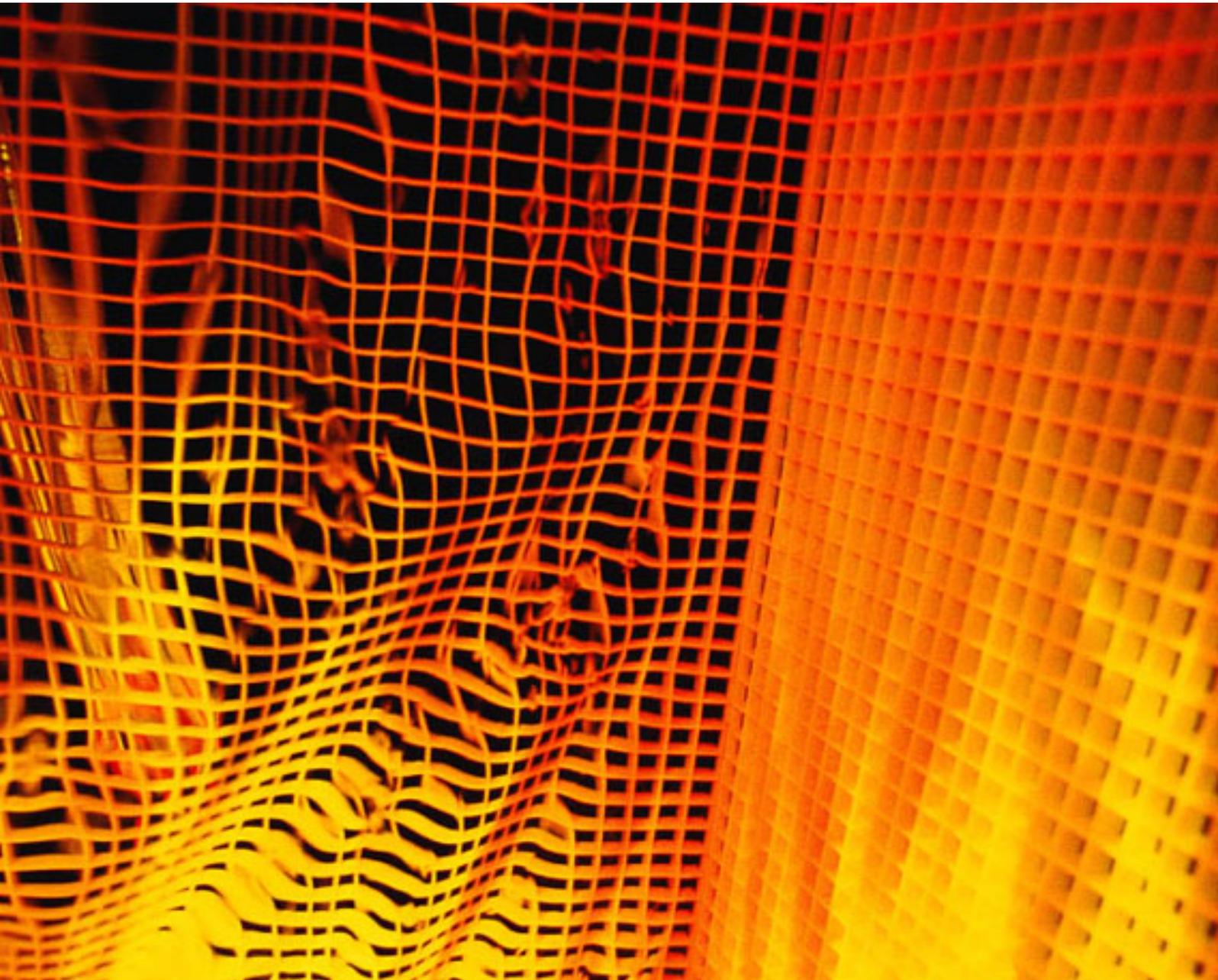




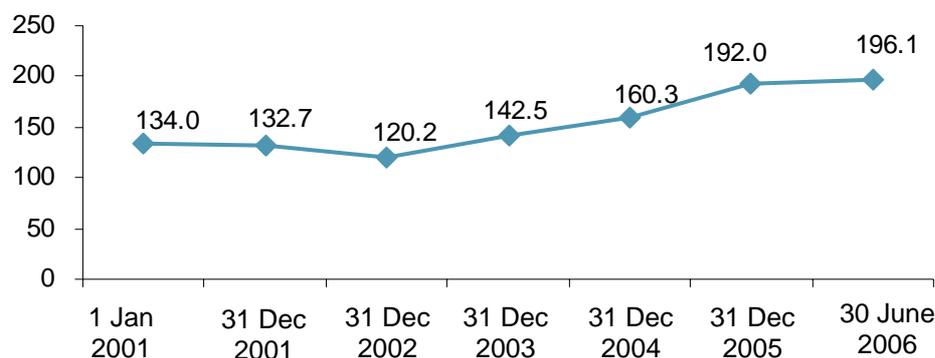
**Interim report 2006**  
**1 January - 30 June**



## Summary of six months ended 30 June 2006

- ◆ Turbulent equity markets and rising interest rates restricted gains in the AP3 portfolio during the first half of the year. Net profit totalled SEK 3.4 billion, corresponding to a return of 1.7% after expenses. Return before expenses was 1.8%.
- ◆ Fund capital stood at SEK 196.1 billion on 30 June, an increase of SEK 4.1 billion since the start of the year.
- ◆ The market-listed portfolio posted a return of 1.1% before expenses, which was identical to the benchmark index. As a result, active return was zero in the first half.
- ◆ Currency exposure was 13.9% at 30 June, compared to 14.7% at the start of the year.
- ◆ The Fund has generated total returns of SEK 44.7 billion since its inception in 2001, corresponding to an average nominal return of 4.8% per year. Of this increase, about SEK 3.0 billion is active return (outperformance of the index). Including net inflows, fund capital has risen by SEK 62.1 billion.

Fund capital, SEK billion



## Statement by the CEO

During the first half of the year AP3 succeeded in increasing the value of its portfolio in spite of tough market conditions, with falling equity markets and rising interest rates.

Macroeconomic and financial market developments came as no real surprise. As early as the start of 2005 our forecasts were indicating that a period of lower returns on financial assets lay in store. Our expectations were for interest rates to rise, the krona to