

**VER**

VALTION ELÄKERAHASTO  
STATENS PENSIONSFOND  
THE STATE PENSION FUND

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Annual Report 2007

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## Contents

The State Pension Fund	3
Key Indicators	4
Current Issues in 2007	5
Managing Director's Review	6
Investment Environment	8
Fixed-Income Investments	12
Equity Investments	14
Other Investments	16
General Investment Principles	18
The State Pension Scheme	21
18 Years of the State Pension Fund	22
Administration	24
Financial Statements	27
Balance Sheet	28
Contact Information	30

## The State Pension Fund

VER is a fund established in 1990, whose proceeds the State uses to prepare for the financing of future pension liabilities and balancing of pension costs. VER is an investment organisation with the task of managing and investing the assets allocated to it by the State. VER's investments totalled EUR 12.1 billion in 2007.

Employers and employees covered by the State Pension Scheme make pension contributions to the State Pension Fund. All State pensions are paid out from appropriations reserved for that purpose in the State budget. VER's assets are transferred to the budget on an annual basis. In practice, the State Treasury handles pension matters on the State's behalf.

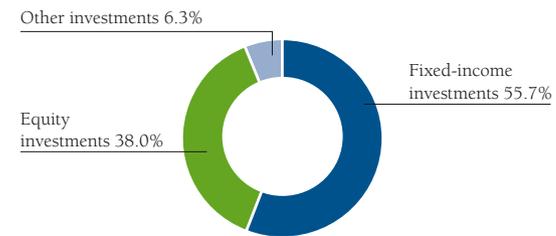
## Mission

The State Pension Fund manages the assets entrusted to it over the long term. VER must ensure that the investments are secure, deliver a high return, can be converted into cash and are appropriately diversified.

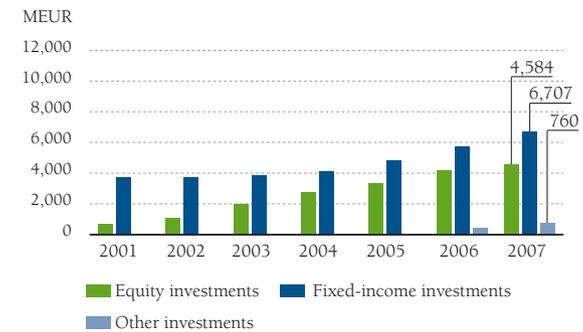
## Vision

VER is a respected and successful pension investor, emphasising excellent professional skills and ethics throughout its operations.

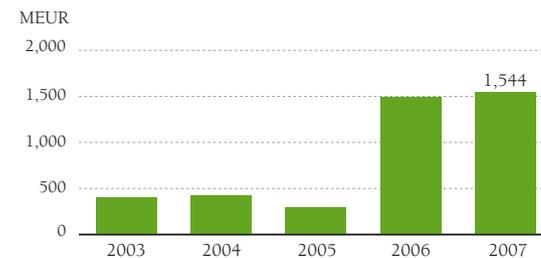
The State Pension Fund's investment portfolio breakdown on 31 December 2007



The trend in the VER's investments 2001–2007



VER's net premium; 5 years



# Key indicators 2003–2007

	2003	2004	2005	2006	2007
<b>Total investments, MEUR</b>	<b>5,795</b>	<b>6,867</b>	<b>8,201</b>	<b>10,306</b>	<b>12,051</b>
Fixed-income investments, MEUR	3,821	4,113	4,848	5,722	6,707
Fixed-income investments, %	66%	60%	59%	56%	56%
Equity investments, MEUR	1,974	2,754	3,353	4,163	4,584
Equity investments, %	34%	40%	41%	40%	38%
Other investments, MEUR				420	760
Other investments, %				4%	6%
<b>Income from investment operations, %</b>					
Return on investments	9.4	9.6	14.9	7.0	1.8
Fixed-income investments	4.0	7.0	5.4	0.1	1.8
Equity investments	20.7	14.4	30.8	17.4	0.7
Other investments				6.7	9.5
<b>Operating expenses (% of average capital)</b>	<b>0.05</b>	<b>0.05</b>	<b>0.05</b>	<b>0.04</b>	<b>0.04</b>
Personnel	11	13	15	14	16
Income from pension premiums, MEUR	1,324	1,380	1,462	1,491	1,542
Net premiums, MEUR	408	431	296	1,496	1,544
Transfer to state budget, MEUR	917	952	1,175	0.1	3.5
Balance sheet total, MEUR	5,898	6,620	7,337	9,185	11,165
Pension provision, MEUR	55,100	56,300	57,600	79,300	82,700
Funding rate, % <sup>1)</sup>	11%	12%	14%	13%	15%

<sup>1)</sup> Investments / pension provisions

## Preparations for increasing pension costs

The State's pension costs will increase significantly within a few years as the baby boom generation reaches retirement age. Correspondingly, the State has prepared for increases in its pension liability by reducing transfers of VER's assets to the State budget in 2006 and 2007. This decision resulted in approximately EUR 3 billion in additional capital for VER. VER's statutory target is a 25 per cent funding ratio.

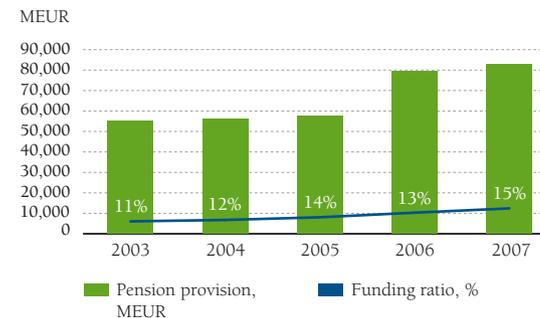
## The Ministry of Finance issues more specific investment orders

The Ministry of Finance issued orders concerning the investment of VER's assets in 2006 and 2007.

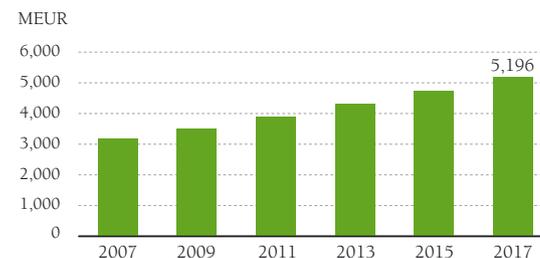
The first order was issued in the autumn of 2006, according to which at least 45 per cent of VER's assets had to be in fixed-income investments. Equity investments were not to exceed 45 per cent, and other investments were not to exceed 10 per cent. The order was changed in November 2007 so that other investments might constitute a maximum of 12 per cent of VER's investment portfolio.



Funding ratio



Trend in State pension expenses 2007 and forecast ► 2017



# VER grows by 46 per cent in two years

**As a whole, the investment year 2007 was challenging, with substantial changes. Our return can be considered reasonable in such a difficult market environment.**

The State Pension Fund VER has continued to grow substantially as investment assets at the end of 2007 exceeded EUR 12 billion. Moreover, the Fund has grown by 46 per cent in two years as a result of State contributions and profitable investments. Our ambition is to manage the assets entrusted to VER in a responsible and professional manner.

