Trinidad and Tobago

Heritage & Stabilisation Fund

QUARTERLY INVESTMENT REPORT

JULY - SEPTEMBER 2012

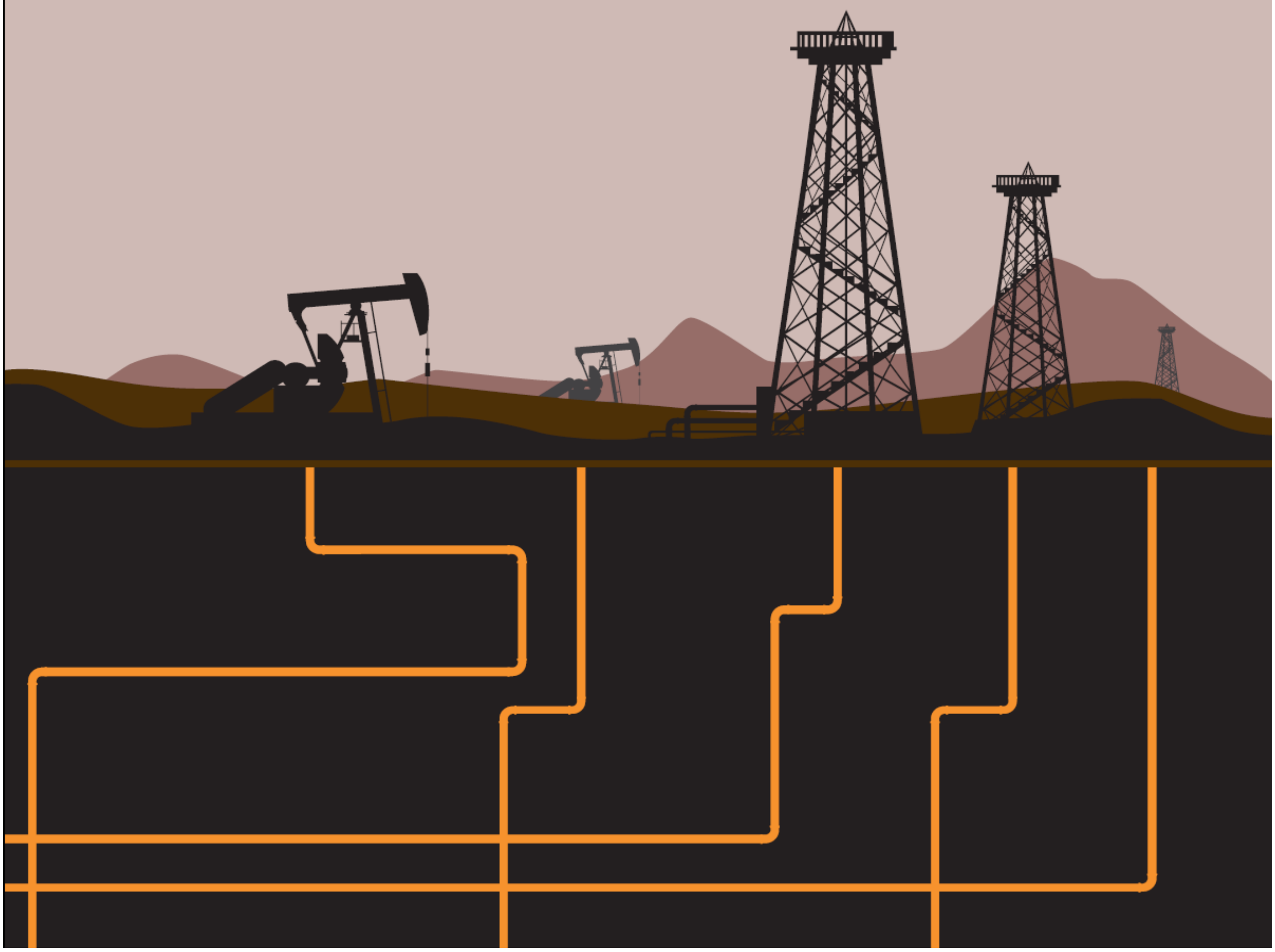


TABLE OF CONTENTS

EXECUTIVE SUMMARY

The global economic continued to face heightened uncertainty, mainly due to the sovereign debt crisis in Europe, with the risk of contagion spreading to emerging markets and developing countries. The looming “fiscal cliff” in the United States also added to global uncertainty. The International Monetary Fund (IMF) has even lowered its global growth forecast for 2012 to 3.3 per cent, from its previous forecast of 3.5 per cent. In response to this weaker economic outlook, the major central banks announced policy measures which were geared at stabilizing financial markets and stimulating economic growth.

In the **United States (US),** real GDP expanded at an annualised rate of 2 per cent in the third quarter of 2012, up from 1.3 per cent in the previous quarter. Data for the manufacturing sector suggested that activity expanded in September 2012 for the first time in four months, while the housing and labour markets, though depressed, have shown some improvements. In an effort to further stimulate the US economy, the Federal Reserve in mid-September 2012 announced a new round of quantitative easing which involves the substantial purchase of mortgage-backed securities at a pace of US$ 40 billion per month. The Federal Reserve also extended its window for near zero rates until mid-2015.

Economic indicators for the **Euro zone** disappointed as they were generally worse than expected during the third quarter of 2012. In addition, financial market tension was elevated at the start of period, as Spain requested financial assistance from the European Union for its banking system. Fears eased following the European Central Bank (ECB)’s statement that it would do “whatever it takes” to keep the Euro zone together. The ECB later announced a potentially unlimited short-maturity bond buying programme called Outright Monetary Transactions (OMT) which is intended to stabilize the region’s troubled debt markets.

In the **United Kingdom (UK),** the economy appeared to have pulled out of recession during the third quarter of 2012, while in **Japan** the latest available indicators suggested a further slowdown in growth and re-emergence of deflationary risks. As such, the Bank of Japan decided in October 2012 to increase by 11 trillion yen to 91 trillion yen, the total size of its asset purchase programme. This followed an increase of 10 trillion yen in September 2012.

Despite the heightened volatility at the start of the third quarter, financial markets benefitted from coordinated policy actions which boosted investor optimism and was reflected in increased demand for relatively riskier assets. As a result, equities and credit-sensitive fixed income securities performed well. In the US, the Standard and Poor's (S&P) 500 index made a quarterly gain of 5.8 per cent while other developed market equities as measured by the MSCI EAFE index increased 6.1 per cent. In the global fixed income market, government bond yields declined over the three months to September 2012.

For the quarter ended September 2012, the HSF investment portfolio posted a return of 3.5 per cent, compared with a return of 3 per cent for the Strategic Asset Allocation (SAA) benchmark. The equity portion of the Fund, which benefitted from the "risk on" environment, was the main driver of the overall portfolio's performance, contributing 2.5 per cent to total return. Meanwhile, the fixed income mandates had modest performances, collectively contributing the remaining 1 per cent. On an asset class level, all four mandates outperformed their respective benchmarks during the third quarter of 2012.

Contribution to Quarterly Return,
For the period July 2012 – September 2012
/per cent/

	SAA Weights	Portfolio Weights as at 30-Sep- 2012	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	100.00	3.53	2.98
US Core Domestic Fixed Income	40.00	38.13	0.88	0.64
US Core Domestic Equity	17.50	18.82	1.26	1.00
Non US Core International Equity	17.50	17.22	1.20	1.20
US Short Duration Fixed Income	25.00	23.46	0.15	0.12
Cash	0.00	2.37*	0.00	0.00

*This represents the cash contribution made by the Government on September 28, 2012.
NB: Differences in totals are due to rounding.

