

Petroleum Fund of Timor-Leste

Quarterly Report

31 MARCH 2015

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INTRODUCTION

This report is produced in accordance with Article 13 of the Petroleum Fund Law which requires the Central Bank to report on the performance and activities of the Petroleum Fund of Timor-Leste, referred to in this report as the Fund unless the context suggests otherwise.

All monetary references in this report are to United States dollars as the official currency of Timor-Leste.

While every effort has been made to ensure accuracy, the information is based on management and custodial reports and has not been independently audited or reviewed and is subject to change, in which case the changes will be incorporated into subsequent reports.

EXECUTIVE SUMMARY

The Petroleum Fund was formed by the enactment of the Petroleum Fund Law promulgated on 3 August 2005 as amended on 28 September 2011. The law gives the Central Bank of Timor-Leste the responsibility for the operational management of the Fund.

This report covers the period from 1 January 2015 to 31 March 2015.

Key statistics for the quarter include:

- The capital of the Fund at the end of the previous quarter was \$16.5 billion while the current quarter was \$ 16.8 billion.
- Gross cash inflows to the fund from royalties and taxes were \$273.22 million
- Outflows for the quarter were \$215.0 million, being transfers to the state budget.
- The profit for the quarter was 226.2 million, representing a gross of fees return of 1.38% compared with the benchmark return of 1.36%.

The Fund performance for the quarter, including the performance of the relative asset classes, was as follows:

Table 1

	QTR	FYTD	1 Year	3 Years	5 years	Since Inc
Total Fund	1.38	1.38	3.53	4.85	4.19	4.28
Benchmark	1.36	1.36	3.56	4.74	4.11	4.25
<i>Excess</i>	<i>0.02</i>	<i>0.02</i>	<i>-0.03</i>	<i>0.11</i>	<i>0.08</i>	<i>0.02</i>
International Fixed Interest	0.69	0.69	1.84	1.24	1.82	3.03
Benchmark	0.65	0.65	1.80	1.18	1.77	3.02
<i>Excess</i>	<i>0.04</i>	<i>0.04</i>	<i>0.04</i>	<i>0.06</i>	<i>0.05</i>	<i>0.01</i>
International Equities	2.37	2.37	6.22	12.52	n.a	11.44
Benchmark	2.31	2.31	6.03	12.19	n.a	10.70
<i>Excess</i>	<i>0.05</i>	<i>0.05</i>	<i>0.19</i>	<i>0.33</i>	<i>n.a</i>	<i>0.75</i>

1. INVESTMENT MANDATE

A revised Management Agreement between the Ministry of Finance and the Central Bank was signed on 25 June 2009. Annex 1 was further updated subsequently to reflect the latest developments. The benchmarks as of March 2015 were as follows:

Table 2

	31-Dec-14	31-Mar-15
BOA Merrill Lynch 3-5 Years Treasury Bond Index	40.00%	40.00%
BOA Merrill Lynch 5-10 Years Treasury Notes and Bond	10.00%	10.00%
Barclays Global Treasury Developed Market ex US, 30%	10.00%	10.00%
Total Fixed Income	60%	60%
MSCI World Index Dividends Reinvested	40.00%	40%
Total Equities	40%	40%
Total	100%	100%

2. MARKET TRENDS DURING THE QUARTER

Global Market Trend

During the quarter economic momentum started to build in the Eurozone with positive economic data. Meanwhile, economic data from the USA tended to disappoint.

Central Banks – the Federal Reserve and the European Central Bank – continue to dominate market attention. Despite weakening global inflation on the back of falling oil prices and monetary easing by a number of central banks, the timing of the first interest rate hike by the Fed remained uncertain.

The US dollar continued to rise against all other currencies, gaining nearly 13% against the Euro.

