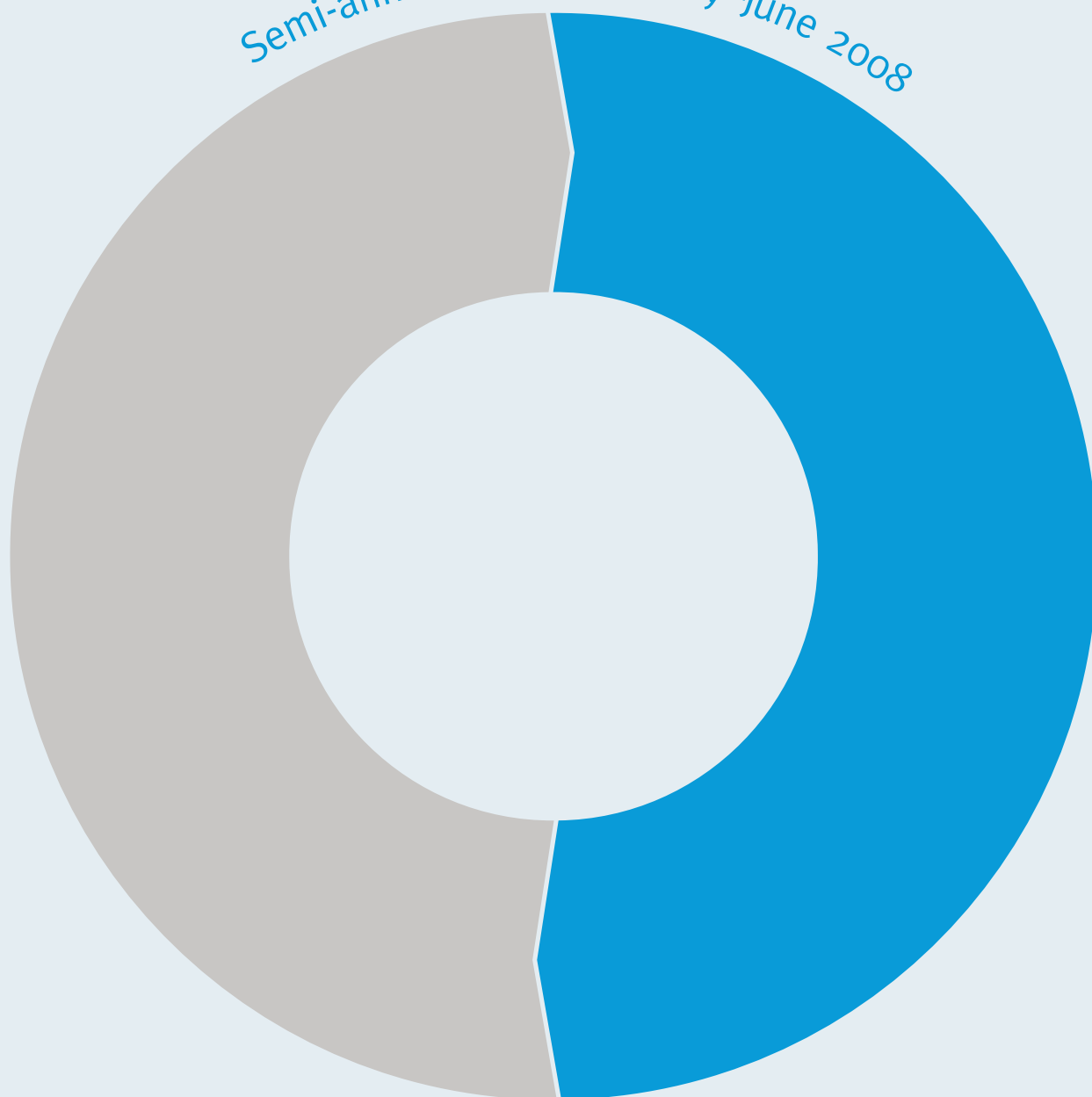


Semi-annual report January–June 2008



## Contents

A turbulent half year .....	3
Fund assets and performance .....	4
Return .....	5
Active management.....	7
Portfolio composition .....	8
Corporate governance .....	9
Income statement .....	10
Balance sheet .....	11
Glossary .....	12

Första AP-fonden (AP<sub>1</sub>) 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 2007 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](http://www.ap1.se).

