

Petroleum Fund of Timor-Leste

Quarterly Report

30 June 2023

Inside This Report

1. Introduction.
2. Executive summary.
3. Investment mandate.
3. Market trends.
5. Management during the quarter.
6. Portfolio performance.
10. Management costs.
10. Transfers to state budget.
10. Compliance statement.
11. Financial Information.

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 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 01 April to 30 June 2023.

Key statistics for the quarter include:

- The capital of the Fund at the end of the Current quarter was \$18.076 billion while the previous quarter was \$17.691 billion.
- Gross cash inflows to the fund from royalties and taxes were \$332.21 million.
- Outflow for the quarter were \$192.86 million, being transfers to the state budget of \$190 million while \$2.856 million was for management costs.
- The profit and loss for the quarter was \$242.34 million, representing a gross of fees return of 1.39%. The return on financial market investments was 1.43% compared with the benchmark return of 1.53%.

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	1.39	5.02	3.64	2.53	4.02	4.13
Benchmark	1.48	5.11	4.57	2.53	3.96	4.07
<i>Excess</i>	<i>-0.09</i>	<i>-0.09</i>	<i>-0.93</i>	<i>0.00</i>	<i>0.06</i>	<i>0.05</i>
Financial Market Investments	1.43	5.19	4.63	2.88	4.25	4.19
Benchmark	1.53	5.25	4.37	2.29	3.86	4.04
<i>Excess</i>	<i>-0.09</i>	<i>-0.06</i>	<i>0.26</i>	<i>0.59</i>	<i>0.40</i>	<i>0.15</i>
Investment in Petroleum Operations	0.32	0.32	-19.79	-6.40	n.a	-3.34
Benchmark	1.10	2.21	4.50	4.50	n.a	4.50
<i>Excess</i>	<i>-0.79</i>	<i>-1.90</i>	<i>-24.29</i>	<i>-10.90</i>	<i>n.a</i>	<i>-7.84</i>

Table 2

%	QTR	FYTD	1 Year	3 Years	5 years	Since Inc
Total Financial Market Investments	1.43	5.19	4.63	2.88	4.25	4.19
Benchmark	1.53	5.25	4.37	2.29	3.86	4.04
<i>Excess</i>	<i>-0.09</i>	<i>-0.06</i>	<i>0.26</i>	<i>0.59</i>	<i>0.40</i>	<i>0.15</i>
Liquidity Portfolios	0.73	1.90	2.39	n.a	n.a	0.48
Benchmark	0.80	1.97	2.36	n.a	n.a	0.56
<i>Excess</i>	<i>-0.07</i>	<i>-0.07</i>	<i>0.03</i>	<i>n.a</i>	<i>n.a</i>	<i>-0.08</i>
Growth Portfolios	1.62	6.02	5.24	n.a	n.a	-2.21
Benchmark	1.60	6.06	5.59	n.a	n.a	-2.30
<i>Excess</i>	<i>0.02</i>	<i>-0.03</i>	<i>-0.35</i>	<i>n.a</i>	<i>n.a</i>	<i>0.09</i>

1. INVESTMENT MANDATE

A revised Management Agreement between Ministry of Finance and the Central Bank was signed on 25 June 2009. The Annexes of the Management Agreement was subsequently amended to reflect the actual investments.

From 1 November 2020, the Private Debt Instrument is separated from the financial market investments portfolio. From 1 July 2021, the Financial Market Investment portfolio is segmented into the Liquidity Portfolio and the Growth Portfolio. The benchmarks of the Total Fund and Financial Market Investment as of June 2023 were as follows:

Table 3

Mandates	Apr-23	May-23	Jun-23
Total Fund	100%	100%	100%
Investment in Petroleum Operations	3.02%	4.05%	3.93%
Financial Market Investment	96.98%	95.95%	96.07%
Total Financial Market Investment	100%	100%	100%
Liquidity Portfolio	19.69%	19.77%	19.24%
Growth Portfolio	80.31%	80.23%	80.76%
Total Liquidity Portfolio	100%	100%	100%
USD Cash	88.20%	78.26%	78.06%
US Government Short-term Treasury Notes	11.80%	21.74%	21.94%
Total Growth Portfolio	100%	100%	100%
US Government Treasury Notes 3-5 Years	35.00%	35.00%	35%
US Government Treasury Notes 5-10 Years	10.00%	10.00%	10%
Global Developed Market Sovereign Bond, Hedged	10.00%	10.00%	10%
US Treasury Inflation Protected Securites 1 - 10 Years (FT)	5.00%	5.00%	5%
US Treasury Inflation Protected Securites 1 - 10 Years (BR)	5.00%	5.00%	5%
Developed Market Equities	35.00%	35.00%	35%

2. MARKET TRENDS DURING THE QUARTER

Global Macroeconomic Trends

1) Labour Market

The labour market has seen significant wage growth in both the US and UK. In the US, the Atlanta Fed's median wage growth tracker showed wages growing at a robust 6%, indicating a tight labor market and strong demand for workers. Similarly, the UK experienced an even stronger wage growth, rising by 7% year on year. This suggests that employers are having to pay more to attract and retain workers, which could potentially lead to inflationary pressures.

2) Global Growth and Inflation

Inflation has been a key theme in global markets. In the US, inflation fell sharply from a peak of 9% down to 4%, largely due to favorable base effects from oil prices, which peaked last June and have come down significantly since. However, core inflation, which excludes volatile items like food and energy, remained stickier. This could be helped by a moderation in shelter inflation ahead, as the material slowdown in house price and rent growth starts to be reflected in the official core inflation numbers. In the UK, core services inflation accelerated, reflecting the pick-up in wage growth, which could potentially lead to higher consumer prices.

3) Global Fiscal and Monetary Policy

Monetary policy has varied across the globe. The Bank of Japan maintained its yield curve control policy to anchor government bond yields, while interest rates ratcheted higher in most other countries. The Bank of England, in particular, raised interest rates rapidly to 5% in response to rising inflation. This divergence in monetary policy could have implications for currency markets and capital flows.