The Ministry of Finance's role as a supervisor and issuer of guidance was strengthened in late 2006. According to the Act governing the State Pension Fund, the Ministry of Finance may issue general orders to VER. The first such order was issued in November 2006 and further specified twice during 2007.

The most substantial guideline restricting operations was the setting of allocation limits. According to this guideline, VER must invest at least 45 per cent of its portfolio value in fixed-income instruments. Since November 2007, the maximum for equity investments has been 45 per cent, and 12 per cent for other investments. VER's Board of Directors has made its allocation decisions within these limits. In recent years in particular, VER has increased the proportion of other investments.

## Moderate return in 2007

The return in 2007 can be considered moderate, due to a difficult market environment. Among the asset categories, the return from fixed-income investments has been low for two years, due to rising interest rates. This has affected VER's return, since a substantial proportion of its assets are invested in fixed-income instruments. On the other hand, fixed-income investments have stabilised our returns in the recent uncertain market conditions. We are satisfied with the fact that VER's average return over five years has been 8.5 per cent annually.

In 2007, the diversification of other investments continued, the total amount of other investments and investment commitments approaching one billion euro. The invested amount was EUR 758 million and its return exceeded 9 per cent. Other investments

include real estate, infrastructure and private equity funds, as well as absolute return funds. VER uses these to diversify its investment portfolio and decrease its dependency on the fixed-income and equity markets. We have been successful in achieving this target. According to our selective strategy, efforts in these new areas will continue in 2008, the intention being during the first year half to refine our strategy covering the next few years.

## The year had an active start but ended with uncertainty

The year 2007 saw a clear division, the first part of the year being better than expected as share prices increased substantially. Interest rates rose, and the global economic outlook was positive. The latter half of the year was characterised by the subprime crisis, with the banking and finance sector encountering difficulties due to a lack of confidence and declining market liquidity. This uncertainty continued until the end of the year and market fluctuations were dramatic.

The global capital market saw a revolution in the balance of power in 2007. A new group of investors – Sovereign Wealth Funds – appeared in the investment market. The capital of these funds has already reached some 3,000 billion dollars and is expected to grow substantially over the next few years. Sovereign Wealth Funds have assisted international banks with their capital requirements. They have diversified their assets globally and created a new balance of power in which the significance of emerging markets and oil-producing countries is further increasing.

The development of the economy and capital markets is playing a key role in VER's future. We expect to achieve our target of returns exceeding the cost of the national debt over the long term.

We now have a history of four profitable years, and will continue our efforts bent towards diversification and balancing the investment portfolio within the specified limits.

I would like to convey my warmest thanks to our staff and partners for the past year.

*Timo Löyttyniemi*  
*Managing Director*



“The return in 2007 can be considered moderate,  
due to a difficult market environment.”

# Economic environment offers growth and turbulence

**While the economies of the euro area and Asia grew in 2007, the US Federal Reserve had to respond to market turbulence and ease its monetary policy. A strengthened euro slowed down the growth of European exports.**

Global economic growth continued at an extraordinary strong rate for most of the first half of 2007. In the latter half of the year, mounting credit losses in the US subprime market caused concern over the state of financial institutions and funds that have invested in such securities.

One of the turning points in the generation of this market turbulence was an almost complete loss of liquidity in the credit derivatives market in the late summer. From time to time, the liquidity of the cash market for sovereign bonds was also weak in the euro area. On the one hand, the adjustment of corporate bond premiums can be considered a rectification and on the other hand, a return to the normal pricing of risk.

## Central banks began stabilisation immediately

A rapid and, at times, almost complete loss of liquidity in the market required the immediate intervention of central banks in order to secure the stability of the financial markets. The central banks increased market liquidity through various types of financing operations, which slightly eased the acute crisis.

At the same time, economic indicators published in the United States indicated that the cycle was turning towards more moderate growth, a weak housing market and increased financing costs hampering household consumption. Turbulence in the financing market also shook the confidence of consumers and businesses with regard to the future. As a result, the market consensus on gross domestic product development declined.

At the end of the year, the US Federal Reserve retuned its monetary policy from a neutral to a stimulant package, decreasing the Federal Funds rate from 5.25 per cent to 4.25 per cent by the end of the year.

**“The central banks increased market liquidity through various types of financing operations.”**

## Exports boosted economic growth in the euro area

In 2007, the eurozone economy grew quite rapidly, this growth rate declining slightly only by the middle of the year. While growth was sustained by exports, the euro's rapid strengthening against other major currencies probably indicates the end of peak growth in exports.

Strong exports also resulted in a rapid increase in investments. However, tax increases slowed down the development of household consumption. Due to the strong economy and accelerating inflation, the European Central Bank increased its central bank rate to 4 per cent.

## Dualism characterising economic growth in Asia in 2007

Growth accelerated in Japan in the first part of the year but slowed to a moderate level towards the year end. Partially deflatory price developments prevented the Bank of Japan from normalising its interest rates, while the strengthening yen helped dampen growth.

In contrast, China's economy grew at a rate of more than 11 per cent. Economic growth was restrained through interest rate increases and stricter liquid asset obligations imposed on banks.

## VER's investment portfolio increased to EUR 12 billion

At the end of 2007, VER's investment portfolio had a market value of EUR 12.1 billion (EUR 10.3 billion in 2006). At the end of the year, 55.7 per cent of investments were in fixed-income instruments, 38.0 per cent in equities and 6.3 per cent in other investments.

In 2007, the return on the entire investment portfolio was 1.8 per cent (7.0 per cent), while the benchmark index increased by 1.7 per cent. This return is calculated in accord-

ance with the international GIPS standard, from which operating expenses of EUR 4.0 million (EUR 3.7 million) are deducted.

The tracking error for the entire investment portfolio was 0.28 per cent, entailing that the return on the portfolio was almost identical to the benchmark index.

The portfolio's beta was 0.89, the risk level being lower than that of the reference portfolio, and the behaviour of the portfolio was less intense compared to the reference index. Moreover, the Sharpe indicator was -0.68 and volatility was 3.51 per cent, while the information ratio at the end of the year was 0.23, and Jensen's alpha was -0.20 per cent. Risk indicators are calculated on monthly returns over a period of twelve months.

The effective average cost of the Finnish national debt was 4.1 per cent in 2007.

### Fund's own principles applied to shareholder policy

According to VER's shareholder policy principles, it operates as an independent portfolio investor.

Since the Fund is a long-term investor and major shareholder in a number of companies, it would best promote the successful performance of its portfolio companies by acting as a responsible owner. The companies must ensure the increasing value of their shares over the long term.

VER monitors its portfolio companies and their success in order to be able to take a position on their activities and the principal resolutions brought before General Meetings.

To the extent it deems appropriate, VER can get in touch with other institutional investors on matters concerning resolutions at individual companies' General Meetings or other matters of general importance. VER's personnel are not involved in the management of listed companies in which the Fund has holdings.