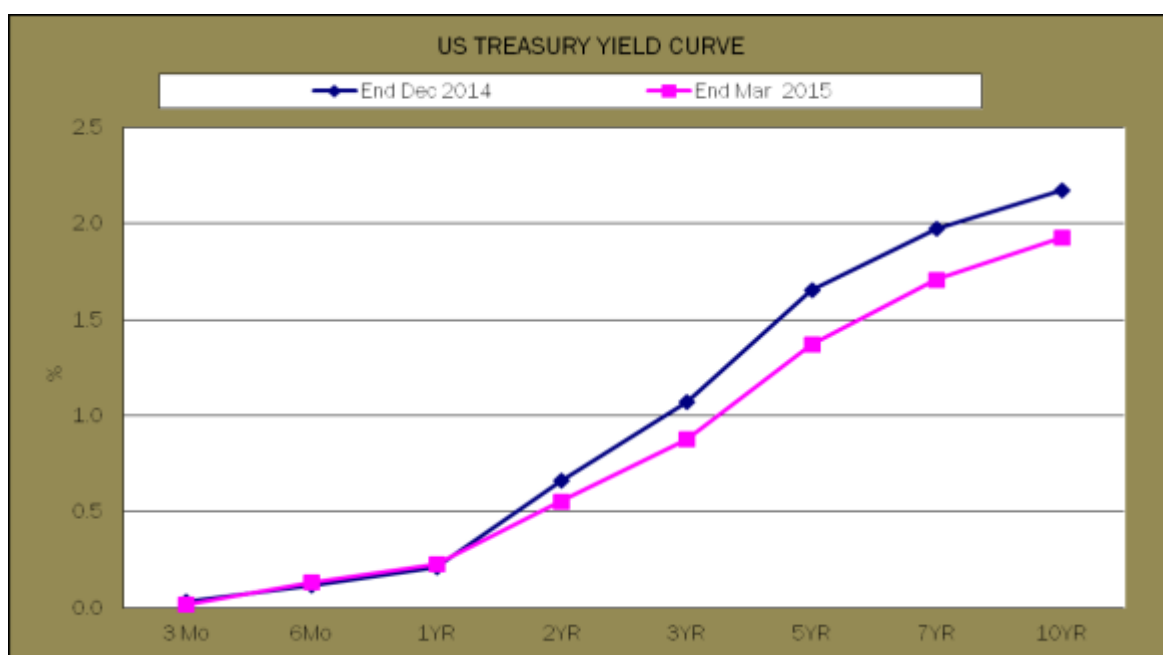
Equities

Global stocks advanced amid rising Mergers and Acquisitions activity, heightened central bank stimulus measures and signs of renewed economic growth in Europe and Japan. Health care stocks enjoyed a strong rally, driven by several large acquisitions, while the energy sector lagged as oil prices continued to slide. U.S. bonds rallied, with investors favoring them for their relative value as yields in Europe and Japan touched record lows.

U.S. stocks posted modest returns despite hitting new record highs in March as investors contended with uncertain global growth, oil price volatility and the timing of the Federal Reserve's impending interest rate hike. European stocks rose sharply, supported by improving economic data, falling oil prices and an aggressive new stimulus program launched by the European Central Bank.

Bonds including US Treasuries

US Treasuries rallied during the quarter, with investors favoring U.S. issues for their relative value as yields in Europe and Japan hit record lows. The Barclays U.S. Aggregate Index rose 1.6%. The yield on the benchmark 10-year Treasury note declined 25 basis points to 1.92%. European bonds strengthened as the European Central Bank's long-awaited quantitative easing program went into full effect. The central bank is expected to buy up to €1.1 trillion of euro-zone bonds over time, including sovereign and corporate debt. The yield on Germany's benchmark 10-year bond declined 36 basis points to end the quarter 0.18%.



3. MANAGEMENT DURING THE QUARTER

Objectives

The Central Bank, as operational manager of the Fund, has implemented the investment mandates through a combination of internal and external management.

The following table shows how the investment mandates have been implemented.

Table 3

Mandate	Management Style	Authorised Managers	Tracking Error	Outperformance Target	Commencement date
BOA Merrill Lynch 3-5 Years US Treasury Bond Index	Passive	BCTL	n/a	Nil	19-Jan-12
BOA Merrill Lynch 5-10 Years US Treasury Notes & Bond index	Enhanced Passive	Bank for International Settlements	0.50%	0.25%	15-Dec-11
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped	Enhanced Passive	AllianceBernstein	0.50%	Nil	3-Jul-14
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped	Enhanced Passive	Wellington Management	0.50%	Nil	4-Dec-14
MSCI World Index Net Dividends Reinvested	Passive	State Street Global Advisors	0.35%	Nil	18-Jan-12
	Passive	Black Rock	0.35%	Nil	21-Feb-13
	Enhanced Passive	Schroder Investment Management	1.00%	1.00%	7-Oct-10

Cash received by the Fund is invested or assigned to external managers in a timely manner, with the Central Bank being accountable for the returns on overnight investments.

