

OWNERSHIP REPORT 2014



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BRIEF FACTS

- Första AP-fonden is one of five funds that manage buffer capital in the Swedish national income pension system (the AP funds). The capital reserves in the AP funds are used when disbursements from the pension system exceed contributions to it.
- Första AP-fonden shall manage assets with a long-term approach in order to attain a high return with a consolidated financial risk.
- Första AP-fonden manages a global portfolio consisting of equities, fixed income securities, real estate, private equity funds and hedge funds, to a value of SEK 267 billion (30 June 2014).
- Första AP-fonden is a long-term investor and an engaged owner. In its investment decisions and as an owner, the Fund imposes strict demands on sustainable value creation.

SUSTAINABLE OWNERSHIP

Första AP-fonden pays due consideration to the environment, ethics, labour rights issues, the climate issue, social issues and many other sustainability matters in its investing activities. For us, consideration for such matters and maintaining long-term high return are not contradictory. Quite the opposite. Companies and operations that are run sustainably will, over time, show better profits and lower costs than those that neglect sustainability matters. Owners and companies thus share the same interest.

In their investments, the AP funds shall not take prevailing industrial or economic government policies into account. However, the funds shall "give due consideration to environmental and ethical matters without compromising the overall objective of attaining a high return", which means that the objective of consideration for environmental and ethical matters is subordinate to return. Första AP-fonden owns global assets worth SEK 267 billion. Around half that amount (SEK 134 billion) consists of shares in listed companies, and the rest is allocated among bonds, unlisted shares, real estate, and so on. Because of its substantial ownership, the Fund's return and risk are strongly affected by how the companies run their operations. The way in which companies address sustainability matters affects their profitability and, ultimately, the Fund's return. It is therefore important that we have sound knowledge of the companies in which we invest. The Fund therefore invests in a small number of companies rather than diversifying investments across the entire market. When investments are made, risks and opportunities in sustainability matters play a major role – together with purely financial considerations. Only when a company is socially, environmentally and financially sustainable can truly sustainable value creation be attained.

"Only when a company is socially, environmentally and financially sustainable can truly sustainable value creation be attained."

In its capacity of a major shareholder, Första AP-fonden is able to influence the companies in which it invests – shareholder activism. The Fund's influence shall be exerted such that it helps increase the Fund's long-term return. In our view, active ownership makes our investments more sustainable. We are involved and influence the companies in which we own shares, taking them in what we consider to be the right direction. It can be a case of board composition, remuneration and incentive programmes, capital structure, labour rights issues, the environment and safety. We work in a structured manner with sustainability analysis both ahead of an investment, and as owners.

Första AP-fonden's sustainable ownership work was intensified in 2014. In 2015, the integration of sustainability matters into investment decisions will continue. An overarching question in managing assets is resource efficiency – that is, how the companies in which we invest work with the earth's finite resources. Resource efficiency analysis marks a broadened approach compared with studying the climate issue on a stand-alone basis. However, climate remains an important issue that will stay in focus in 2015.

1) The Swedish National Pension Funds Act (2000:192) (the AP Funds Act).

In our position of power as a major institutional investor, we will continue with our work to promote greater boardroom diversity and equality – not least in Sweden. We will persevere with our work on remuneration matters such as board fees and value-creating remuneration.

“In our view, active ownerships makes our investments more sustainable.”

Through the Ethical Council of the AP Funds, in which the First, Second, Third and Fourth AP funds collaborate in sustainability matters, the Fund exerts influence on companies. Together, the funds are a more powerful force in dialogues and voting at AGMs.

For Första AP-fonden, it is important to describe how we work with our investments. The 2014 ownership report takes further steps to clarify an important part of our operations. The report aims to describe and explain what we do in the areas in which we exert shareholder influence on the businesses in which we have invested – shareholder activism and sustainable value creation.

Ossian Ekdahl
Head of Communication and ESG



SUSTAINABLE VALUE CREATION

– our view

How companies manage sustainability issues has a bearing on their ability to attract and keep customers. It also affects their ability to recruit and retain staff, and to raise financing on decent terms.

Första AP-fonden is convinced that, over time, companies with effective management of environmental and social issues have greater opportunities to create higher profits

“For a long-term investor, it is therefore important that sustainability matters are systematically included in the investment analysis.”

and reduce risks than others. For a long-term investor, it is therefore important that sustainability matters are systematically included in the investment analysis.

There is, in the Fund's view, no contradiction between the task of creating long-term high return and consideration for sustainability aspects in asset management – quite the contrary. Constant work to continually improve and develop the analysis is thus needed. As part of this work, a training initiative for staff of the Fund was carried out in 2014. The purpose, besides enhancing knowledge, is to intensify discussions in the area because the issues are complex and there are no given answers. In order to further increase long-term return, the Fund is an engaged owner that influences companies into further improving their operations in terms of sustainability.