appreciate and the dollar to weaken over a three-year horizon. We prepared for this by adjusting the portfolio to reduce risk in the fixed income portfolio and by decreasing currency exposure. In hindsight, this reallocation took place a little earlier than necessary. Not until the end of 2005 and first half of 2006 did our forecasts materialise.

Six months is a very short time for a long-term asset manager like AP3. I would therefore like to expand on the Fund's performance from a broader perspective. Between our inception in 2001 and 30 June 2006, AP3 has delivered total returns of SEK 44.7 billion, corresponding to a nominal annual return of 4.8%. In real terms (adjusted for inflation), the annual return is 3.3%. The contribution made by active management (our outperformance relative to the index) in the first five and a half -

years was SEK 3.0 billion, or 0.3 percentage points per year.

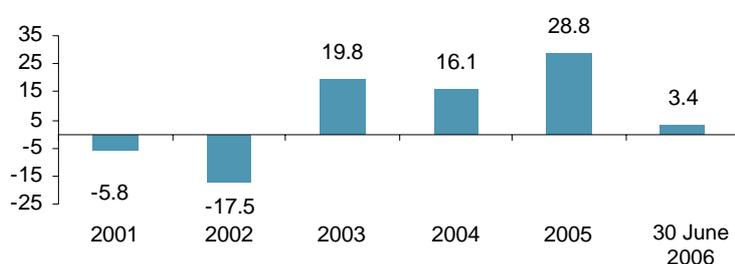
In a long-term context, I am pleased with the returns AP3 has generated for the pension system. Our strategy of putting strong emphasis on forward-looking analysis when selecting the strategic portfolio has proven successful and our day-to-day active management has generated considerable value.

The government review of the AP funds' operations in 2001-2005 notes that AP3's strategic decisions have generated substantial gains for the pension system and that AP3 has made the largest contribution to the system of any buffer fund. Moreover, the review shows that AP3's returns exceed those of the benchmark index by a certain margin after allowing for expenses.

