

Return over 2004: 11.5%; recovery ongoing, but not yet sufficient

Main points:

- Return over fourth quarter: +4.8%
- Interest-rate fall leads to premium rise
- Transition to nominal interest rate in 2005

Heerlen, 19 January -- Stichting Pensioenfonds ABP announces that it realised an investment return of 11.5% in 2004. The return over the fourth quarter was + 4.8%. Fund assets grew by €18 billion over 2004, from €150 billion to €168 billion. Given an assumed interest rate of 4%, liabilities rose by €5 billion in 2004, from €138 billion to €143 billion, while the coverage ratio rose from 109% to 118% over the same period.

Jean Frijns, CEO of ABP Investments, said: " The return of 11.5% over 2004 was comfortably above our target. The recovery in the fund's financial position is ongoing but is not yet complete. An important factor is that lower interest rates make (new) pensions more expensive. That affects the premium, which must therefore rise by 2.6 percentage points of the basis for premium calculations. In salary terms this means a rise of 1.65 percentage points, of which 0.5 percentage points will be for the account of the ABP participant.

The year 2004 was marked by low wage rises in the governmental and educational sector, and a return of more than 11%. Both factors benefit the development of the fund's financial position. However, the fall in capital-market interest rates to a historically low level (from 4.9% to 4.2% in 2004) has thrown a spanner in the works, because when interest rates are low, the value of future pension liabilities rises. This effect does not arise as long as valuation takes place at a fixed assumed interest rate of 4%. However, as ABP values its liabilities at the nominal market interest rate in view of the introduction of the new Financial Assessment Framework, consequences do ensue. The nominal coverage ratio, which stood at 124.6% at year-end 2003, fell by more than 3 percentage points over the course of 2004 to a level of 121.5%.

The ABP scheme offers nominal pensions with conditional indexation (compensation for wage rises). ABP will not index pensions fully as long as the coverage ratio has not reached the required level. Each year the ABP board determines whether to apply indexation, and if so to what extent, based on the financial position at the time. The indexation percentage for 2005 has been set at 79%. As the relevant wage rise for the sector was 0.15%, this means that pensions will be indexed by 0.12% in 2005.

Most important key figures

	year end 2003*	4 th quarter 2004	up to end of 4 th quarter 2004	change in 2004
Fund position (%)				
coverage ratio at 4% assumed interest rate	109		118	9
Assets (€billion)				
	150.2		168.4	18.2
Liabilities (€billion)				
discounting at 4%	137.8		142.8	5.0
Return on investment portfolio (%)				
Fixed-income securities	0.3	2.5	6.8	
Shares and property	9.7	7.0	16.0	
• Shares	12.6	7.1	12.4	
• real estate	14.2	11.9	30.5	
• Private equity	1.5	5.7	11.2	
• Commodities	-0.7	-10.0	18.8	
Other investments	5.2	3.7	5.8	
Total	11.0	4.8	11.5	
Composition of investment portfolio (%)				
Fixed-income securities	46		43	
Shares and property	52		54	
Other investments	2		3	

* Asset returns over 2003 do not include USD hedging

The return over the fourth quarter was 4.8%, achieved thanks mainly to the high returns on shares and property. Almost 10% of the high return on commodities was lost due to the fall in energy prices. Returns on property were exceptionally high for the second successive year. In 2005, ABP will once again carry out an ALM study to examine whether the current composition of the portfolio is tailored to future liabilities.

Other developments in the fourth quarter

Developments regarding the solvency framework: valuation of liabilities based on current nominal market interest rate

As of 2005, ABP intends to value the liabilities of the pension fund based on the current nominal market interest rate, which is appropriate for a pension scheme with conditional indexation. In doing so ABP is responding to the Financial Assessment Framework, under which the valuation of investments and liabilities at current market value (or "fair value") is also the departure point. This means that in future quarterly reports, the fund's financial position, as expressed by the coverage ratio, will also be based on current values and no longer on a fixed assumed interest rate of 4%, which had been the case until now.