A CONCENTRATED PORTFOLIO

– fundamental to sustainability analysis and owner engagement

In our view, possessing solid knowledge about the companies in which the Fund invests is fundamental to creating healthy return over time. The Fund has therefore selected an investment model in which the internal management is based on relatively concentrated portfolios with few holdings – around 30 Swedish companies in the equity portfolio and around 90 for remaining developed countries (Europe, the US and parts of Asia). This affords better possibilities of analysing each portfolio company, and better opportunities to influence the companies.

Investment philosophy at the core of value creation

Första AP-fonden's investment philosophy generally describes the foundation of the Fund's work with investments based on its mandate and market mechanisms.

The portfolio shall have **high and controlled financial risk** in order to deliver optimally on its mandate. Short-term fluctuations in value in the Fund can be substantial, but this shall not affect portfolio composition.

The Fund shall take account of **sustainability factors** in its investment analysis and owner engagement. In this context, the benefits of a long analysis, investment and evaluation horizon are reaped.

The investment process shall be based on **concious choices** because markets are not entirely efficient. Internal independent analysis of high quality and diversification are important for sound risk-adjusted return.

The actions of the Fund shall ensure that public **confidence** is upheld. A clear structure with clear allocation of responsibilities and cost efficiency are important to results and confidence.

The Fund's investment philosophy rests on its view of six fundamental conditions: diversification, investment horizon, market efficiency, risk, costs and sustainable value creation:

Diversification – Successful diversification between asset classes, risk, investment horizon and strategies increases risk-adjusted return. It requires allocation with sound insight into the underlying drivers and risk factors of assets.

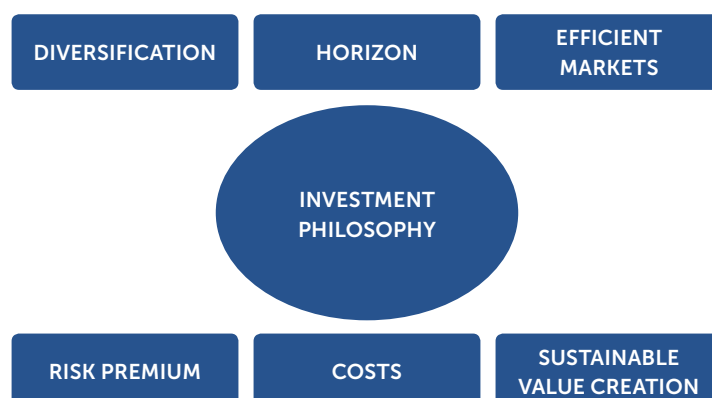
Horizon – A long-term approach enables higher return over time. When market pricing is set with a short investment horizon, lucrative investment strategies beyond that horizon emerge.

Efficient markets – Financial markets are not entirely efficient. Therefore, well-devised management with active selection can bear fruit.

Risk premium – Risk-taking on financial markets generates a positive return over time. Risk premiums vary over time and are obtained by investing in specific asset classes or strategies or in risks that other investors are unable or unwilling to take.

Costs – Cost-efficiency is key because it is return after expenses that makes up the Fund's contribution to the pension system.

Sustainable value creation – Focus on sustainable value creation can provide possibilities to increase return in the long term and reduce financial risk because the markets are not always efficient in pricing risk and opportunity in the area of sustainability.



CLIMATE CONSIDERATIONS IN INVESTMENT DECISIONS

Climate change is currently a key part of Första AP-fonden's investment analysis, both in terms of individual stock selection, and our long-term portfolio composition.

The investment process for the internally managed equity portfolio is built on fundamental analysis based on an assessment of future profits and risk level in relation to current valuation. The strategy involves identifying equities that are undervalued in relation to future gains and which are expected to generate a high return. The investment horizon is long. Hence, a changed climate, its impact on investments, overall balancing of risk and opportunities and the ability of the individual company to adapt thereto are paramount in investment decisions.

Carbon footprint measurement

In the second half of 2014, the Fund commissioned measurement of the carbon footprint of the equity portfolio². It was measured at company, sector and portfolio level and showed that, as a whole, the equity portfolio had a carbon footprint that was 16 per cent lower than equivalent markets. There are regional differences, but for all regions the carbon footprint of our portfolio is lower than average.

- Sweden: 50 per cent lower than the market
- Emerging markets: 12 per cent lower
- Other regions: 5 per cent lower
- Total portfolio: 16 per cent lower

The low numbers are the result of actively taken, well considered investment decisions in which Co2 efficiency is weighed in with other factors.