Global Equity Market Trends

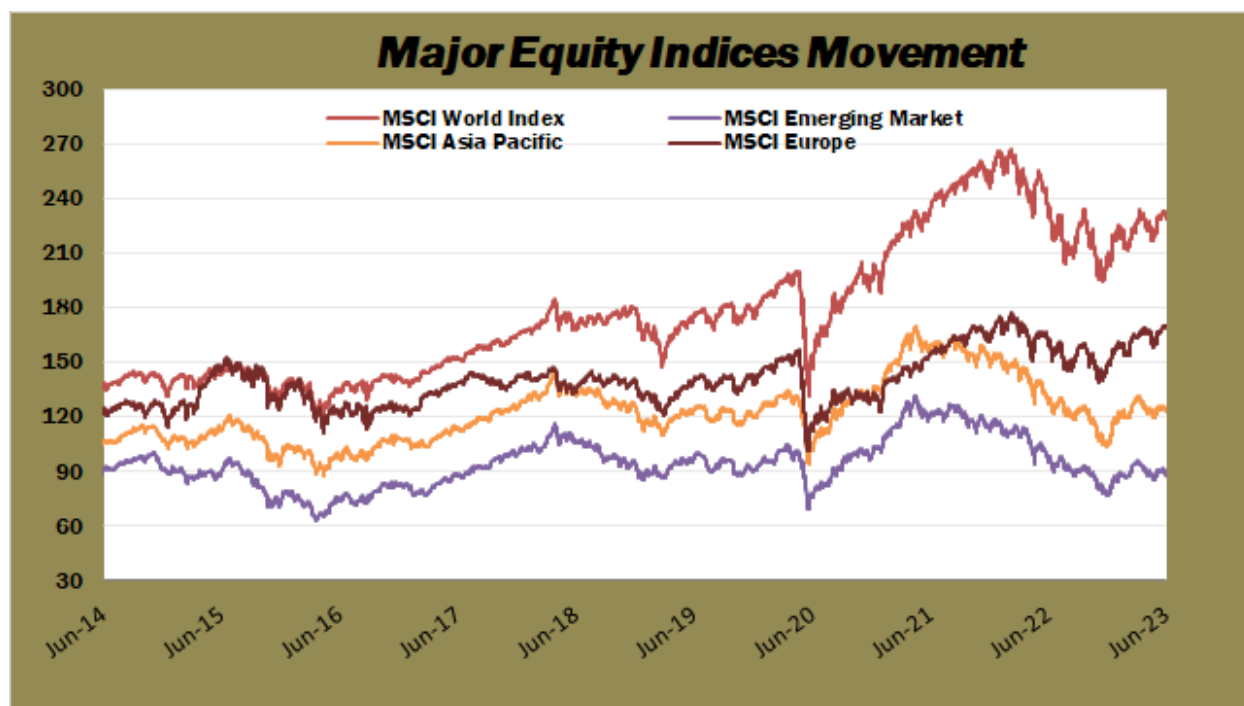
1) MSCI World Index

Developed market equities have performed well, delivering 18.5 year to date and 6.8% over the quarter. The best-performing major equity market in local currency terms, both over the quarter (up 14%) and the first half of the year (up 23%), was Japan. This strong performance was despite the fact that interest rates remained low in Japan and the Bank of Japan maintained its yield curve control policy.

2) Value stocks vs. Growth stocks

The performance between value and growth stocks has diverged. The big growth stocks, which fell sharply last year, bounced back strongly, returning 27% year to date and 11% over the quarter. In contrast, value stocks lagged, up only 5% year to date. This suggests that investors are favouring companies with strong growth prospects over those that appear undervalued based on their fundamentals. US stocks were the next best-performing market in local currency terms, up 9% over the quarter and 17% for the year to date. These gains were driven almost entirely by the largest growth stocks (think "mega-cap tech"), which are disproportionately found in the US. The rest of the market delivered much more muted returns so far this year, suggesting a concentration of returns in a few large companies.

Graph 01 Major Equity Indices Movement (USD)



Global Treasury Bonds include U.S Treasuries

1) Global Sovereign Bonds – Developed Markets only

Bonds, which were hit hard last year, are yet to recover meaningfully. Global government bonds are only up 1% year to date, while UK government bonds fell 6% over the quarter, leaving them down 4% year to date. This suggests that investors may be demanding higher yields to compensate for the risk of rising inflation.

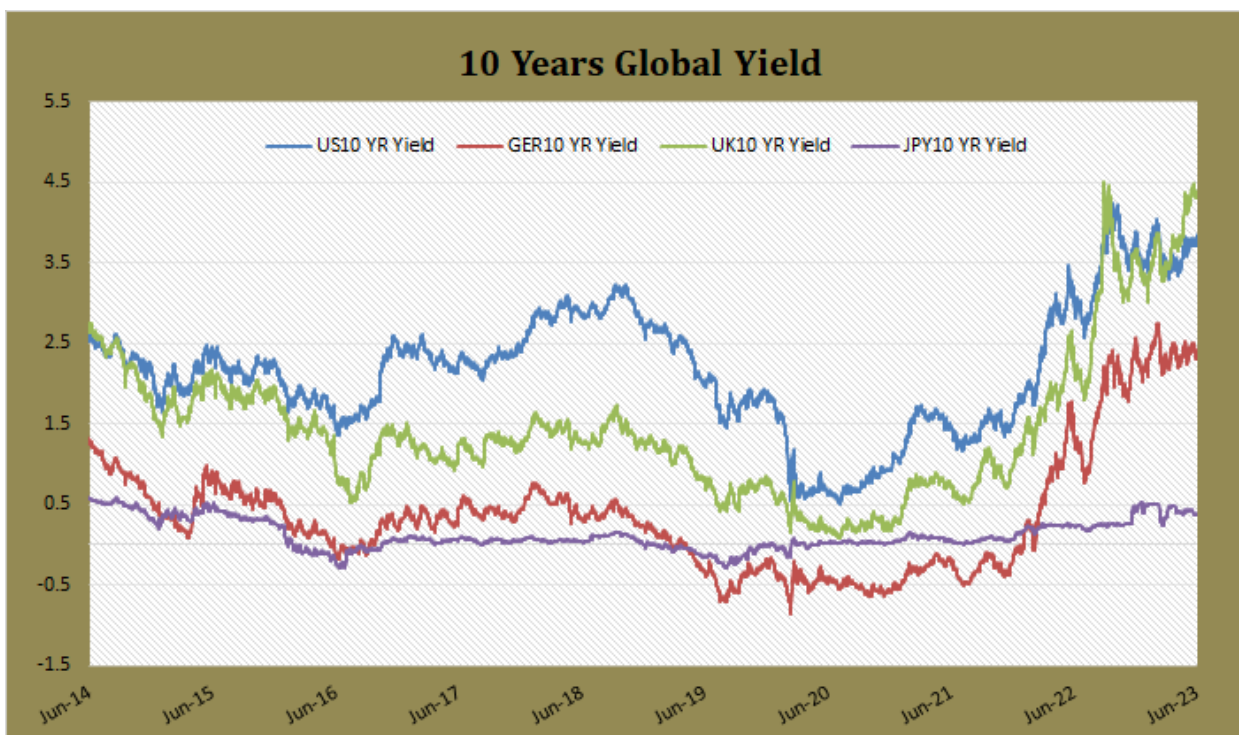
2) US Treasury Market including Treasury Inflation-Protected Securities