As at end of September 2012, the **net asset value of the HSF was US$4,712.4 million**, an increase from US$4,378.9 million at the end of June 2012. During the third quarter of 2012, the Government made two cash contributions to the Fund which totalled US$181.3 million. In July 2012, the contribution amounted to US$69.4 million in respect of the second quarter of 2012, while the second contribution of US$111.9 million was deposited on September 28 2012 for the third quarter of 2012. In the three months to September 2012, the weights of the fixed income and equity segments of the Fund remained within the (+/- 5 per cent) range in which they are allowed to vary from their Strategic Asset Allocation.

SECTION 1 – INTERNATIONAL ECONOMIC ENVIRONMENT

United States

Preliminary estimates indicated that the US economy expanded at an annualised rate of 2 per cent during the third quarter of 2012, compared with growth of 1.3 per cent in the previous quarter. This outturn primarily reflected accelerations in personal consumption expenditure and federal government spending and a decline in imports. While data for the manufacturing sector have generally been disappointing, the housing and labour market indicators showed encouraging signs.

The Institute of Supply Management's Purchasing Managers Index[1] (PMI) indicated that activity in the manufacturing sector expanded in September 2012 after contracting for three consecutive months. This heightened activity reflected increases in the new orders and employment sub-indices. In September 2012, the PMI read 51.5, up from 49.7 in June 2012. Meanwhile, activity in the non-manufacturing sector continued to grow as the ISM Non Manufacturing Index (NMI) measured 55.1 in September 2012 compared with 52.1 three months earlier.

On the labour market front, conditions improved during the quarter as nonfarm payroll employment increased by a monthly average of 146,000 jobs compared with an increase of 67,000 jobs in the second quarter of 2012. These employment gains occurred mainly in the health care, transportation and warehousing industries. In September 2012, the unemployment rate fell below 8 per cent for the first time since January 2009, measuring 7.8 per cent compared with 8.2 per cent three months earlier.

---

[1] An index value in excess of 50 per cent indicates an expansion in activities in the manufacturing sector, while a posting below 50 per cent represents a contraction.

The housing market also showed some marked improvement over the September 2012 quarter as record-low mortgage rates helped to attract creditworthy buyers. The S&P/Case-Shiller Home Price Indices, which are the leading measures of US home prices, increased 1.5 per cent for the 10-City Composite and 1.6 per cent for the 20-City Composite in July 2012. These represented the third consecutive month that both Composites recorded positive monthly changes. Other housing market indicators including housing starts, existing home sales and building permits applications also showed encouraging signs over the quarter.

Consumer prices rose during the third quarter of 2012, mainly on account of higher gasoline prices. In September 2012, the year-on-year inflation rate measured 2 per cent, up from 1.7 per cent in June 2012. Nonetheless, the Federal Reserve still believes that inflation has been subdued and that longer-term inflation expectations remain stable.

At its September 2012 meeting, the Federal Open Market Committee announced a new round of quantitative easing in an effort to stimulate the economy and reduce unemployment. The Federal Reserve intends to purchase agency mortgage-backed securities at a pace of $40 billion per month and indicated that it stands ready to take further actions, if there is no significant improvement in employment conditions. The Committee reiterated that a highly accommodative monetary policy stance will be maintained and kept the target range for the Federal Funds rate unchanged at 0 to 0.25 per cent. It was further added that the Federal Fund rate is likely to stay near zero at least through mid 2015.

Euro zone

The Euro zone's economic indicators continued to show a dismal path, as real GDP contracted during the second quarter of 2012, manufacturing activity in the third quarter continued to wane, unemployment remained elevated and additional policy measures failed to boost consumer and business confidence.

In the second quarter of 2012, real GDP in the Euro zone contracted by 0.2 per cent following a flat performance in the previous quarter. Despite the 0.3 per cent growth in the region's largest economy, Germany, this was more than offset by the fall-off in output in some of the other economies including Italy, Spain and Portugal. Given the worse-than-expected data released recently, it appears likely that the Euro zone's GDP will contract for the three months ended September 2012. This will push the region into its second recession in three years. The IMF has already lowered the Euro Area's growth forecast for 2012, indicating that the economy is likely to contract by 0.4 per cent, compared with its earlier forecast of a 0.3 contraction.

According to Markit's Purchasing Managers Index, manufacturing activity in the Euro zone contracted in September 2012 for the fourteenth successive month as the Index continued to linger below the 50-mark threshold that indicates an expansion. Nonetheless, the rate of contraction slowed as the PMI read 46.1, up from 45.1 in June 2012.

Conditions in the labour market remained depressed as the unemployment rate stood at 11.4 per cent in August 2012, the same level recorded in June 2012. Spain and Greece, which are at the forefront of the Europe's debt crisis, registered the highest unemployment rates among the Euro zone countries of 25.1 per cent and 24.4 per cent, respectively.

The Governing Council of the ECB announced in September 2012 its government bond buying programme called "Outright Monetary Transactions" (OMT) which allows for unlimited buying of short-maturity government bonds (1-3 years) on the secondary market. This measure is aimed at reducing the borrowing costs of debt-plagued Euro zone member states. While the announcement of the OMT programme helped to alleviate tensions in some Euro Area financial markets during September, business sentiment for the region fell in September 2012 to a three-year low. At its October 2012 meeting, the ECB's Governing Council decided to keep its main refinancing rate unchanged at 0.75 per cent.

United Kingdom

The UK economy expanded by 1 per cent in the third quarter of 2012, partly due to the effects of the recently held Olympic and Paralympic Games. This outturn followed three consecutive quarters of contraction. Meanwhile, industrial production grew on a year-on-year basis to July 2012 by 2.8 per cent, the highest monthly increase in 25 years, before declining by 0.5 per cent in August 2012. Meanwhile, manufacturing activity continued to contract over the quarter as inflows of new export orders remained lacklustre. The Purchasing Managers Index stood at 48.4 in September 2012, unchanged from the level in June 2012.

Inflationary pressure eased slightly in September 2012 as the year-on-year inflation rate measured 2.2 per cent, down from 2.4 per cent in June 2012. The categories of items mainly responsible for this downward pressure were furniture, housing and household services and clothing and footwear. These declines were partially offset by upward pressure from the transport component, in particular motor fuels.

At its meeting on October 4 2012, the Bank of England's Monetary Policy Committee decided to maintain the official Bank Rate paid on commercial bank reserves at 0.5 per cent. The Committee also voted to continue with its programme of asset purchases totalling GBP 375 billion. These purchases are expected to be completed in November 2012.

Japan

Economic growth in Japan slowed to 0.2 per cent during the second quarter of 2012 compared with 1.3 per cent in the previous quarter. The latest available indicators suggest that economic activity slowed further in the third quarter of 2012 as industrial production and manufacturing output declined. According to Japan's Purchasing Managers' Index, activity in the manufacturing sector continued to contract over the three months to September 2012, with the index falling to 48 from 49.9 in June 2012. In addition, industrial production declined by 4.7 per cent on a year-on-year basis to August 2012 compared with a fall-off of 0.2 per cent in June 2012.

Consumer prices in Japan resumed its declining trend during the third quarter of 2012, measuring -0.4 per cent for the twelve months to September 2012 compared with 0.2 per cent in June 2012. Given the economic and price developments, the Bank of Japan decided in October 2012 to increase by 11 trillion yen to 91 trillion yen the total size of its asset purchase programme. This followed an increase of 10 trillion yen in September 2012. The Bank also left its benchmark interest rate unchanged at the range of 0 to 0.1 per cent.