Complex measurement

The usual carbon footprint measurement method, and that which is used here, measures the direct Co2 emissions of companies. It takes no account of how use of products and services affect the Co2 level in the atmosphere, or the impact of subcontractors. Neither does it capture work aimed at reducing dependence on fossil energy. The analysis must thus be supplemented with other considerations.

The value of companies with substantial fossil energy reserves (oil, gas and coal) is to some extent uncertain. Första AP-fonden has analysed energy reserves in its equity portfolio and determined that the Fund's equity portfolio has 34 per cent lower exposure to fossil energy reserves than comparable markets.

Participation in an international study

In order to gain a better idea of the long-term climate risks and increase our knowledge of the consequences of global warming for our long-term return, we are participating, as the only Swedish pension fund, in an international study alongside other pension funds and climate experts. The study is geared to both asset classes (equities, fixed-income securities, infrastructure, real estate, etc.) and regions and sectors. The results will be published in the first half of 2015.

²) Measurement was performed by Trucost, one of the leading companies in carbon footprint measurement.

SUSTAINABILITY OF EXTERNAL MANAGERS

A great deal of the Fund's portfolio is managed by external managers. The Fund's procurements of external management services include sustainability criteria in the tendering documentation and in manager assessments. Sustainability aspects also form an important part of the annual evaluation and the ongoing dialogue with external managers.

In 2014 the Fund performed a broad analysis of the sustainability work of external managers. All external equity and fixed income managers, and the most important private equity managers, were analysed with follow-up discussions on investment decisions. This analysis will be developed in 2015.



SUSTAINABILITY ASPECTS IN AGRICULTURAL INVESTMENTS

Första AP-fonden's agricultural investments consist of close to 20 agricultural properties in Australia and around ten in New Zealand.

The challenges in agricultural investments are considerable – this is an industry confronted by all types of sustainability risks. Analysis of sustainability factors is therefore an important element of the Fund's investment process and a key part of the ongoing monitoring of agricultural investments. As a basis for this analysis, the Fund uses PRI's Principles for Responsible Investment in Farmland, which have been endorsed both by the Fund and our managers. The principles cover the environment, labour rights, human rights, land and resource rights and business ethics.

Agricultural investments are made through external managers selected based on e.g. their sustainability work.

In New Zealand, the investments consist entirely of farmland for milk production. In Australia, the investments consist of farmland for grain cultivation, cattle rearing and milk production, as well as a project to restore afforestation to farmland.

All investments are preceded by an independent eco-audit in order to identify flora and fauna of particular ecological value. Follow-up is systematically performed in the operating activities using a database in which all measures are registered.

Read more about sustainability aspects and agricultural investments at ap1.se.

A CONCENTRATED PORTFOLIO PAVES THE WAY FOR SUSTAINABLE MANAGEMENT

As a state pension manager and major institutional investor, the wishes of various stakeholders regarding the focus of asset management are often directed at Första AP-fonden and other AP funds.

In December 2013, Mikael Angberg took up his position of Chief Investment Officer of Första AP-fonden, responsible for a global portfolio of SEK 267 billion in total. He joined the fund with a clear mandate to further sharpen focus on sustainability.

All sectors

In recent years, Första AP-fonden has converged towards increasingly concentrated ownership, with much fewer companies in the equity portfolio. The ambition has been to have a portfolio in which we know what we own, and the number of holdings has thus been reduced from just shy of 3,000 to around 600, with a core of 100 companies that make up the part of the portfolio we work actively with.

"Concentrated ownership is fundamental to the credibility of our sustainability analysis," comments Mikael Angberg.

The Fund's active management model, in which the portfolio is concentrated and the number of companies has been reduced, better enables analysing and monitoring each holding. Första AP-fonden invests in all sectors and performs thorough analyses in each investment.

"We have chosen the approach not to exclude sectors or industries, but work with, for example, identifying companies in industries with high 'sustainability risk' which we nevertheless consider to have a sustainable strategy," he continues.

"It could be a subcontractor in the oil sector which, besides its core operations, develops business concepts in renewable energy. Such a company could have a low sustainability rating, but prove a good investment in the long term, looking at where it is headed," continues Mikael Angberg.



"Concentrated ownership is fundamental to the credibility of our sustainability analysis."

"A major energy company could, for example, have greater operations in renewable energy than a small company in the renewable energy niche, but this does not come to light when our investments are measured from a fossil weight perspective," he explains.

Climate – a risk to be managed

Climate impact is an issue being raised more and more by investors. At Första AP-fonden, the climate issue is high on the agenda, according to Mikael Angberg.