The leading benchmark for bonds (Bloomberg Barclays US Aggregate Bond Index) realized a slightly negative return for the second quarter, as the strong economy and hope of a near-term end to rate hikes led investors to embrace riskier assets. Looking deeper into the fixed-income markets, shorter-duration bonds outperformed those with longer durations in the second quarter, as bond investors priced in a near-term end to the Fed's rate hike campaign, while optimism regarding economic growth caused investors to rotate out of the safety of longer-dated fixed income.

3) US Yield Curve

In June, the Federal Reserve left the Federal Funds rate unchanged at 5.00% to 5.25%. They also released their revised Summary of Economic Projections, which showed that all but two FOMC participants expected at least one more rate hike, and a majority expected two or more. The U.S. Treasury curve remains inverted, which is a closely followed recessionary signal. The 2-year/10-year spread ended the quarter at (-102 bps) reversing the steepening experienced during the regional bank stress.

Graph 02. 10 Years Global Yield



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 4

Mandate	Management Style	Authorised Managers	Tracking Error	Outperformance Target	Commencement date
Liquidity Portfolio					
3 Month USD Treasury Bills/Cash	Passive	BCTL	n/a	Nil	August-18
BOA Merrill Lynch 1-3 Years US Treasury Bond Index					July-21
Growth Portfolio					
BOA Merrill Lynch 3-5 Years US Treasury Bond Index	Passive	BCTL	0.25%	Nil	January-12
BOA Merrill Lynch 5-10 Years US Treasury Bond Index			0.50%		May-20
Global Developed Market Sovereign Bond, Hedged	Enhanced Passive	BIS	0.50%	0.15%	April-20
US TIPS Treasury Bonds 1 - 10 Years	Enhanced Passive	Franklin Templeton	0.50%	0.20% to 0.25%	April-23
US TIPS Treasury Bonds 1 - 10 Years		Barings			April-23
MSCI World Index ex Australia Net Dividends Reinvested	Equity Factor	Schroders	3.0%	Nil	August-19
		SSgA			
MSCI World Index ex Australia Net Dividends Reinvested	Passive	SSgA	0.35%	Nil	January-12
		BlackRock			February-13
MSCI Australia	Passive	BCTL	0.50%	Nil	July-16
Alternative		BCTL	n/a		April-19

