

# Interim Report

1 January – 30 June 2019



**AP3** Third Swedish National Pension Fund

LONG-TERM ASSET MANAGEMENT ACROSS GENERATIONS

## AP3 summary 1 January – 30 June 2019

### Results and payments

- AP3 recorded a **net result** of **SEK 36,511** million (11,165) for the first six months of 2019.
- The **total return** was 10.8% (3.3) **after expenses**. The Equities and Inflation risk categories made the largest contributions to this performance.
- The annualised **asset management cost ratio** was 0.10% (0.09), of which operating expenses totalled 0.06% (0.06).
- **Fund capital** rose to **SEK 374,138** million (340,668 at 31 Dec 2018), an increase of SEK 33,470 million.
- **SEK 3,040 million** (3,320) was paid from fund capital to the **Swedish Pensions Agency** in the first half of 2019 to cover the difference between paid-in pension contributions and outgoing pensions and to meet pension system costs.
- AP3 has generated an **annual average return** of 8.6% over the last five years and 9.1% over the last 10 years.
- **Return** underperformed the **LSP benchmark portfolio** by 0.8 percentage points during the period.

**36.5**

SEK bn net result  
for first six  
months

**10.8**

% return after  
expenses

**374**

SEK bn in fund  
capital

### Summary of AP3's interim results at 30 June 2019

	30-06-2019	30-06-2018	30-12-2018
Fund capital at 30 June, SEK bn	374.1	353.1	340.7
Net result for the period, SEK bn	36.5	11.2	2.2
Net payment to the pension system, SEK bn	3.0	3.3	6.8
Fund capital at 1 January, SEK bn	340.7	345.2	345.2
Return after expenses, %	10.8	3.3	0.6
Real return after expenses, %	9.9	2.2	-1.4
Asset management cost ratio, operating expenses, percentage of assets under management*	0.06	0.06	0.06
Asset management cost ratio, commission expenses, percentage of assets under management*	0.04	0.03	0.03
Total asset management cost ratio, percentage of assets under management*	0.10	0.09	0.09
Annualised return after expenses, 5.0 years, %**	8.6	10.1	7.8
Annualised return after expenses, 10.0 years, %**	9.1	7.3	8.5
Annualised real return after expenses 10.0 yrs, %**	7.9	6.5	7.4

\* The interim report measures the asset management cost ratio on a full-year basis

\*\* The interim report also shows annualised return for 10.0 and 5.0 years respectively

## Statement by the CEO

The first six months of the year brought solid growth in the AP3 portfolio. Equity markets recovered swiftly from the sharp downturn in the last quarter of 2018. Financial market risk levels dropped after the US Federal Reserve began the year by signalling a restrictive approach to continued interest rate hikes and later guided the market to prepare for cuts during the year. All asset categories delivered positive returns during the period. Equity markets made the largest single positive contribution – 10.8% – and the Fund’s real estate investments also performed strongly.

New investment rules for the AP funds came into effect on 1 January. These reduced the floor for investments in fixed income instruments with a low credit risk from 30% of portfolio assets to 20%. The funds were also given increased scope to invest in unlisted assets. In response, the AP3 board of directors decided to adjust the level of risk in the long-term static portfolio (LSP), which consists of liquid assets and serves as the Fund’s investment benchmark. This was achieved by raising equity risk from 50% to 55% and increasing weight in index-linked bonds and currency exposure. This did not change the Fund’s investment allocation during the period. However, the strength of the equity market during the first six months and the higher equity weight in the LSP led the AP3 portfolio to underperform the LSP during the period.

Large holdings of unlisted assets give the AP3 portfolio a higher level of diversification than the LSP. This means that the AP3 portfolio will lag the LSP when stock markets make rapid gains. Conversely, the AP3 portfolio will outperform the LSP when stock markets fall sharply.



The AP3 portfolio underperformed the LSP by 0.8 percentage points during the first six months. However, AP3 significantly outperformed the LSP in the second half of 2018, and for the year ended 30 June 2019 outperformed it by 1.5 percentage points. The AP3 portfolio has the attributes we seek in our allocation strategy, namely to limit losses during large reversals on equity markets.

The new investment rules also apply clearer sustainability standards. In February, the board of directors adopted new sustainability goals for 2019-2025 which raise the Fund’s ambitions in sustainable investment and governance. During the spring, AP3 partnered with AP1 and AP4 to found Polhem Infra, an investment firm that will focus on unlisted sustainability-focused Swedish infrastructure companies. This will bring long-term benefits both for the pension system and the wider community.

