

# Alternative investments

**The Fund's external asset management mandates are gathered in the Alternative investments group. These are asset classes that differ from each other, but which still present certain common challenges.**

Several of the Alternative investment mandates manage illiquid assets. Illiquidity is one of several systematic risk premiums that give a return, and one to which AP2, as a long-term investor with predictable flows, would like to be exposed.

The change in the investment rules for the buffer funds that entered into force in 2019 increased the Fund's opportunities to invest in illiquid assets. The rules that may enter into force in 2020 are expected to further increase these opportunities.

"We may not see the results of the investments we make today before five to seven years have elapsed. So we need to think ahead a great deal, to make wise investment choices. You need to be on your toes all the time, and ask whether we are missing anything? What is the best long-term strategy for our portfolios? Do the asset managers have a clear sustainability focus?" says Anders Strömblad, Head of Alternative Investments.

## Shared challenges

The Fund's external management mainly takes place via funds, but sometimes also via companies that the Fund owns together with like-minded institutional investors that share the Fund's long-term strategy and sustainability values. One example is Vasakronan within real estate. Even though the characteristics of a good asset manager vary for the differ-

ent asset classes, the group's members face the same challenge – to have skilled managers that suit AP2.

"It's not just a question of delivering a good return at low cost, but also of having asset managers with whom we can share knowledge. For us it's important to understand our managers' process, not least when it comes to sustainability," says Patrik Jonsson, who is responsible for the Fund's external managers of listed assets.

## Developing the sector

Sustainability is an area that has increased in significance for society and the investment world in recent years, and this trend is expected to continue to rise in the future. The Fund's sustainability work is expressed in different ways. For the Alternative Investments group, this partly concerns being involved in and developing the sector.

AP2's CEO Eva Halvarsson is a member of the Board of Principles for Responsible Investment (PRI), a UN-supported body that works to promote sustainable investments. Anders Strömblad is a member of PRI's Committee for Private Equity, and the Board of ILPA (Institutional Limited Partners Association), the trade organisation for investors in private equity funds, which are both involving in setting guidelines for the sector. Furthermore, Helena Olin, who is responsible for the Fund's real estate

investments, is a member of the committee that supports GRESB (the ESG Benchmark for Real Assets) in its work.

## Ongoing assessment

The day-to-day work concerns assessment of the asset managers' processes and follow-up on their reporting. This takes place in different ways, depending on the asset class involved. Within real estate, the GRESB sustainability assessment is an important tool.

"All of our funds and companies must be members of GRESB and we annually follow up on their results in the assessment. The aim is year-on-year improvement. For our companies, we also have an annual sustainability day, when we review the past year and assess how we can become better," says Helena Olin.

The Fund's real estate investments now have a GRESB score that averages 95 out of 100, which is one of the best in the sector.

For the assets for which the department holds the asset management responsibility, the sustainability work is an important element of both the due diligence process for new asset managers, and of the ongoing development.

"There's a multi-faceted scale of questions regarding sustainability, with both risks and opportunities, which makes this an important focus area for us," says Anders Strömblad.

*"So we need to **think ahead** a great deal, to make wise **investment choices**"*

## Listed external mandates

**Patrik Jonsson, responsible for external managers of listed assets**

Over the years, AP2 increased its internal management of equities and thereby took home several mandates from external managers. Some are still left, however, including for Chinese A-shares listed on Chinese mainland exchanges.

“The challenge is to find managers with whom we can cooperate. We want to learn how this works in China and also raise their level within sustainability, for example,” says Patrik Jonsson.

The focus during the year included assessment of a new asset class – non-listed credits.

“This is a continuation of a theme we saw after the financial crisis in 2008. When banks’ lending opportunities are reduced, the demand for alternative credits increases,” says Patrik Jonsson.

## Real estate

**Helena Olin, responsible for traditional real estate**

Within real estate, AP2 requires long-term investments in expanding regions, with focus on offices. In developed countries, investments are made via companies, such as Vasakronan in Sweden, together with like-minded investors.

“The biggest challenge is to conduct good board work and stay updated on developments concerning markets, technical development and changed customer behaviour. The challenge now is also to identify good investments, since valuations are at a historically high level,” says Helena Olin.

During the year, the Fund focused on increasing investments in Asia, which are made via funds and affiliated investments to these, and on individual large projects in the European and American companies.

“US Office Holdings has almost 30 per cent of the portfolio in projects, so this has taken up a lot of time during the year,” says Helena Olin.

## Private equity investments

**Camilla Axvi, responsible for private equity investments**

Within private equity, the Fund adheres to a target allocation between different geographies and investment styles, such as venture, growth and buy-out. The challenge is to stay updated on the market’s development and to find high-quality asset managers who are assessed to have the capability to deliver good future returns.

“We have a global portfolio in which we are now increasing our allocation, after changed investment rules and a new strategic target allocation, which entails that we will be making more and, in specific cases, larger investments. As part of the portfolio structure, existing managers and strategies are assessed actively against new alternatives. We can see that the range of strategies and the number of managers in the private equity markets have increased, which has increased our own opportunities. For example, there are now funds with a more pronounced focus on sustainability, which is interesting,” says Camilla Axvi.

“More opportunities require discipline, however, in terms of having a stringent selection process for our choice of strategy, and also that the overall assessment to a great extent concerns safeguarding processes, and assessing people and organisation cultures. This requires frequent meetings and that we also meet the investment team and their on-site organisation,” says Camilla Axvi.

## Timberland and farmland investments

**Jessika Ingvarsson, responsible for timberland and farmland investments**

A challenge within timberland and farmland investments is to find formats that match the Fund’s investment horizon, which for these investments extends to at least 20 years. Customary fund structures often have an investment horizon of ten years, which is too short.

“Our farmland investments are therefore via companies together with other investors, who share our values concerning long-term strategies and sustainability. Due to the nature of these investments, we have a very strong focus on sustainability. Via board work in the companies, we can be involved in influencing the asset managers’ sustainability work, and we can gain new knowledge and make proposals for further development and improvement within the area,” says Jessika Ingvarsson.

The trade war between China and the USA strongly affected both the timberland and farmland markets during the year.

“We’re monitoring the conflict closely, but since we’re fully invested, there’s not so much we can do. We can nonetheless see the value of our geographical diversification. When exports and commodities prices in the USA are declining, for example, this benefits other regions in which we have invested,” says Jessika Ingvarsson.