brochure_final.pdf



Andra AP-fonden
Second Swedish National Pension Fund - AP2