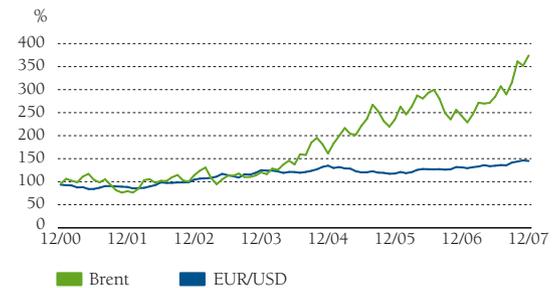
### Responsibility emphasising sustainable development

VER's investment operations are partly controlled through an investment policy of sustainable development. Enterprises compliant with sustainable development are often successful within their industries and thus constitute safe investments.

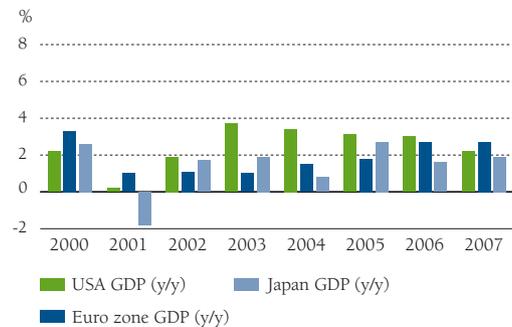
When selecting potential investment targets, VER uses sustainable development indices as a basis for comparison. VER invests primarily on the basis of the expected return from the investment target, but between any two companies equal in this respect, the one selected for the portfolio will be that represented in any sustainable development index.

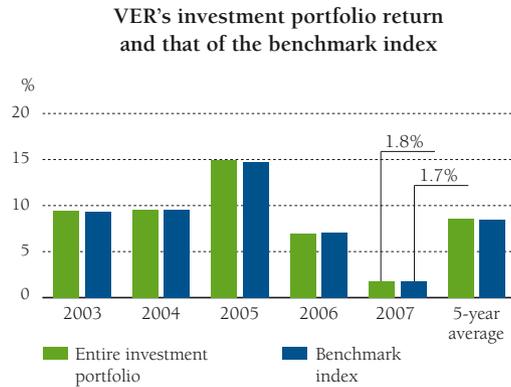
VER applies social responsibility principles to its investments, avoiding direct investments in companies deriving a substantial share of their turnover from the alcohol, tobacco, firearms, pornography or gambling industries. The same pertains to countries

**Trend in the Brent and euro/dollar exchange rate (31 December 1999 = 100)**



**GDP trend in the United States, euro zone and Japan**





and enterprises which do not respect human rights and the fundamental rights confirmed by the International Labour Organisation (ILO).

Responsibility for VER's personnel forms part of the organisation's social responsibility. VER's personnel strategy is based on the shared values of State administration and public service ethics. Its values include professionalism, ethical conduct and openness. VER seeks to be an appreciated and successful fund investor that aims to secure the development of its employees and work community while promoting well-being at work.

## Risk management plays a central role in success

The identification, assessment, limitation and control of risks are key factors in investment operations. It is the task of risk management to ensure that any realised risks will not cause substantial financial losses, endanger the continuity of operations or weaken the confidence of interest groups. The main risks in investment operations are as follows:

Interest rate risk is associated with changes in the market values of bonds as the interest rate level varies. The longer the maturity, the greater the risk of interest rate fluctuations during the investment period.

Credit risk refers to the risk associated with an investment in the case of the bankruptcy of the counterparty.

Liquidity risk refers to the minimum transaction costs involved in entering and exiting the market. This is illustrated by the spread between bid and ask prices.

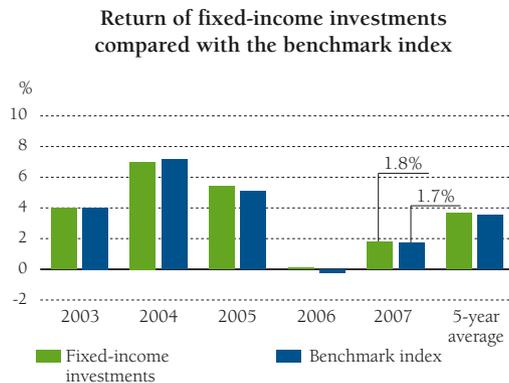
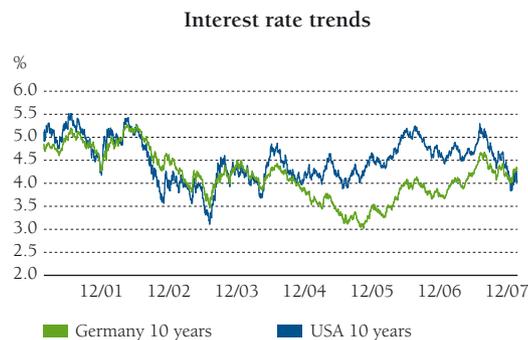
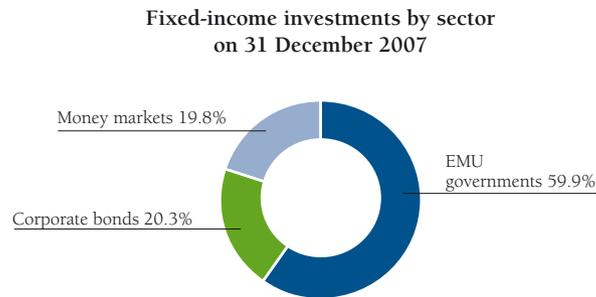
Investments involve foreign exchange risk when investments are made in commitments denominated in currencies other than the euro.

VER's comprehensive risk management plan defines the most important operational risks, risk management objectives, limits of risk exposure, responsibilities, indicators and control principles. In defining the limits of risk exposure, VER's risk taking and risk bearing capacity have been taken into account. The risk management plan also accounts for outsourced operations.

A risk survey has been implemented jointly with PriceWaterhouseCoopers, from 2004 to 2007.



# The fixed-income market year was divided into two



VER's fixed-income portfolio yielded 1.8 per cent in 2007 (0.1 per cent in 2006), while the benchmark index increased by 1.7 per cent. The fixed-income portfolio was characterised by lower duration in the first half of the year, but was raised over the index duration in the latter half.

Corporate bonds and money market investments had a close to neutral allocation at the end of the year. The fixed-income portfolio's volatility was 2.16 per cent, while the corresponding figure for the benchmark index was 2.39 per cent. Moreover, the portfolio's beta was 0.82 and the information ratio at the year end was 0.32.

Risk indicators for the fixed-income portfolio are calculated on monthly returns over a period of twelve months. Calculated according to market values, VER's fixed-income portfolio grew from EUR 5.7 billion at the beginning of the year to EUR 6.7 billion at the end. During the year, bonds were bought and sold for EUR 4,958 million while money market investments totalled EUR 4,144 million during the corresponding period.