*Stockholm, August 2019*

**Kerstin Hessius**

## Sustainability at AP3

In the first six months of 2019 AP3 worked closely on sustainability initiatives with AP1, AP2 and AP4 via the AP Funds' Council on Ethics and also with other international pension funds.

### International investor collaboration on tailings dam safety standards

Following the collapse of the Vale tailings dam in Brumadinho, Brazil, in January 2019 and the tragic loss of life and livelihoods and environmental destruction, the Council on Ethics joined forces with the Church of England pension fund and global investors (with combined assets of more than \$10 billion) to promote improved safety standards at tailings dams. The investors are demanding the creation of a publicly available global database on all tailings dams to provide information for governments, investors and civil society. The investors have written to 680 mining companies, calling on them to publish technical data on every dam that they own or partly own. The investors, among whom the Council on Ethics and the Church of England pension fund also represent the Principles for Responsible Investment in an international working group, are campaigning for

the introduction of global safety standards for tailings dams. Such standards would help avoid future accidents.

### Investor-led initiative for publisher responsibility on social media platforms

AP3 and the Council on Ethics support an investor-led initiative to encourage Facebook, Alphabet (Google) and Twitter to work harder to protect users and communities from content carried on their social media platforms. The initiative came in the wake of the Christchurch massacre in New Zealand in March this year and involves the Council on Ethics supporting engagement with platform owners on personal data management.

### Corporate governance at AGMs in 2018-2019

AP3 has been steadily increasing its voting at investee AGMs. This year the Fund voted at around 1,000 such meetings, 75 of which were held by Swedish companies. AP3 engages actively in a range of stewardship issues, including executive pay system structure, corporate board diversity, capital structure, anti-fraud and labour protection. The Fund encourages investees to develop a climate strategy by measuring and reporting carbon footprint and by reducing climate impact in business activities.

## AP3's new sustainability goals for 2025

- 1. The AP3 asset portfolio will continue to contribute to a reduced risk of global warming.**
  - AP3 will continue to measure and report on carbon footprint.
  - AP3 will perform scenario-based portfolio analysis of climate risks and opportunities.
  - AP3 will again halve the Fund's carbon footprint, primarily by encouraging investees to reduce their climate impact.
- 2. AP3 will double sustainable investments by 2025.**
  - Investments in green bonds will double to SEK 30 billion.
  - Sustainable investments will double to SEK 25 billion.
- 3. AP3's directly owned companies will be leaders in sustainability.**
  - AP3 will continue to ensure that its directly owned unlisted real estate and infrastructure companies take a lead in sustainability by focusing on sustainable production and construction.

## Income statement

Income			
SEK m	Jan-June 2019	Jan-June 2018	Jan-Dec 2018
Net interest income	1,434	1,092	2,491
Dividends received	5,230	4,234	5,316
Net income from listed shares and investments	21,184	1,236	-11,676
Net income from unlisted shares and investments	2,122	3,230	9,029
Net income from fixed income assets	2,994	-772	-679
Net income from derivatives	200	-3,072	-6,818
Net income from currencies	3,518	5,378	4,860
Commission expenses	-63	-61	-117
<b>Total income</b>	<b>36,619</b>	<b>11,265</b>	<b>2,404</b>
<b>Operating expenses</b>			
Staff costs	-67	-66	-129
Other administrative expenses	-40	-34	-73
<b>Total operating expenses</b>	<b>-108</b>	<b>-100</b>	<b>-202</b>
<b>Net result for the period</b>	<b>36,511</b>	<b>11,165</b>	<b>2,202</b>

## Balance sheet

ASSETS			
SEK m	30-06-2019	30-06-2018	31-12-2018
Shares and investments			
Listed	171,683	154,343	137,256
Unlisted	72,290	61,775	67,905
Bonds and other fixed income assets	132,789	147,437	139,427
Derivatives	3,096	4,369	4,600
Cash and cash equivalents	829	983	1,005
Other assets	8,642	7,932	7,836
Prepaid expenses and accrued income	1,144	1,146	1,083
<b>Total assets</b>	<b>390,473</b>	<b>377,985</b>	<b>359,111</b>
<b>FUND CAPITAL AND LIABILITIES</b>			
Liabilities			
Derivatives	2,412	8,554	1,713
Other liabilities,	13,872	16,276	16,673
Deferred income and accrued expenses	51	71	59
<b>Total liabilities</b>	<b>16,334</b>	<b>24,901</b>	<b>18,444</b>
Fund capital			
Fund capital at start of period	340,668	345,239	345,239
Net payments to the pension system	-3,040	-3,320	-6,773
Net result for the period	36,511	11,165	2,202
Total fund capital	374,138	353,084	340,668
<b>Total fund capital and liabilities</b>	<b>390,473</b>	<b>377,985</b>	<b>359,111</b>

