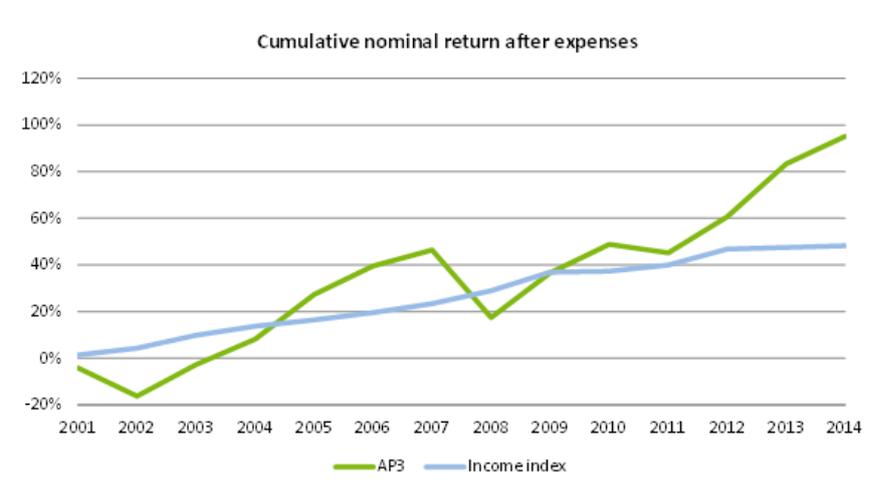


INTERIM REPORT 1 JANUARY – 30 JUNE 2014

Income of SEK 16.6 billion and a doubling of fund capital since inception

- **Profit for the six months ended 30 June 2014 totalled SEK 16,571 million (12,462)**, corresponding to a return of 6.5% (5.4) after expenses.
- **AP3 has generated average annual returns of 8.2% (8.5) in the last five years** and 6.4% (6.0) over 10 years, compared to annual increases of 1.6% and 2.5% in the income index in these respective timeframes. This represents considerable outperformance of the income index, which is used to keep pensions in line with inflation and a substantial contribution to the Swedish pension system during both periods.
- **Annual real return – return adjusted for inflation – was 7.2% (7.3) in the last five years** and 5.1% (4.7) over 10 years. Hence, the Fund has surpassed its real total return target of 4% per annum over time.
- According to an international study, **AP3's costs are 41% lower than the average** of a group of similarly sized pension funds. AP3's return after expenses over the last five years exceeded the combined return of the benchmark group by 21%, demonstrating the Fund's high level of cost-efficiency at the same time.
- AP3 is working **to continue to diversify the portfolio** and make it more robust. This is a gradual process that is being achieved by increased exposure to alternative investments such as real estate and infrastructure and higher exposure to risk premium strategies. We completed further investments in both these areas during the first six months of the year.
- **AP3 drives long-term sustainable value through a variety of activities.** The Fund has integrated sustainability in the investment process and during the period made new investments in green bonds via the Generation Climate Solutions Fund II. AP3 also has an outstanding investment in the Generations Global Credit Fund, which invests in fixed income markets based on a sustainability perspective.



FUND CAPITAL

Fund capital stood at SEK 272,579 million on 30 June 2014, an increase of SEK 14,104 million (9,332) from 1 January. During the period SEK 2,468 million (3,130) was transferred from fund capital to the Swedish Pensions Agency to help cover a shortfall between incoming pension contributions and outgoing pensions.

It should be noted that fund capital at the end of the period was more than double the figure at the Fund's inception in 2001. There has been a net outflow of funds to the pension system since 2009 due to incoming pension contributions being lower than paid-out pensions. Indeed, the total net flow since 2001 has been negative, resulting in AP3 making a net contribution to help cover the deficit between incoming pension contributions and outgoing pension commitments. This is a facet of AP3's role as a pension system buffer fund – a role that also includes stabilising pension outgoings by helping to ensure that pension system assets grow at least as fast as the income index, which is used as the basis for keeping pensions in line with inflation. AP3 has generated an average annual return of 8.2% (8.5) in the last five years and 6.4% (6.0) over the last 10 years. This compares to annual increases of 1.6% and 2.5% in the income index over these respective timeframes.