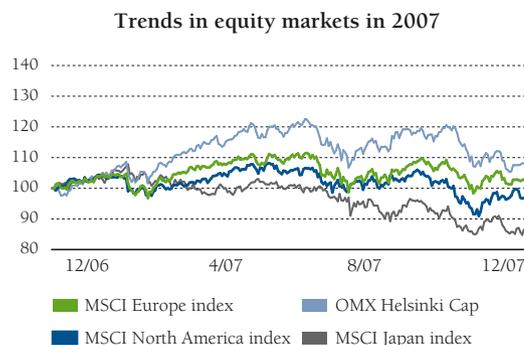
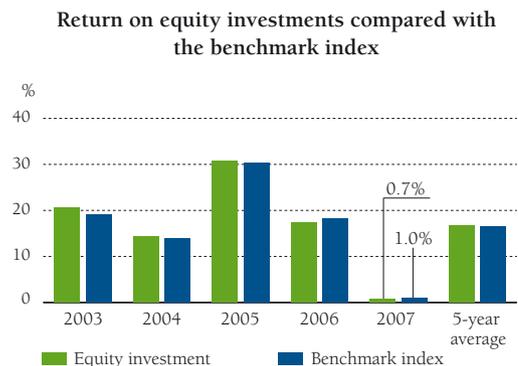
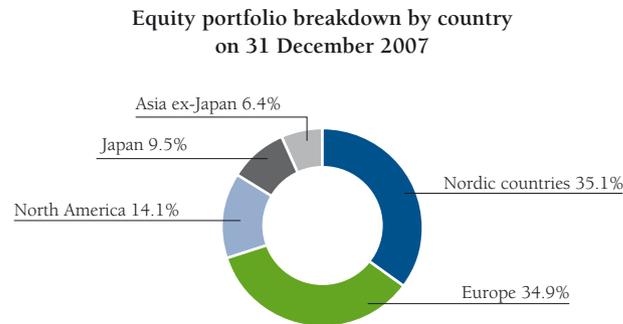
Principally, the VER makes its own direct income investments in sovereign bonds, Investment Grade corporate bonds and money market instruments, while other investments are made through mutual funds. Direct investments accounted for approximately 90 per cent of the aggregate fixed-income portfolio at the year-end, while direct fixed-income investments comprised 197 commitments, and fund units were held in 16 funds.

## Major fixed-income investments on 31 December 2007

			EUR	Percentage of fixed-income portfolio
Government of Italy	1.8.2014	4.25%	146,211,816.52	2.5%
Government of France	25.7.2032	3.15% i/L	144,581,477.76	2.4%
Government of Finland	15.9.2012	4.25%	142,136,537.70	2.4%
Government of Greece	22.10.2022	5.90%	135,141,042.62	2.3%
Government of Greece	18.4.2008	3.5%	122,725,455.74	2.1%
Government of Italy	1.2.2009	3.0%	120,122,739.13	2.0%
Government of France	25.7.2020	2.25%	111,405,190.15	1.9%
Government of France	25.10.2014	4.0%	109,213,686.34	1.8%
OKO ECP	14.1.2008		99,835,369.00	1.7%
Government of France	25.7.2012	3.0%	95,987,149.23	1.6%



# A challenging year for equity investments



The year 2007 proved challenging for equity investments. The apparent upward price trend in equities, which had lasted more than four years, ended in the summer with the outbreak of the US subprime crisis.

At the year-end, the return on VER's equity portfolio was at the modest level of 0.7 per cent (17.4 per cent in 2006), while the benchmark index yielded 1.0 per cent. Small companies yielded lower returns than large ones across the board, which burdened the proportional return on the equity portfolio compared to the benchmark index.

During the year, VER's equity portfolio increased from EUR 4.2 billion to EUR 4.6 billion. This growth was supported by cash flows into the fund, part of which was invested in the equity market in accordance with the neutral allocation. Equities were maintained at a slight overweight during the first part of the year but, from the summer on, the proportion of equities was decreased through allocating incoming cash flows mainly to fixed-income instruments. Equities had a weighting of 38 per cent of the investment portfolio by the year-end.

## Diversification into almost 200 investments

The risk level of the portfolio was maintained at lower-than-market risk for the entire year, with the beta being 0.87. However, Jensen's alpha was negative as the return on the equity portfolio dropped below risk-free interest rates, and the information ratio was negative (-0.50) as the equity portfolio performed worse than its reference index. The equity portfolio's tracking error was 1.35 per cent – in other words, the portfolio closely tracked its benchmark index. Risk indicators for the equity portfolio are calculated over a 12-month period based on monthly figures.

At the end of the year, 59 per cent of VER's equity portfolio was invested through funds and 41 per cent managed as direct investments. Direct equity investments at the year-end consisted of shareholdings in 136 companies, and fund units were held in 53 funds.

During the year, equities were acquired for EUR 1,163 million and sold for EUR 529 million. The dividend yield on VER's direct equity portfolio was EUR 70 million. VER's equity portfolio has yielded an average of 16.8 per cent annually for the last five years.

## Major Nordic equity investments on 31 December 2007

	MEUR	Percentage of the equity portfolio
Fortum Corporation	151,277,100	3.3%
Nokia Corporation	151,164,000	3.3%
Sampo plc	79,732,800	1.7%
Nordea AB	76,671,222	1.7%
TeliaSonera AB	70,515,061	1.5%
Stora-Enso Corporation	54,272,000	1.2%
UPM-Kymmene Corporation	50,443,000	1.1%
Metso Corporation	48,529,000	1.1%
Neste Oil Corporation	47,053,500	1.0%
KONE Corporation B	44,095,600	1.0%

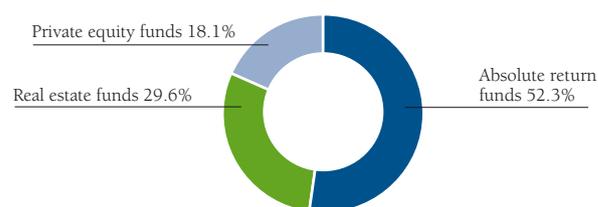
## Major mutual fund investments on 31 December 2007

	MEUR	Percentage of the equity portfolio
Vanguard European Stock Fund	248,036,655	5.4%
Vanguard Japan Stock Index Fund	195,833,604	4.3%
BGI Europe ex UK Index Fund	192,874,854	4.2%
Mandatum North America Enhanced Index	151,369,068	3.3%
iShares DJ Euro Stoxx 50 ETF	127,571,500	2.8%
Mandatum Europe Enhanced Index	120,560,268	2.6%
Vanguard U.S Futures Fund	104,666,551	2.3%
BGI US Index Sub Fund	101,894,442	2.2%
BGI Japan Index Sub Fund	91,066,147	2.0%
BGI UK Index Sub Fund	83,323,771	1.8%

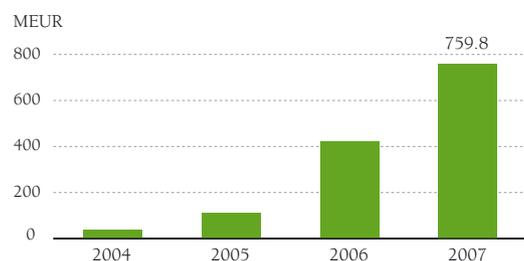


# Return on other investments 9.5 per cent

Breakdown of other investments on 31 December 2007



Market value of other investments 2004–2007



VER's other investments constitute investments in real estate and private equity funds and absolute return funds. New investment opportunities in these sectors were actively surveyed during the year and, as a result, the share of other investments in the total allocation increased to 6.3 per cent (4.1 per cent in 2006).