SECTION 2 – CAPITAL AND MONEY MARKET REVIEW

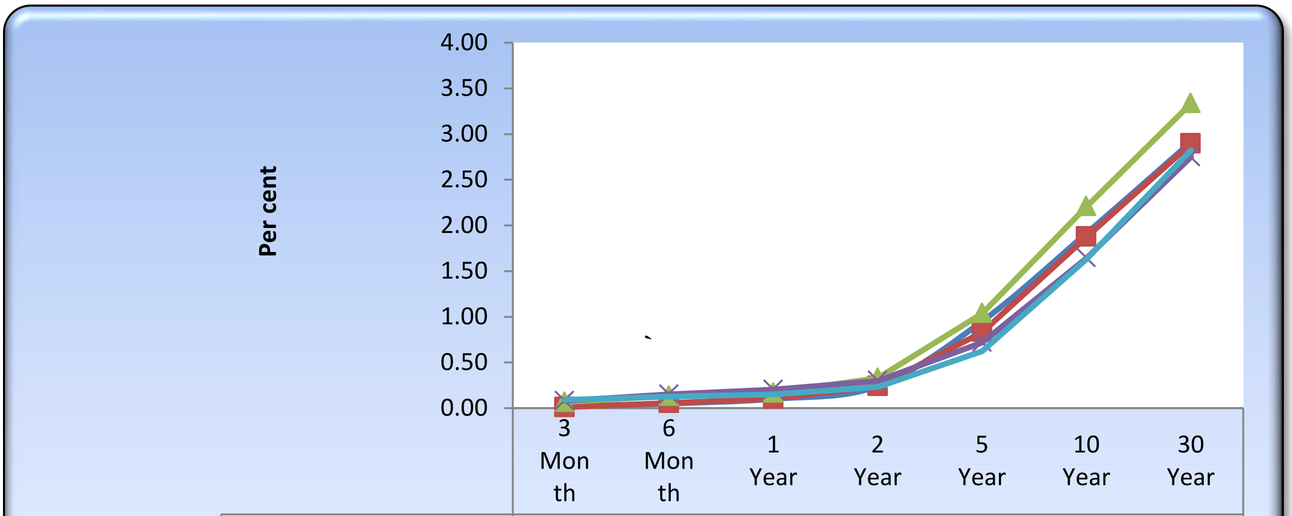
During the third quarter of 2012, coordinated policy actions by the major central banks boosted financial markets, resulting in broad-based gains for most financial assets. Although the review period started with great uncertainty, market volatility gradually declined and remained at extremely muted levels as investors were eagerly anticipating the ECB's bond buying programme and the Federal Reserve's third round of quantitative easing. The expectation for these actions kept investors' optimism elevated and increased their risk appetite.

The Chicago Board Options Exchange Volatility Index (VIX), which is a barometer of investor sentiment and market risk, ended the third quarter at 15.7 points, down from 17.1 points at the end of June 2012. The VIX closed above the 20-point threshold for only one day during the three months to September 2012 and averaged 16.2 for the quarter, down from an average of 20 points for the prior three months. In this "risk-on" environment, equities and the credit-sensitive fixed income securities generated robust returns. The Standard and Poor's (S&P) 500 index gained 5.8 per cent in the third quarter of 2012 compared with a loss of 3.3 per cent in the previous quarter, while the MSCI EAFE index which gauges the performance of non-US Developed equity markets rose 6.1 per cent compared with a loss of 8.4 per cent in the June 2012 quarter. On the fixed income side, all segments of the market outperformed US Treasury securities of a similar duration.

Fixed Income

In the US, the movement in Treasury yields over the quarter ended September 2012 was mixed as 1-month, 3-month and 30-year yields increased, while those for the 6-month to 10-year portion of the curve declined. Despite the overall trend, investors experienced mixed sentiments throughout the quarter as weak economic conditions, domestically and overseas, dominated headlines at the start of the period. This resulted in "flight to quality" trades which placed a downward pressure on yields. The 10-year benchmark US Treasury yield, which was the most volatile segment of the US curve, reached a quarterly low of 1.4 per cent on July 24, down from 1.6 per cent at the end of June 2012. Subsequently, statements made by the ECB's President and the announcement of the OMT bond purchase programme were viewed favourably by the market, causing investors' fear to turn into renewed optimism. This resulted in an increased demand for relatively higher risk assets. As such, US Treasury yields rose and the 10-year yield reached a quarterly high of 1.9 per cent on September 14. By the end of September 2012, this yield declined to 1.6 per cent, 1 basis point less than the rate at the end of June 2012. This latter movement reflected the Federal Reserve's stronger-than-anticipated policy response which was aimed at placing downward pressure on long term rates.

Figure 1
US Treasury Yield Curve
/per cent /

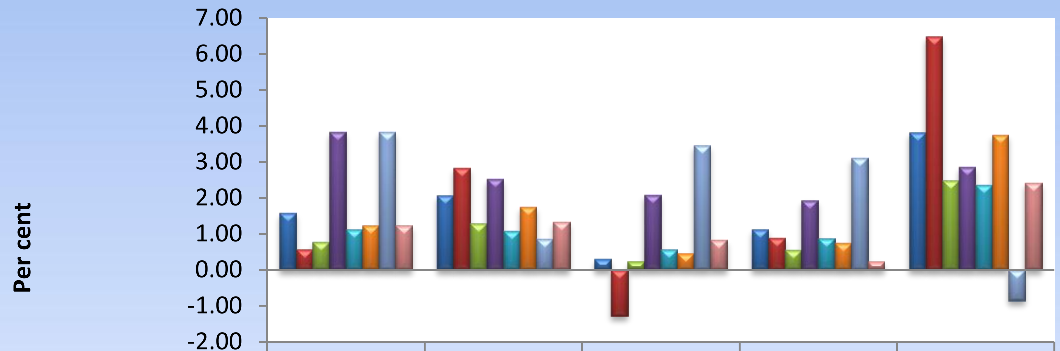


	3 Month	6 Month	1 Year	2 Year	5 Year	10 Year	30 Year
September 30, 2011	0.02	0.05	0.10	0.24	0.95	1.92	2.91
December 31, 2011	0.01	0.06	0.10	0.24	0.83	1.88	2.89
March 31, 2012	0.07	0.13	0.17	0.33	1.04	2.21	3.34
June 30, 2012	0.08	0.15	0.20	0.30	0.72	1.64	2.75
September 30, 2012	0.09	0.13	0.15	0.23	0.63	1.63	2.82

Source: Bloomberg.

According to the Barclays Capital US Aggregate Bond index, the broader US fixed income market returned 1.6 per cent for the third quarter of 2012 compared with a return of 2.1 per cent for the prior three months. Given the improvement in investor risk appetite, spreads versus US Treasuries tightened over the quarter. The best performing sectors were Commercial Mortgage Backed Securities (CMBS) and Investment Grade Corporates which both returned 3.8 per cent. Conversely, the US Treasury sector which posted the highest return in the June 2012 quarter was the worst performer, returning 0.6 per cent.

Figure 2
Returns on Fixed Income Indices
/per cent/



	QTR ended Sep-12	QTR ended Jun-12	QTR ended Mar-12	QTR ended Dec-11	QTR ended Sep-11
Barclays U.S. Aggregate	1.58	2.06	0.30	1.12	3.82
U.S. Treasuries	0.57	2.83	-1.29	0.89	6.48
U.S. Agencies	0.78	1.29	0.24	0.55	2.48
U.S. Corporate	3.83	2.52	2.08	1.93	2.85
U.S. MBS	1.13	1.08	0.57	0.88	2.36
G-7 Global Bonds (Hedged)	1.23	1.75	0.46	0.74	3.75
CMBS Index	3.83	0.86	3.46	3.11	-0.86
ABS Index	1.23	1.33	0.83	0.23	2.42

Source: Barclays Capital.