Operational Implementation

The allocation of the capital of the Fund to the various mandates as at the end of the quarter was as follows:

Table 4

	Managers	Benchmark	Tolerance	Actual
BOA Merrill Lynch 3-5 Years Treasury Bond Index	BCTL	40%	± 2.5%	40.09%
BOA Merrill Lynch 5-10 Years Treasury Notes and Bond Index	Bank for International Settlements	10%	± 1%	10.46%
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped	AllianceBernstein	5%	± 0.5%	4.92%
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped	Wellington Management	5%	± 0.5%	4.92%
Total Fixed Income		60%		60%
	State Street Global Advisors			17.28%
	Black Rock	35%	± 4.0%	17.40%
MSCI World Index Net Dividends Reinvested	Schroder Investment Management	5%	± 1.5%	4.93%
Total Equities		40%		40%

4. PORTFOLIO PERFORMANCE

This section contains a number of tables and charts describing the performance of the Petroleum Fund.

The following notes are intended to assist in interpreting this information:

- The percentage figures show the return of the Fund, or a part of it, which is compared with the performance of the corresponding benchmark. The benchmark represents the investment strategy established by the Minister and is used as a goal against which the performance of the actual investments is measured. The Minister's benchmarks for the Petroleum Fund are described earlier in this report.
- The excess is the difference (which may be negative) between the benchmark and the portfolio being measured. In general a portfolio and its benchmark will respond in a similar manner to movements in the financial markets. The excess occurs because the benchmark does not recognise transaction costs, and because the actual portfolio usually contains a different mix of financial instruments to the benchmark.

GLOBAL PORTFOLIO

In the course of the quarter the Petroleum Fund balance was as follows:

Table 5

Capital Account, Quarter January-March 2015	\$'000
Opening book value (January 2015)	16,538,617
Receipts during the period	273,225
Transfer to General State Budget	-215,000
Investment Return	226,244
Closing book value (31 March 2015)	16,823,086

The Fund was invested as follows:

Table 6

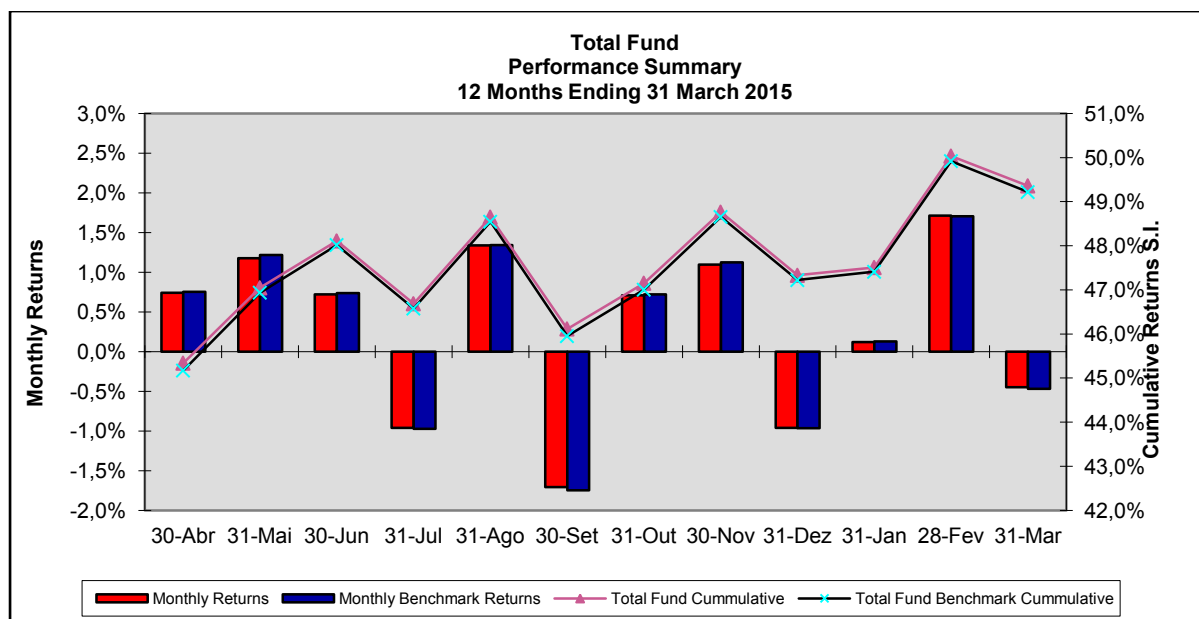
Assets	\$'000
Cash and Cash Equivalents	134.390
Other Receivables	41.929
Financial assets held at fair value through profit or loss	16.689.042
Less:	
Payable for Securities Purchased	-37.277
Accounts Payable	-4.997
Total	16.823.086