Change in fund capital in SEK million	Jan-Jun 2014	Jan-Dec 2013
Fund capital at 1 Jan	258,475	232,956
Pension contributions	29,304	56,839
Pension disbursements	-31,659	-63,488
Administration fee to Swedish Pensions Agency	-112	-230
Income for the period	16,571	32,398
Total fund capital at end of period	272,579	258,475

INCOME

AP3 reported income for the first six months of SEK 16,571 million (12,462), representing a return of 6.5% (5.4) before expenses and 6.5% (5.4) after expenses. Allowing for deflation of 0.1% during the period, the real return was 6.6% (5.6). In the last five and ten years, the Fund has generated real returns of 7.2% (7.3) and 5.1% (4.7) respectively, thus surpassing its long-term target of a 4% annual real return.

AP3 measures the portfolio against a long-term static portfolio (LSP) consisting exclusively of listed equities and fixed income assets. The LSP has an asset allocation geared to achieving a real return of 4%. Projections of returns on the different asset classes are based on long-term series of historic data and thereby qualify as generally acceptable financial market forecasts. The aim of the LSP process is to examine whether AP3's strategy of implementing a more diversified and advanced portfolio structure is successful over time. AP3 continued to outperform the LSP during the first six months of 2014. The LSP was introduced in 2012 and AP3 has subsequently outperformed it by approximately 5 percentage points¹.

Return

AP3 divides portfolio assets into seven risk categories. Allocating the portfolio on these lines enables us to analyse and project future returns and risk in the different asset categories and their contributions to the total portfolio. These projections, combined with macroeconomic analysis, valuations and assessments of investors' risk appetite, form the basis for asset allocation.

¹ AP3's income after expenses is shown, while the LSP does not include transaction or asset management expenses.

Return per risk category 30 June 2014	Return in percent	Contribution to total return in percentage points
Equities	6.5	3.2
Fixed income	4.7	0.9
Credits	2.2	0.2
Inflation	4.7	0.9
Currencies	-	1.0
Other exposure ⁱ	-	0.1
Absolute return strategies ⁱⁱ	-	0.2
AP3 total	6.5	6.5

ⁱ Other exposure consists largely of derivative holdings, which means return cannot be fairly measured.

ⁱⁱ Absolute return strategies consist of risk mandates to which no capital is allocated and for which return can therefore not be fairly measured.

The **equities** risk category reported a return of 6.5% (8.6) in the six months and was the largest contributor to total portfolio return. Equity markets gained ground steadily during the period, with the Swedish market posting a strong rise of 8.3% including dividends, and the US and European markets gaining 7.4% (in local currency terms) and 6.3% respectively. By contrast, Japanese equities fell by 3.0% during the period. As at 30 June listed equities comprised 46.2% of the total portfolio, with Swedish equities accounting for 11.0 percentage points of this figure. The ratio of unlisted equity amounted to 3.8%.

The **fixed income** risk category, which consists primarily of investments in government bonds, produced a return of 4.7% (-0.6) during the period. Average duration, or date to maturity, of the fixed income portfolio was 6.7 years (3.0). Bond prices, particularly prices of Swedish bonds, rose steadily throughout the period, with the yield on Swedish 10-year bonds falling by around 0.7 percentage points. This outcome was beneficial because AP3 has held the majority of its fixed income exposure in Swedish bonds.

The **credits** risk category primarily comprises mortgage bonds and investment grade corporate bonds in Sweden and the US. It reported a return of 2.2% (1.1). Average duration of the credits portfolio was 3.2 years (2.0). The modest return reflected the Fund's cautious approach to this investment class.

The **inflation** risk category, which consists of investments in index-linked bonds, real estate, infrastructure assets, timberland and agricultural land, generated a return of 4.7% (2.9). The international real estate portfolio performed particularly well during the period.

The **currencies** risk category groups the Fund's currency exposure, which is primarily used as a tool to diversify overall portfolio risk. The weakness of the Swedish krona on international markets during the period had a significant and beneficial effect on return from currency exposure. Income from currencies contributed 1.0 percentage points (0.3) to total income for the period. Among the major currencies, the Japanese yen and British pound strengthened by 8.0% and 7.5% percent respectively against the krona. The US dollar, euro and most emerging-market currencies also gained ground against the krona.

The **other exposure** risk category consists mainly of investments in insurance-related bonds and risk premium strategies. Since much of this exposure is in derivatives, it is not practicable to calculate the return on invested capital. This risk category contributed 0.1 percentage points (0.2) to total return.

