Trinidad and Tobago

Heritage & Stabilization Fund

Quarterly Investment Report

April – June 2013

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EXECUTIVE SUMMARY

The **United States (US)** economic expansion continued in the first quarter of 2013, as GDP grew by 1.8 per cent annualized, compared to the 0.4 per cent annualized gain in the fourth quarter of 2012. This reflected the biggest increase in consumer spending in two years outweighing a reduction in defense spending. During the quarter ended June 2013, US economic data was mostly positive pointing to continued expansion albeit at a slower pace. The housing market, manufacturing and retail sales contributed positively to the economic outturn. On the policy front, the Federal Reserve left its monetary policy rates and size of its asset purchase programme unchanged during the quarter. However, on June 19th, 2013 the Fed announced its intention to taper its asset purchase programme later in the year depending on the health of the economy. The Fed's statement together with the positive outlook for the US economy led to a broad sell-off in asset classes and increased market volatility in the latter part of June.

The recession in the **Euro zone** deepened during the first quarter of 2013 as real GDP contracted by a further 0.3 per cent following a decline of 0.6 per cent in the prior three months. Economic indicators were not all bad in the Eurozone as both the manufacturing and services sectors recorded positive trends during the second quarter of 2013. This notwithstanding, there were deteriorations in the labour market with the unemployment rate increasing marginally to 12.2 per cent, from 12.1 per cent in March. Conversely, prices remained somewhat subdued during the period. At its May meeting, the Governing Council of the European Central Bank took the decision to lower the interest rate on its main refinancing operations of the Eurosystem by 25 basis points and the rate on the marginal lending facility by 50 basis points. The rate on the overnight deposit facility however remained unchanged[1]. More recently in its July statement, in what is considered a shift in policy, the ECB introduced forward

[1] The deposit facility is the overnight rate that allows commercial banks to make deposits into the eurosystem.

guidance, with the Governing Council indicating that the key interest rate is expected to remain at lower levels for an extended period of time and that monetary policy tightening is not likely anytime soon

The **United Kingdom (UK)** economy grew by 0.3 per cent in the first quarter of 2013, owing to the growth in inventories during the period. This improvement was in line with expectations and provided some minor respite given the decline of 0.2 per cent recorded in the previous quarter. Moreover, the economic recovery in the UK gained further momentum, with improvements in the services, manufacturing and housing sectors being recorded in the second quarter of 2013.
On the policy side, the Monetary Policy Committee, at its meeting on July 3 and 4, 2013, decided to maintain the official rate at 0.5 per cent and the size of its asset purchase programme at GBP 375 billion.

In **Japan**, real GDP expanded by 4.1 per cent in the first quarter of 2013, up from a 1.2 per cent annualized rate in the fourth quarter of 2012. Economic data for the second quarter of 2013 continues to be encouraging, buoyed by positive trends observed in both the manufacturing and services sectors during the period. Accordingly, these positive trends augur well for the economy and may be indicative of further improvements in domestic activity. Of note as well during the quarter, Prime Minister Shinzo Abe unveiled details of the “third arrow” of “Abenomics”, which comes after a period of significant monetary and fiscal stimulus packages. This “third arrow” intends to focus on structural reforms to boost Japan’s long term economic performance.

During the second quarter of 2013, the financial markets were impacted by positive economic data out of the US; slightly improved economic activity in Europe; a hawkish stance by the Fed; continued accommodative monetary policies in Japan and heated public demonstrations and protests in Brazil and Egypt. These factors however did not unsettle investors as expected. In fact, investors continued to be encouraged by the positive news from the US over the period and their bullish outlook continued for the majority of the second quarter. The Chicago Board Options Exchange Volatility Index (VIX) averaged 14.8 points this quarter, slightly higher than the previous quarter's average of 13.5 points. The equity markets' performances were mixed over the period with the US Standard and Poor's (S&P) 500 index gaining 2.4 per cent, the Japanese Nikkei 225 index advancing 10.2 per cent and the MSCI EAFE losing 2.11 per cent over the quarter from the previous quarter. In the global fixed income markets, yields in G-10 countries rose modestly, with the US and Germany leading the way, while yields in Italy declined by over 20 basis points.