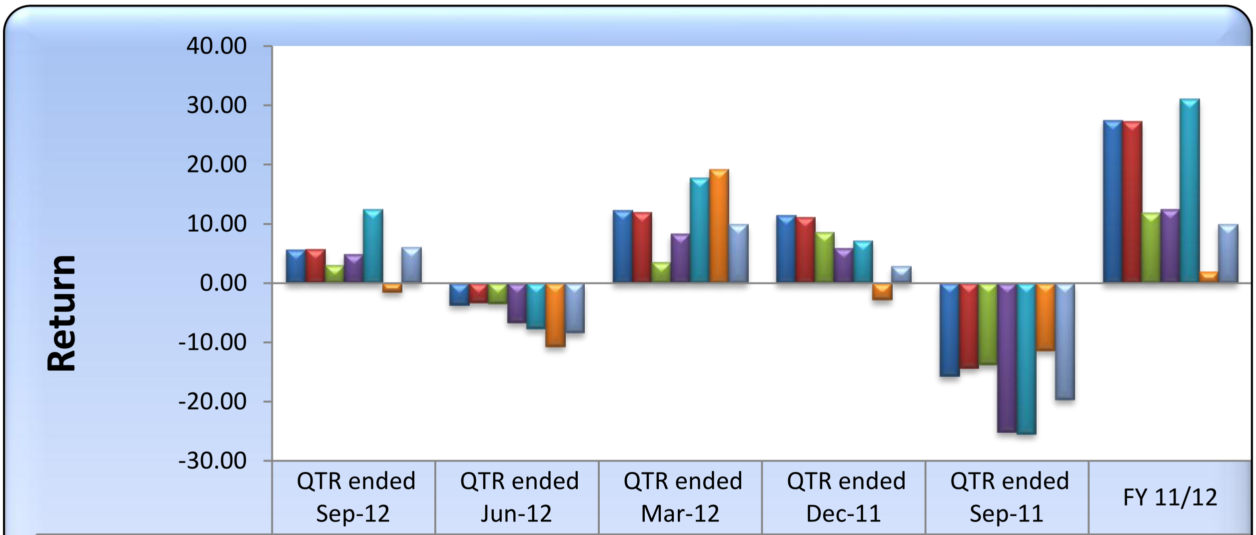
In other developed markets, sovereign bond yields declined over the third quarter. However during the month of July 2012, some Euro zone countries including Spain, Italy and Greece saw their cost of borrowing climb to unsustainable levels before the ECB's efforts to calm these markets. By the end of the quarter, the yield on the Spanish Government ten-year bond declined to 5.9 per cent from 6.3 per cent at the end of June 2012. Meanwhile, the yield on the Italian Government ten-year bond fell to 5.1 per cent from 5.8 per cent three months earlier and the yield on Greek bonds moved to 19.4 per cent, down from 25.8 per cent at the end of June 2012. Elsewhere in the Euro zone, German bunds which are perceived as safer investments also saw their ten-year yields decline to 1.4 per cent from 1.6 per cent in June 2012. Similar movements in yields were observed in the UK and Japan.

Equity Markets

Despite further signs of slower global growth, most equity markets posted solid gains during the third quarter of 2012, after returning losses in the three months to June 2012. This performance was driven largely by monetary stimulus measures which seemed to encourage investors to take more risk. Over the review period, all the major equity market produced gains which were broad-based as most sectors performed well. The notable exception was the Japanese stock market which returned losses.

In the US, the S&P 500 index rose 5.8 per cent during the third quarter of 2012 following a decline of 3.3 per cent in the previous quarter. Nine of the ten sectors generated gains led by the Energy and Telecommunication sectors. The worst performing stocks were from the Utilities sectors which lost 0.5 per cent. In the Euro zone, the Germany DAX 30 index increased 12.5 per cent, contributing to a quarterly return of 8.8 per cent for the region's equity market. These gains drove the performance of the MSCI EAFE index, which returned 6.1 per cent for the quarter. The MSCI EAFE index measures the performance of developed equity markets in Europe, Australia, New Zealand and Far East Asia.

Figure 3
Returns on Equity Indices
/Per cent/



	QTR ended Sep-12	QTR ended Jun-12	QTR ended Mar-12	QTR ended Dec-11	QTR ended Sep-11	FY 11/12
Russell 3000	5.68	-3.65	12.32	11.50	-15.70	27.53
S&P 500	5.76	-3.29	12.00	11.15	-14.33	27.33
FTSE 100 - UK	3.07	-3.42	3.52	8.65	-13.74	11.96
CAC 40 - France	4.95	-6.63	8.35	5.96	-25.12	12.50
DAX 30 - Germany	12.47	-7.64	17.78	7.20	-25.41	31.15
Nikkei 225 - Japan	-1.52	-10.68	19.26	-2.82	-11.37	1.95
MSCI EAFE	6.14	-8.37	9.98	2.86	-19.60	10.01

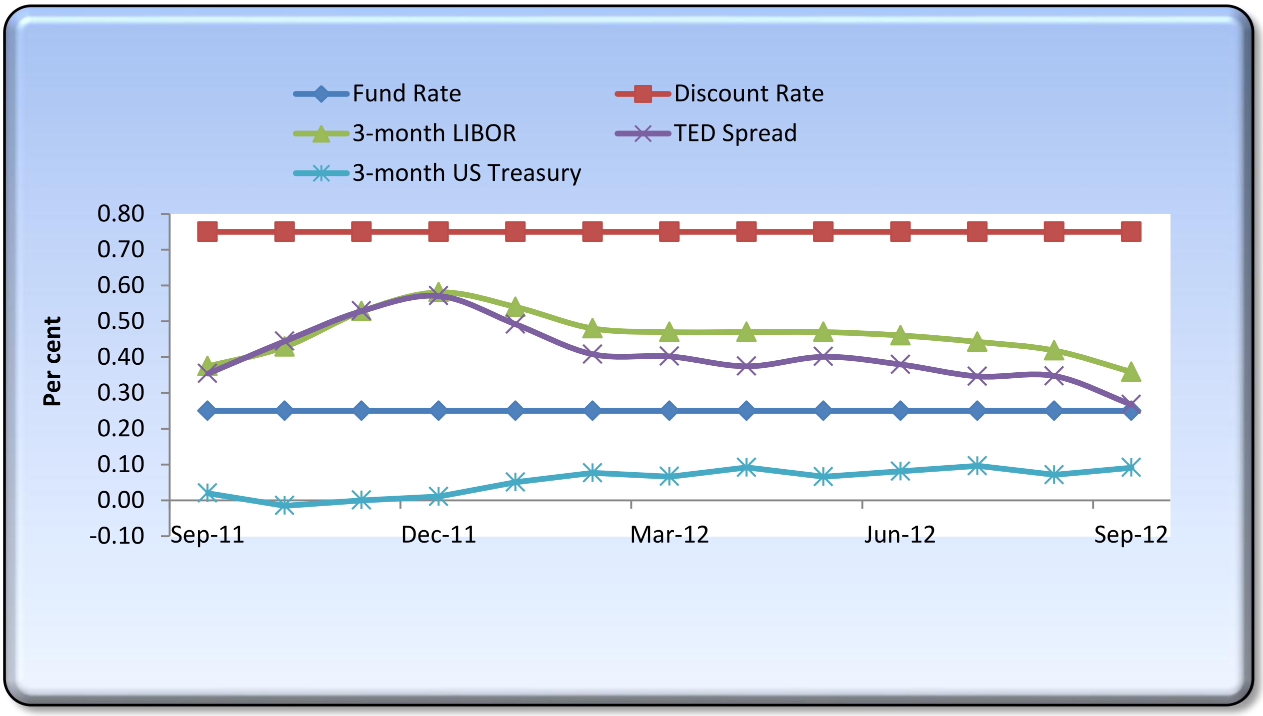
Source: Bloomberg.