The **absolute return strategies** risk category covers mandates that set out to generate an absolute return. Here, capital allocations are limited and the board of directors assigns risk mandates to managers. The 30 or so mandates are managed both internally and externally. Income from absolute return strategies totalled SEK 477 million (243) during the period, contributing 0.2 percentage points (0.1) to total return.

Exposure

Exposure is defined as underlying value that is subject to changes in value arising due to market movements. AP3's exposure can be greater or smaller than underlying fund capital because derivatives are used to manage risk and ensure efficient asset management. The Fund's total exposure at 30 June was 104.0% (108.5) of fund capital. Derivatives can be an effective way to rapidly adjust the portfolio to new realities during periods of volatility on the capital markets.

Risk category 30 June 2014	Exposure, SEK m	Exposure, %
Equities	133,536	49.0
Fixed income	61,930	22.7
Credits	21,043	7.7
Inflation	47,620	17.5
Currencies ¹	64,129 ¹	23.5
Other exposure	8,532	3.1
Absolute return strategies	10,685	3.9
AP3 total	283,346	104.0

¹ Currency exposure is shown as the portion of fund capital that is unhedged and cannot be added to other exposure.

AP3 gradually scaled back its equity exposure during the period, from 52.6% on 1 January to 49.0% on 30 June. Reallocations were made primarily to fixed income, as well as to investments in real estate, infrastructure assets and risk premium strategies.

As at 30 June, fixed income exposure was 22.7%, an increase of 8.6 percentage points from 1 January. The increased weighting in fixed income reflected a cautious investment approach in the light of asset valuations, risk appetite and our assessment of macroeconomic conditions.

Exposure to credits was reduced by 5.6 percentage points to 7.7%, largely because valuations were felt to be high in this risk category.

In the inflation risk category we completed further investments in alternative assets via our wholly owned real estate company, Trophi Fastighets AB, which continued to acquire retail property in Sweden and Finland. The company now owns close to 250 retail properties in more than 160 locations in Sweden and Finland with a market value of approximately SEK 5 billion at 30 June. AP3 also established a joint venture company with Prudential Real Estate Investors to acquire retail property in Germany. The joint venture acquired two portfolios with a combined holding of 83 properties across Germany and with a market value of approximately SEK 2.5 billion.

Currency exposure rose by just over 3 percentage points to 23.5%, an increase that is expected to enhance the stability of the portfolio.

We also committed a further SEK 1 billion to green bonds as part of an investment programme in this financial instrument that has been ongoing since 2008. As at 30 June this portfolio had a total value of SEK 3.3 billion.

Risk

Risk in the AP3 portfolio is expressed using the Value at Risk metric. VaR is defined as a 95% probability that the daily negative change in the value of the portfolio will not exceed a specific amount. It is measured on the basis of portfolio exposure and market volatility. Risk expressed as VaR stood at SEK 976 million on 30 June. VaR is a static measure that under normal market conditions provides an accurate indication of portfolio risk. However, because VaR is based on historic volatility and does not capture individual events or rapid market changes, it must always be supplemented with other risk measures.

Market volatility also dropped markedly during the period, which can lead to VaR underestimating de facto portfolio risk.

Value at Risk per risk category 30 June 2014	Value at Risk, SEK m	Value at Risk, %	Contribution to total risk, percentage points
Equities	1,040	0.38	105.9
Fixed income	177	0.06	-0.8
Credits	26	0.01	-0.6
Inflation	172	0.06	15.4
Currencies	349	0.13	-24.8
Other exposure	126	0.05	3.2
Absolute return strategies	53	0.02	1.6
AP3 total	976	0.36	100

The table shows the breakdown of total portfolio risk into AP3's seven risk categories. Due to the covariance between the risk categories, total risk is lower than the total risk for each risk category. This is known as the diversification effect.

Equities are the largest of AP3's risk categories. Currencies and fixed income have a negative covariance with equity risk and thus help to reduce the overall level of risk in the portfolio. Credits include both credit risk, which has a positive covariance with equity risk, and interest rate risk, which has a negative covariance with equity risk and often predominates in this risk category. AP3 deploys a diversification strategy between asset classes and geographic markets geared to limiting total portfolio risk. The aggregate risk per risk category is thus higher than the risk for the total portfolio, with the difference between the two figures reflecting the so-called diversification effect.