The HSF investment portfolio returned -0.3 per cent for the quarter ended June 2013, compared with a return of -0.7 per cent for the Strategic Asset Allocation (SAA) benchmark. While the Fund's exposure to equity contributed positively, the fixed income exposure weighed down absolute returns. This brought HSF investment portfolio return to 4.51 per cent for the financial year to June 30, 2013, compared to 3.66 per cent for the benchmark. There were no deposits to or withdrawals from the fund over the reporting period but a deposit of US$42.5 million was received in July with respect to energy revenues of the quarter ended June 2013.

At the end of June 2013, the net asset value of the HSF was US$4,914.4 million, a decrease from the US$4,933.3 million reported at the end of March 2013.

Contribution to Quarterly Return,
For the period April 2013 – June 2013
/per cent/

	SAA Weights	Portfolio Weights as at 30-June-2013	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	100.00	-0.30	-0.69
US Core Domestic Fixed Income	40.00	37.11	-0.90	-0.93
US Core Domestic Equity	17.50	20.64	0.71	0.54
Non US Core International Equity	17.50	18.95	0.07	-0.11
US Short Duration Fixed Income	25.00	23.30	-0.15	-0.17

NB: Differences in totals are due to rounding.

Comparative Quarterly Returns
For the Quarters ended December 2012 – June 2013
/per cent/

	3 Months Weighted Return as at 30-Jun-2013		3 Months Weighted Return as at 31-Mar-2013		3 Months Weighted Return as at 31-Dec-2012	
	HSF	**Bench-mark**	**HSF**	**Bench-mark**	**HSF**	**Bench-mark**
Composite Portfolio	-0.30	-0.69	2.90	3.29	1.49	1.44
US Core Domestic Fixed Income	-0.90	-0.93	-0.05	0.00	0.19	0.09
US Core Domestic Equity	0.71	0.54	1.90	1.95	0.03	0.10
Non US Core International Equity	0.07	-0.11	1.00	1.27	1.25	1.25
US Short Duration Fixed Income	-0.15	-0.17	0.04	0.05	0.02	0.01

Comparative Financial Year to Date Returns
For the periods June 2012 & June 2013
/per cent/

	Financial Year to Date Return as at 30-Jun-2013		Financial Year to Date Return as at 30-Jun-2012	
	HSF	Bench-mark	HSF	Bench-mark
Composite Portfolio	4.51	3.66	6.95	6.98

SECTION 1 – INTERNATIONAL ECONOMIC ENVIRONMENT

United States

The US economy continued its expansion in the first quarter of 2013, as GDP grew by 1.8 per cent annualized, revised downward from a previously reported 2.4 percent pace. Notwithstanding, the downward revision, this compared favourably to the 0.4 per cent annualized gain in the fourth quarter of 2012. The acceleration in growth reflected the biggest increase in consumer spending in two years outweighing a reduction in defense spending. Despite the continued improvement in output indicators, the IMF in its most recent update to its World Economic Outlook, slightly lowered its 2013 and 2014 forecasts for US growth from 1.9 per cent and 2.9 per cent respectively to 1.7 per cent and 2.7 per cent. The IMF's revision reflects the new assumption that sequestration of public spending which has been a drag on economic growth will continue into 2014.

For the quarter ended June 2013, US economic data continued to be mostly positive pointing to continued expansion in the second quarter albeit at a slower pace. Housing market activity during the quarter remained buoyant, although cooling somewhat when compared to the previous quarter as the record-low mortgage rates that consumers enjoyed earlier in the year began to move upwards. In June, housing starts fell to an 836,000 annual rate compared to 1.05 million annual rate in March. New home sales and building permits however both increased during the quarter.

Retail sales in the US continued its trend of modest growth during the second quarter, increasing by 5.7 per cent in the twelve months to June compared to 3.2 per cent in March 2013.