The market value of the portfolio at the end of the year was EUR 760 million, while the amount of open investment commitments was EUR 319 million. Of the total amount of invested assets and open investment commitments, indirect real estate investments amounted to 31.0 per cent, listed real estate investments to 1.5 per cent, private equity investments to 30.6 per cent and absolute return funds to 36.8 per cent.

VER's other investments yielded a total return of 9.5 per cent. Absolute return funds yielded 5.6 per cent, private equity funds 15.7 per cent and real estate funds 13.4 per cent.

## Other major investments on 31 December 2007

Real estate funds	Investment commitment	
Aberdeen Indirect Property Partners	40,000,000	European fund of real estate funds
Morgan Stanley Eurozone Office Fund	40,000,000	European open-ended real estate fund
CapMan Real Estate I Ky	30,000,000	Finnish real estate fund
Franklin Templeton European Real Estate Fund of Funds	30,000,000	European fund of real estate funds
NV Kiinteistörahasto I Ky	30,000,000	Finnish real estate fund
Private equity funds	Investment commitment	
Crown European Private Equity	40,000,000	European buy-out fund of funds
Access Capital Fund III Mid-market Buy-out Europe	35,000,000	European buy-out fund of funds
Partners Group European Buy-Out 2005 (A)	35,000,000	European buy-out fund of funds
Absolute return funds	Purchase price	
Green Way Arbitrage - The Diversified Fund II	80,113,991	Multistrategy hedge/absolute return fund of funds
R2 Alpha Strategies I Fund	60,095,846	- " -
UBS Global Alpha (F)	59,134,957	- " -



# Target of funding 25 per cent of the State's pension liability

The State Pension Fund is external to the State budget, VER being established to secure the payment of State pensions in the future and balance the costs arising thereof. VER is accumulating assets for the purpose of balancing the cost burden of pensions payable to the baby boom generation during peak years through the controlled dissolution of the Fund.

The Fund's operations are governed under a specific Act. Moreover, the Fund has a Board of Directors appointed by the Ministry of Finance that decides on the Fund's investment principles and which is responsible for its operations.

VER does not pay pensions out of its own assets but the State Treasury pays State pensions from appropriations made in the State budget. An amount corresponding to 40 per cent of the State's pension costs is transferred annually from VER to the budget.

At the end of 2007, the Fund's capital at market value stood at EUR 12.1 billion. The Fund will be accumulated until its capital corresponds to 25 per cent of the State's pension liability, and the use of assets after the funding target is reached shall be regulated separately.

## VER diversifies its investments

VER ensures that its investments are secure, deliver a high return, can be converted into cash and are appropriately diversified.

The Fund's goal is to be a respected and successful pension investor, emphasising excellent professional skills and ethics throughout its operations. Correspondingly, the Fund seeks to demarcate and develop its corporate image as an independent portfolio investor.

## Investing in the long term

Since no insolvency requirement is placed on the Fund, the characteristics of its investment operations are defined by the expected return and the choice of risk level.

The expected return and risk of VER's investment portfolio have been assessed on the basis of long-term historical returns and expert assessments. In this respect, the Fund's long-term expected return corresponds to a real return of approximately 3 to 4 per cent.

## Neutral basic allocation as a guide

VER's annual investment plan defines a neutral basic allocation for the investment portfolio, according to which investments are allocated to different investment categories. Here, the goal is to create a portfolio that yields the best possible return over the long term at the risk level defined by the Board of Directors.

The neutral basic allocation refers to an index-linked and feasible distribution of investments. It is continuously monitored and changed according to need.

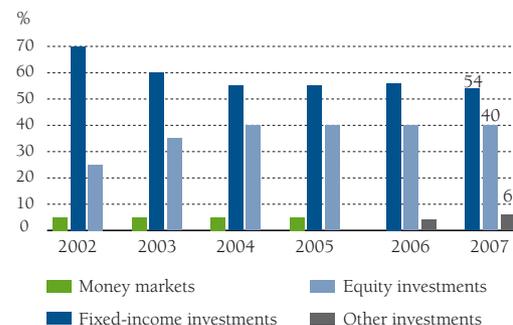
The neutral basic allocation guides investment operations in the long term. Changes are not made too often since this would render the control and prediction of operations too difficult, while increasing the risks and costs of investing.

## Co-operation networks creating benefits

VER's staff aims to create a functional co-operation network in support of its operations. This network includes the management of companies in which VER invests, public authorities, Finnish and foreign providers of investor and brokerage services, as well as other European pension investors.

The strong confidence of external parties in VER's stability helps in obtaining reliable expert services. Indeed, VER's reputation as a professional partner also results in economic

Basic allocation of VER's portfolio



benefits, giving it a stronger position in negotiating investment service prices. This good reputation also helps in fulfilling the Fund's recruitment needs.

### Buffer fund's operating model

VER is a so-called buffer fund, which means that unlike TEL (EPA) pension companies, it does not have any pension liabilities to be individually covered. Therefore, VER is not subject to regulations governing its solvency.

VER is a long-term investor. It applies an investment policy that allows the return on investments to vary considerably over the short term. Investment decisions are taken on the basis of the Fund's required return and the yield potential of prospective investments, taking risk levels into account. Risks are diversified through investing in different investment categories, different markets and industries, different instruments, different companies, as well as bonds issued by different governments and of different maturities.

VER operates as an independent portfolio investor. It does not intervene or participate in the administration of companies that it holds but this does not prevent discussions with corporate management, such direct contacts improving the Fund's expertise and competence as an investor. VER representatives can attend General Meetings in order to attend to shareholder interests, and the organisation has its own shareholder policy principles.

All instruments belonging to the investment portfolio can be bought and sold, and external advisors can be used in this process. The Fund's investments are always made based on the best available information, knowledge and understanding.

### Operations assessed as a whole

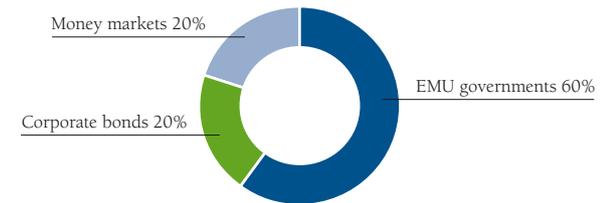
The success of investment activities is analysed on a long-term basis, chiefly considering the portfolio from an overall perspective. While the fixed-income and equity portfolios' performances are monitored separately, the success of other investments is monitored in relation to a constructed fixed benchmark index.

The international GIPS standard is applied to the calculation of the fund's returns. This unifies the different methods of return and risk calculation and renders the figures comparable.