“When we speak in terms of approach to climate change, we focus primarily on two lines of attack: first, how we can choose to invest and act as an owner to contribute to reduced climate change. Second, how we can select assets that will generate long-term sustainable return given a changed climate or altered requirements.”

In his view, the latter makes the climate factor a risk to manage together with other risks in investment decisions. A factor with growing visibility in the debate on sustainable investment is resource consumption; that is, the consumption of businesses of finite or scarce resources such as fossil fuels, water, various metals and also waste management.

“Looking at resource consumption in the investment analysis gives us an even broader view compared with climate impact alone. The dependence of a business on scarce resources is an evident risk to observe in identifying long-term sustainability.”

Long-term ownership

Mikael Angberg reverts to the point that Första AP-fonden is a long-term owner, and that it has therefore always been natural to be at the forefront in terms of analysis of which sustainability is an integral part.

Wishes are regularly expressed by various stakeholder organisations for the AP funds to divest parts of or entire sectors from the portfolio. For example, pressure has been exerted regarding stranded assets – mainly coal and oil that cannot be used in combustion if the climate target of a temperature increase of a maximum of two degrees is to be reached.

“Första AP-fonden invests in companies considered sustainable in the long term. This encompasses all aspects, including the risk of them being unusable or stranded,” explains Mikael Angberg. “If in our view a company has a strategy to manage this and we also believe in the company as a good investment in terms of return, the company remains in our portfolio.”

Nothing new and here to stay

Sustainability is high on several agendas at present, and Första AP-fonden has received many questions related to sustainable management in recent years. However, this is nothing new for the Fund’s equity management. The Fund has always taken sustainability factors into consideration in analysis and investment decisions.

“The managers always make a comprehensive assessment of each investment, and that hasn’t changed. A difference of late is that we work in a more structured and visible manner with sustainability as an integral part of the decision-making process. We also now have an analyst specialised in sustainability who serves as support in our investment decisions,” continues Mikael Angberg.

Who has power over energy systems?

International Energy Agency (IEA) has worked out that, out of all the USD 40,000 billion investments in energy systems until 2035, nation-states account for 80 per cent of the investment decisions. The companies in which investors may buy shares, such as global listed oil companies, account for around 20 per cent of all investment over the same period, and the investments made by such companies are pretty much self-financed and thus do not require further shareholder contributions.

Politicians and state-owned oil companies thus account, directly or indirectly, for the majority of all investment decisions in the energy sector. It is also national parliaments that decide on emission rules for the transport and industrial sector, and which determine Co2 taxes or other fees that can affect demand for fossil fuels.

PRI

Första AP-fonden has endorsed the UN initiative Principles for Responsible Investment – PRI – an international network in which investors work together to increase understanding of the effects of sustainability for them. It also serves as support for participants in including such matters in their investment decisions and shareholder activism.

Just over 1,300 institutional investors worldwide have endorsed the PRI. This gives the network a strong voice globally on responsible investment matters. At the same time, it is a valuable network for Första AP-fonden to be part of. The six principles of the PRI are well in line with Första AP-fonden's rationale. The Fund was therefore an early endorser of the principles. By endorsing the PRI, Första AP-fonden has undertaken to comply with the principles and since endorsement it has worked to fulfil all six principles, which it now does.

1. We will incorporate ESG (environmental, social and governance) issues into investment analysis and decision-making processes.

We include ESG factors in the same way as other analysis factors in analysis and decision-making processes in our management. Providing support to the managers is a dedicated ESG analyst who analyses and prepares source materials for decision-making. External analysis and data collection are also used in the Fund's investment decisions.

2. We will be active owners and incorporate ESG issues into our ownership policies and practices.

We are engaged owners and take ESG factors into consideration in our actions as owners. We participate actively in AGMs and conduct dialogues on an ongoing basis throughout the year, both in Sweden and abroad. For example, Första AP-fonden has endorsed the Stewardship Code in the UK.

3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.

We support various initiatives to improve companies' reporting, such as the Carbon Disclosure Project and Global Reporting Initiative. Together with other major Swedish investors, we collaborate in the evaluation "Hållbart värdeskapande" (Sustainable Value Creation), in which around 100 Swedish companies report their sustainability efforts.

4. We will promote acceptance and implementation of the Principles within the investment industry.

We encourage our external managers to endorse the PRI and are provided with their accounts of how they follow the principles.

5. We will work together to enhance our effectiveness in implementing the Principles.

We work together through the Ethical Council of the AP funds. For certain matters, we collaborate with many other investors, both in Sweden and globally. For example, the Secretary General of the Ethical Council is the chair of the PRI's Clearing House Project. Första AP-fonden has also participated in a work group and submitted proposals for the further development of the PRI.