## The period in brief

- In the wake of the US subprime mortgage crisis, the first half of 2008 was marked by severe financial turbulence, declining growth and fears of rising inflation.
- Falling stock markets were the main explanation behind the Fund's negative investment earnings of SEK -17.6 billion for the first half of 2008, corresponding to a total return of -8.1%. Return before operating expenses was -8.0%.
- Första AP-fonden's active management contributed 0.25 percentage points, or SEK 0.5 billion in investment income, to the Fund's total return. All investment units except one contributed positively to active return.
- At 30 June 2008 Första AP-fonden had net assets under management of SEK 201.8 billion.
- The Fund's equity exposure was 61%, while exposure to the fixed income market was 37% and exposure to alternative investments was 3%. Foreign exchange exposure was just over 20%.
- A new ALM study was completed during the period. The conclusion of the study is that the Fund should raise the share of real assets in the portfolio and increase its credit exposure.
- On 1 March 2008 Johan Magnusson succeeded William af Sandeberg as Managing Director of Första AP-fonden.

# A turbulent half year

In my first months as Managing Director the financial markets have been dominated by great uncertainty and high volatility, with a particularly steep dive in the equity market. This challenging climate is the main factor behind the Fund's negative value growth in the first half of 2008. However, the direct impact of the US subprime crisis on the Fund's fixed income portfolio has been limited thanks to our low exposure to credit risk and structured products.

While it is obviously negative for the Fund's asset value to fall in periods with bearish stock markets, this is also a logical consequence of our relatively high equity exposure. However, our mission to maximize long-term return with a low level of risk means that the Fund needs to maintain a high proportion of equities in order to capture the higher returns over time offered by the equity market relative to other assets, such as bonds. In the short term the Fund will occasionally post negative returns, as in the current period. However, it should be kept in mind that the Fund has delivered an annual return of nearly 12% for the past five years, which underlines the importance of evaluating the Fund's management over a longer time horizon. The Swedish Government's evaluation for the past five-year period indicates that Första AP-fonden has a competitive return in line with the established targets.

## Long-term asset mix

The Fund's single most important decision is the choice of long-term asset mix to ensure the best possible prospects of fulfilling our mission to the pension system. In the spring we completed a new ALM study to determine the Fund's optimal long-term asset allocation, where the conclusion was that the Fund should have a higher share of real assets in the portfolio. We believe that the time is right to gradually raise equity and credit exposure in the portfolio. AP Fastigheter's acquisition of Vasakronan is also well in line with our long-term strategy to increase the share of real estate.

Furthermore, the study indicates that less restrictive investment rules could improve our ability to produce high returns and thereby benefit the entire pension system. It is therefore my hope that our investment rules will be reviewed and revised.

## Strong management organization

We have every confidence in our investment model based on a large degree of active management to further boost return on net assets. It is therefore gratifying to note that the majority of investment teams have outperformed their indices both since the Fund's inception in 2001 and in the first half of 2008, which is an excellent track record. Our active management in the first half of 2008 generated earnings of SEK 500 million (0.25 percentage points), with the largest contribution from fixed income management.

Given the Fund's strong performance in active management, I naturally wish to continue enhancing the already positive investment environment so that we can achieve even higher returns. But it is at least equally important that we strengthen our focus on the strategic asset allocation and study the potential for further diversification of the portfolio.

## Active corporate governance

Since the beginning of 2007, analysis of the Fund's environmental, social and corporate governance (ESG) issues is carried out in cooperation with AP2, AP3 and AP4 through the Ethical Council. Already it is clear that this cooperation has enhanced our efficiency and widened our international network. The next step is to evaluate the scope to incorporate ESG issues into our daily investment decisions.