Manufacturing activity continued to expand in June though at a slower pace when compared to the previous quarter as the Manufacturing Purchasing Managers' Index

(PMI) declined to 52.2 compared with a reading of 52.3 one month earlier and 54.6 in March. The slowdown in activity reflects a contraction in new export orders and a slower expansion in employment. Meanwhile, industrial production expanded by 2.0 per cent in the twelve months to June 2013, compared with 3.1 per cent in March 2013.

In the labour market, conditions improved somewhat during the quarter according to the latest data. In June, nonfarm payrolls increased by 195,000 compared with an increase of 195,000 one month earlier and an increase of 142,000 in March 2013. The unemployment rate however was unchanged in June when compared to the previous quarter, holding steady at 7.6 per cent.

Inflationary pressures as measured by the Consumer Price Index remained modest during the quarter, as the index increased 1.8 per cent (year-on-year) in June, up from 1.5 per cent in the twelve months to March 2013.

On June 19th 2013, the Federal Open Market Committee announced its decision to leave its benchmark rate unchanged as long as the unemployment rate remains above 6.5 per cent and the inflation rate does not exceed the Committee's long-run goal of 2 per cent. The Fed also decided to leave the pace of its asset purchase program unchanged while noting improvements in economic activity, household spending and business fixed investment, the housing sector, and labour conditions – despite an elevated unemployment rate. On the tapering of its asset purchase program, Federal Reserve Chairman Ben Bernanke stated that the Fed intends later this year to start gradually scaling down its monthly purchase of Treasury securities and Mortgage Backed Securities until the unemployment rate reaches 7 per cent - this is anticipated to occur by the middle of 2014. Chairman Bernanke however, emphasized that the timing of the retreat would be highly dependent on the health of the economy: if growth falters, the

Fed would slow or even reverse the process. Analysts expected that the Fed would then take several more years to unwind the rest of its stimulus package which should result in a steady increase in short-term interest rates from essentially zero per cent to more normal levels.

From as early as May 2013, financial markets began to price in the gradual withdrawal of support by the Federal Reserve given the improvement in US economic data. The Fed's statement together with the positive outlook for the US economy, led to a broad sell-off in asset classes in the latter part of June 2013.

At its latest meeting, the Federal Reserve Open Market Committee acknowledged the improvement of portions of the economy but voiced concerns about fiscal policy restraining economic growth. As such, the Committee decided to keep the benchmark interest rate unchanged at the range 0-0.25 per cent and to continue its purchases of additional agency mortgage-backed securities at a pace of $40 billion per month and longer term Treasury securities at a pace of $45 billion per month. The Fed currently anticipates that this exceptionally low range for the Federal Funds rate will be appropriate as long as unemployment remains above 6.5 per cent and the inflation rate does not exceed 2.5 per cent.

Euro zone

The recession in the Euro zone deepened during the first quarter of 2013 as real GDP contracted 0.3 per cent following the decline of 0.6 per cent in the prior three months. This marked the sixth consecutive quarterly contraction in economic activity. The 0.3 per cent decline also exceeded analysts' estimates of a 0.1 per cent moderation. In its latest forecast, the IMF stated that the Euro zone will remain in recession in 2013, with growth rising to just below 1 per cent in 2014, noting that the recession in the Euro area was deeper than expected. In July, the IMF revised downward its Euro area output projections for 2013 and 2014 by 0.2 and 0.1 per cent respectively to -0.6 and 0.9 per cent.

Economic conditions in the Euro zone have shown signs of improvement in the second quarter of 2013 despite manufacturing and services remaining in contractionary territory. The Markit Eurozone manufacturing PMI index increased to 48.8 in June compared to 47.8 in March, signaling a slowdown in the rate of contraction. This was the highest reading of the index over the past sixteen months. Similarly, the services PMI rose to 48.3 in June from 47.5 in March.

The Euro area composite PMI increased more than expected to 48.7 in June, from 46.5 in March indicative of easing in the rate of contraction. Additionally, the July reading of the index was 50.4, above the 50 no change level for the first time since January 2012. Conversely, industrial production in the Euro zone contracted in May by 0.3 per cent (month-on-month) compared with a revised expansion of 0.9 per cent March.