Clarity is emphasised throughout the Fund's operations. The responsibilities and roles of personnel responsible for investment activities are defined, improving the controllability of investment activities.

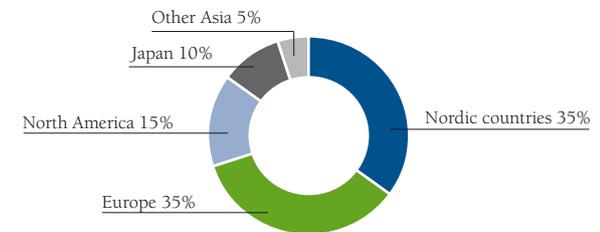
#### Neutral allocation of fixed-income investments at the end of 2007

Basic allocation weight %



#### Neutral allocation of equity investments at the end of 2007

Basic allocation weight %

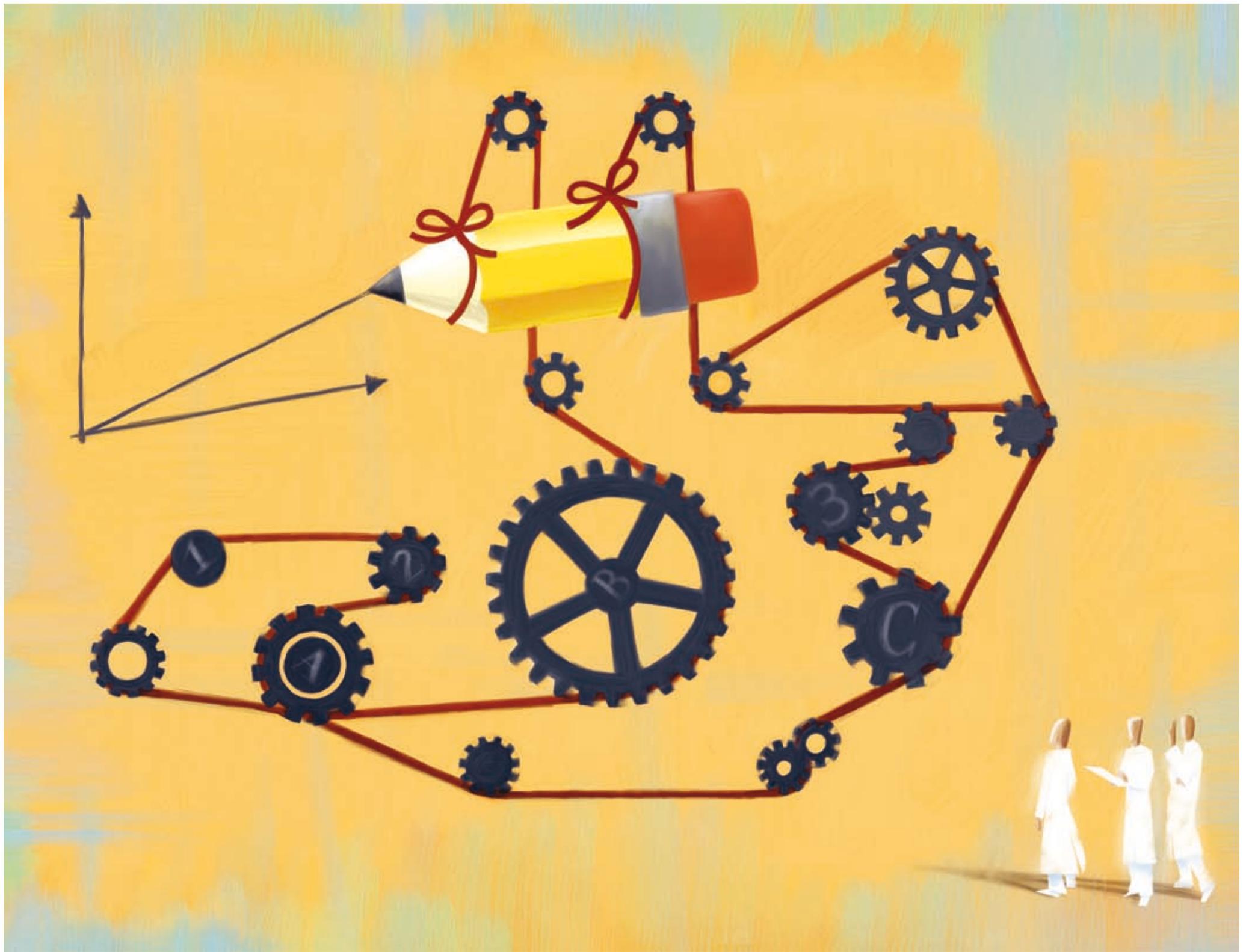


#### Fixed-income portfolio benchmark indices:

Effas EMU Government	45%
Barcap EMU HICP Linked	15%
JP Morgan Cash Index	20%
Lehman Euro Aggregate ex Treasuries	20%
	100%

#### Equity portfolio benchmark indices:

OMX Helsinki Cap	24.5%
OMX Stockholm Benchmark Cap	10.5%
MSCI Europe	24.5%
MSCI Europe Value	10.5%
MSCI North America	15%
MSCI Japan	10%
MSCI AC Far East Free ex Japan	5%
	100%



# VER balances the financing of pension costs

## The State uses the State Pension Fund to prepare for the financing of future pensions, particularly for balancing upcoming pension costs for the baby boom generation.

In 2007, the State Pension Act covered roughly 180,000 people, of whom 130,000 were State employees. Benefits were paid to 316,000 people. The State Treasury made 19,000 pension decisions and paid pensions of EUR 3.2 billion.

Since the pension reform, in force since the beginning of 2005, the State pension scheme has in most respects been similar to other employment pension schemes in Finland, and State pension cover is at a level corresponding to the municipal and private sector.

The pension reform also introduced the career model to State pensions, according to which pensions are calculated on the basis of employment income and an accumulation percentage for each year. The life expectancy factor also affects the amount of pension.

Through the State Pension Fund, the State prepares for financing pensions payable in the future and for the year-to-year evening out of pension expenditure, which will increase within the next few years due to the baby boom generation. The State is responsible for paying accrued pensions in the future.

VER's investment activities are directed by the Board of Directors appointed by the Ministry of Finance, including representatives from the Ministry as well as employees' organisations.

## Pension expenses EUR 82.7 billion

The State aims at a 25 per cent funding rate in proportion to the pension liability. Moreover, the State Treasury is responsible for implementing the State Pension Scheme and calculating the amount of the State pension liability.

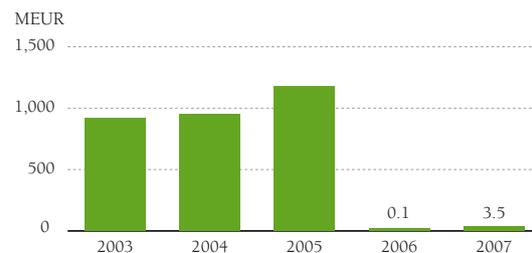
At the end of 2007, the State's pension liability stood at EUR 82.7 billion (EUR 79.3 billion at the end of 2006). It is estimated that the pension expenses in 2017 will be EUR 5.2 billion.