We remain committed to promoting shareholder scrutiny of corporate incentive schemes. Första AP-fonden favours the use of incentive schemes, but only to the extent that these are structured to meet shareholder requirements for enduringly profitable companies. In order for the boards to devise



*Johan Magnusson took over as Managing Director of Första AP-fonden on 1 March 2008. Photo: Bruno Ebrs*

effective incentive solutions, it is vital that earlier schemes are examined to understand what has worked well and what can be improved. As a result, in 2007 the Fund initiated discussions with the companies in which we have holdings regarding evaluation of incentive schemes and it is our ambition to extend and deepen this dialogue.

I feel great enthusiasm for the responsible task of managing the Swedish people's pension capital together with the Fund's skilled and dedicated staff.

Stockholm, August 2008

Johan Magnusson

# First half of 2008

## Net assets and earnings

At 30 June 2008 the Fund had net assets under management of SEK 201,801 million, a decrease of SEK 16,990 since year-end 2007. The change consists almost exclusively of the Fund's net investment income of SEK -17,630 million, since the capital inflow from the pension system and from the Fourth AP Fund's special management fund was limited to SEK 640 million.

### Net assets and investment income

	2008
SEK bn	Jan-June
<b>Opening net assets</b>	<b>218.8</b>
Contributed capital	0.6
Net investment income	-17.6
<b>Closing net assets</b>	<b>201.8</b>

## Operating expenses

Operating expenses for the first half of 2008 totalled SEK 94 million (82). Commission costs, i.e. fixed external management fees and custodian fees that are deducted directly from operating income, amounted to SEK 65 million (76) for the same period.

Measured in relation to the average value of net assets, this represents an annual expense ratio of 0.09% (0.08). If commission costs are included, the Fund's expense ratio is 0.15% (0.15). The number of employees at mid-year was 66 (64).

## Return

The first half of 2008 was a period defined by declining growth, inflationary fears and unrest in the financial markets. The weakening trend was most pronounced in the US market, but growth in Sweden has also decelerated noticeably. On the other hand, continued buoyancy in many emerging market economies has helped to curb the global slowdown.

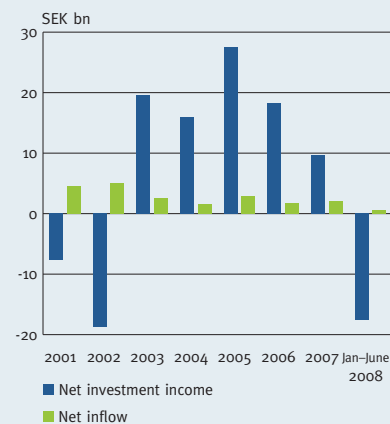
The financial unrest triggered by events in the US subprime mortgage market during the second half of 2007 caused prices on the international equity markets to plummet. This financial crisis has gradually also had repercussions on the real economy.

## Total return

Following several consecutive years of positive performance, the Fund has posted a negative total return for the first time since 2002 as a result of falling prices on the equity markets. Only fixed income and alternative investments generated positive returns in the first half of 2008.

Total return for the first half of 2008 was -8.0%, equal to net investment income of SEK -17.5 billion before commission costs and operating expenses. Return on listed assets, which make up close to 97% of the Fund's total portfolio, amounted to -8.3% during the period. The remainder of the portfolio consists of alternative investments, primarily securities in unlisted real estate companies and participations in private equity funds, which returned 1.6%.

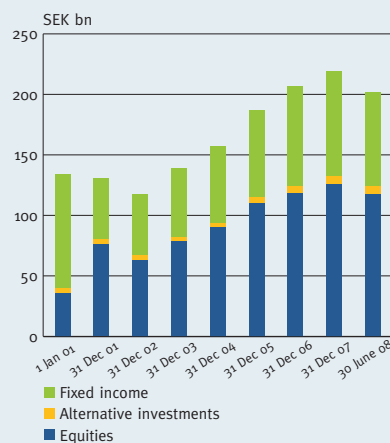
### Net investment income and net inflow



Total return Jan-June 2008	Contribution to return investment income %	SEK bn
Equities, Swedish	-2.3	-5.0
Equities, non-Swedish	-4.8	-10.7
Equities, emerging markets	-1.1	-2.4
Fixed income	0.7	1.6
Asset allocation and foreign exchange	-0.5	-1.1
Alternative investments	0.0	0.1
<b>Total excl. operating expenses</b>	<b>-8.0</b>	<b>-17.5</b>

### Development of net assets

(including a net inflow of SEK 21 bn to the Fund in 2001-2008)



**Equities**

Price volatility in the global equity markets was substantial in the first half of 2008. Return was negative in virtually all major equity markets, with the weakest development in Europe and Asia. Overall the global index declined by 11% measured in local currency. The Swedish stock market fell more steeply, by close to 20%, over the same period. Development by sector has varied widely. High raw material prices pushed up indices for Energy and Materials by 8%, while Financials dropped by 22% during the period.