The market trends of the last six months clearly demonstrate the advantages of our strategy of diversifying risk across a variety of assets and regions, combined with active asset allocation over the medium term. This approach is aimed at increasing income stability and securing higher returns for the pension system.

Kerstin Hessius  
CEO

**Total return after expenses, SEK billion**



## Fund capital

The market value of AP3's fund capital stood at SEK 196.1 billion on 30 June 2006. In the first six months of the year fund capital grew by SEK 4.1 billion, of which SEK 3.4 billion was net profit and SEK 0.7 billion was net inflows from the pension system.

Operating expenses for the first half were SEK 61 million, SEK 39 million of which

were staff expenses. In addition, AP3 has commission expenses of SEK 90 billion. These are expensed in the income statement and consist of fixed commissions for external mandates, agreed commissions for private equity funds, and custody account expenses. In the first half, AP3's asset management cost ratio was 0.15% including commission expenses and 0.06% excluding commission expenses.

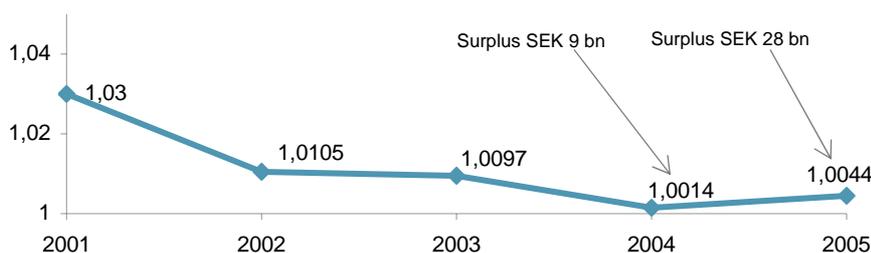
Changes in fund capital , SEK million	Jan-June 2006	Jan-Dec 2005
Fund capital at 1 Jan	191 950	160 254
Pension contributions	22 635	44 833
Pension disbursements	-21 827	-42 277
Administration fee to Swedish Social Insurance Agency	-149	-294
Transfers from phase-out funds	83	593
Net profit for the period	3 437	28 791
<b>Total fund capital</b>	<b>196 129</b>	<b>191 950</b>

## Swedish pension system annual report

In April the Swedish Social Insurance Agency published its annual report on the Swedish pension system for 2005. This reported a pension system surplus of SEK 28 billion, or 0.44%, at the end of 2005. During the year the AP funds generated a combined return for the system of SEK 115 billion, of which AP3's share was SEK 29 billion.

The returns of the buffer funds thus played an important role in guaranteeing the value of Swedish pensions. In its annual review of the AP funds' performance, the government noted that automatic balancing would have occurred in 2003 had it not been for the income generated by the AP funds.

### Pension system balance figure



## Portfolio and markets

AP3's portfolio	Exposure of portfolio, %	Market value at 30 June 2006, SEK bn	Portfolio return, Jan-June 2006, %	Index return, %	Contribution to absolute return, %
Swedish equities	11.5	22.6	4.2	4.1	0.5
Foreign equities <sup>1)</sup>	40.7	79.9	1.5	1.5	0.6
Fixed Income <sup>1)</sup>	43.0	84.3	0.0	-0.3	0.0
Tactical Asset Allocation, active currency management etc.	0.0	0.0			-0.1
<b>Total listed assets</b>	<b>95.2</b>	<b>186.8</b>	<b>1.1</b>	<b>1.1</b>	<b>1.0</b>
Real estate	2.4	4.8	18.8		0.4
Unlisted equities	2.3	4.5	16.9		0.3
<b>Total portfolio</b>	<b>100.0</b>	<b>196.1</b>	<b>1.7</b>		<b>1.7</b>

1) Foreign equities and Fixed Income include currency hedging.

The global economy during the first half of 2006 was dominated by higher interest rates, forecasts of increased inflation and fears of slower growth. Both long-term and short-term market interest rates rose and the return on AP3's fixed income portfolio was practically zero. At the same time, a narrower spread between short-term and long-term rates had a favourable impact on returns thanks to the Fund's decision to halve portfolio duration at the start of 2005. Had this strategy not been in place, the fixed income portfolio would have fallen in value.