LOW COSTS

Operating expenses stood at SEK 90 million (87) for the period and do not include SEK 82 million (82) of commission expenses, which are recognised separately in the income statement. Commission expenses consist of fixed commissions for external mandates, agreed commissions for unlisted equity, and custody account expenses. Total expenses (operating expenses plus commission expenses) totalled 0.13% (0.14) of assets under management on an annualised basis. Internal expenses (that is, operating expenses) totalled 0.07% (0.07) of assets under management.

Asset management expenses	Jan-June 2014	Jan-June 2013
Operating expenses, SEK m	90	87
Commission expenses, SEK m	82	82
Operating cost ratio, % ¹	0.07	0.07
Asset management cost ratio ²	0.13	0.14

¹ Annualised operating expenses as a percentage of average fund capital.

² Annualised asset management expenses (that is, operating expenses plus commission expenses) as a percentage of average fund capital.

AP3 aims to generate favourable risk-adjusted returns with high cost-efficiency. The strategy for ensuring effective asset management is based on constant improvement and a decision-making model that projects return, risk and cost.

International cost benchmarking survey

For the last nine years AP3 has taken part in an annual cost-effectiveness benchmarking survey against 17 global pension funds with a similar investment profile. The study, performed by Canadian consultants Cost Effectiveness Measurement (CEM), examines total asset management costs, the value of assets under management, portfolio structure and the ratio of active management. The most recent survey, for 2013,

showed AP3's costs to be 41% lower than the benchmark average and 28% lower than the peers recalculated benchmark. The main reasons for this are that AP3 pays less for its external management mandates than the benchmark group and that it has a higher ratio of internal management. It can also be noted that AP3's net return in the last five years AP3's net return has exceeded that of the benchmark group by 21%, highlighting the Fund's high level of cost-efficiency.

CORPORATE STEWARDSHIP AND ESG

Sustainable business practices are fundamental to the ability of the companies in which AP3 invests being able to generate favourable and stable returns over time. Active and responsible ownership helps create well managed companies that deliver higher returns at a lower level of risk over the long term. AP3 bases corporate stewardship on its stewardship policy, which contains guiding principles for corporate governance and sets out the Fund's stance on social and environmental responsibility. The principles are general in character and apply to all companies in which the Fund invests, whether domiciled in Sweden or abroad.

As of 2006 AP3 is a signatory of the UN Principles for Responsible Investment (PRI), which encourage investors to integrate environmental and social governance (ESG) in financial analysis and decision-making processes. Signing the PRI signalled our support for the initiative and our intention to comply with the principles in our business activities. AP3 reports annually to the PRI on ESG.

AP3 aims to report its stewardship engagements as openly as possible. During the period, AP3 voted at 53 Swedish annual general meetings and 500 foreign AGMs. Prior to the 2014 AGM season, AP3 held seats on the nomination committees of four listed companies (Aerocrine, Agrokultura, Arise and Karolinska Development) and two unlisted companies (Bergvik Skog and Vasakronan). A detailed presentation of AGM-related activities and AP3's environmental and social governance (ESG) work during the 12 months ended 30 June 2014 will be published on the [Fund's website](#).

AP3 coordinates its ESG work vis-à-vis foreign companies together with AP1, AP2 and AP4 via a joint Ethical Council. The Ethical Council's annual report, which includes information on ongoing corporate dialogues, was published in April 2014 and is available [here>>](#).

During the period, AP3 integrated ESG throughout the investment process as a means to enhancing control of portfolio risk and building trust and confidence in the fund as a portfolio manager. All internal management mandates are required to comply with the Fund's principles on sustainability in portfolio investments. For external mandates, AP3 has clear reporting requirements for managers and conducts regular monitoring.

AP3 has for several years been a member of the Global Real Estate Sustainable Benchmark (GRESB), an international industry association for real estate investors. AP3's unlisted real estate holdings – Vasakronan, Hemsö and Trophi – all report to the GRESB database. Our timberland holdings are certified by the Forest Stewardship Council (FSC), an organisation that promotes environmentally sound, socially beneficial and economically prosperous management of the world's forests.

During the period the Fund initiated and completed various investments and activities in the ESG field:

- Since 2008 we have invested actively in green bonds and during the first six months of 2014 committed a further SEK 1 billion. As at 30 June the green bond portfolio had a value of SEK 3.3 billion.
- AP3 invested in the Fund Generation Climate Solutions Fund II. We apply an investment strategy based on a firm belief that that ESG should be integrated in a strictly traditional investment process and can deliver favourable returns. AP3 has a pre-existing investment in the Generations Global Credit Fund, which also takes an ESG-based approach to fixed income investment.
- We also launched a project to measure the carbon footprint of companies in our portfolios. The project is due to be completed during autumn 2014.