Money Market

The continued accommodative monetary policy stance by the major central banks helped to keep short-term rates at very low levels. The US Federal Reserve's extension of the likely period of low interest rates to mid-2015 led to a further decline in the 3-month London Inter-Bank Rate (LIBOR), which reached 36 basis points at the end of September 2012 compared with 46 basis points three months earlier. Meanwhile the 3-month US Treasury bill rate rose marginally to 9 basis points at the end of September 2012 from 8 basis points in June 2012. The TED spread, which represents the difference between the 3-month

Treasury bill rate and 3-month LIBOR, tightened by 11 basis points to 27 basis points in September 2012 compared with 38 basis points three months earlier.

Figure 4
US Money Market Rates
/per cent/

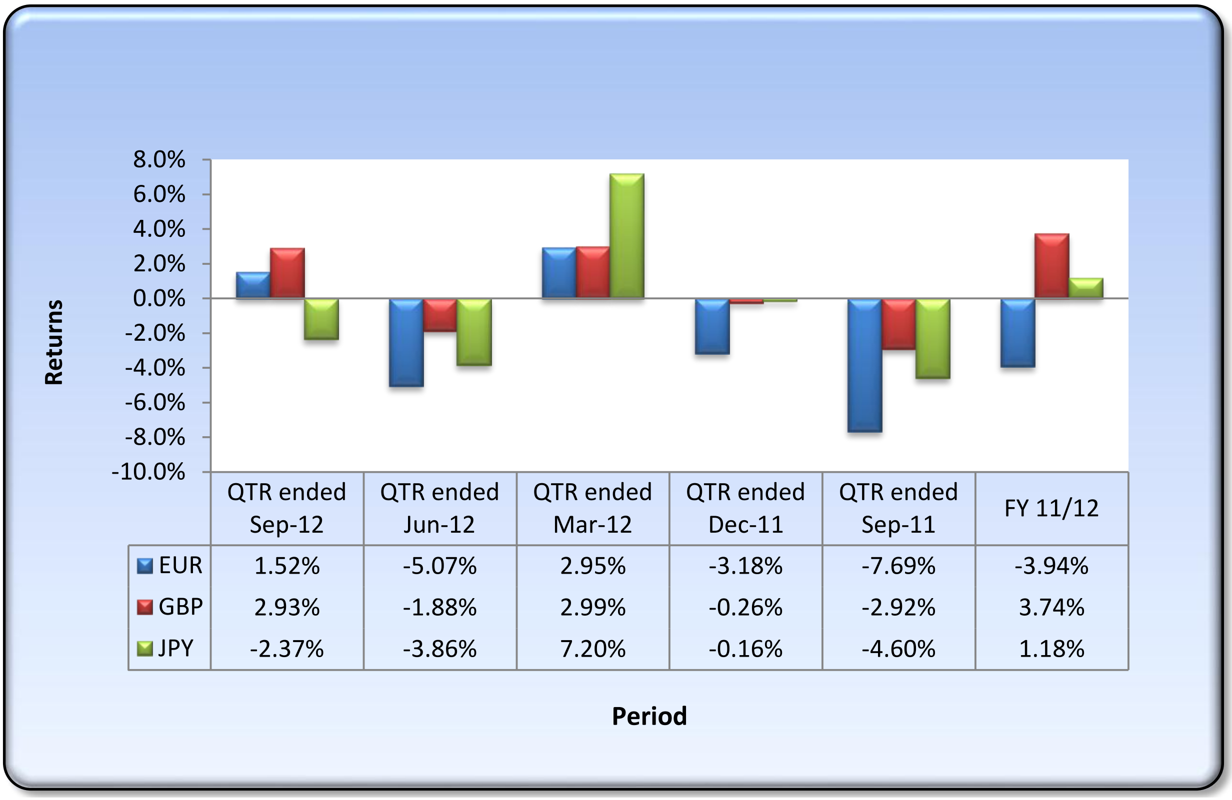


Source: Bloomberg.

Currency Markets

Currency movements were volatile over the third quarter of 2012 as risk sentiments deteriorated towards the start of the period before improving thereafter when growing expectations for policy actions emerged. The US dollar, which strengthened against the currencies of major economies in July 2012, made a directional change when investors' risk aversion declined. Over the quarter ended September 2012, the Euro, Pound and Yen appreciated 1.5 per cent, 2.9 per cent and 2.3 per cent, respectively vis-à-vis the US dollar. The US dollar index, which indicates the international value of the US dollar against other major currencies, declined 2 per cent to close September 2012 at 79.9, from 81.6 in June 2012.

Figure 5
Foreign Exchange Returns for Major Currencies vis-à-vis the US Dollar
/per cent/



	QTR ended Sep-12	QTR ended Jun-12	QTR ended Mar-12	QTR ended Dec-11	QTR ended Sep-11	FY 11/12
EUR	1.52%	-5.07%	2.95%	-3.18%	-7.69%	-3.94%
GBP	2.93%	-1.88%	2.99%	-0.26%	-2.92%	3.74%
JPY	-2.37%	-3.86%	7.20%	-0.16%	-4.60%	1.18%

Source: Bloomberg.

SECTION 3 – PORTFOLIO PERFORMANCE

Strategic Asset Allocation

During the quarter ended September 2012, the asset classes of the Fund deviated from their Strategic Asset Allocation (SAA) but their weights were all within the (+/- 5 per cent) range in which they are allowed to vary. The approved SAA for the HSF investment portfolio is as follows:

i.	***US Short Duration Fixed Income Mandate***	*25.0%*
ii.	***US Core Domestic Fixed Income Mandate***	*40.0%*
iii.	***US Core Domestic Equity Mandate***	*17.5%*
iv.	***Non US Core International Equity Mandate***	*17.5%*

Throughout the quarter, the US Core Domestic Equity mandate was the only asset class that had an overweight allocation relative to its SAA weight. This over-exposure to US equities, however, was reduced at the end of September 2012 when the Government made a deposit representing approximately 2.4 per cent of the Fund. Over the period July to September 2012, the Government made two cash contributions to the Fund which totalled US$181.3 million. On the first occasion, the contribution amounted to US$69.4 million in respect of the second quarter of 2012, while the second contribution of US$111.9 million was deposited on September 28 2012 for the third quarter of 2012. On August 01 2012, the first contribution was transferred to the external asset managers in proportions such that the four mandates were closer to their approved SAA weight.

At the end of September 2012, the total net asset value of the Fund was US$4,712.4 million, compared with US$4,378.9 million at the end of the previous quarter. Of this total, the investment portfolio was valued US$4,710 million while the remaining portion (US$2.4 million) was held in cash to meet the day-to-day expenses that arise from the management of the Fund. The Fund's target asset allocation and the portfolio weighting for the period December 31 2011 to September 30 2012 are shown below in Table 1.

