

Semi-annual report January–June 2009

09

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Första AP-fonden (AP1) is one of five buffer funds in the Swedish pay-as-you-go pension system, and is regulated by the Swedish National Pension Funds Act. All monetary amounts in this report are expressed in Swedish kronor. Millions of kronor are abbreviated as SEK m and billions as SEK bn. Figures in brackets refer to 2008 unless otherwise stated. Internal data is used in the tables and diagrams in cases where no other sources are specified. For more information about Första AP-fonden visit the Fund's website, www.ap1.se.
The report has not been reviewed by the Fund's independent auditors.

The period in brief

- The global financial crisis and weak development in the real economy continued to impact the financial markets in the first half of 2009.
- On the upside, rising stock markets contributed to net investment income of SEK 11.5 billion for the first half of 2009, equal to a total return of 6.7 percent after expenses. Return before operating expenses was 6.8 percent.
- At 30 June 2009 Första AP-fonden had net assets under management of SEK 181.4 billion.
- Första AP-fonden has introduced a new investment model with a stronger focus on strategic allocation. The aim is to concentrate the Fund's resources in the area with the greatest influence on total return, in order to produce the level of return required by the pension system. As a consequence of the new investment model, the number of employees has been reduced.
- Operating expenses fell by approximately SEK 10 million to SEK 149 million. Measured in relation to the average value of the Fund's net asset, this represents an annual expense ratio of 0.17 percent.
- The Fund's equity exposure at 30 June 2009 was 56 percent, while exposure to the fixed income market was 39 percent and exposure to alternative investments was 5 percent. Currency exposure was 22 percent.

Positive value growth

Första AP-fonden's total return after expenses for the first half of 2009 was 6.7 percent, equal to net investment income of more than SEK 11 billion.

The financial markets started to rebound in the spring and a new sense of optimism is emerging. This may seem strange in light of the dismal development we see every day in the real economy, but the markets are forward-looking and tend to discount the future. Any predictions about the future are, by nature, hazy and speculative. This is especially true after the past year's financial system meltdown and the extraordinary actions taken by central banks and governments, the effects of which are difficult to assess, not least in a longer perspective.

There is reason for concern about how global economies will react to the strains caused by the necessary readjustment to more normal monetary and financial policy. Managing long-term pension assets in this environment is no easy task, but it is both exciting and stimulating, since new conditions create new opportunities. As a result, the ability to think along new lines and question the accepted truths is especially important today as we face a more uncertain future.

New investment model

In view of the challenges and opportunities inherent to long-term management of pension assets, Första AP-fonden has decided to channel most of its research resources to the Fund's strategic asset allocation, i.e. the overall mix of assets in the portfolio over time. Although the Fund has previously been successful in active management with an ambition to have higher return than an index, we are now reducing our emphasis on this area to enable the change and have also carried out a reorganization that will support the new focus. One effect of the reorganization is that some 20 employees left the Fund during the spring. Our new investment model not only gives us better scope to focus on the increasingly important asset allocation, but will also reduce our operating expenses by over SEK 100 million annually. The savings will be achieved mainly through lower personnel costs, a higher share of index management and lower transaction-related costs.

Furthermore, we are working together with the Second, Third and Fourth AP funds (AP2, AP3 and AP4) to identify additional efficiency gains through increased cooperation between the funds.

We will continue striving to raise the long-term share of real assets in our portfolio, such as equities and real estate. We will supplement the portfolio with international real estate and exploit the potential for opportunistic investments. The new investment model does not entail any change in our ambitions for alternative investments. Our cautious private equity strategy, to gradually increase our exposure to around 5 percentage points of the total portfolio, stands firm.

Active ownership

The Swedish Government's new guidelines for the AP funds state that "in companies where the AP funds have holdings directly or through another company, the AP funds and the company, in dialogue with other shareholders, should take measures to ensure that the guidelines are applied as far as possible." We will continue working with other shareholders and boards in the affected companies in a way that leads to respect and influence. This means that each company should feel confident that the Fund is acting in its best interests (and therefore also in the best long-term interests of current and future pensioners), and that the Fund is a realistic discussion partner that, after a process of give and take, can take responsibility for an agreement. As a result, Första AP-fonden will still be able to vote in favour of incentive schemes that do not meet the government guidelines if the proposal has been formed through constructive dialogue.

In the ethical and environmental area we have once again proven the success of our strategy to actively influence the companies where we have holdings through the AP funds' joint Ethical Council, together with other major pension managers, rather than selling the shares. Read more about our environmental and social governance activities on the Fund's website www.ap1.se.