A three-year upturn on equity markets ended with a sharp correction in May. After a recovery in June, equities ended the first half slightly higher in local currency terms

in all major markets bar Japan. However, the appreciation of the Swedish krona resulted in lower returns in domestic currency terms, especially for dollar-based investments.

The negative impact of a stronger krona was nevertheless limited by the Fund's decision at the start of 2005 to further reduce its currency exposure. This put the Fund underweight in currency risk and positioned us for a stronger krona. At the half-year mark, currency risk totalled 13.9% of the total portfolio, or SEK 27.2 billion, compared to a risk level of 14.7% at the start of the period.

## Private equity

The private equity portfolio generated a first-half return of 16.9%. During the period AP3 made nine new investment commitments totalling SEK 1.6 billion in private equity funds. The Fund has up to now made investment commitments to 63 funds. As of 30 June, these commitments were valued at SEK 10.8 billion (of which SEK 4.6 billion had been invested).

## Real estate

AP3's real estate investments consist of holdings in AP Fastigheter and timberland. AP Fastigheter performed strongly during the period, due primarily to an increase in the value of its real estate portfolio. The AP3 holding in AP Fastigheter was worth SEK 4.0 billion at the half-year point and generated a return of 19.3% for the period.

The Fund's investment commitments in timberland totalled SEK 1.0 billion on 30 June (of which SEK 600 million had been invested). The value of the Fund's holdings stood at SEK 760 million.

## Alternative investments

AP3 has two portfolios under construction in alternative investments: life science and infrastructure. The life science portfolio had a market value of SEK 349 million at 30 June. Investment commitments in infrastructure totalled SEK 600 million, of which SEK 50 million had been invested.

## Governance issues

AP3 exercised its voting rights at 69 AGMs in the first half of the year, which amounts to almost every company in our Swedish equity portfolio. Prior to the 2006 AGM season, the Fund was represented on the nomination committees of Nobia, Haldex, Swedish Match, Castellum and Ratos.

A more detailed account of AP3's corporate governance activities in connection with AGMs in 2006 can be found on our website at [www.ap3.se](http://www.ap3.se).

## Other events during the period

- ◆ At year-end AP3 began investing in emerging market equities in its strategic portfolio. Exposure to these markets at the half-year mark was SEK 5.3 billion, corresponding to around 5% of the Fund's total equity portfolio.
- ◆ AP3 is engaged in a continual effort to ensure cost efficiency across its operations. In the second half of the year we will focus on ensuring that our asset management structure (the allocation of active contra passive management) and selection of external managers creates an optimal balance between returns and expenses.
- ◆ A new system for measuring and tracking return and risk in the portfolio was purchased. The new system strengthens the Fund's analysis of market risks.
- ◆ AP3 signed the UN Principles for Responsible Investment (PRI), an initiative to encourage investors to integrate environmental, social and governance considerations in their financial analysis.
- ◆ The AP3 Board of Directors approved a global corporate governance policy for the Fund's foreign holdings.
- ◆ A performance-based remuneration system was introduced for all employees bar the CEO. It will entitle staff to a maximum bonus of two months' salary if they meet certain fixed targets and AP3 generates positive returns. The structure and extent of the programme fall within Ministry of Industry, Employment and Communications guidelines for state-owned companies. There have been no general salary increases in 2006.

## Full-year report

The full-year financial statements and annual report for 2006 will be published in February 2007.

# Income statement and balance sheet

## Income statement

SEK million

	Jan- June 2006	Jan- June 2005	Jan- Dec 2005
<b>Revenue</b>			
Net interest income	1 020	1 767	2 526
Dividens received	2 185	2 121	2 730
Net income from listed shares and units	1 738	6 476	19 181
Net income from unlisted shares and units	1 196	752	1 226
Net income from interest-bearing assets	-1 279	966	19
Net income from derivative securities	154	-308	744
Net income from currencies	-1 426	2 156	2 641
Net commission expenses <sup>1)</sup>	-90	-67	-149
<b>Total revenues</b>	<b>3 498</b>	<b>13 863</b>	<b>28 918</b>
<b>Operating expenses</b>			
Staff expenses	39	37	72
Other administrative expenses	22	28	55
<b>Total operating expenses</b>	<b>61</b>	<b>65</b>	<b>127</b>
<b>Net profit for the period</b>	<b>3 437</b>	<b>13 798</b>	<b>28 791</b>