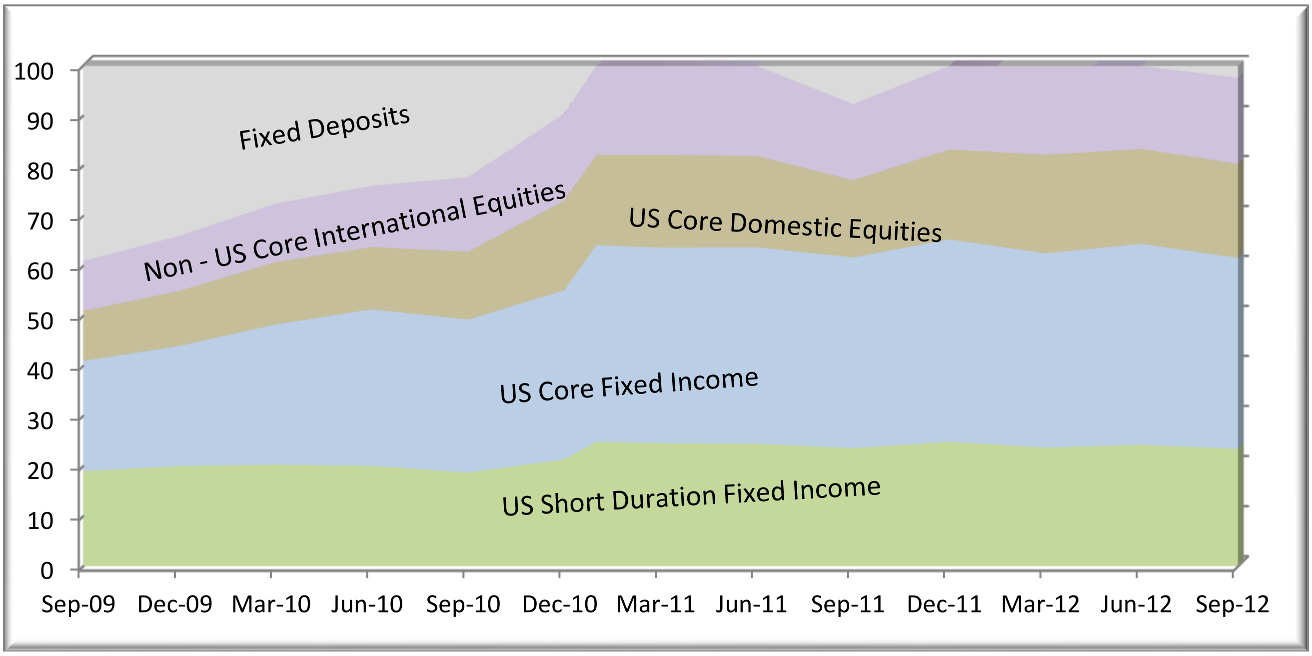
Table 1

Portfolio Composition relative to the Approved SAA
/per cent/

Portfolio Weights — Asset Class	Target Weight SAA	Dec-11 Actual % of Fund	Mar-12 Actual % of Fund	Jun-12 Actual % of Fund	Sep-12 Actual % of Fund
Cash	0.00	0.00	0.00	0.00	2.37*
US Short Duration Fixed Income	25.00	24.86	23.70	24.26	23.46
US Core Domestic Fixed Income	40.00	40.46	38.83	40.16	38.13
US Core Domestic Equity	17.50	17.98	19.72	18.99	18.82
Non-US Core International Equity	17.50	16.70	17.75	16.59	17.22

*This cash represents the contribution made by the Government on September 28, 2012.

Figure 6
Asset Composition of the HSF Portfolio
/per cent/



Performance of the Investment Portfolio

For the quarter ended September 2012, the HSF investment portfolio posted a return of 3.5 per cent, outperforming its SAA benchmark[2] which gained 3 per cent. The equity portion of the Fund which benefitted from the “risk on” environment was the main driver of the overall portfolio’s performance, contributing 2.5 per cent to total return. Meanwhile, the fixed income mandates had modest performances, collectively contributing the remaining 1 per cent. On an asset class level, all four mandates outperformed their respective benchmarks during the quarter.

In absolute terms, the **Non-US International Equity** mandate generated the highest return, gaining 7.2 per cent for the third quarter of 2012 compared with a return of 7 per cent for its benchmark, the MSCI EAFE ex Energy index. This mandate had exposure to equities in Australia, New Zealand, Europe and Far East Asia, all of which posted gains for the quarter. The Far East was the worst performing region, returning only 0.5 per cent as it was adversely impacted by the negative performance of the Japanese market. The outperformance of this mandate reflected favourable stock selection decisions, particularly within the consumer discretionary and financials sector. The gains made on these selections more than outweighed the losses made on the poor selections within the Industrials and Consumer Staples sectors. On a regional basis, the greatest contribution to excess returns came from the holdings in Europe. For the financial year to September 2012, this mandate returned 14.1 per cent compared with 13.6 per cent for the benchmark. The net asset value of this mandate as at September 30, 2012 was **US$811.2 million**, compared with US$726.2 million at the end of June 2012. This increase in value partly reflected the transfer of US$32 million to this mandate on August 01 2012.

---

[2] The SAA benchmark is a blended benchmark which comprises, Bank of America/Merrill Lynch US Treasury 1-5 Years Index (25%), Barclays US Aggregate Bond Index (40%), Russell 3000 ex Energy Index (17.5%), and MSCI EAFE ex Energy Index (17.5%).

The other equity mandate, which is exposed to **US Core Domestic Equities,** returned 6.8 per cent during the third quarter of 2012, outperforming its benchmark, the Russell 3000 ex Energy Index which gained 5.8 per cent. This relatively better performance was due to managers' decisions to select stocks with higher returns than those in the benchmark. On a sectoral level, the holdings in the Consumer Discretionary, Technology and Health Care sectors added the most to excess returns while Utilities stocks detracted the greatest from performance. In addition, the portfolio's performance benefitted from its exposure to companies with higher earnings revisions as well as stocks which had low price-to-earnings (P/E) ratios relative to similar stocks. For the financial year to September 2012, this mandate returned 31.4 per cent compared with 30.7 per cent for the benchmark. The net asset value of this mandate as at September 30 2012 was **US$886.4 million**, compared with US$831.3 million at the end of June 2012.

The downward trajectory of US Treasury yields over the quarter benefitted the fixed income portion of the Fund. The **US Short Duration Fixed Income** mandate returned 0.6 per cent during the third quarter of 2012, compared with a return of 0.5 per cent for its benchmark, the Bank of America Merrill Lynch US Treasury 1-5 Year Index. This mandate's outperformance can be attributed to the holding of out-of-benchmark securities, in particular, agency mortgages and foreign government guaranteed bonds whose spreads tightened versus US Treasuries. Given the volatility of Treasury yields, the duration of this mandate remained relatively close to that of the benchmark throughout the quarter. For the financial year to September 2012, this mandate gained 1.6 per cent compared with 1.3 per cent for the benchmark. The mandate's net asset value as at September 30 2012 was **US$1,105 million** compared with US$1,061.7 million at the end of June 2012. This increase in value partly reflected the transfer of US$37 million to this mandate on August 01 2012.

The **US Core Fixed Income mandate** also outperformed its benchmark, returning 2.2 per cent during the third quarter of 2012 compared with a return of 1.6 per cent for the Barclays Capital US Aggregate Bond index. The better-than-benchmark performance of this mandate reflected the increased exposure to spread products at the expense of Treasury securities which was the worst performing sectors in the benchmark. The corresponding overweight allocations were in CMBS and corporate bonds which were the strongest performers. Also contributing positively to excess returns was the overweight exposure to agency MBS. This sector outperformed duration-neutral Treasuries as the Federal Reserve made a commitment to purchase these securities monthly and extended its Operation Twist until the end of 2012. In addition, the demand for lower coupon agency MBS continued to be robust as investors sought high quality spread products in this exceptionally low interest environment. For the financial year to September 2012, this mandate gained 6.7 per cent compared with 5.2 per cent for the benchmark. The net asset value of this mandate at September 30 2012 was **US$1,795.8 million**, compared with US$1,757.6 million at the end of June 2012.