A long-term perspective, commitment and cost-efficiency are the guiding principles for our ongoing efforts to create high returns for the pensioners of today and tomorrow.



Stockholm, August 2009

Johan Magnusson
Managing Director of Första AP-fonden

Greater flexibility in the long-term investment model

In the first half of 2009 Första AP-fonden implemented a new investment model, where the change is aimed at increasing the focus on strategic asset allocation. The guiding principles for the new model are long-term perspective, flexibility, commitment and cost-efficiency. The new model is even more clearly shaped by the Fund's mission in the pension system than its predecessor. According to the Fund's analyses of the Swedish pension system, the AP funds need to generate high long-term returns after expenses over time. Furthermore, analyses have been carried out to ascertain how Första AP-fonden – for the benefit of current and future pensioners – can best meet its return target without taking excessive risks.

Two fundamental changes have been made in Första AP-fonden's investment model as a result of the analysis – the focus in asset management and the methods for reallocation.

Focus on absolute return

The focus in asset management has shifted from active management to strategic allocation. Several studies show that up to 90 percent of an asset manager's return is determined by the chosen asset mix. In light of this, the Fund has decided to shift its focus to absolute return. Return in relation to a benchmark index will therefore be less important and the Fund will no longer use this as a sub-goal for its management.

In the first six months of 2009, much of the organization's energy has been devoted to finding the best way to implement the new model. During the spring the Fund carried out a reorganization that led to the redundancy of over 20 employees. The new investment organization is made up of four

investment units, all of which contribute to allocation decisions alongside their own management mandates. In addition to a reduction of up to 25 percent in operating expenses, fees to external asset managers and transaction-related costs will also decrease. All in all, it is estimated that the Fund's operating expenses will be reduced by more than SEK 100 million annually when the changes have been fully realized. As a consequence of the new investment model, the Fund has also revised its system for variable remuneration.

Target portfolio shows future direction

The methods for allocation between asset classes have also changed in the new investment model. The central aspect of the new model is the creation of a so-called target portfolio that establishes the mix of equities, bonds and alternative investments in the Fund's future investments as well as specifying the Fund's currency exposure. The target portfolio is based on a long-term analysis of the Swedish pension system and the level of return it requires over time. Long-term return must be at least 5.5 percent annually to minimize automatic balancing of the pension system as far as possible, which is why Första AP-fonden has chosen this as an explicit goal for asset management: *The goal for Första AP-fonden's asset management is to achieve a total annual return after expenses of 5.5 percent on the total portfolio measured over rolling five-year periods.*

In defining the target portfolio, the Fund also studies a number of different scenarios and analyses. These scenarios are formulated and discussed in the Fund's strategic committee, which is made of individuals from all internal investment units. The committee

regularly gathers information and assessments that serve as input data for analysis of existing and new strategies. In the target portfolio, possible scenarios are weighed together to create the allocation desired by the Fund within a time horizon of 12 to 18 months. The target portfolio is thus a forward-looking, desirable portfolio that specifies how the existing assets should be reallocated in the coming year. The strategic committee develops strategies and action plans to steer the Fund's portfolio toward the target portfolio, with consideration to market development and other conditions.

The target portfolio is reviewed at least once a year and the Fund's allocation unit is responsible for ensuring that such changes are prepared and implemented.

Performance measurement

The Fund's performance will be monitored in new ways. In addition to assessing whether the Fund has met its long-term return target, performance measurement will include a higher degree of qualitative analysis than before and will be based on several different approaches. The Fund's performance will be evaluated partly with the help of various statistical methods and comparisons with other possible investment alternatives and partly in relation to other similar funds around the world, including the Second, Third and Fourth AP funds.

On the whole, the new investment model will give Första AP-fonden better scope to generate high returns for current and future pensioners through a long-term perspective, commitment and cost-efficiency.

First half of 2009

Return

The global economy continued to contract throughout the first half of 2009. A combination of impaired economic development, declining GDP growth and falling inflation, with a risk for deflation, has led the central banks to lower their key interest rates and take other measures in the financial markets. Development in the US economy remains feeble and the Swedish economy also got off to a weak start in 2009. In the equity markets, however, price gains were positive in the first half of the year.

After the previous year's negative total return, the Fund posted a positive total return for the first half of 2009. Return after expenses for the first half of 2009 was 6.7 percent, equal to net investment income of 11.5 billion. Before operating expenses, return was 6.8 percent.

For the listed assets, which make up around 95 percent of total portfolio, return at the end of June 2009 was 7.5 percent before expenses. The unlisted assets, or alternative investments, which consist mainly of real estate companies and participations in private equity funds, returned -4.4 percent for the same period.