Operational Implementation

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

Table 5

Mandates	Actual weight in FMI		
	Apr-23	May-23	Jun-23
Total Financial Market Investment	100%	100%	100%
Total Liquidity Portfolio	19.69%	19.77%	19.24%
BCTL 3 Month US Treasury Bill Index	17.37%	15.47%	15.02%
BCTL 1-3 year US Treasury Bonds Index	2.32%	4.30%	4.22%
Total Growth Portfolio	80.31%	80.23%	80.76%
Total Fixed Income	52.77%	51.83%	51.06%
BCTL 3-5 year US Treasury Bonds	26.93%	27.45%	27.17%
BCTL 5-10 year US Treasury Bonds	7.67%	7.99%	7.79%
BIS Global Developed Market Sovereign Bond, Hedged	8.11%	8.44%	8.30%
US TIPS Treasury Bonds 1 - 10 Years	10.05%	7.94%	7.80%
Total Global Equities	27.54%	28.40%	29.70%
SSGA Equity Factor	3.47%	3.54%	3.68%
Schroders Equity Factor	3.44%	3.57%	3.75%
SSGA International Equity Passive	8.27%	8.54%	8.94%
BlackRock International Equity Passive	11.71%	12.10%	12.67%
BCTL Australia Equities Passive	0.65%	0.64%	0.67%

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 recognize 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 \$18.076 billion as follows, which has been adjusted with the D&P valuation reports of 2022:

Capital Account	\$'000
Opening book value (01 April 2023)	17,691,276
Receipts during the period	332,214
Transfer to General State Budget	-190,000
Investment Return	242,346
Closing book value (30 June 2023)	18,075,836

The Fund was invested as follows:

Assets	\$'000
Cash and Cash Equivalents	4,677,376
Other Receivables	79,231
Financial assets held at fair value through profit or loss	15,227,194
Less:	
Payable for Securities Purchased	(1,813,801)
Accounts Payable	(94,163)
Total	18,075,836

The income for the quarter was as follows:

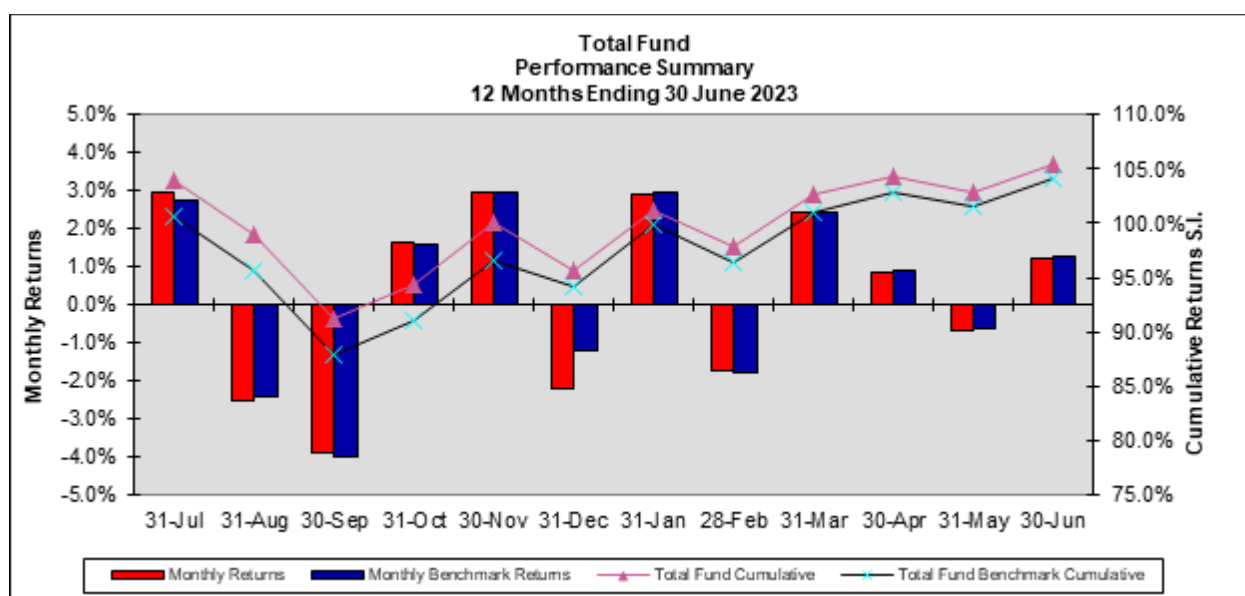
Income	Table 8 \$'000
Interest income	89,665
Dividend income	32,447
Unit Trust distributions	971
Other Investment income	646
Net gains/(losses) on Financial Assets at fair value	117,593
Net foreign exchange gains/(losses)	6,702
Less:	
External manager, custody fees	-1,537
Central Bank management expenses	-1,202
IAB Expenses	-34
Other expenses	-84
Withholding taxes	-2,823
Total Investment Income	242,346