## Funds to the State budget

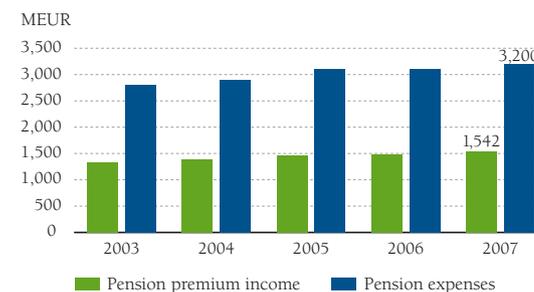
The transfer of funds to the State budget is a crucial factor regulating VER's growth. The State Pension Fund Act stipulates a specified amount for this transfer, which is 40 per cent of annual state pension expenditure.

By the end of 2007, a total of almost EUR 15 billion in VER assets had been transferred to cover the State budget. In accordance with Parliamentary decisions, the transfers of VER assets to the State budget were substantially reduced for 2006 and 2007, increasing the funding of pensions more than previously.

Assets transferred from VER to the State



VER's pension premium income and the State's pension expenses



# 18 Years of the State Pension Fund

## 1989

- The State Pension Fund is established within the State Treasury.
- The funding target is set for the year 2010.

## 1991

- Pension contributions from State offices, institutions and enterprises are directed to VER.

## 1993

- Pension contributions from State employees are directed to VER.
- Investment activities are expanded.
- The transfer of funds to the budget is restricted (3/4 of pension expenditure).
- A Board of Directors is appointed to bear responsibility for the Fund's investment activities.

## 1999

- Municipalities start to pay pension contributions for teachers to VER.

## 2000

- The budget transfer is reduced to one-third of annual pension expenditure until the end of 2006 (one-half subsequent to this).
- The funding target was set at 1.5 times the total of State wages and salaries, a minimum of 20 per cent of the State pension liability, in 2010.
- Designated staff are hired for the Fund.
- Investment activities are extended to equity investments.

## 2003

- A Managing Director is appointed.

## 2005

- The funding target is set at 25 per cent of the State pension liability.
- The annual transfer from VER to the State budget is prescribed as equalling 40 per cent of annual pension expenditure until the funding ratio is achieved. Subsequently, the amount of the transfer will be specified annually in the State budget.

## 2006

- The role of the Ministry of Finance as VER's supervisor was defined more precisely, and the Ministry was granted the right to issue general regulations concerning VER's administration, finances and investment policies.
- The tasks of the VER's Board of Directors are enshrined in law.
- The duties of VER's auditors are enshrined in law.
- The transfer of VER assets to the State budget is reduced for 2006 and 2007.
- The Ministry of Finance issues its first operating guideline to VER in November.

## 2007

- In March and November 2007, the Ministry of Finance specifies the operating guideline, issued in 2006, in more detail.



The State Pension Fund is administered by the Board of Directors and the Managing Director, assisted by a management team. The Minister of Finance appoints the Board of Directors that decides on the Fund's investment policies, this Board of Directors constituting seven ordinary and two expert members. There are six deputy members. Each member's term of office is three years. The Board of Directors convened ten times in 2007.

The Board of Directors appoints a Consultative Committee of seven members for the Fund. The members are external investment and finance professionals. The Consultative Committee assesses the Fund's investment plan, monitors its realisation and reports to the Board of Directors. The Consultative Committee convened twice in 2007.

VER's management team consists of the Managing Director and five other members, and convenes weekly.

## Board of Directors



Eino Keinänen, born 1939  
Master of Political Science  
Chairman



Teuvo Metsäpelto, born 1949  
Licentiate of Laws, Vice Chairman,  
State Labour Market Director,  
Ministry of Finance



Tiina Astola, born 1953  
Licentiate of Laws, Permanent  
Under-Secretary of State,  
Ministry of Justice

### Deputy member:

Veikko Liuksia  
Senior Adviser, Legal Affairs  
Ministry of Finance

### Deputy member:

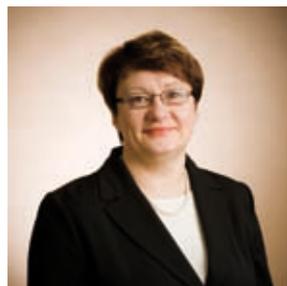
Marja-Leena Rinkineva  
Senior Adviser, Legal Affairs  
Ministry of Trade and Industry



Risto Kangas, born 1954  
Comprehensive school teacher,  
Director of Public Sector Negotiating  
Commission, Organisation of  
Public Sector Professionals JUKO

### Deputy member:

Jarmo Pätäri  
Lawyer, AKAVA - Confederation  
of Unions for Academic Profes-  
sionals



Pirjo Mäkinen, born 1955  
Master of Science, Human  
Resources Manager, Trade  
Union for the Public and  
Welfare Sectors JHL

### Deputy member:

Ilkka Alava  
Head of Research and Social Policy  
Trade Union for the Public and  
Welfare Sectors JHL



Antti Palola, born 1959  
Sea captain, Chairman,  
Confederation of Salaried  
Employees Pardia

### Deputy member:

Seppo Väänänen  
Chief of Negotiations  
Confederation of Salaried  
Employees Pardia



Helena Tarkka, born 1955  
Master of Political Science,  
Associate in Laws, Budget  
Counsellor, Ministry of Finance

### Deputy member:

Raine Vairimaa  
Senior Adviser, Legal Affairs  
Ministry of Finance

Experts



Pertti Saarela, born 1957  
Master of Laws, Director,  
Administration, Employers’  
Association for Transport and  
Special Services (VR Group)



Veikko Liuksia, born 1947  
Master of Laws, Senior  
Adviser, Legal Affairs,  
Ministry of Finance

Management Team



Jukka Järvinen, Head of Fixed Income    Timo Löyttyniemi, Managing Director    Jan Lundberg, Head of Equities

Tiina Tarma, Legal Counsel    Maarit Säynevirta, Head of Other  
Investments since 2 January 2008    Seija Kettunen, Head of  
Administration

**Investment Consultative Committee**

Chairman

Eva Liljebloom, Professor,  
The Swedish School of Economics  
and Business Administration