Equities

The equity markets recovered in the first half of 2009. All equity indices in the total portfolio showed positive returns, where the emerging markets, Sweden and the Pacific region showed the strongest growth. The Swedish stock market outperformed its European and US counterparts. Measured in Swedish kronor, however, the differences are smaller. The global index rose by 4.8 percent in local currency, while the Swedish stock market rallied by a full 23.8 percent. Emerging markets and the Pacific region generated returns of 29.6 and 17.2 percent, respectively. Return on the Fund's total equity investments in the first half of 2009 was 10.7 percent, equal to net investment income of SEK 10.0 billion.

Fixed income

Access to credit in the fixed income market began to ease, a trend that led to falling interest rates on credit-related securities and yielded substantial gains in certain segments of the credit market. In the first half of 2009 the Fund's fixed income investments produced a return of 3.1 percent, equal to net investment income of SEK 2.1 billion before operating expenses.

Foreign exchange

The foreign exchange market remained volatile during the period. In the first few months of 2009 the Swedish krona fell to new record lows, but has since then strengthened at the same time that confidence has returned to the financial markets.

In the first half of 2009 the Fund's open currency positions made a marginal positive contribution to the Fund's total return.

Alternative investments

The Fund's alternative investments include real estate holdings (mainly via Vasakronan), participations in private equity and hedge funds, and opportunistic investments. The Fund's participations in private equity funds consist partly of three customized mandates in the international market, and partly of direct fund holdings in the Nordic market.

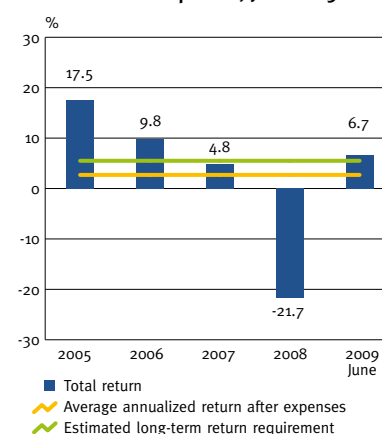
Return in the first half of 2009 was -4.4 percent, which is equal to a net investment loss SEK 400 million. The decrease is mainly explained by a write-down of close to 6 percent in the opening market value of real estate. Holdings in private equity funds have also been written down by SEK 195 million. In the other holdings, value gains/losses were limited during the period.

Net investment income, June 2009 ¹⁾	Market return, %	Contribution	
		SEK bn	%-points
Equities, Swedish	23.8	4.4	2.7
Equities, foreign markets ²⁾	2.9	2.2	1.3
Equities, emerging markets	33.3	3.5	2.2
Fixed income ²⁾	1.0	2.1	1.3
Allocation and foreign exchange		-0.1	-0.0
Total listed assets		12.0	7.5
Alternative investments		-0.4	-0.3
Total		11.6	6.8

¹⁾ Before expenses.

²⁾ Currency hedged return.

Total return after expenses, June 2005–2009



Operating expenses

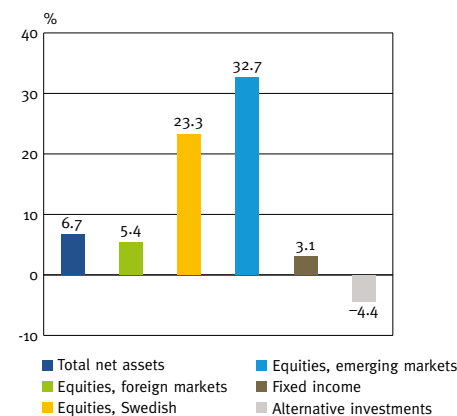
Operating expenses for the first half of 2009 totalled SEK -92 million (-94). Commission costs, i.e. fixed external management fees and custodian fees that are deducted directly from operating income, amounted to SEK -57 million (-65) for the same period. Measured in relation to the average value of net assets, this represents an annual expense ratio of 0.10 percent. If commission costs are also included, the Fund's expense ratio is 0.17 percent. As a consequence of the Fund's new investment model, the number of employees has been reduced and amounted to 44 (68) at 30 June 2009.

Net assets

At 30 June 2009 the Fund had net assets under management of SEK181.4 billion, an increase of SEK 9.8 billion since year-end 2008. The change consists mainly of the Fund's net investment income of SEK 11.5 billion. For the first time since the Fund's inception in 2001 the Swedish pension system showed a net outflow, causing the Fund's net assets to decrease by SEK -1.7 billion (including administrative contributions to the Swedish Social Insurance Agency, SSIA). The underlying reason is that birth cohorts from the 1940s are starting to retire to a greater extent. According to the SSIA's calculations, the contribution asset will continue to deteriorate until around 2020. In the mid-2040s, the contribution asset will once again be positive.