- AP3 established an ESG employee training programme that will operate at different levels within the organisation. All employees, for example, will receive basic training in ESG from *Responsible Investment Fundamentals*.

EMPLOYEES

The number of employees was 56 at 30 June.

BOARD OF DIRECTORS

There were no changes in board membership during the period.

GOVERNMENT REVIEW OF THE AP FUNDS

The government's annual review the AP funds operating activities noted that AP1, AP2, AP3 and AP4 generated combined income of SEK 128 billion in 2013 and held total assets of SEK 1,058 billion. The funds' combined asset management costs were 0.14% of total assets, unchanged from the previous year. Since inception in 2001, the funds have generated an annual return of 4.7%, comfortably outpacing the rise in the income index.

As of 2009, payments of outgoing pensions have exceeded incoming pension contributions, requiring the AP funds to cover the deficit. In 2013 AP1, AP2, AP3 and AP4 transferred a total of SEK 27.5 billion to the Swedish Pensions Agency to meet pension commitments that year. The pension system deficit stems from the fact that the large cohort of people born during the 1940s has started to enter retirement. The AP funds will continue to help finance the shortfall for the foreseeable future.

The combined capital of the AP funds is included when calculating the assets of the income pension system, which means the funds' investment returns play a key role in determining whether or not automatic balancing takes place. The AP funds' capital currently accounts for 13% of total pension system assets, compared to 10% at inception in 2001.

By generating investment returns that have significantly outpaced the growth of the income index, the AP funds have contributed to the long-term financing of the system. The government review noted that in spite of very challenging conditions on financial markets during the 2000s, the buffer funds were building the income pension system's asset base, as envisaged when the current system was introduced in 2001, and hence creating scope for future retirees to enjoy a good pension while avoiding activation of the so-called automatic balancing mechanism.

In its report, the government pinpointed integration of ESG as a matter of prime importance to both AP funds and to public confidence in the funds and the pension system. In ESG, the AP funds are strong performers when compared internationally with other pension funds. The government is positive to the funds' ESG-related efforts but wants the funds to identify opportunities to go further, based on recommendations issued.

In the report summary, the government mentioned changes proposed by the Pensions Group to the AP funds' structure and investment rules and other changes aimed at ensuring cost-effective asset management. At the same time, the government noted that the current system works as it was intended to do and that the AP funds contribute both to its financing and asset building.

FURTHER INFORMATION

A list of assets and other data as at 30 June 2014 is available on the AP3 website at www.ap3.se under "Asset management".

NEXT REPORTING DATE

The full-year financial statements and annual report for 2014 will be published in February 2015.

ACCOUNTING POLICIES

This interim report was prepared in compliance with the accounting and valuation principles jointly developed and approved by the AP funds. These are presented in the 2013 annual report on page 40 under Note 1. The annual report is available on the AP3 website at www.ap3.se.

This interim report has not been reviewed by AP3's auditors.

Stockholm, 29 August 2014

Kerstin Hessius, CEO

Income statement	Jan - June 2014	Jan - June 2013	Jan - Dec 2013
Income, SEK m			
Net interest income	1,409	1,398	2,909
Dividends received	2,920	2,109	2,854
Net income from listed shares and investments	5,376	6,652	21,709
Net income from unlisted shares and investments	1,451	1,731	4,765
Net income from fixed income assets	3,094	-1,238	-1,597
Net income from derivatives	753	1,444	3,746
Net income from currencies	1,740	535	-1,659
Commission expenses	-82	-82	-155
Total income	16,661	12,549	32,572
Operating expenses			
Staff costs	-60	-54	-110
Other administrative expenses	-30	-33	-64
Total operating expenses	-90	-87	-173
Profit for the period	16,571	12,462	32,398
 Balance sheet			
Assets, SEK m	30 June 2014	30 June 2013	31 Dec 2013
Shares and investments,			
Listed	127,081	117,782	128,515
Unlisted	31,721	28,345	29,086
Bonds and other fixed income assets	129,451	99,808	107,494
Derivatives	1,195	2,116	3,081
Cash and cash equivalents	897	1,217	1,443
Other assets	23,947	18,882	11,606
Prepaid expenses and accrued income	1,612	1,311	1,470
Total assets	315,904	269,461	282,695
Fund capital and liabilities			
Liabilities			
Derivatives	4,198	3,630	1,899
Other liabilities	39,085	23,498	22,262
Deferred income and accrued expenses	42	45	58
Total liabilities	43,326	27,173	24,220
Fund capital			
Fund capital at 1 Jan	258,475	232,956	232,956
Net payments to pension system	-2,468	-3,130	-6,880
Profit for the period	16,571	12,462	32,398
Total fund capital	272,579	242,288	258,475
Total fund capital and liabilities	315,904	269,461	282,695