Return on the Fund's total equity investments in the first half of 2008 amounted to -14.0%, equal to SEK -18.0 billion before operating expenses.

**Fixed income investments**

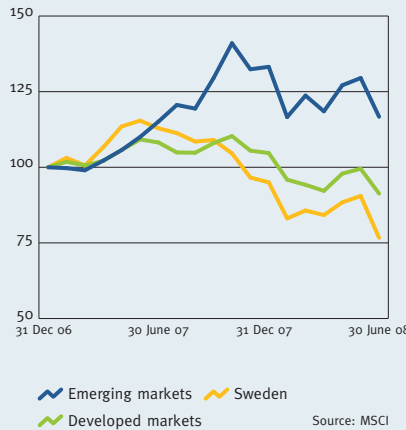
Long-term interest rates dipped during the first quarter but then rebounded somewhat in the second. At the mid-year shift, bond rates were up somewhat from the beginning of the year. The financial turmoil that arose in the residential mortgage market during 2007 has affected valuation of more high-risk bonds so that these continue to produce weak returns. However, the Fund's fixed income portfolio has not incurred any credit losses as a result of the mortgage crisis.

In the first half of 2008 the Fund's fixed income investments yielded a return of 1.9%, equal to investment income of SEK 1.6 billion before operating expenses.

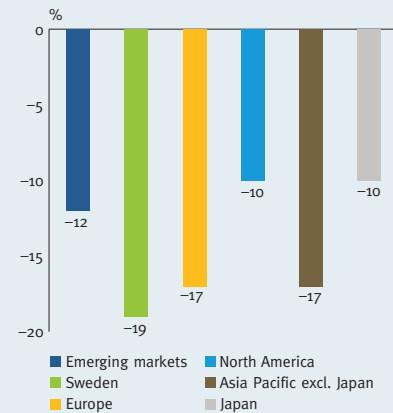
**Foreign exchange**

In the first half of the year the US dollar lost ground against the majority of developed currencies, including the Swedish krona. Against the euro, however, the Swedish krona weakened only marginally. The earnings impact of the Fund's open currency positions in the first half of 2008 thus made a negative contribution to the Fund's total return.

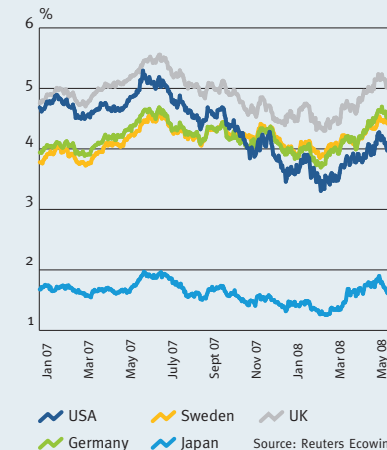
**Stock market development**  
(local currency; index=100 January 2007)



**Return on equities, Jan-June 2008**  
(local currency)



**10-year bond rates**



**Alternative investments**

The Fund's alternative investments consist of holdings in AP Fastigheter, three investments via specially tailored fund-of-fund solutions in the international venture capital market, a couple of smaller holdings in two Swedish venture capital funds with a Nordic focus and participations in the Cevian Capital 1 and 2 hedge funds. Alternative investments generated a return of 1.6%, equal to investment income of SEK 0.1 billion before commission costs and operating expenses. Value gains/losses in the various programs were limited in the first half of the year.