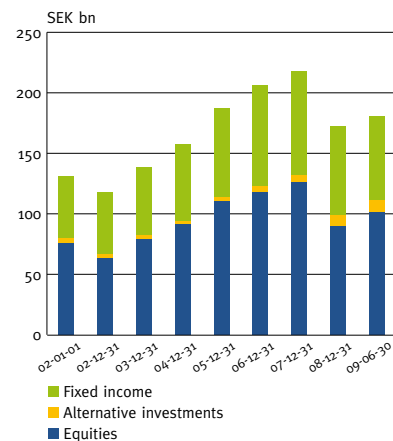
SEK return by asset class, June 2009

(local currency)

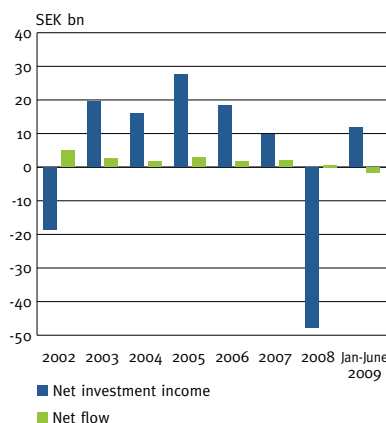


Development of net assets

(Including net flow to the fund 2002–2009 of SEK 19,2 billion)



Net investment income and net flow



Fund asset development

	2009 Jan-June
Net assets, SEK bn	
Opening net assets	171.6
Net pension contributions from SSIA ¹⁾	-1.6
Administrative contribution to SSIA ¹⁾	-0.1
Transferred from liquidation funds	0.0
Net investment income for the period	11.5
Closing net assets	181.4

1) Swedish Social Insurance Agency.

Five-year overview	Jan–June				
	2009	2008	2007	2006	2005
Net assets (at end of period), SEK bn	181.4	171.6	218.8	207.1	187.3
Net flow from/to the pension system, SEK bn	-1.7	0.9	2.0	1.7	2.9
Net investment income, SEK bn	11.5	-48.0	9.7	18.2	27.6
Total return before expenses, %	6.8	-21.7	4.8	9.8	17.5
Operating expenses, % of asset under management	0.10	0.09	0.08	0.08	0.08
Commission costs, % of asset under management	0.07	0.07	0.07	0.07	0.07
Return after expenses, %	6.7	-21.9	4.6	9.6	17.4
Inflation, %	-0.6	0.9	3.5	1.6	0.82
Real return after expenses, %	7.3	-22.6	1.1	8.0	16.6
Return and risk in the listed portion of the portfolio					
Return, % Portfolio	7.5	-22.4	4.4	9.2	17.0
Index	N/A	-21.7	4.0	8.6	15.5
Active	N/A	-0.7	0.4	0.6	1.5
Annualized risk (standard deviation), % Portfolio	12.9	18.0	7.9	6.8	4.9
Index	N/A	17.8	7.6	6.6	4.7
Active	N/A	1.0	0.5	0.6	0.4
Exposure, %					
Equities	55.9	54.6	59.2	59.8	58.6
Fixed income	37.8	40.1	39.2	37.8	34.3
Alternative investments	5.1	5.5	2.9	2.5	2.3
Currency exposure, %	22.1	22.2	18.2	16.0	20.0
Share of external management in total portfolio, %	41.8	39.7	36.0	34.2	37.7

Portfolio return, % before expenses	Jan–June				
	2009	2008	2007	2006	2005
Equities, Swedish	23.3	-40.0	-3.8	24.9	34.4
Equities, non-Swedish ¹⁾	3.5	-39.9	3.8	13.7	14.3
Equities, emerging markets	32.7	-41.5	30.6	12.5	62.5
Total equities	10.7	-40.1	4.7	16.1	22.1
Fixed income ¹⁾	3.1	8.3	4.2	1.3	4.0
Total listed assets	7.5	-22.4	4.4	9.2	17.0
Alternative investments	-4.4	-3.5	18.6	38.4	47.6
Total return	6.8	-21.7	4.8	9.8	17.5

¹⁾ Currency hedged return with the exception of equities in emerging markets, where return is reported without hedging due to a lack of hedge opportunities.

Portfolio composition

At 30 June 2009, exposure to equities in the total portfolio was 56.0 percent (54.6). Exposure to the fixed income markets including cash/foreign exchange was 42.0 percent (40.1) and exposure to alternative (unlisted) investments was 5.1 percent (5.5). The Fund's

open currency exposure at the end of June was 22.1 percent.