Conditions in the labour market deteriorated further in May 2013, as the unemployment rate continued its record breaking ascension, reaching 12.2 per cent, up from 12.1 per cent in March. Among the member states, Spain and Greece continued to register the highest rates of 26.9 per cent and 26.8 per cent, respectively, while the lowest rates were recorded in Austria (4.7 per cent) and Germany (5.3 per cent).

In the second quarter of 2013, consumer prices continued to be relatively subdued in the Euro zone with the inflation rate decelerating to 1.6 per cent in the twelve months to June 2013, down from 1.7 per cent in March, reflecting a decline in energy prices when compared to the previous quarter.

At its meeting on May 2, 2013, the Governing Council of the European Central Bank took the decision to lower the interest rate on its main refinancing operations of the Euro-system by 25 basis points to 0.50 per cent and the rate on the marginal lending facility by 50 basis points to 1.00 per cent. The rate on the deposit facility however remained unchanged at 0.00 per cent. According to the ECB, the factors that impacted the decision included low underlying price pressure and continued weak economic sentiment. The ECB noted that the lower rate should contribute to support prospects for a recovery later in the year. Additionally, the ECB indicated that the monetary policy stance would remain accommodative for as long as needed.

More recently in its July statement, in what is considered a shift in policy, the ECB introduced forward guidance, with the Governing Council indicating that the key interest rate is expected to remain at lower levels for an extended period of time and that monetary policy tightening is not likely anytime soon. The ECB also left its policy benchmark rates unchanged.

United Kingdom

The UK economy grew in line with expectations in the first quarter of 2013. GDP improved 0.3 per cent compared to a decline of 0.2 per cent increase in the previous quarter. This improvement in output was largely due to growth in inventories which added 0.4 percentage points to GDP and consumer spending which added 0.1 percentage points. Exports and business investment fell. The year-on-year change in GDP was a 0.6 per cent increase, which was the most in more than a year. More recently in its preliminary estimate of second quarter GDP, the Office for National Statistics indicated that the UK economy expanded by 0.6 per cent with services being the largest contributor to growth. In its July update to the World Economic Outlook, the IMF revised upward its forecast for output in the UK to 0.9 per cent from 0.6 per cent for 2013 and left 2014 unchanged at 1.5 per cent.

During the second quarter of 2013, the economic recovery in the UK gained momentum, with improvements being recorded in services, manufacturing and housing. By the end of the quarter, manufacturing PMI rose to 52.5 in June compared to 48.3 in March, to post its strongest reading since May 2011. The services PMI accelerated to 56.9 in June, the highest since March 2011 and up from 52.4 in March 2013. Additionally, construction PMI rose to 51 in June compared to 47.2 in March. Meanwhile in the housing sector, the Royal Institute of Chartered Surveyors (RICS) house price gauge increased over the quarter to 21 in June, the highest since May 2010 from -1 in March. In addition, the Nationwide House Price index rose to 0.3 per cent in June, up from 0.0 per cent in March, on a month on month basis.

Labour market conditions continued to be stable during the second quarter of 2013, as the unemployment rate in May measured 7.8 per cent, unchanged from the level recorded in March 2013. Meanwhile, inflationary pressures were unchanged as of June 2013 at 3.3 per cent year-on-year, when compared to the previous quarter-end, despite minor fluctuations in the rate in April and May. The rate of inflation however has consistently been above the Bank of England's target rate of 2.0 per cent.

At its meeting on July 3 and 4, 2013, the Bank of England's Monetary Policy Committee voted to maintain the official Bank Rate paid on commercial bank reserves at 0.5 per cent. The Committee also voted to maintain the stock of asset purchases financed by the issuance of central bank reserves at £375 billion.

Japan

During the first quarter of 2013, final results for GDP in the Japanese economy showed growth being recorded at 4.1 per cent annualized up from a 1.2 per cent annualized rate in the fourth quarter of 2012. GDP growth was driven by strong private sector demand. In the July 2013 IMF World Economic Outlook update, the forecast for GDP for 2013 was revised upward by 0.5 per cent from the previous forecast, to 2.0 per cent. The forecast for 2014 however was revised downward by 0.3 per cent to 1.2 per cent. According to the IMF, the stronger forecast for 2013 reflects the effects of the recent accommodative policies while the reduced expectation for 2014 is indicative of a weaker global environment.