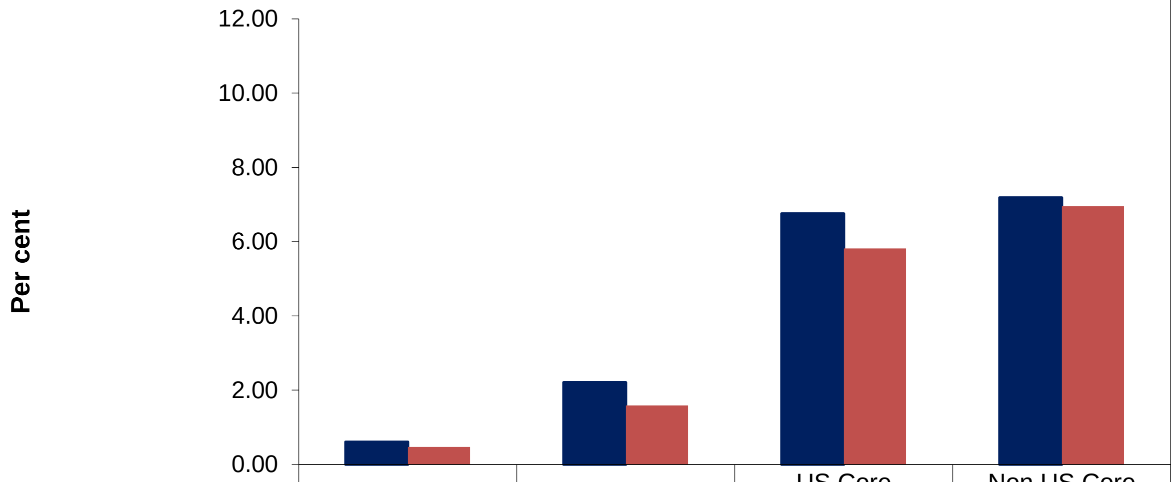
Over the next quarter, market volatility is expected to increase as investors would be focused on the US Presidential elections and subsequently, the issues surrounding the January 2013 “fiscal cliff”. While recent stimulus measures have buoyed financial markets, these measures may face diminishing efficacy. This, combined with slower global growth, can lead to increase market headwinds. While the Fund’s investment managers may not all share the same views about the prospects for financial markets over the short-term, it is expected that they would take tactical positions that would allow them to outperform their respective benchmarks.

Table 2
Contribution to Quarterly Return,
For the period July 2012 – September 2012
/per cent/

	SAA Weights	Portfolio Weights as at 30-Sep- 2012	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	100.00	3.53	2.98
US Core Domestic Fixed Income	40.00	38.13	0.88	0.64
US Core Domestic Equity	17.50	18.82	1.26	1.00
Non US Core International Equity	17.50	17.22	1.20	1.20
US Short Duration Fixed Income	25.00	23.46	0.15	0.12
Cash	0.00	2.37*	0.00	0.00

*This represents the cash contribution made by the Government on September 28, 2012.
NB: Differences in totals are due to rounding.

Figure 7
Absolute Returns by Asset Class
For the period July 2012 – September 2012
/per cent/



	US Short Duration	US Core Fixed Income	US Core Domestic Equities	Non US Core International Equities
Composite Portfolio Return	0.61	2.21	6.75	7.19
SAA Benchmark Return	0.47	1.59	5.82	6.95

SECTION 4 –COMPLIANCE AND PORTFOLIO RISKS

Compliance

During the quarter ended September 30 2012, there was no breach of the Investment Guidelines.

Portfolio Risks

The main risks for the HSF portfolio are Credit, Equity, Concentration, Interest Rate, and Currency risks. The following paragraphs give a description of how these risks are mitigated.

Credit Risk and Equity Risk

For the **money market portion** of the Fund, Credit Risk is minimized by the strict adherence to the following standards: (i) all counterparties must have a minimum credit rating of either A-1 from the Standard and Poor's rating agency or P-1 from Moody's; and (ii) a maximum exposure limit for counterparties of no more than 5.0 per cent of the market value of the portfolio.

For **fixed income instruments**, Credit Risk is mitigated by the use of credit concentration limits as well as minimum credit quality ratings. Bonds must have an implied investment grade rating as defined by Standard and Poor's, Moody's or Fitch. Should the required ratings on an existing fixed income security fall below the minimum standards, the security must be sold within an agreed upon timeframe. Table 3 below shows the Average Credit Quality of the US Short Duration and US Core Fixed Income Portfolios as at September 30 2012.

Table 3
Average Credit Rating

Mandate	Portfolio	Benchmark
US Short Duration	AA+	AA+
US Core Fixed Income	AA-	AA

For the **equity portfolios**, Equity Risk is managed by imposing a maximum percentage holding of 3.0 per cent of any security's outstanding shares, as well as a maximum sector deviation relative to the benchmark of 5.0 per cent. Throughout the quarter, these limits were all adhered to by the external managers.

Concentration Risk

Concentration or Diversification Risk is minimised by investing across various asset types. The portfolio is currently invested across four asset groupings as follows - US Short Duration Fixed Income, US Core Domestic Fixed Income, US Core Domestic Equity and Non-US Core International Equity. Asset classes in which the Fund invests react differently under a given market condition and when one asset class has strong returns, another may have lower returns. The Fund's investments are also diversified across a number of assets with the aim of securing a positive return under a range of market conditions and to lower the total risk of the portfolio.

Interest Rate Risk

Interest Rate Risk is managed using a weighted average effective duration limit on the respective portfolios, with an allowable range of one (1) year longer or shorter than the weighted average duration of the respective benchmark. Table 4 shows the weighted average duration for the US Short Duration and US Core Domestic Fixed Income portfolios as at September 30, 2012.

Table 4
Weighted Average Duration
/Years/

Mandate	Portfolio	Benchmark
US Short Duration	2.68	2.67
US Core Domestic Fixed Income	4.72	4.67

Currency Risk

Currency Risk is managed by containing and managing the exposure to non-US dollar instruments. For the Fixed Income and US Core Domestic Equity mandates, no more than 10 per cent of the market value of the portfolio can be invested in securities which are denominated in currencies other than the US Dollar. The Non-US Core International Equity Portfolio is comprised primarily of non-US dollar denominated securities, and the Fund accepts the currency risk inherent in the relevant benchmark. For this mandate, currency hedging is permitted up to 15 per cent of the market value of the portfolio using the US dollar as the base currency. At the end of September 2012, the currency exposure for this portfolio was 100 per cent of its market value. During the quarter, all the portfolios were within their respective limits.

Appendix I
HSF Portfolio
Historical Performance since Inception

Quarter End	Current Returns			Fiscal YTD			Annualised Return Since Inception		
	Portfolio %	Benchmark %	Excess bps	Portfolio %	Benchmark %	Excess bps	Portfolio %	Benchmark %	Excess bps
FY 2010									
December	0.96	0.89	6.65	0.96	0.89	6.65	3.85	3.91	-6.58
March	1.61	1.68	-6.20	2.59	2.58	0.49	4.12	4.20	-8.40
June	-1.83	-1.89	6.05	0.71	0.64	6.69	3.18	3.23	-5.55
September	5.33	5.08	24.73	**6.07**	**5.75**	**31.93**	**4.61**	**4.59**	**2.29**
FY 2011									
December	2.29	2.21	8.15	2.29	2.21	8.15	5.01	4.97	4.69
March	1.62	1.54	7.24	3.94	3.79	15.68	5.18	5.11	6.60
June	1.88	1.81	6.68	5.89	5.67	22.91	5.41	5.32	8.21
September	-4.82	-4.28	-53.66	**0.79**	**1.14**	**-34.89**	**3.80**	**3.87**	**-7.13**
FY 2012									
December	2.74	3.03	-28.52	2.74	3.03	-28.52	4.27	4.41	-13.94
March	5.04	4.46	57.50	7.92	7.63	29.29	5.27	5.27	-0.10
June	-0.90	-0.60	-30.42	6.95	6.98	-3.72	4.80	4.87	-7.37
September	3.53	2.98	55.01	**10.73**	**10.18**	**55.01**	**5.38**	**5.33**	**5.20**

Notes:

(1) Differences in totals are due to rounding.

(2) In May 2008, US Treasury instruments were added to the HSF portfolio. As a result, the performance benchmark for the HSF portfolio became a blended benchmark which comprised of 2.5 Merrill Lynch US Treasury 1-5 Years Index and 97.5 US One-month LIBID Index.