The income for the quarter was as follows:

Table 7

Income	\$'000
Interest income	35,426
Dividend income	42,382
Unit Trust distributions	1,287
Other Investment income	5
Net gains/(losses) on Financial Assets at fair value	394,928
Net foreign exchange gains/(losses)	-241,869
Less:	
External manager, custody fees	-2,407
Central Bank management expenses	-1,653
IAB Expenses	0
Other expenses	-2
Withholding taxes	-1,854
Total Investment Income	226,244

Global Benchmark over the same period is shown in the following graph.



FIXED INTEREST

The performance of the investments in Fixed Interest for the quarter, including the performance of the managers responsible for those investments, was as follows:

Table 8

	%	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
International Fixed Interest		0.69	0.69	1.84	1.24	1.82	3.03
Benchmark		0.65	0.65	1.80	1.18	1.77	3.02
<i>Excess</i>		0.04	0.04	0.04	0.06	0.05	0.01
BCTL 3-5 yr US Treasury		1.55	1.55	3.29	1.61	n.a	1.40
BoA Merrill Lynch 3-5 Years US Treasury Passive		1.48	1.48	3.21	1.54	n.a	1.28
<i>Excess</i>		0.07	0.07	0.08	0.07	n.a	0.12
Bank for International Settlements		2.25	2.25	6.58	2.76	n.a	2.29
BoA Merrill Lynch 5-10 Years US Treasury Enhanced Passive		2.23	2.23	6.72	2.77	n.a	2.29
<i>Excess</i>		0.01	0.01	-0.14	-0.02	n.a	0.00
Wellington Management		-4.29	-4.29	n.a	n.a	n.a	-10.26
Barclays Global Treasury DM ex US Enhanced Passive		-4.19	-4.19	n.a	n.a	n.a	-10.53
<i>Excess</i>		-0.10	-0.10	n.a	n.a	n.a	0.27
Alliance Bernstein		-4.17	-4.17	n.a	n.a	n.a	-5.05
Barclays Global Treasury DM ex US Enhanced Passive		-4.19	-4.19	n.a	n.a	n.a	-5.02
<i>Excess</i>		0.01	0.01	n.a	n.a	n.a	-0.03

INTERNATIONAL EQUITIES

The performance of the investments in global developed market equities for the quarter, including the performance of the managers responsible for those investments, was as follows:

Table 9

	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
International Equities	2.37	2.37	6.22	12.52	n.a	11.44
Benchmark	2.31	2.31	6.03	12.19	n.a	10.70
<i>Excess</i>	0.05	0.05	0.19	0.33	n.a	0.75
Schroder Investment Management	1.98	1.98	5.33	12.88	n.a	11.62
MSCI World Enhanced Passive	2.31	2.31	6.03	12.19	n.a	10.70
<i>Excess</i>	-0.33	-0.33	-0.70	0.70	n.a	0.92
SSgA International Equity	2.47	2.47	6.38	12.42	n.a	14.23
MSCI World Passive	2.31	2.31	6.03	12.19	n.a	13.83
<i>Excess</i>	0.16	0.16	0.35	0.23	n.a	0.40
Black Rock Investment Management	2.40	2.40	6.36	n.a	n.a	13.32
MSCI World Passive	2.31	2.31	6.03	n.a	n.a	13.07
<i>Excess</i>	0.08	0.08	0.34	n.a	n.a	0.26

5. MANAGEMENT COSTS

A management fee of \$4.1 million for operational management costs was charged to the fund during the quarter.