Liisa Jauri, Head of  
Business infrastructure,  
Nordea

Vesa Puttonen, Professor,  
Helsinki School of Economics

Hanna Kaleva, Director, Institute  
for Real Estate Economics

Vice Chairman

Paavo Prepula, Managing Director,  
Prestart Oy

Topi Piela,

Managing Director,  
Umo Capital Oyj

Jari Sokka, Executive Director  
The Local Government Pensions  
Institution



# Financial Statements

PROFIT AND LOSS STATEMENT	1 Jan – 31 Dec 2007		1 Jan – 31 Dec 2006	
<b>OPERATING INCOME</b>				
Other operating income				
Sales gains on equities and shares	156,964,403.40		159,528,251.73	
Pension contributions from State offices and institutions	854,382,543.74		822,544,491.87	
Other pension contribution income	393,061,002.07		380,392,864.12	
Employees' pension contributions	294,371,726.97		287,910,535.48	
Disability insurance contribution income	5,503,028.50		5,036,973.00	
Other operating income	89,209.32		0.00	
Write-downs on receivables from other operations	0.00	1,704,371,914.00	0.00	1,655,413,116.20
<b>OPERATING EXPENSES</b>				
Materials, supplies and goods				
Purchases during the period	122,987.97		39,981.79	
Personnel expenses	1,280,808.78		1,432,192.26	
Rents	178,717.37		133,625.83	
Outsourced services	2,282,513.27		1,871,956.75	
Other expenses				
Other expenses	159,849.11		132,449.65	
Sales losses on equities and shares	5,287,982.21		6,449,757.98	
Depreciation	9,634.13	-9,322,492.84	112,061.27	-10,172,025.53
<b>SURPLUS I</b>		1,695,049,421.16	1,645,241,090.67	
<b>FINANCIAL INCOME AND EXPENSES</b>				
Financial income		251,256,957.56		202,579,182.18
<b>SURPLUS II</b>		1,946,306,378.72	1,847,820,272.85	
<b>INCOME AND EXPENSES FROM TRANSFERS</b>				
Income				
From trade and industry				
Transfer fees	0.00		-172,686.81	
From financial and insurance institutions				
Returns of pension entitlement	0.00	0.00	0.00	-172,686.81
<b>SURPLUS III</b>		1,946,306,378.72	1,847,647,586.04	
<b>SURPLUS/DEFICIT FOR THE PERIOD</b>		1,946,306,378.72	1,847,647,586.04	

# Balance sheet

Financial Statements | VER ANNUAL REPORT 2007 | 28

ASSETS	31.12.2007		31.12.2006	
<b>FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS</b>				
<b>INTANGIBLE ASSETS</b>				
Intangible assets	234.04		1,170.19	
Other long-term expenditure	0.00	234.04	0.00	1,170.19
<b>TANGIBLE ASSETS</b>				
Machinery and equipment	9,214.33		13,822.07	
Furniture and fittings	144,568.00	153,782.33	21.88	13,843.95
<b>SECURITIES HELD AS FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS</b>				
Purchases of bonds denominated in euros	4,876,681,743.10		4,961,251,965.43	
Other long-term investments denominated in euros	3,427,194,774.55		2,506,864,988.85	
Other long-term investments denominated in foreign currency	1,470,668,575.40	9,774,545,093.05	1,226,656,712.15	8,694,773,666.43
<b>TOTAL FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS</b>		<b>9,774,699,109.42</b>		<b>8,694,788,680.57</b>
<b>CURRENT RECEIVABLES</b>				
Accrued credits and deferred charges	225,263,187.82		213,141,633.53	
Other current receivables	3,443,212.54		14,027.29	
Advance payments	17,426.47	228,723,826.83	4,804.74	213,160,465.56
<b>FINANCIAL SECURITIES AND OTHER SHORT-TERM INVESTMENTS</b>				
Purchases of bonds denominated in euros		1,085,061,656.82		209,406,385.88
<b>CASH, BANK DEPOSITS AND OTHER FINANCIAL ASSETS</b>				
Joint account receivable from the State	3,518,155.36		2,234,973.63	
Other bank accounts	72,913,827.24	76,431,982.60	65,180,156.30	67,415,129.93
<b>TOTAL INVENTORIES AND FINANCIAL ASSETS</b>		<b>1,390,217,466.25</b>		<b>489,981,981.37</b>
<b>TOTAL ASSETS</b>		<b>11,164,916,575.67</b>		<b>9,184,770,661.94</b>

EQUITY AND LIABILITIES	31.12.2007		31.12.2006	
<b>EQUITY</b>				
Fund capital	-13,663,783,855.12		-13,663,679,855.12	
Accrued changes in capital	22,847,855,259.59		21,000,207,673.55	
Budget transfers	-3,540,000.00		-104,000.00	
Surplus/deficit for the period	1,946,306,378.72	11,126,837,783.19	1,847,647,586.04	9,184,071,404.47
<b>LIABILITIES</b>				
<b>CURRENT</b>				
Accounts payable	114,396.86		71,191.26	
Items to be rendered forward	-666.79		20,772.37	
Accrued charges and deferred credits	37,928,206.65		571,762.23	
Other current liabilities	36,855.76	38,078,792.48	35,531.61	699,257.47
<b>TOTAL LIABILITIES</b>		<b>38,078,792.48</b>		<b>699,257.47</b>
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>11,164,916,575.67</b>		<b>9,184,770,661.94</b>

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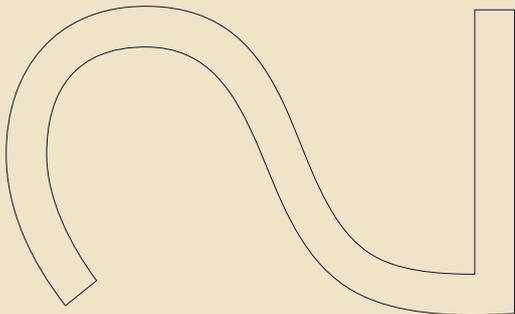
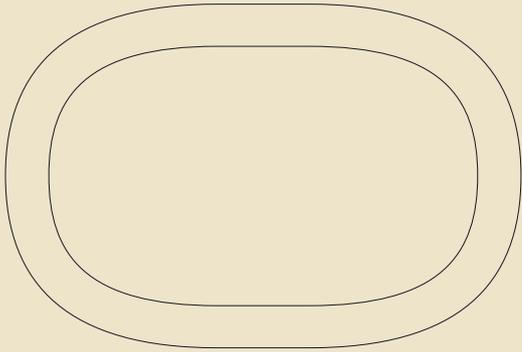
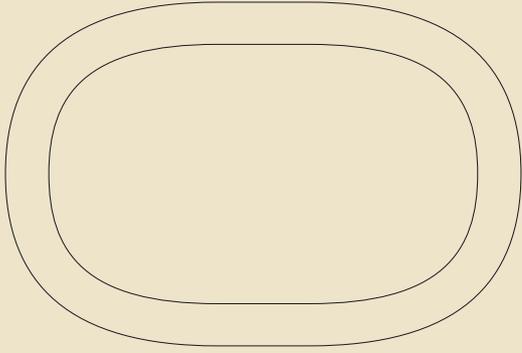
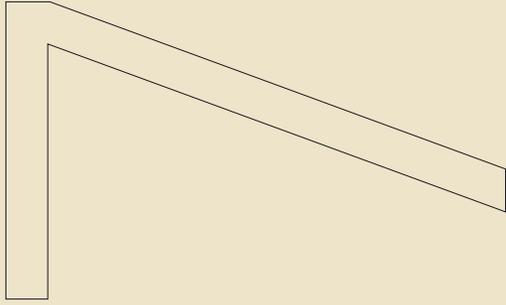
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