Economic data for the second quarter of 2013 continues to be encouraging and is indicative of further growth. Positive trends were observed in the manufacturing sector during the quarter, with this sector expanding at the fastest pace in 28 months, while the rate of expansion in services cooled somewhat. The Manufacturing PMI increased to 52.3 in June compared to 50.4 in March while the Services PMI was 52.3 in June compared to 54.0 in March when it reached a five-year high. The strong outturn in manufacturing can be attributed to an increase in new orders to its strongest rate in three years.

Business sentiment among Japanese large manufacturers and large non-manufacturers increased as the Tankan survey diffusion index of current business conditions continued to improve in June to +4 from -8 in March and to +12 from +6, respectively. Meanwhile, conditions in the labour market were unchanged thus far during the quarter, as the unemployment rate held steady at 4.1% between March and May 2013. Labour force participation increased to 59.7 per cent in May in comparison to 58.9 per cent in March.

The general price level, measured by the Consumer Price Index (CPI) continued to remain in deflationary territory as the rate declined 0.3 per cent year-over-year in May compared to a 0.9 per cent decline in March.

During the quarter, Prime Minister Shinzo Abe unveiled details of the third arrow of 'Abenomics', which comes after significant monetary and fiscal stimulus packages. The third arrow which focuses on structural reforms to boost Japan's long term economic performance was largely seen as a disappointment by investors and the market as a whole. It includes policy measures aimed at promoting trade and investment, strengthening agriculture and improving career opportunities for women.

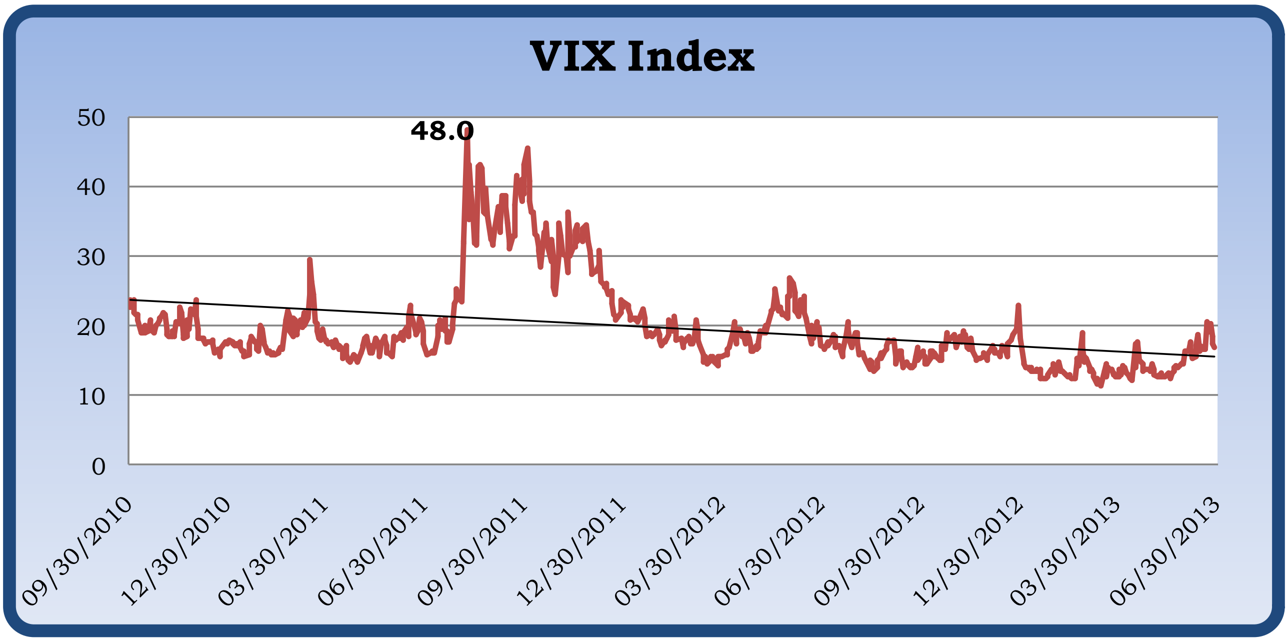
SECTION 2 – CAPITAL AND MONEY MARKET REVIEW