Five-year summary	Jan-June				
	2008	2007	2006	2005	2004
Closing net assets, SEK bn	201.8	218.8	207.1	187.3	156.8
Net inflow, SEK bn	0.6	2.0	1.7	2.9	1.6
Net investment income, SEK bn	-17.6	9.7	18.2	27.6	15.9
Total return before expenses <sup>1)</sup> , %	-8.0	4.8	9.8	17.5	11.4
Active return before expenses <sup>1)</sup> , %	0.2	0.4	0.6	1.5	0
Expense ratio, total, %	0.15 <sup>2)</sup>	0.15	0.15	0.15	0.17
Expense ratio excl. commission costs, %	0.09 <sup>2)</sup>	0.08	0.08	0.08	0.09
Active risk, realized, %	0.5	0.5	0.6	0.4	0.3
Currency exposure, %	20.2	19.2	16.2	20.5	20.9
Share of active management <sup>3)</sup> , %	99.4	97.5	98.0	94.8	77.4
Share of external management, %	35.9	36.0	34.2	37.7	24.0

1) Active return refers to the listed portion of the portfolio.

2) Annualized rate.

3) Including enhanced mandates.

Portfolio return, %	Jan-June				
	2008	2007	2006	2005	2004
Equities, Swedish	-17.9	-3.8	24.9	34.4	26.6
Equities non-Swedish <sup>1)</sup>	-12.3	3.8	13.7	14.3	12.1
Equities, emerging markets	-16.7	30.6	12.5	62.5	15.8
<b>Total equities</b>	<b>-14.0</b>	<b>4.7</b>	<b>16.1</b>	<b>22.1</b>	<b>15.5</b>
Fixed income <sup>1)</sup>	1.9	4.2	1.3	4.0	6.9
<b>Total listed assets</b>	<b>-8.3</b>	<b>4.4</b>	<b>9.2</b>	<b>17.0</b>	<b>11.4</b>
Alternative investments	1.6	18.6	38.4	47.6	13.2
<b>Total return</b>	<b>-8.0</b>	<b>4.8</b>	<b>9.8</b>	<b>17.5</b>	<b>11.4</b>

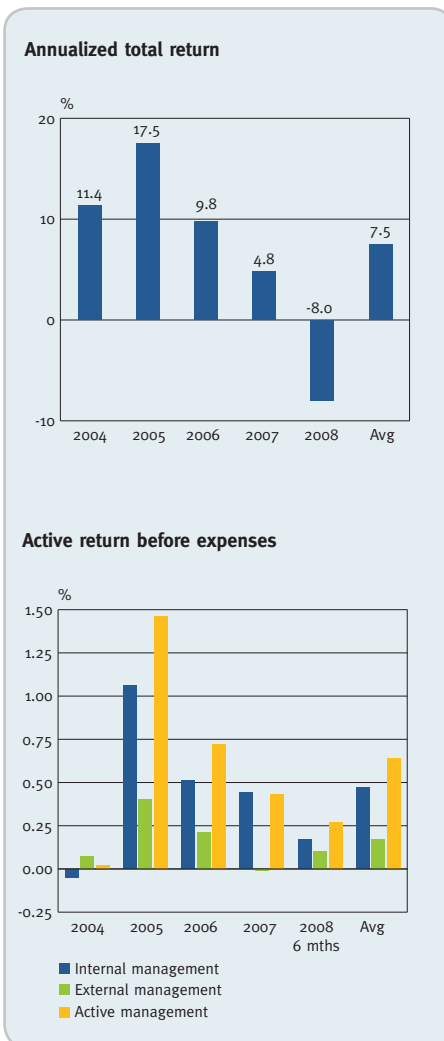
1) Currency hedged return.

**Active management**

The Fund's investment model is based on a large degree of active management, where the goal is to outperform return on the strategic benchmark. In the first half of 2008 the Fund earned a return on listed assets of -8.3%, compared to -8.5% for the strategic benchmark. Active return thus amounted to 0.25 percentage points, which is on par with the annual target of at least 0.5 percentage points. The period's active return for the first half of 2008 is equal to investment gains of approximately SEK 0.5 billion.

The Fund's active return is generated in six investment units. In the first half of 2008 all investment units except one made a positive contribution to the Fund's total active return. The largest contribution came from the Fund's fixed income management.