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

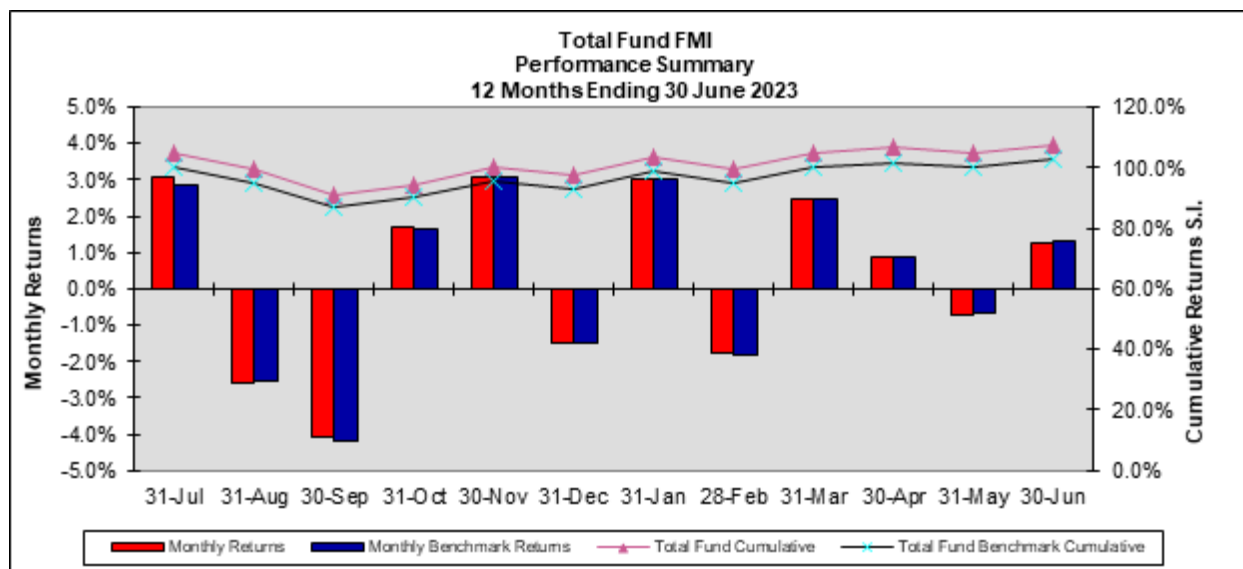
- Unit trust distribution is the income received from listed property investment entities.
- Other expenses relate to derivative trading costs which are deducted directly from the Fund.

The global Fund Performance of absolute and benchmark over the same period are shown in the following graph.

Graph 03 Total Fund Performances



Graph 04 Total Financial market Investments Performance



Liquidity Portfolio

The performance of the investments in the short-term liquidity portfolio 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
Liquidity Portfolio	0.73	1.90	2.39	n.a	n.a	0.48
Benchmark	0.80	1.97	2.36	n.a	n.a	0.56
<i>Excess</i>	<i>-0.07</i>	<i>-0.07</i>	<i>0.03</i>	<i>n.a</i>	<i>n.a</i>	<i>-0.08</i>
BCTL Cash Management	1.13	2.22	3.17	0.92	1.26	1.25
ICE BoA ML 3 Month US Treasury Bill Index	1.17	2.25	3.59	1.27	1.59	1.40
<i>Excess</i>	<i>-0.04</i>	<i>-0.03</i>	<i>-0.42</i>	<i>-0.36</i>	<i>-0.33</i>	<i>-0.15</i>
BCTL ML 1-3 Year US Treasury Index	-0.70	0.80	0.35	n.a	n.a	-1.37
BoA Merrill Lynch 1-3 Years US Treasury Note Index	-0.57	0.97	-0.08	n.a	n.a	-1.73
<i>Excess</i>	<i>-0.12</i>	<i>-0.17</i>	<i>0.43</i>	<i>n.a</i>	<i>n.a</i>	<i>0.36</i>