Of the Fund's total net assets at 30 June 2009, 41.3 percent were under external management and were divided between 19 management mandates.

Portfolio composition

Asset class	Portfolio value ¹⁾	%	Exposure ²⁾	Portfolio value ¹⁾	%	Exposure ²⁾
	SEK m 30 June 2009			SEK m 31 Dec 2008		
		of net assets	%		of net assets	%
Equities						
Swedish	23,351	12.9	12.5	17,983	10.5	11.2
Non-Swedish ³⁾	64,323	35.5	36.0	60,966	35.5	37.2
Emerging markets	13,679	7.5	7.5	10,627	6.2	6.2
Total equities	101,353	55.9	56.0	89,576	52.2	54.6
Fixed income⁴⁾						
Nominal Swedish	26,243	14.5		22,835	13.3	
Nominal non-Swedish ³⁾	24,010	13.2		26,174	15.3	
Index-linked	18,408	10.1		18,112	10.6	
Total fixed income⁴⁾	68,660	37.8	41.0	67,120	39.1	40.1
Cash/foreign exchange³⁾	2,154	1.2	1.0	5,577	3.3	0.9
Total listed assets	172,167	94.9	98.0	162,273	94.5	95.6
Alternative investments	9,223	5.1	5.1	9,354	5.5	5.5
Total portfolio	181,390	100	103.1	171,627	100	101.1
Currency exposure	40,051		22.1	38,182		19.6

¹⁾ Market value of spot and derivative positions plus cash and cash equivalents.

²⁾ Also including the nominal amount of derivative positions with a market value of zero.

³⁾ Including 100 percent currency hedge.

⁴⁾ Managed as a single portfolio, for which reason no specification of exposure by type of security is possible. In calculating exposure to fixed income assets, consideration has been given to the interest sensitivity (duration) of the investments.

Management structure, 30 June 2009

Portfolio value, SEK bn	Internal	External
Allocation	0.0	
Equities, Sweden	23.4	
Equities, Europe	21.0	
Equities, North America		33.2
Equities, Pacific and Japan		10.1
Equities, emerging markets	1.6	12.1
Fixed income	57.3	11.3
Foreign exchange	2.1	
Alternative investments		9.2
Total	105.5	76.0

Currency exposure, SEK m	USD	GBP	EUR	JPY	Other currencies	Total
Net currency exposure, 30 June 2009	19,668	3,795	4,744	1,868	9,976	40,051
Net currency exposure, 31 Dec 2008	13,571	2,994	12,116	1,441	8,060	38,182
Net currency exposure, 30 June 2008	12,872	3,444	18,914	-5,175	10,700	40,755

Income statement

SEK m	30 June 2009	30 June 2008	31 Dec 2008
Operating income			
Net interest income	1,659	2,204	4,557
Dividends received	1,997	2,958	4,204
Net gains/losses, listed shares and participations	8,340	-23,350	-66,890
Net gains/losses, unlisted shares and participations	-594	-282	-1,331
Net gains/losses, fixed income assets	457	-969	937
Net gains/losses, derivatives	198	575	282
Net gains/losses, foreign exchange movements	-405	1,393	10,513
Commission costs	-57	-65	-139
Total operating income	11,595	-17,536	-47,867
Operating expenses			
Personnel costs	-58	-60	-116
Other administrative expenses	-34	-34	-64
Total operating expenses	-92	-94	-180
Net investment income	11,503	-17,630	-48,047

Balance sheet

SEK m	30 June 2009	30 June 2008	31 Dec 2008
Assets			
Shares and participations, listed	100,052	116,492	89,252
Shares and participations, unlisted	4,727	4,414	4,913
Bonds and other fixed income assets	76,381	75,795	78,174
Derivatives	1,899	1,587	2,340
Cash and bank balances	640	1,017	1,295
Other assets	1,219	7,956	813
Deferred expenses and accrued income	1,468	1,410	1,420
Total assets	186,386	208,671	178,207
Liabilities			
Derivatives	2,428	834	5,460
Other liabilities	2,556	5,985	987
Deferred income and accrued expenses	12	51	133
Total liabilities	4,996	6,870	6,580
Net assets			
Opening net assets	171,627	218,791	218,791
Net flow from/to the pension system	-1,740	628	831
Transferred from liquidation fund/special management fund	0	12	52
Net investment income for the year	11,503	-17,630	-48,047
Total net assets	181,390	201,801	171,627
Total net assets and liabilities	186,386	208,671	178,207

The applied accounting and valuation standards and definitions are presented in the Fund's annual report for 2008 www.ap1.se.

This report has not been reviewed by the Fund's independent auditors.