## Five-year summary

	Jun 2019	2018	2017	2016	2015
<b>Income and flows</b>					
Net result, SEK bn	36.5	2.2	28.2	28.0	19.6
Net flow from pension system, SEK bn	-3.0	-6.8	-7.4	-6.6	-4.9
Fund capital, SEK bn	374.1	340.7	345.2	324.4	303.0
<b>Return and expenses, total portfolio</b>					
Return before expenses, %	10.8	0.7	8.9	9.5	6.9
Operating expenses, %*	0.06	0.06	0.06	0.06	0.06
Commission expenses, %*	0.04	0.03	0.05	0.06	0.06
Return after expenses, %	10.8	0.6	8.8	9.4	6.8
Income (incl. commission expenses), SEK bn	36.6	2.4	28.4	28.2	19.8
Operating expenses, SEK bn	0.1	0.2	0.2	0.2	0.2
Income after expenses, SEK bn	36.5	2.2	28.2	28.0	19.6
<b>Annualised return after expenses, %</b>					
5.0 years**	8.6	7.8	10.5	10.9	8.4
10.0 years**	9.1	8.5	6.1	5.7	5.7
<b>Return compared to LSP benchmark portfolio</b>					
Return, percentage points	-0.8	3.1	2.1	2.3	4.3
Average annual return since 2012, percentage points	2.2	2.5	2.4	2.5	2.5
<b>Risk</b>					
Risk (1-yr standard deviation), %***	4.3	5.4	3.5	6.2	7.0
Sharpe ratio	5.4	0.3	2.8	1.6	1.0
<b>No. of employees at end of period</b>	58	59	57	57	51

\* The interim report measures the asset management cost ratio on a full-year basis

\*\* The interim report shows annualised return for 10.0 and 5.0 years respectively