Market prospects: moderately favourable expectations

ABP continues to base its investment policy on a relatively favourable economic scenario over the medium term. Investors face a moderate relationship between expected return and risk, however, due to high valuations in the most important financial markets. This implies that it would be unjustified to extrapolate the past two years' returns into the coming years. The realisation of the long-term target return of 7% per year would appear to be unachievable in 2005.

A number of important developments in the final quarter of 2004 should be explained, given their relevance to the investment climate in 2005.

The US dollar continued to fall against the euro. A structural reversal of this trend will require either a strong increase in expected returns on US financial titles and the belief amongst investors that the correction in the dollar's value has been sufficient, or co-ordinated policy action. We regard such developments as unlikely and expect to see continuing downward pressure on the dollar, with Asian currencies gradually coming to bear a portion of the dollar's weakness.

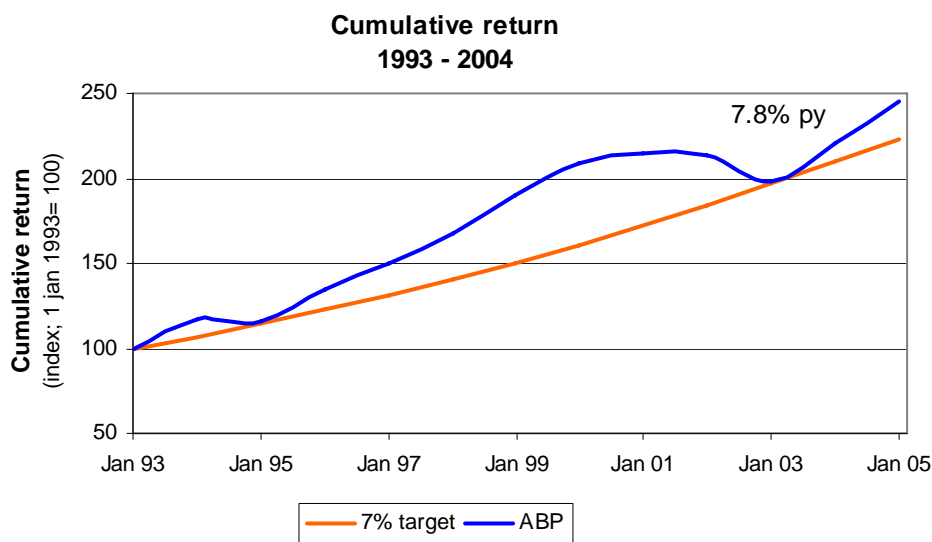
Secondly, long-term interest rates fell in the US, despite substantial economic growth, a strong rise in the oil price, a substantial budget deficit, increasing inflation risks and the change in US monetary policy. US government bonds appear expensive. Given continuing normalisation of monetary policy in the US (and Asia), there is a risk of a firm downward price correction in this market.

Finally, capital-market interest rates fell in the Eurozone as well, to an even greater extent than in the US. Disappointing growth forecasts and a strengthening euro worked to the benefit of holders of European fixed-income instruments. The interest rates on very long-term public debt instruments, important to pension funds, also followed suit. If during the next few quarters the European economy fares better than forecast, then it would be reasonable to expect a turnaround in this trend. At the same time, partly as a consequence of population ageing and tightened supervision of the European financial sector, future long-term interest rates may be expected to be at structurally lower levels than those of the 1980s and 1990s, both in nominal and market terms.

The greatest risk to the pension fund in the coming year is that of disappointments in the demand side, particularly in the Eurozone, because this could bring interest rates down to new record lows. Although this risk is certainly present, we expect that the economic recovery will continue and that interest rates will rise in the US, and eventually in the Eurozone too. Rising interest rates imply moderate returns on the bonds portfolio and pressure on share and property values.

Long-term return

The graph below shows the cumulative return since 1993. The value of each € 100 invested in 1993 had grown to approximately € 246 by year-end 2004. The average annual return was 7.8% and therefore above the target of 7%.



Profile

Stichting Pensioenfonds ABP (ABP) is the sectoral pension fund for employers and employees amongst governmental and educational institutions in the Netherlands. ABP has 2.5 million customers and assets under management of € 168.4 billion (as at year-end 2004), making it one of the largest funds in the world.

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