1) Accounting principles, see next page

## Balance sheet

SEK million

	Jan- June 2006	Jan- June 2005	Jan- Dec 2005
<b>Assets</b>			
<b>Investment assets</b>			
Shares and units			
Listed	99 417	97 847	103 673
Unlisted	6 493	4 175	5 096
Bonds and interest-bearing assets	88 381	75 592	78 811
Derivatives	3 874	225	468
<b>Total investment assets</b>	<b>198 165</b>	<b>177 839</b>	<b>188 048</b>
<b>Receivables and other assets</b>			
Cash and cash equivalents	3 007	2 186	3 379
Other assets	1 754	233	216
Prepaid expenses and accrued income	1 549	1 460	1 669
<b>Total receivables and other assets</b>	<b>6 310</b>	<b>3 879</b>	<b>5 264</b>
<b>Total assets</b>	<b>204 475</b>	<b>181 718</b>	<b>193 312</b>
<b>Fund capital and liabilities</b>			
Derivatives	548	5 228	1 176
Other liabilities	7 667	595	47
Deferred income and accrued expenses	131	95	139
<b>Total liabilities</b>	<b>8 346</b>	<b>5 918</b>	<b>1 362</b>
<b>Fund capital</b>			
Fund capital at 1/1	191 950	160 254	160 254
Net payments from the pension system	659	1 553	2 312
Transfers from special asset management and phase-out funds	83	215	593
Net profit for the period	3 437	13 798	28 791
<b>Total fund capital</b>	<b>196 129</b>	<b>175 800</b>	<b>191 950</b>
<b>Total fund capital and liabilities</b>	<b>204 475</b>	<b>181 718</b>	<b>193 312</b>

## Changes in accounting principles

As of 2005, AP3 together with AP1, AP2 and AP4 adjusted their income statement formats to comply with the general standards for securities companies. The change means that all external costs directly related to asset management are expensed in the income statement. It came into effect for the first-half report of 2005.

As of the full-year report for 2005, the AP funds adopted new accounting principles that affect the presentation of variable commissions payable to external managers and the fees payable to private equity funds. The new principles seek to provide a more accurate picture of the funds' costs and to adapt their presentation to that of similar institutions in Sweden and abroad. As a result, variable commissions are recognised directly against net income for the asset class in which they arise and are not included under commission expenses. Comparative income statement figures for the first half of 2005 have been adjusted to reflect the new principles.

A more detailed explanation of the principles can be found on pages 50-51 of the 2005 annual report.

## Auditors' review

We have reviewed this interim report in accordance with the recommendations of FAR. Such a review is significantly less rigorous than an audit. Our review has given us no reason to believe that the interim report does not accord with the Swedish National Pension Funds Act.