6. We will each report on our activities and progress towards implementing the Principles.

We report annually to PRI regarding our implementation of the Principles. We also report our owner engagement and integration of ESG into our management on the Fund's website, www.ap1.se, in this ownership report and in our annual report

SHAREHOLDER ACTIVISM IN 2014

By engaging as an owner, the Fund increases the possibility of raising return and controlling financial risk in the long term.

We see that companies with a solid grasp of sustainability matters generally have higher profits, lower risks and in many cases higher long-term return on equity than others. Also, markets are not always efficient in terms of information regarding sustainability matters and shareholder activism. The risk of political decisions and regulations in the area is high, and not always priced in. Because of this we, through our ownership and voting rights at AGMs, are able to influence companies in the right direction. Shareholder activism work is based on the Fund's ownership policy, reviewed and decided by the Board each year.

Ownership policy

Första AP-fonden's ownership policy addresses a number of matters which we as owners find important in order for the companies in which we invest to generate as high a long-term return as possible.

A fundamental issue is the possibility of exercising the right to vote provided by the shareholding – a factor not always obvious in all countries. The same applies to the principle of non-discrimination – not favouring certain shareholders and disfavouring others. Another core issue is the efficient management of companies. This encompasses companies refraining from preserving capital that is not needed in the operations – such capital must be distributed to shareholders.

The owners shall not decide on strategies for and governance of the companies – the company's own board of directors must see to this. An important area of the ownership policy is therefore the requirements of the Fund in terms of influencing the election of board members, and how boards should work.

Senior executive remuneration at the companies is a key issue because it affects employee behaviour at all levels. It is incumbent upon the board of directors to ensure that the companies have a remuneration system that works. At the same time, as owners, we have a vested interest in being able to exert influence so that boards meet that requirement. At Swedish companies, the possibility of owners to influence remuneration matters is high, while it is much lower in many other countries, even though owner influence in such matters has been strengthened in recent years due to e.g. regulation in the EU and US.

The ownership policy also sets out the requirements, in terms of environmental and social issues, imposed by the Fund on all the operations in which we have invested. The Fund's unlisted real estate companies, in which the Fund has

substantial influence (Vasakronan, CityHold and Willhem) shall, besides complying with the ownership policy of the Fund, also follow its ownership directives, published on the Fund's website. Companies shall follow the "Government's Guidelines for Senior Executives in state-owned Companies" (09/04/2009).

Class action

On certain markets – primarily in the US but also in the UK – possibilities of influencing companies by voting at AGMs are lower than in Sweden. Hence, active and engaged owners must use other ways to influence the companies. Första AP-fonden works with other owners by submitting or supporting resolutions at American AGMs and participating in class action lawsuits. In 2014 the Fund was the lead plaintiff in three class action lawsuits, two of which were in the US and one in the UK. The Fund is also a plaintiff in just over 80 lawsuits, 30 of which were concluded during the year. The purpose of the lawsuits is to bring legal action against the companies or their management to regain part of funds lost due to mismanagement or similar circumstances. Through the 30 lawsuits ended in 2014 (until 30 November), the Fund managed to collect just over USD 850,000. The Fund does not risk having to pay any damages or legal expenses, even if a case is lost.

Organisation and responsibility

The Board of Directors of the Fund decides on the ownership policy and delegates implementation thereof to the CEO. With a view to strengthening integration of sustainability issues into investment decisions, the Fund's sustainability expert forms part of the investment organisation and is a member of the Portfolio Group that is the work group in which overarching investment decisions are made. Ownership matters are also discussed in the Fund's corporate governance board.

Corporate governance in Sweden

Ahead of the 2014 AGM season, Första AP-fonden owned Swedish equities to a value of just over SEK 30 billion. This makes us one of the 25 largest owners on the stock exchange, enabling us to influence decisions made at AGMs. In 2014 the Fund participated in all of the AGMs of our Swedish portfolio companies. We have the greatest opportunity of influencing decisions if we discuss key issues with the companies' boards and management teams ahead of AGMs. This often enables reaching a joint solution or at least a proposal for a compromise that is acceptable to all parties.

In 2014 Första AP-fonden mainly acted in three matters: senior executive remuneration, board fees and the anti-corruption work of companies. The table below shows the Fund's actions in dialogues with Swedish companies with respect to these matters. In order to enable a sustained credible dialogue, we have chosen to omit the names of the companies. In addition, the Fund has discussed greater equality and diversity on Swedish boards with a number of nomination committees.