The financial markets generated mixed results over the second quarter of 2013 amid mixed data out of Europe (decelerating declines in manufacturing but a worsening labor market), continued accommodative stance out of Japan and speculation on whether the Fed will begin to taper its bond purchasing program in the third quarter of this year. However, investor anxiety was tempered by positive US economic data.

The Chicago Board Options Exchange Volatility Index (VIX), which is a proxy for investor anxiety and market risk, rose during the second quarter of 2013 to 16.86 points from 12.7 points at the end of March 2013. The index averaged approximately 14.8 points this quarter, compared with 13.5 points in the previous three months.

The equity market posted moderate gains this quarter, with the US Standard and Poor's (S&P) index reaching its highest level on record. Japan was the best performing non-US developed market as the Nikkei 225 index advanced by 10.32 per cent from the previous quarter. Benchmark 10-year yields rose in many of the G-10 nations over the quarter, except in Italy, where yields fell by over 20 basis points.

Figure 1
Market Volatility in the US
/points /

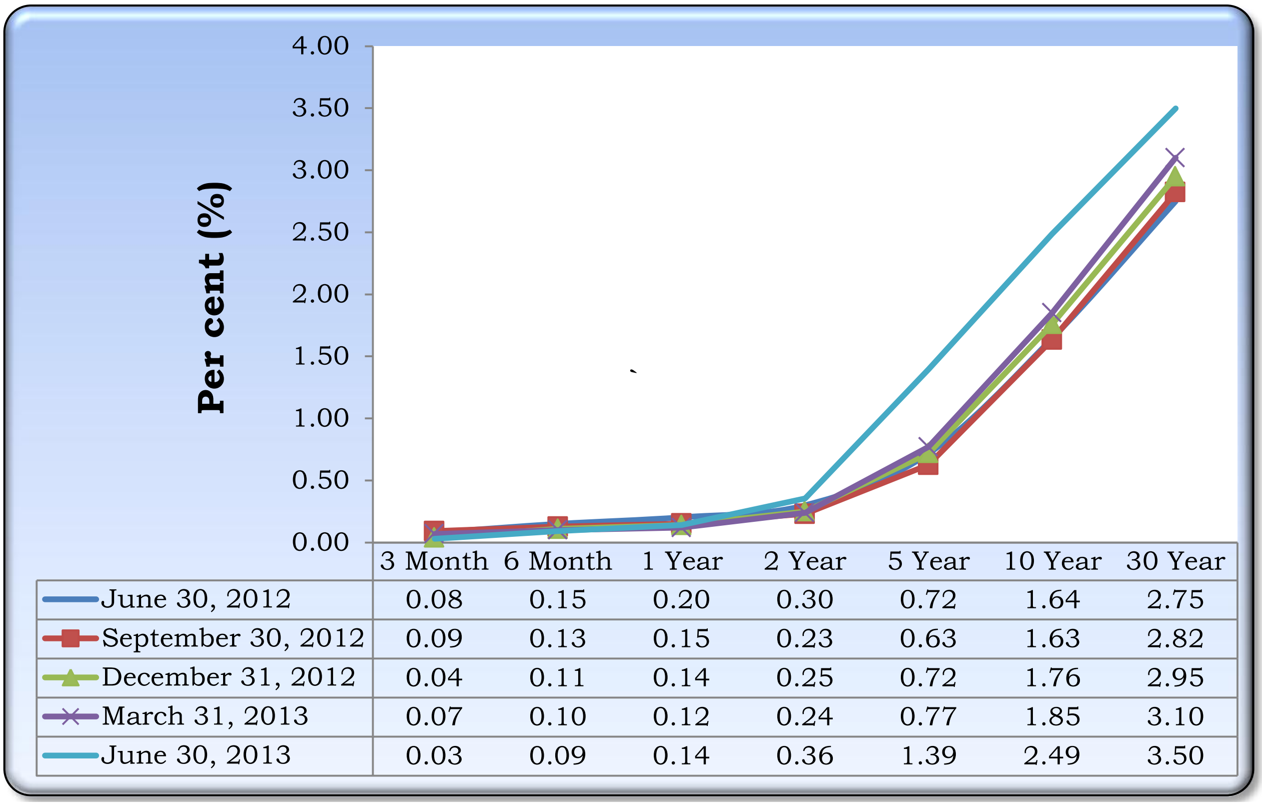


Source: Bloomberg.

Fixed Income

US Treasury yields rose significantly over the second quarter of 2013 and the curve steepened some 28 basis points between the 2-year and the 30-year sectors. Front end yields less than one year marginally declined – as the 3-month yield fell to 0.03 per cent from 0.07 per cent as at March 