Stockholm, 30 August 2006

Anders Bäckström  
Authorised public accountant

Anna Hesselman  
Authorised public accountant

# Summary 2001 - June 2006

	Jan-June 2006	Jan-Dec 2005	Jan-Dec 2004	Jan-dec 2003	Jan-Dec 2002	Jan-Dec 2001	Annualised 2001-June 2006 (5 1/2 years)	Accumulated 2001-June 2006 (5 1/2 years)	
<b>Income and inflows</b>									
<b>SEK billion</b>									
Net inflows from the pension system	0.7	2.9	1.7	2.6	5.0	4.5			
Net profit for the period	3.4	28.8	16.1	19.8	-17.5	-5.8			
Fund capital at end of period	196.1	192.0	160.3	142.5	120.2	132.7			
<b>Returns and expenses total portfolio <sup>1)</sup></b>									
<b>%</b>									
Return before expenses	1.8	17.9	11.4	16.4	-12.4	-4.1			
Operating expenses	0.06 <sup>1)</sup>	0.07	0.10	0.10	0.10	0.08			
Commission expenses	0.09 <sup>1)</sup>	0.09	0.11	0.08	0.04	0.00			
Return after expenses	1.7	17.7	11.2	16.2	-12.6	-4.2	4.8		
Inflation	1.0	0.9	0.3	1.3	2.1	2.7	1.5		
Real return after expenses	0.6	16.7	10.9	14.7	-14.4	-6.7	3.3		
<b>SEK billion</b>									
Return before expenses	3.5	28.9	16.3	20.0	-17.3	-5.7			
Expenses	0.06	0.13	0.28	0.24	0.18	0.11			
Return after expenses	3.4	28.8	16.1	19.8	-17.5	-5.8			
<b>Return and risk listed portfolio</b>									
Return %	Portfolio	1.1	17.3	11.4	17.2	-12.9	-4.4	4.7	28.8
	Index	1.1	16.1	11.4	17.3	-13.5	-4.6	4.4	26.6
	Active	0.0	1.2	0.0	-0.1	0.6	0.2	0.3	2.3
Risk (standard deviation) %	Portfolio	7.4	4.5	5.4	8.6	12.5	11.2	8.9	
	Index	7.2	4.3	5.3	8.5	12.6	10.9	8.8	
	Active	0.5	0.5	0.5	0.9	0.8	1.0	0.7	
Information ratio		0.0	2.2	0.0	neg	0.7	0.2	0.5	
Sharpe ratio		n/a	3.4	1.6	1.6	neg	neg	n/a	

1) For 2001-2004, return before expenses refers to return before all expenses. For 2005-2006 it refers to return after performance-based expenses.

## Summary 2001 - June 2006, continued

	Jan-June 2006	Jan-dec 2005	Jan-Dec 2004	Jan-Dec 2003	Jan-Dec 2002	Jan-Dec 2001	Annualised 2001-June 2006 (5 1/2 years)	Accumulated 2001-June 2006 (5 1/2 years)
<b>Currency exposure</b>								
% of strategic portfolio	13.9 <sup>2)</sup>	14.7 <sup>2)</sup>	19.3	10.8	9.6	7.7		
<b>Active management</b>								
% of total portfolio	80.4	74.1	87.8	80.6	84.8	73.9		
<b>External management</b>								
% of total portfolio	46.9	45.3	30.8	28.8	28.4	23.2		
<b>Asset management expenses</b>								
% of assets under management								
Operating expenses	0.06 <sup>3)</sup>	0.07	0.1	0.1	0.1	0.08		
Operating expenses + commission expenses	0.15 <sup>3)</sup>	0.16	0.21	0.18	0.14	0.08		
<b>Portfolio structure</b>								
<b>SEK billion</b>								
Total portfolio	196.1	192.0	160.3	142.5	120.2	132.7		
of which								
Swedish equities	23.0	30.7	27.3	23.8	19.4	23.8		
Foreign equities	84.0	80.2	61.7	57.0	48.2	44.6		
Nominal Swedish fixed income	17.7	25.6	28.4	25.6	19.7	23.2		
Nominal foreign fixed income	44.1	42.5	24.8	22.7	19.5	27.8		
Index-linked Swedish fixed income	12.0	6.7	6.7	10.2	9.8	9.5		
Index-linked foreign fixed income	10.5	1.9	7.9	0.0	0.0	0.0		
Real estate (incl. timberland)	4.8	4.4	3.5	3.2	3.6	3.8		
<b>Number of employees</b>								
	49	48	46	45	41	34		

2) Excluding exposure through SEK-listed companies with a foreign domicile.

3) Expenses converted to annualised rates.

## About AP3

AP3 is one of five national pension funds (known as AP funds) that manage the so-called buffer assets of the Swedish pension system. The assets of the AP funds serve as a buffer to even out any surpluses or deficits that arise in the pension system. The combined assets of AP1, AP2, AP3, AP4 and AP6 correspond to about 12% of the state's future pension liabilities. AP3's assets under management totalled SEK 196.1 billion on 30 June 2006.



**Third Swedish National Pension Fund** · PO Box 1176 · SE 111 91 Stockholm  
**Visiting address:** Vasagatan 11, Stockholm, Sweden  
**Phone** +46 (0)8-555 17 100 · **Fax** +46 (0)8-555 17 120 · [www.ap3.se](http://www.ap3.se)