In the forthcoming AGM season, the Fund continues to focus on the board composition of Swedish companies. By increasing boardroom diversity, for instance by electing in more women, the quality of board work can improve. The share of women on Swedish boards has increased in the past few years, albeit slowly. In October 2014 the Swedish Corporate Governance Board issued instructions on how

companies, nomination committees and owners ought to handle the matter of equality on Swedish boards. Första AP-fonden concurs with the instructions of the board.

The Fund will also continue to exert influence so that the senior executive remuneration of companies is devised in a way that supports the value creation processes of the company. All too often, the performance requirements of the remuneration systems are misaligned with the company's value drivers. Furthermore, the Fund requires that nomination committees, ahead of the 2015 AGMs, will justify proposed increases to board fees more thoroughly than before. In general, substantial improvement can be achieved in terms of the justifications of companies and nomination committees in instances of deviations from Code rules. The previous year's focus on companies' anti-corruption work will also be followed up on.

Overview of Första AP-fonden's work with remuneration issues ahead of 2014 AGMs

Company	Case	Fund's action	Company's response	Decision	Comment
SENIOR EXECUTIVE REMUNERATION					
A	Incentive programme lacking sufficient performance requirements and heavily subsidised	Dialogue with demands for improvement	Reduced subsidy	Yes	The Fund ought to attempt to further improve the programme next year
B	New proposal regarding and history of not heeding minority shareholders	Dialogue with demands for tighter performance requirements	Improved	Yes	The Fund ought to attempt to further improve the programme next year
C	Slight changes to the weighting of performance requirements	-	performance requirements	Yes	The proposals were improvements
D	Improvements to long-term	-	-	Yes	The proposals were improvements
E	incentive programme	Dialogue	-	Yes	A matter for the board, not the owners
F	Approval of maximum variable salary	Dialogue	Motivation	Yes	A matter for the board, not the owners
G	Approval of maximum variable salary	Dialogue	Motivation	Yes	A matter for the board, not the owners
H	Approval of maximum variable salary	-	Motivation	Yes	Slight change
I	Increased number of participants in long-term incentive programme	Questions ahead of the AGM	-	Yes	Clear information ahead of the AGM
J	Amended policies for senior executive remunerations	Dialogue with demands for motivation	Sound motivation	Yes	Company with a history of good information and sound evaluations
BOARD FEES					
K	Sharp increase in board fees	Joint proposal at AGM	None	Own proposal	Fees should not be increased for some years
L	Sharp increase in board fees	Proposal at AGM backed by many other institutional investors	None	Own proposal	Fees should not be increased for some years
M	Sharp increase in board fees (from a low level)	Discussions	-	Yes	Now on a par with peers
N	Sharp increase in board fees	Support for nomination committee member	The nomination committee did not submit proposals	-	New proposal probable in 2015
ANTI-CORRUPTION WORK					
O	Low points in the Fund's own survey	Dialogue	Several improvements		Continued dialogue
P	Low points in the Fund's own survey	Dialogue requested	-		Continuing to urge commencing a dialogue
Q	Low points in the Fund's own survey	Dialogue	Several improvements		Continued dialogue
R	Corruption accusation	Dialogue	Several improvements		Continued dialogue
S	Corruption accusation	Dialogue	Several improvements		Continued dialogue

Corporate governance at foreign companies

Första AP-fonden voted at 251 AGMs of foreign companies in 2014. How the Fund voted at the AGMs is described in detail at www.ap1.se. In order to enable carefully considered voting in so many companies, analysis and voting recommendations from external suppliers are used, although the Fund itself always ultimately decides on how to vote. The supplier adapts its recommendations to the Fund's ownership policy.

In certain selected matters in which the Fund votes against the board's proposal, the Fund contacts the companies and sets forth its arguments. Such a matter is that the CEO and chairman of many foreign companies is the same person, which is particularly commonplace among American companies. The board will have difficulty in evaluating the CEO of the company when he or she is also the chairman of the board. We therefore propose through and through that the chairman shall be independent of the company and its management. In Sweden, the Companies Act prohibits having the same person as CEO and chairman.

Another area in which Första AP-fonden often finds reason to contact the companies when we have voted against the board's proposal is remuneration matters, such as remuneration programmes that reward management without any performance requirements, or programmes that reward management for factors they do not influence, such as a generally bullish stock market or changed commodity prices.

Many companies also wish to introduce some type of barrier to protect the company in buyout situations. This can be the right of the board to issue new shares at a discount to all or one of the current shareholders in order to put a stop to a potential bidder. Other examples are board resolutions to pay major remuneration to management if a bid goes through. In Första AP-fonden's opinion, the shareholders shall determine matters of bids on the company. The owners shall have the opportunity to take a position on the bid and determine whether or not it should be accepted.