The Fund's active positions give rise to active risk, i.e. fluctuations in return caused by over- and underweights relative to the strategic benchmark. Active risk is an important metric that is both measured historically and forecasted continuously. The Fund's realized active risk during the period was in the range of 0.3-0.7% and averaged at 0.5%.



# Portfolio composition

Until 2008 the Fund's long-term investment orientation, the strategic benchmark, was largely based on the ALM study performed by the Fund in connection with the Swedish parliament's decision to reorganize the AP funds in 2001. A new ALM study was completed in the first half of the year and its conclusions were that the Fund should raise the share of real assets in the portfolio and increase its credit exposure.

At 30 June 2008 the market value of the Fund's net assets was SEK 201.8 billion. The total portfolio consisted of 61% equities (59), 37% fixed income investments including cash and foreign exchange (40), and 3% alternative (unlisted) investments (3). Currency exposure at 30 June was just over 20% (19).

The Fund's net investments in the first half of 2008 amounted to SEK 0.6 billion,

equal to the year's capital inflow from the pension system and Fjärde AP-fonden's special management fund.

Of the Fund's total net assets, 97% were placed under active or enhanced management at 30 June. A combined 36% of the Fund's assets were under external management and were divided between 23 management mandates, of which 22 refer to equity investments.

## Portfolio composition

Asset class	Portfolio value <sup>1)</sup>	% of net	Exposure <sup>2)</sup>	Portfolio value <sup>1)</sup>	% of net	Exposure <sup>2)</sup>	Benchmark 30 June 2008, %
	SEK m, 30 June 2008	assets	%	SEK m, 31 Dec. 2007	assets	%	
<b>Equities<sup>3)</sup></b>							
Swedish	24,308	12.0	13.2	27,781	13.8	13.0	13.0
Non-Swedish <sup>4)</sup>	79,431	39.4	41.2	84,844	42.0	40.0	40.7
Emerging markets	14,122	7.0	7.0	13,597	6.7	6.2	6.5
<b>Total equities</b>	<b>117,861</b>	<b>58.4</b>	<b>61.3</b>	<b>126,222</b>	<b>62.5</b>	<b>59.2</b>	<b>60.2</b>
<b>Fixed income<sup>3)</sup></b>							
Nominal Swedish	24,495	12.1		19,061	9.4		7.8
Nominal non-Swedish <sup>4)</sup>	40,305	20.0		44,635	22.1		20.1
Index-linked	9,989	4.9		21,008	10.4		8.8
<b>Total fixed income</b>	<b>74,789</b>	<b>37.1</b>	<b>39.0<sup>5)</sup></b>	<b>84,704</b>	<b>42.0</b>	<b>39.2<sup>5)</sup></b>	<b>36.7</b>
<b>Cash and foreign exchange<sup>3)</sup></b>	<b>2,643</b>	<b>1.3</b>	<b>-1.7</b>	<b>1,405</b>	<b>0.7</b>	<b>0.7</b>	<b>0.0</b>
<b>Total listed assets</b>	<b>195,293</b>	<b>96.8</b>	<b>98.6</b>	<b>212,331</b>	<b>105.2</b>	<b>99.1</b>	<b>96.9</b>
Alternative investments	6,508	3.2	3.2	6,460	3.2	2.9	3.1
<b>Total</b>	<b>201,801</b>	<b>100.0</b>	<b>101.8</b>	<b>218,791</b>	<b>100.0</b>	<b>102.1</b>	<b>100.0</b>
<b>Currency exposure</b>	<b>40,755</b>		<b>20.2</b>	<b>41,930</b>		<b>19.2</b>	<b>15.2</b>

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

2) Also including the nominal amount of derivative positions with a market value of zero. In calculating exposure to fixed income assets, consideration has been given to the duration of the investments.

3) Including tactical and global macro allocation.

4) Including 100% currency hedge.

5) Managed as a single portfolio, for which reason no specification of exposure by type of security is possible.

# Corporate governance

## AGMs in spring 2008

To achieve a high long-term return, it is vital for the Fund to be an active owner. In keeping with this objective, during the first half of 2008 the Fund participated in all shareholder meetings of the Swedish companies in which it has significant holdings.