Growth Portfolio

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

Table 10

	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
Growth Portfolio	1.62	6.02	5.24	n.a	n.a	-2.21
Benchmark	1.60	6.06	5.59	n.a	n.a	-2.30
<i>Excess</i>	0.02	-0.03	-0.35	n.a	n.a	0.09
International Fixed Interest	-1.25	1.33	-1.18	-3.36	0.25	1.84
Benchmark	-1.23	1.25	-1.33	-3.39	0.33	1.84
<i>Excess</i>	-0.01	0.08	0.16	0.03	-0.08	-0.01
BCTL 3-5 year US Treasury Bonds	-1.37	1.00	-1.15	-2.98	0.74	0.85
BoA Merrill Lynch 3-5 Years US Treasury Passive	-1.32	0.88	-1.34	-3.00	0.78	0.84
<i>Excess</i>	-0.05	0.11	0.20	0.03	-0.04	0.01
BCTL 5-10 year US Treasury Bonds	-1.77	1.61	-2.48	-5.13	n.a	-5.01
BoA Merrill Lynch 5-10 Years US Treasury Passive	-1.73	1.40	-3.43	-5.30	n.a	-5.13
<i>Excess</i>	-0.05	0.21	0.95	0.18	n.a	0.11
BIS Global Treasury Developed Marked Hedged	-0.29	2.51	-0.45	-3.78	n.a	-3.50
Global Treasury Developed Market - Hedged	-0.38	2.68	-0.95	-3.97	n.a	-3.68
<i>Excess</i>	0.09	-0.16	0.50	0.19	n.a	0.18
Barings LLC 1-10 Years US TIPS	n.a	n.a	n.a	n.a	n.a	-1.66
US 1-10 years Tips	n.a	n.a	n.a	n.a	n.a	-1.61
<i>Excess</i>	n.a	n.a	n.a	n.a	n.a	-0.05
Franklin Templeton 1-10 years US TIPS	n.a	n.a	n.a	n.a	n.a	-1.41
US 1-10 years Tips	n.a	n.a	n.a	n.a	n.a	-1.61
<i>Excess</i>	n.a	n.a	n.a	n.a	n.a	0.20
International Equities	6.79	14.87	18.40	12.86	9.26	9.76
Benchmark	6.83	15.09	18.51	12.18	9.07	9.34
<i>Excess</i>	-0.04	-0.22	-0.11	0.69	0.19	0.42
SSgA Equity Factor	5.82	12.64	16.23	13.30	n.a	9.60
MSCI ex. Australia Net Dividends Reinvested	6.97	15.36	18.67	12.21	n.a	10.15
<i>Excess</i>	-1.16	-2.72	-2.44	1.09	n.a	-0.55
Schroders Equity Factor	7.74	16.14	18.41	14.88	n.a	11.54
MSCI ex. Australia Net Dividends Reinvested	6.97	15.36	18.67	12.21	n.a	10.15
<i>Excess</i>	0.77	0.78	-0.26	2.68	n.a	1.39
SSGA International Equity Passive	7.02	15.43	18.95	12.49	9.28	10.36
MSCI ex. Australia Net Dividends Reinvested	6.97	15.36	18.67	12.21	9.16	10.10
<i>Excess</i>	0.05	0.07	0.28	0.28	0.12	0.26
BlackRock International Equity Passive	6.99	15.48	19.08	12.56	9.38	9.85
MSCI ex. Australia Net Dividends Reinvested	6.97	15.36	18.67	12.21	9.16	9.57
<i>Excess</i>	0.02	0.11	0.41	0.36	0.22	0.28
BCTL Australia Equity Passive	0.29	3.03	11.21	10.40	4.64	6.78
MXAU Australia Net Dividends Reinvested	0.27	3.07	11.19	10.52	4.95	7.00
<i>Excess</i>	0.02	-0.04	0.02	-0.12	-0.31	-0.22

Private Debt Instrument for Petroleum Operations

The performance of the investment in Private debt instrument for Petroleum Operations for the quarter was as follows:

Table 11

	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
Private debt instrument for Petroleum Operations	0.32	0.32	-19.79	-6.40	n.a	-3.34
Benchmark	1.10	2.21	4.50	4.50	n.a	4.50
<i>Excess</i>	-0.79	-1.90	-24.29	-10.90	n.a	-7.84

The Private debt instrument is maintained at its independently verified fair value for December 2022 until the new valuation for December 2023 is undertaken.