Dialogue with foreign companies is often conducted in collaboration in the Ethical Council of the AP funds. In 2014 the Ethical Council conducted around 230 dialogues with foreign companies. The yearly reports on the operations of the Ethical Council are available at www.apfonderna.se.

Excluded companies

In cases where the companies in which Första AP-fonden has invested conduct operations in a manner that is not in line with the Fund's values, a dialogue with the company is initiated. In many cases, this is done jointly with other investors, chiefly through the Ethical Council of the AP funds.

Influence through dialogue is, in the opinion of the Fund, preferable to divesting the holding. The problems do not disappear because Första AP-fonden sells its shares. However, successful dialogue with the company can lead to rectification of the problems. In turn, this means that the value of the company can increase.

In certain cases, the dialogue held by the Fund and other investors with the company does not lead to any improvement in a reasonable amount of time. In some cases, the companies' operations are not in line with the Fund's values. In such cases, the Fund excludes the company from future investment. In the table below, the Fund's currently excluded companies are shown.

Companies excluded by Första AP-fonden	
Alliant Techsystems inc	Potash Corp of Saskatchewan
Freeport-McMoRan Copper and Gold Inc.	Poongsan Holdings Corporation
Gencorp Inc	Raytheon Company
General Dynamics Corp	Singapore Technologies Engineering
Elbit Systems	Textron
Incitec Pivot Limited	Wal-Mart Stores Inc
L3 Communications Hldgs	Wal-Mart de Mexico
Lockheed Martin Corp	Wal-Mart Chile
Massmart Holdings Limited	

Besides the list above, Första AP-fonden also follows the sanctions issued by the EU against certain Russian companies and individuals. As government authorities, the AP funds follow the sanctions supported by the Swedish government. Hence, the funds follow the sanctions decided by the EU and UN. In terms of sanctions issued by bodies other than Sweden, the EU and UN, the AP funds are under no obligation to follow them.

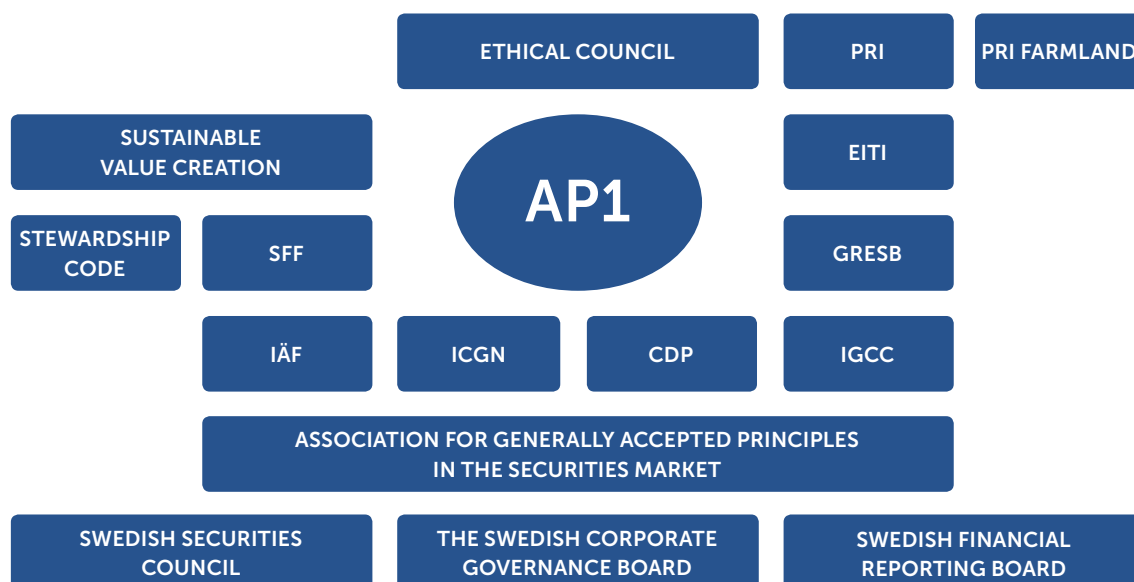
Shares on loan

With a view to increasing return on the equity portfolio, Första AP-fonden lends shares when beneficial. This only occurs in ten countries (Finland, Germany, Hong Kong, Italy, Japan, Mexico, Norway, Poland, Singapore, the UK, South Africa, South Korea, Spain, Switzerland and the US). Shares in Swedish companies are not subject to lending. The Fund lends a maximum of 85 per cent of each individual position and hence remains as an owner and obtains all the information directed to shareholders. So as not to lose the possibility of voting at an AGM or EGM, the Fund reserves the right to recall shares on loan at short notice.