28, 2013- reflecting the Fed's commitment to maintain rates at current low levels until mid-2015. Medium-term to long-term yields rose sharply in May and June, as investors' demand for riskier assets increased due to positive economic data out of the US. In addition to the positive economic data from the US, the Fed Open Market Committee increased investors' fears by suggesting that they might begin to reduce its asset purchase program in the third quarter of 2013, thus dampening the demand for US fixed income securities.

Figure 2
US Treasury Yield Curve
/per cent/

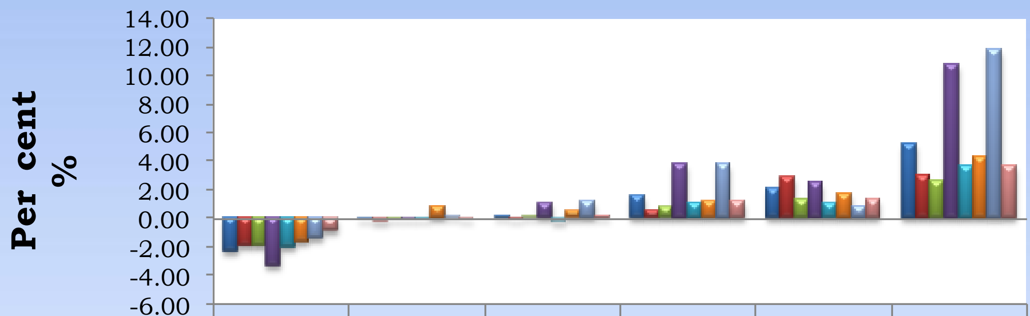


	3 Month	6 Month	1 Year	2 Year	5 Year	10 Year	30 Year
June 30, 2012	0.08	0.15	0.20	0.30	0.72	1.64	2.75
September 30, 2012	0.09	0.13	0.15	0.23	0.63	1.63	2.82
December 31, 2012	0.04	0.11	0.14	0.25	0.72	1.76	2.95
March 31, 2013	0.07	0.10	0.12	0.24	0.77	1.85	3.10
June 30, 2013	0.03	0.09	0.14	0.36	1.39	2.49	3.50

Source: Bloomberg.

All of the major fixed income sectors produced negative returns during the second quarter of 2013. The broader US fixed income market as measured by the Barclays Capital US Aggregate Bond index, lost 2.32 per cent in the second quarter of 2013, compared with a decline of 0.12 per cent in the previous three months. The performance of US Treasuries and the U.S. Corporate sector detracted from the overall performance of the index. The Asset Backed Securities (ABS) and Commercial Mortgage Backed Securities (CMBS) sectors posted the highest returns, declining only 0.80 per cent and 1.44 per cent, respectively.