The AGM of Carnegie in April resolved on discharge from liability for the former board of directors. From a legal standpoint, the matter was complicated by the fact that the errors and deficiencies criticized by the Swedish Financial Supervisory Authority (FSA) took place in a subsidiary to the company. Nonetheless, Första AP-fonden's position was that responsibility for this should also have repercussions on the earlier board

of the parent company. The Fund – together with several other shareholders – therefore voted against discharge from liability for the former board that was criticized by the FSA (with the exception of one member). A sufficient number of shareholders at the AGM supported Första AP-fonden's demand and the AGM resolved to deny the former board discharge from liability. The new board of directors was instructed by the AGM to investigate whether the company should sue for damages from the earlier board members. Following two independent inquiries, the board found that the company should not sue for damages since the probable economic outcome would not outweigh the costs and other disadvantages arising from a lawsuit.

Although Första AP-fonden understands this conclusion, it would be preferable from a general perspective if the matter of board liability were tried in a court of law.

At the AGM of Lundin Petroleum in May, the board of directors did not present any proposal for resolution regarding an incentive scheme, despite the fact that the company had expressed intentions to implement one. In this respect, Lundin Petroleum has not acted in compliance with the Code of Corporate Governance. Furthermore, the incentive scheme as described at the AGM did not contain any performance criteria, which is contrary to Första AP-fonden's ownership policy. The Fund therefore voted against the board's proposed principles for remuneration to senior executives.

## Management structure, 30 June 2008

Portfolio value, SEK bn	Internal		External	
	Active	Passive	Active	Enhanced
Allocation <sup>1)</sup>	0.4			
Equities, Sweden	24.3			
Equities, Europe	29.5			
Equities, North America			3.8	32.7
Equities, Pacific and Japan		1.2	9.9	1.2
Equities, emerging markets			6.6	6.7
Fixed income	69.8			4.9
Foreign exchange <sup>1)</sup>	4.2			
Alternative investments			6.5 <sup>2)</sup>	
<b>Total</b>	<b>128.2</b>	<b>1.2</b>	<b>26.8</b>	<b>45.5</b>

1) These investments are made predominantly in derivative instruments.

2) SEK 4.7 billion refers to the Fund's investment in AP Fastigheter.

## Ethical and environmental responsibility

In accordance with the ownership policy, the Fund expects the companies it invests in to comply with the international conventions ratified by the Swedish Government. As in 2007, efforts to influence the companies in which the Fund has holdings were carried out mainly through the AP funds' joint Ethical Council. As part of this work, the Ethical Council published its first annual report describing the Council's objectives, methods and the companies with which it is currently engaged in dialogue. The report can be downloaded from the Fund's website [www.ap1.se](http://www.ap1.se).

Alongside the work of the Ethical Council, Första AP-fonden has conducted discussions with a handful of Swedish companies in issues related to their sustainability work. In June this year, the Fund also attended PRI's annual conference to share experiences with other asset owners, managers and consultants who have signed the UN's Principles for Responsible Investment.

Currency exposure	USD	GBP	EUR	JPY	Other currencies	Total
<b>Net currency exposure, 30 June 2008</b>	<b>12,872</b>	<b>3,444</b>	<b>18,914</b>	<b>-5,175</b>	<b>10,700</b>	<b>40,755</b>
Net currency exposure, 31 Dec. 2007	15,738	7,177	15,003	-2,528	6,540	41,930
Net currency exposure, 30 June 2007	12,727	7,436	10,200	-1,419	12,384	41,328

# Income statement

SEK m	Jan–June 2008	Jan–June 2007	2007
<b>Operating income</b>			
Net interest income	2,204	1,294	2,914
Dividends received	2,958	3,009	3,960
Net gains/losses, listed shares and participations	-23,350	10,069	2,616
Net gains/losses, unlisted shares and participations	-282	140	493
Net gains/losses, fixed income assets	-969	-2,332	727
Net gains/losses, derivatives	575	612	-388
Net gains/losses, foreign exchange movements	1,393	459	-338
Commission costs	-65	-76	-153
<b>Total operating income</b>	<b>-17,536</b>	<b>13,175</b>	<b>9,831</b>
<b>Operating expenses</b>			
Personnel costs	-60	-50	-102
Other administrative expenses	-34	-32	-62
<b>Total operating expenses</b>	<b>-94</b>	<b>-82</b>	<b>-164</b>
<b>Net investment income for the period</b>	<b>-17,630</b>	<b>13,093</b>	<b>9,667</b>