(3) In August 2009, International Equities and Fixed Income Securities were added to the HSF portfolio. The performance benchmark for the HSF portfolio became a blended benchmark which comprise, Bank of America/Merrill Lynch US Treasury 1-5 Years Index, US One-month LIBID Index, Barclays US Aggregate, Russell 3000 ex Energy, and MSCI EAFE ex Energy.

(4) In January 2011, the HSF Portfolio achieved its Strategic Asset Allocation where the portfolio was invested in four assets classes. US Short Duration Fixed Income (25), US Core Fixed Income (40), US Equity (17.5) and Non-US International Equity (17.5).

Appendix II
Heritage and Stabilisation Fund
Quarterly Portfolio Valuation (USD)

Valuation Date	Net Asset Value	Quarterly Income	Accumulated Surplus & Unrealized Capital Gains/Losses	Contributions
March 15, 2007	1,402,178,155	0	0	
March 31, 2007	1,405,448,567	3,270,412	3,270,412	-
June 30, 2007	1,424,094,965	18,646,398	21,916,810	-
September 30, 2007	1,766,200,701	20,301,027	41,966,361	321,706,043
December 31, 2007	1,788,304,749	22,204,785	64,035,501	-
March 31, 2008	1,804,531,743	16,631,853	80,514,798	-
June 30, 2008	1,997,251,772	13,715,988	93,124,304	180,210,617
September 30, 2008	2,888,421,556	15,341,508	110,379,131	873,963,840
December 31, 2008	2,909,717,167	16,296,264	131,638,985	-
March 31, 2009	2,911,075,318	4,492,667	133,066,161	-
June 30,2009	2,912,040,600	3,621,489	133,909,143	-
September 30, 2009	2,964,686,478	11,397,337	186,755,766	-
December 31, 2009	2,992,717,167	19,444,496	214,699,141	-
March 31, 2010	3,038,173,194	17,674,928	259,925,615	-
June 30, 2010	3,083,272,124	23,694,244	199,004,184	103,843,621
September 30, 2010	3,621,984,041	27,568,267	364,361,226	373,500,642
December 31, 2010	3,701,961,347	33,317,910	443,906,745	-
March 31, 2011	3,759,689,344	45,854,060	500,513,925	-
June 30, 2011	3,825,639,556	70,691,561	567,222,023	-
September 30, 2011	4,084,016,158	29,885,267	374,074,067	451,400,519
December 31, 2011	4,191,162,904	10,474,106	481,361,876	-
March 31, 2011	4,397,263,070	42,045,281	687,290,865	-
June 30, 2012	4,378,930,036	34,014,167	642,769,982	26,241,964
September 30, 2012	4,712,376,278	38,688,423	794,770,772	181,308,882

Appendix III
Summary Characteristics of Composite Benchmarks
Fixed Income Benchmarks

Key Characteristics	Barclays US Aggregate Index	Merrill Lynch 1-5 Index
Total Holdings	7,917	127
Coupon (%)	3.71	2.04
Duration (Years)	4.53	2.67
Average Life (Years)	6.35	2.76
Yield to Maturity (%)	1.38	0.34
Option Adjusted Spread (bps)	46	1
Average Rating (S&P)	AA	AA+
Minimum Rating (S&P)	BBB-	AA+

Equity Benchmarks

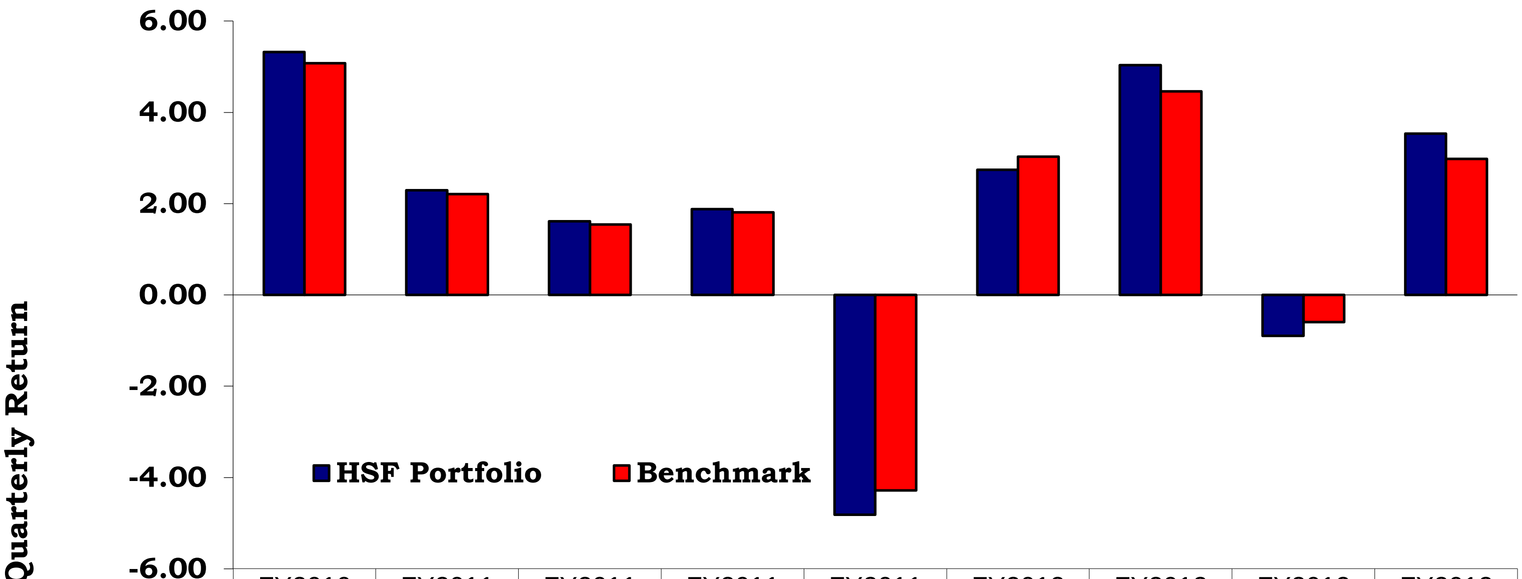
Key Characteristics	Russell 3000 (ex energy)	MSCI EAFE (ex energy)
Total Holdings	2,770	871
Earnings Per Share (EPS Growth 3-5y fwd) ()	11.30	10.73
Price Earnings (P/E fwd)	13.5	8.55
Price / Book (P/B)	2.30	1.35
Weighted Average Market Capitalization (Bn)	$90.9	$47.5

Appendix IV
Summary of the Fund's Net Asset Value by Mandate
/US$ Million/

	December 2011	**March 2012**	**June 2012**	**September 2012**
Total Fund Value	**4,191**	**4,397**	**4,379**	**4,712**
Total Value of Equity	**1,453**	**1,647**	**1,557**	**1,697**
US Core Domestic Equity	753	867	831	886
Non-US Core International Equity	700	780	726	811
Total Value of Fixed Income	**2,736**	**2,749**	**2,820**	**2,901**
US Short Duration Fixed Income	1,041	1,042	1,062	1,105
US Core Domestic Fixed Income	1,695	1,707	1,758	1,796
Total Value of Cash or Cash Equivalents	**2**	**1**	**2**	**114***

*The mainly represented the cash contribution (US$111.9million) made by the Government on September 28, 2012.

Appendix V
HSF Portfolio Quarterly Returns
/per cent/



	FY2010 Q4	FY2011 Q1	FY2011 Q2	FY2011 Q3	FY2011 Q4	FY2012 Q1	FY2012 Q2	FY2012 Q3	FY2012 Q4
HSF Portfolio	5.33	2.29	1.62	1.88	-4.82	2.74	5.04	-0.90	3.53
Benchmark	5.08	2.21	1.54	1.81	-4.28	3.03	4.46	-0.60	2.98

Quarter