5. MANAGEMENT COSTS

A management fee of \$2.856 million for operational management costs was charged to the fund during the quarter. The fee covered the following services (in thousands \$):

External Management and Custody expenses	1,537
Central Bank management expenses	1,202
IAB expenses	34
Other Expenses	84
Total Cost	2,856

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 -\$190 million was transferred to the State Budget account during the quarter.

	In Thousand (\$)
Transfer April 2023	0
Transfer May 2023	-190,000
Transfer June 2023	0
Transfer for this Quarter	-190,000
Total transfers this fiscal year to March 2023	-190,000

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

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 has performed an audit up to quarter ended 31 December 2022.

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 14

BALANCE SHEET	June-23	June-22
In thousands of USD		
ASSETS		
Cash and Cash Equivalents	4,677,376	1,869,942
Receivables	79,231	32,473
Financial assets held at fair value through profit or loss (including PD)	15,227,194	15,975,209
TOTAL ASSETS	19,983,801	17,877,623
LIABILITIES		
Payables for securities purchased	-1,813,801	-2,436
Accounts payable	-94,163	-30,371
TOTAL LIABILITIES	-1,907,965	-32,807
NET ASSETS	18,075,836	17,844,816
CAPITAL		
Opening Balance (January)	17,273,002	19,650,677
PF Law Art. 6.1 (a) Revenue receipts	29,759	194,420
PF Law Art. 6.1 (b) DA receipts	318,284	388,128
PF Law Art. 6.1 (e) Other receipts	5,334	0
PF Law Art 7.1 Transfers to State Budget	-490,000	-450,000
Income for the period	939,458	-1,938,409
CAPITAL	18,075,836	17,844,816

Note: The Fair Value of Private Debt as of December 2022 was \$560.76 million, which is reflected in financial assets held at fair value for 2022 until a new valuation for 2023 is undertaken. The opening balance slightly adjusted to reflect the new Fair Value of the Private Debt as of December 2022 which will also affect the balance of Quarter March 2023.

Table 15

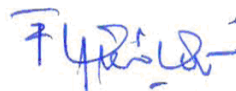
STATEMENT OF PROFIT OR LOSS In thousands of USD	QUARTER		YEAR TO DATE	
	June-23	Jun-22	June-23	Jun-22
INVESTMENT INCOME				
Interest income	89,665	44,151	169,602	81,596
Dividend income	32,447	33,897	60,046	62,177
Trust income	971	896	1,903	1,761
Other investment income	646	250	831	240
Net gains/(losses) on Financial Assets at fair valu	117,593	-1,089,200	702,957	-2,060,995
Net foreign exchange gains/(losses)	6,702	-11,863	15,264	-11,027
Total Investment Income	248,025	-1,021,868	950,603	-1,926,248
EXPENSES				
External management, fees	1,537	1,480	3,173	4,033
Internal operational management fees	1,202	1,888	2,939	3,147
IAB Expenses	34	21	208	147
Other expenses	84	132	223	274
Total expenses	2,856	3,520	6,543	7,601
Profit before tax	245,169	-1,025,389	944,061	-1,933,849
Withholding taxes on investments	-2,823	2,629	-4,602	4,560
Profit/loss for the period	242,346	-1,028,018	939,458	-1,938,409
Other comprehensive income	0	0	0	0
Total comprehensive income for the period	242,346	-1,028,018	939,458	-1,938,409

Note: 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, 28 July 2023



Venancio Alves Maria
Deputy Governor



Abraão de Vasconcelos
Governor