# Balance sheet

SEK m	30 June 2008	30 June 2007	31 Dec. 2007
<b>Assets</b>			
Shares and participations, listed	116,492	122,555	125,641
Shares and participations, unlisted	4,414	3,480	4,247
Bonds and other fixed income assets	75,795	89,824	85,592
Derivatives	1,587	2,185	2,437
Cash and bank balances	1,017	950	856
Other assets	7,956	3,178	359
Prepaid expenses and accrued income	1,410	1,699	1,616
<b>Total assets</b>	<b>208,671</b>	<b>223,871</b>	<b>220,748</b>
<b>Liabilities</b>			
Derivatives	834	660	1,601
Other liabilities	5,985	2,034	285
Accrued expenses and deferred income	51	45	71
<b>Total liabilities</b>	<b>6,870</b>	<b>2,739</b>	<b>1,957</b>
<b>Net assets</b>			
Opening net assets	218,791	207,105	207,105
Net inflow from the pension system	628	826	991
Transferred from liquidation fund/special management fund	12	108	1,028
Net investment income for the period	-17,630	13,093	9,667
<b>Total net assets</b>	<b>201,801</b>	<b>221,132</b>	<b>218,791</b>
<b>Total net assets and liabilities</b>	<b>208,671</b>	<b>223,871</b>	<b>220,748</b>

**The applied accounting and valuation standards and definitions are presented in the Fund's annual report for 2007, [www.ap1.se/2007](http://www.ap1.se/2007).**

As of 1 January 2008, management fees for unlisted assets for which the contracts permit a refund in the event of a future profitable exit and which are deemed probable are recognized together with the respective investment among unlisted assets in the balance sheet. These were previously recognised separately in "Other assets".

**The semi-annual report has not been reviewed by the Fund's independent auditors.**

# Glossary

**Active management**

The management of a portfolio where the objective is to diverge from a benchmark (i.e. to take active positions) in order to improve return on investment (opposite of passive management).

**Active return**

The difference in absolute return between a portfolio and its benchmark. The Fund calls its comparative index a benchmark index.

**Active risk**

The risk that arises due to active management. Most often measured at the standard deviation between the actual return and the benchmark return (i.e. the standard deviation of the active return), which is also known as tracking error.

**ALM study**

Asset Liability Modelling. A study aimed at determining the optimal long-term allocation of the investment assets in order to meet the Fund's commitments. The study is based on the Fund's obligations and the expected return, risk and correlations of different asset classes.

**Benchmark**

A reference index against which the rate of return for the strategic benchmark is compared. The benchmark is used to measure the Fund's performance.

**Duration**

A measure of interest rate risk. The change in the value of a fixed income security that will result from a 1% change in interest rates.

**Information ratio**

A risk-adjusted measurement of fund performance. The information ratio is equal to the active return of a portfolio divided by its tracking error.

**Intermediaries**

Institutions/companies that borrow money from the public/businesses and then lend it to others, such as the residential mortgage institutions in Sweden.

**MSCI**

Morgan Stanley Capital International, an international equity index.

**Passive management**

See active management.

**PRI**

The UN's Principles for Responsible Investment. For more information visit [www.unpri.org](http://www.unpri.org).

**Private equity**

Venture capital funds, indirect investments in unlisted equities.

**Strategic benchmark**

The long-term asset allocation that is deemed to best correspond to the Fund's overall objectives. The strategic benchmark is determined by the Fund's Board of Directors based on the results of ALM studies. The strategic benchmark then functions as the benchmark index against which the Fund's risk and return profile are compared. (For more information visit the Fund's website [www.ap1.se](http://www.ap1.se))