Financial summary	Jan-June 2014	2013	2012	2011	2010	2009
Income and inflows, SEK bn						
Net flows to/from pension system	-2.5	-6.9	-3.8	-1.2	-4.0	-3.9
Profit for the period	16.6	32.4	22.6	-5.5	18.3	29.4
Fund capital at end of period	272.6	258.5	233.0	214.1	220.8	206.5
Return and expenses total portfolio, %						
Return before expenses	6.5	14.2	10.7	-2.4	9.1	16.4
Operating expenses ¹	0.07	0.07	0.08	0.07	0.07	0.08
Commission expenses ¹	0.06	0.06	0.05	0.04	0.07	0.09
Return after expenses	6.5	14.1	10.7	-2.5	9.0	16.3
Inflation	-0.1	0.1	-0.1	2.0	2.3	0.9
Real return after expenses	6.6	14.0	10.7	-4.4	6.5	15.3
SEK bn						
Return	16.7	32.6	22.8	-5.3	18.5	29.6
Operating expenses	0.1	0.2	0.1	0.2	0.2	0.1
Return after expenses	16.6	32.4	22.6	-5.5	18.3	29.4
Annualised return after expenses, %⁵						
Five years	8.2	9.3	1.9			
Ten years	6.4	6.5	6.7			
Risk						
Risk (standard deviation) ³ , %	4.2	4.9	5.3	9.2	7.0	9.9
Risk (standard deviation) for liquid assets, %	4.7	5.7	6.3			
Sharpe ratio	3.0	2.8	1.8	neg.	1.2	2.0
Sharpe ratio for liquid assets	2.6	2.3	1.6			
Currency exposure⁴						
percentage of total portfolio	23.5	20.4	22.0	19.3	11.3	8.3
External management						
percentage of total portfolio	33.7	35.2	35.7	34.8	41.0	40.7
Asset management expenses						
% of assets under management						
Operating expenses ¹	0.07	0.07	0.08	0.07	0.07	0.08
Operating expenses plus commission expenses ¹	0.13	0.13	0.14	0.11	0.14	0.17
Number of employees						
	56	53	56	57	56	55

¹ Annualised figures.

² Measured as change in consumer price index at 30 June compared to 31 December the prior year.

³ As of 2010, figures relate to the total portfolio. Prior to 2010, risk was shown for the listed portfolio only.

⁴ Excluding exposure to SEK-listed companies with foreign domicile.

⁵ Return is annualised by a factor of 4.5 and 9.5, respectively, to maintain comparability with annual financial

statements.

Market value per asset category	Jan-June 2014	2013	2012	2011	2010	2009
Total, SEK bn	272,6	258,5	233,0	214,1	220,8	206,5
<i>of which</i>						
Swedish equities	29.9	32.6	26.2	28.7	32.0	26.5
Foreign equities	96.1	95.4	81.0	76.3	78.8	76.2
Nominal fixed income, Swedish	53.1	50.7	54.2	41.7	31.6	13.6
Nominal fixed income, foreign	35.5	18.2	17.2	14.6	28.7	42.3
Index-linked bonds, Swedish	15.0	14.5	15.3	17.1	1.5	0.1
Index-linked bonds, foreign	0.0	7.1	2.8	4.2	13.7	14.2
Unlisted equity, Swedish and foreign ¹	10.4	9.8	11.4	11.5	10.9	9.8
Real estate exposure	31.5	28.5	19.6	15.7	16.9	16.0
New strategies ²	-	-	-	-	6.9	7.7
Other assets ³	1.1	1.6	5.2	4.2	-	-

¹ Unlisted equity was included listed life science holdings prior to 2008. As of 2008, life science investments are included in "New strategies".

² New strategies were allocated between the various asset categories during 2011. Investments falling outside the scope of the different asset categories are classified as "Other assets".

³ Other assets include investments in convertible bonds and insurance-related risk.