COLLABORATIONS, GUIDELINES AND INITIATIVES ENDORSED BY FÖRSTA AP-FONDEN

In its shareholder activism, Första AP-fonden collaborates with other investors and is a member of a number of national and international networks and organisations. These collaborative efforts not only

give the Fund greater leverage in crucial issues, they also increase the Fund's knowledge about developments in the financial industry and markets.



The Ethical Council of the AP funds

Through the Ethical Council, the First, Second, Third and Fourth AP funds work jointly with environmental and ethical matters in the companies in which they hold shares outside Sweden. Read more about the Ethical Council of the AP funds on page 18 and at www.etikradet.se.

“Hållbart värdeskapande” (sustainable value creation)

A collaborative project initiated by investors. Its purpose is to highlight the importance of companies undertaking structured sustainability work and providing sound sustainability reporting so that investors may make investment decisions and have a solid foundation for influencing companies.

SFF

The Swedish Society of Financial Analysts is a member organisation for financial analysts active in the Swedish capital market. The association has a Corporate Responsibility as well as a risk analysis work group, in which the Fund actively participates.

The Institutional Owners Association for Regulatory Issues in the Stock Market (IÄF)

The aim of the association is to promote sound development of self-regulation on the stock market and is one of the principals behind the Association for Generally Accepted Principles in the Securities Market.



The Association for Generally Accepted Principles in the Securities Market

The purpose of the association is to promote the observation and development of generally accepted practices on the securities market. The association works for this purpose through the Swedish Securities Council, The Swedish Corporate Governance Board and the Swedish Financial Reporting Board.

The Swedish Securities Council

Through statements, advice and information, the Swedish Securities Council promotes sound practices on the Swedish stock market.

The Swedish Corporate Governance Board

The board has the overarching mission of overseeing and administering the Swedish Code of Corporate Governance and otherwise promoting sound corporate governance at listed Swedish companies.

The Swedish Financial Reporting Board

The board works to adapt and develop sound accounting practices and financial reporting for listed companies in Sweden. The board also promotes Swedish interests in accounting issues at the international level.

PRI

Principles for Responsible Investment, a UN initiative for responsible investment.

Carbon Disclosure Project (CDP)

CDP is an international collaborative initiative to increase corporate awareness of climate change.

EITI

Extractive Industries Transparency Initiative is an initiative to increase transparency in extractive industries.

ICGN

International Corporate Governance Network is a global member organisation promoting raising the standard of corporate governance worldwide.

Climate and carbon footprint

Första AP-fonden participates in a number of collaborative projects for climate. The Fund was the only Swedish fund to participate in a major climate research project along with other investors. The Fund is now participating in the follow-up project that will be presented in the first quarter of 2015. The Fund is also a member of the Institutional Investors Group on Climate Change, IIGCC and has endorsed both the Carbon Disclosure Project, CDP and the Montreal Carbon Pledge.

Corporate governance in the UK

The Fund has endorsed the Stewardship Code in the UK.

Anti-corruption

The Fund is a member of the Extractive Industries Transparency Initiative, EITI and has endorsed the Global Compact Call to Action: Anti-Corruption and the global development agenda.

THE ETHICAL COUNCIL OF THE AP FUNDS

The Ethical Council of the AP funds is a collaborative initiative between the First, Second, Third and Fourth AP funds with the purpose of influencing foreign companies owned by the funds towards more sustainable business. The Ethical Council is guided by making a difference by being long-term in its approach, responsible and engaged in its work to influence companies into improving their work with environmental and social issues.

The Ethical Council works proactively and reactively. Problem areas and incidents are systematically identified and analysed by the Ethical Council, which then selects a number of focus areas and companies. In 2014 the funds conducted dialogues with just over 230 companies dispersed across the entire globe through the Ethical Council.

The companies with which the Ethical Council conducts a dialogue are primarily identified by the screening performed twice a year of all of the funds' equity holdings in order to find out whether any company is in violation of any international convention. This screening is performed by

an external consultant. The work is based on the principles regarding engagement, action and change with the goal of making a difference. The Ethical Council identifies companies that can be linked to breaches of a convention and works with influencing companies into addressing violations that have transpired and implementing systems and measures to prevent future violations.

With the purpose of influencing the companies, dialogue is an important tool for the Ethical Council. If companies in which the funds have invested can be linked to breaches of a convention, the fundamental point of departure is that the funds shall use their ownership to put a stop to the breaches, and work to promote the implementation of systems and measures to prevent future violations.

By being engaged and using ownership to act against violations of conventions, and by imposing demands for change, the funds can make a difference. A recommendation from the Ethical Council to divest the funds' holding in the company is considered only if this cannot be achieved. Read more at www.etikradet.se



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