The fee covered the following services (in thousands \$):

Table 10

External Management and Custody expenses	2,407
Central Bank management expenses	1,653
IAB expenses	-
Other Expenses	2
Total Cost	4,061

6. TRANSFERS TO STATE BUDGET

According to Article 7.1 of the Petroleum Fund Law transfers from the Fund may only be made to the credit of a single State Budget account. An amount of \$215 million was transferred to the State Budget account during the quarter .

Table 11

In Thousand (\$)

Transfer January 2015	70,000
Transfer February 2015	70,000
Transfer March 2015	75,000
Transfer for this Quarter	215,000
Total Transfers previous quarters	-
Total Transfers this fiscal year to March 2015	215,000

7. COMPLIANCE STATEMENT

Banco Central de Timor-Leste asserts the following statements relating to compliance with the mandates given by the Minister.

Qualifying Instruments

The Fund was invested in instruments within the investment universes specified in the various mandates at all times during the quarter.

Modified Duration

The modified duration of the Fund's fixed interest investment portfolios remained within the mandate during the quarter.

Tracking Error

The tracking error of each mandate in the Fund's investment portfolio was within the specified range during the quarter.

External Managers

The Central Bank has received representations from the external managers, that external managers' investments were within their mandates during the quarter.

Internal Audit

The provisions of Article 22 of the Petroleum Fund law no. 9/2005 require the Central Bank's Internal Auditor to perform an audit of the Fund every six months. The Internal Auditor performed audit up to quarter December 2014.

8. FINANCIAL INFORMATION

The following financial information is presented for the purpose of assisting the Minister to review the quarterly performance of the Petroleum Fund as set out in this report. The figures have not been audited.

Table 12

BALANCE SHEET		
In thousands of USD	2015 March	2014 March
ASSETS		
Cash and Cash Equivalents	134,390	79,122
Receivables	41,929	34,927
Financial assets held at fair value through profit or loss	16,689,042	15,575,434
TOTAL ASSETS	16,865,360	15,689,483
LIABILITIES		
Payables for securities purchased	-37,277	-16,786
Accounts payable	-4,997	-2,003
TOTAL LIABILITIES	-42,274	-18,789
NET ASSETS	16,823,086	15,670,695
CAPITAL		
Opening Balance	16,538,617	14,952,099
PF Law Art. 6.1 (a) Revenue receipts	150,161	231,180
PF Law Art. 6.1 (b) DA receipts	123,064	312,465
PF Law Art. 6.1 (e) Other receipts	-	0
PF Law Art 7.1 Transfers to State Budget	-215,000	0
Income for the period	226,244	174,950
CAPITAL	16,823,086	15,670,695

Table 13

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME - QUARTER				
In thousands of USD	Quarter		Year to Date	
	March-15	March-14	March-15	March-14
INVESTMENT INCOME				
Interest income	35,426	33,488	35,426	33,488
Dividend income	42,382	52,961	42,382	52,961
Trust income	1,287	921	1,287	921
Other investment income	5	1	5	1
Net gains/(losses) on Financial Assets at fair value	394,928	74,653	394,928	74,653
Net foreign exchange gains/(losses)	-241,869	17,784	-241,869	17,784
Total Investment Income	232,159	179,808	232,159	179,808
EXPENSES				
External management, custody fees	2,407	1,549	2,407	1,549
Internal operational management fees	1,653	1,496	1,653	1,496
IAB Expenses	0	81	0	81
Other expenses	2	0.27	2	0
Total expenses	4,061	3,126	4,061	3,126
Profit before tax	228,098	176,681	228,098	176,681
Withholding taxes on investments	1,854	1,732	1,854	1,732
Profit/loss for the period	226,244	174,950	226,244	174,950
Other comprehensive income	0	0	0	0
Total comprehensive income for the period	226,244	174,950	226,244	174,950

Notes:

The accounting policies and method of computation used to prepare the above figures are the same as disclosed in the most recent annual financial statements of the Petroleum Fund.

Dili, 30 April 2015



Nur Aini Djafar Alkatiri
Deputy Governor



Abraão de Vasconcelos
Governor