\*\*\* The interim report measures risk as six-month standard deviation

## Fund capital 2008-2019

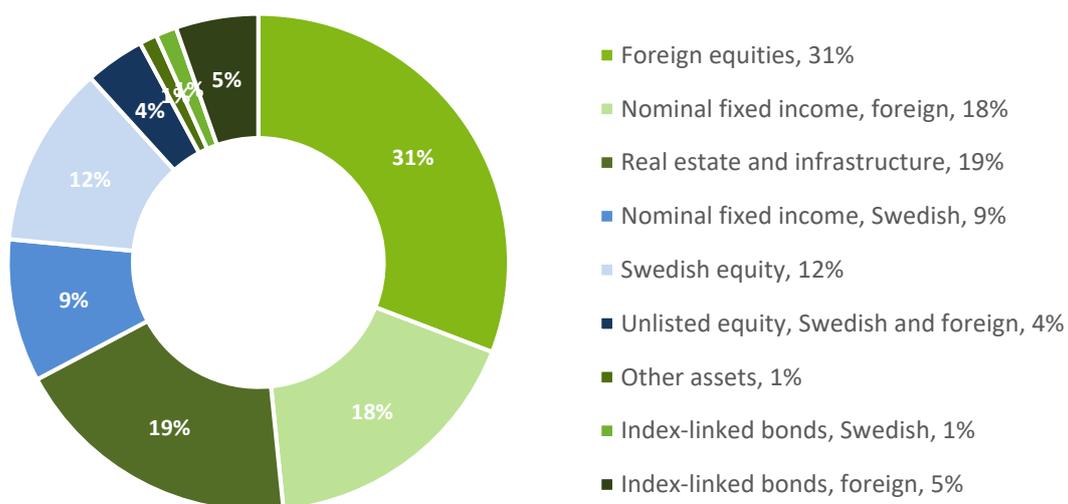


## Market value per asset category

	30-06-2019	2018	2017	2016	2015
<b>Total, SEK bn</b>	<b>374.1</b>	<b>340.7</b>	<b>345.2</b>	<b>324.4</b>	<b>303.0</b>
<i>of which</i>					
Swedish listed equities	44.2	37.3	44.5	40.3	34.2
Foreign listed equities	115.4	90.8	108.4	98.4	98.7
Nominal fixed income, Sweden	34.7	37.3	45.8	45.2	35.9
Nominal fixed income, foreign	65.6	66.6	54.2	54.8	59.9
Index-linked bonds, Sweden	5.0	4.9	4.8	4.8	5.8
Index-linked bonds, foreign	19.9	19.0	16.0	15.7	13.0
Unlisted equity, Swedish and foreign	14.5	13.1	10.3	10.0	10.2
Real estate and infrastructure	70.4	66.4	57.0	52.0	42.6
Other assets <sup>1</sup>	4.3	5.3	4.1	3.0	2.7
<b>Currency exposure</b>					
% of total portfolio	20.8	17.7	15.0	17.5	22.8
<b>External management</b>					
% of total portfolio	31	26	25	29	31

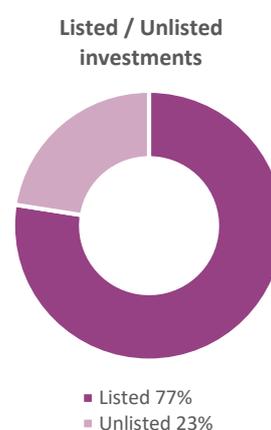
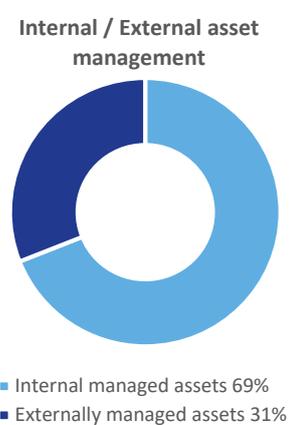
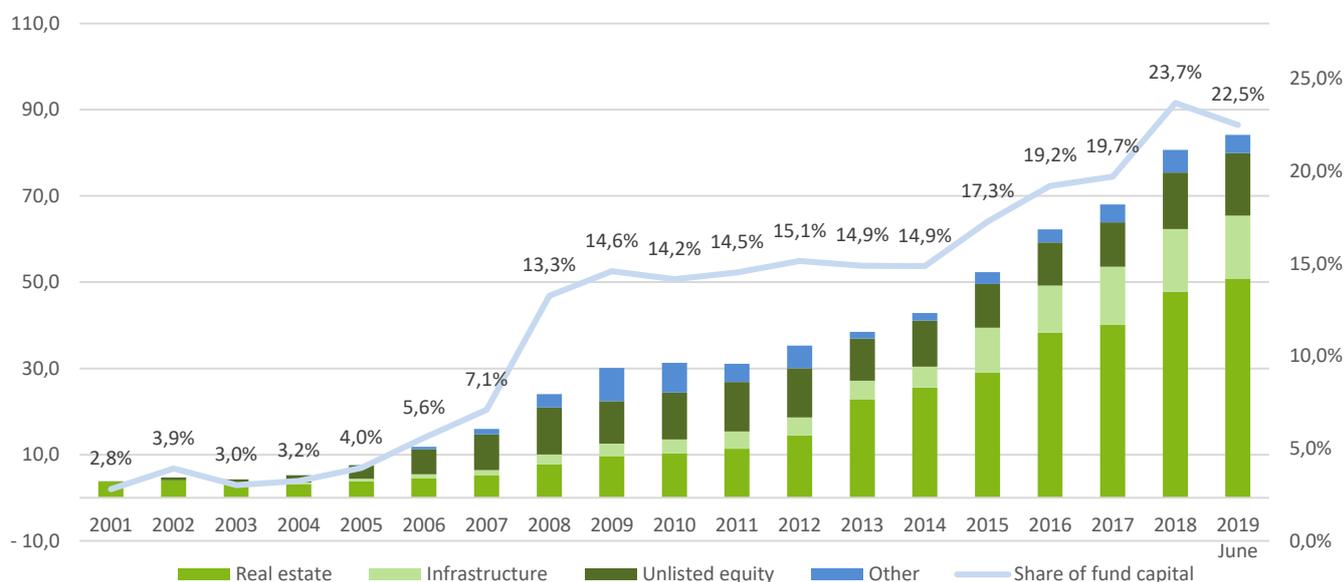
1) Other assets include investments in convertible debentures and insurance-related risk

## Market value per asset category 30 June 2019



## Portfolio overview at June 2019

### Investments in unlisted assets 2001 – June 2019 SEK bn



### Currency exposure from 2015 to 30 June 2019



Read more about AP3, Third Swedish National Pension Fund, at [www.ap3.se](http://www.ap3.se)

**AP3**

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