Figure 3
Returns on Fixed Income Indices
/per cent/



	QTR ended June-13	QTR ended Mar-13	QTR ended Dec-12	QTR ended Sep-12	QTR ended Jun-12	FY 11/12
Barclays U.S. Aggregate	-2.32	-0.12	0.21	1.58	2.06	5.16
U.S. Treasuries	-1.92	-0.19	-0.09	0.57	2.83	2.99
U.S. Agencies	-1.91	-0.03	0.12	0.78	1.29	2.60
U.S. Corporate	-3.31	-0.11	1.06	3.83	2.52	10.76
U.S. MBS	-1.96	-0.05	-0.20	1.13	1.08	3.71
G-7 Global Bonds (Hedged)	-1.66	0.86	0.51	1.23	1.75	4.24
CMBS Index	-1.44	0.13	1.22	3.83	0.86	11.71
ABS Index	-0.80	0.05	0.22	1.23	1.33	3.67

Source: Barclays Capital.

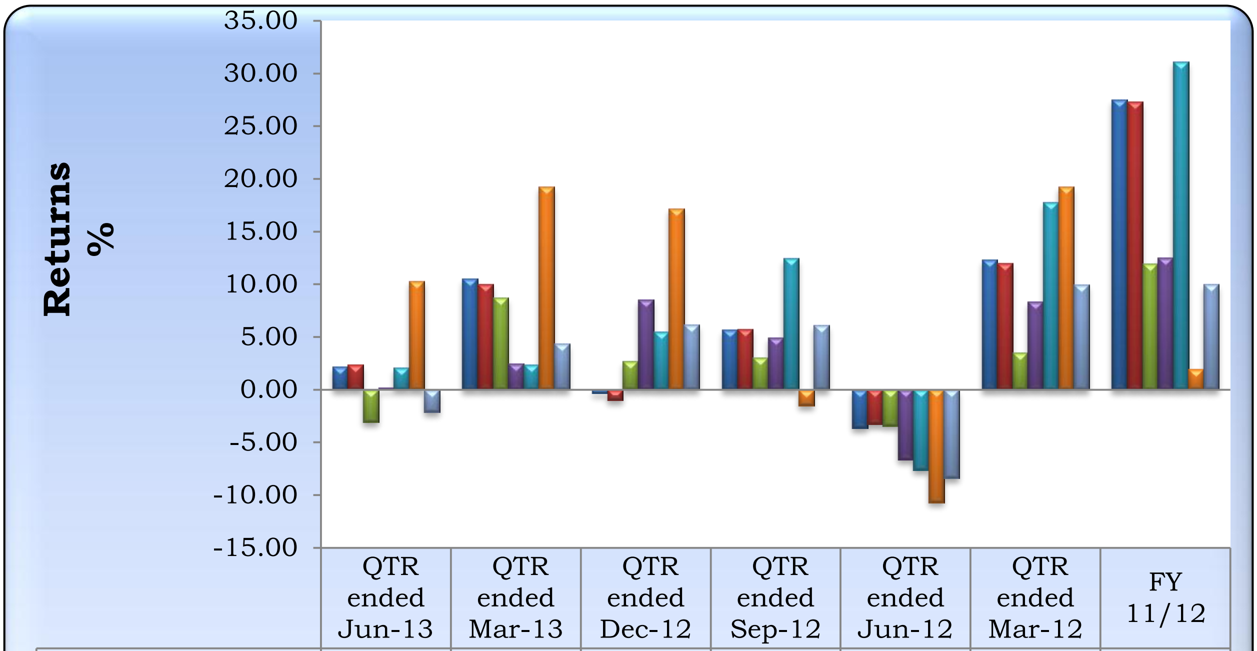
The performance of other developed market sovereign bonds was mixed over the quarter. The benchmark German bund yield rose by 44 basis points to 1.73 per cent, as gains in industrial output and expansion in the services industry pointed to strength in the economy. Meanwhile yields on Italian bonds fell over the period as global central bank actions increased demand for risker assets and the country's political deadlock was resolved by the formation of a new government.

Equity Markets

The equity markets' performances were mixed in the second quarter of 2013 and were impacted by continued improvements in the US housing and labor sectors and positive economic growth in the first quarter of 2013. By the end of the quarter however, some of the gains were eroded due to market speculation of the continuation of the Fed's asset purchase program as well as evidence of a slowdown in China.

In the US, the S&P 500 index gained 2.36 per cent, compared with a gain of 10.03 per cent in the previous three months. The index hit an all-time high of 1,669.16 on May 21st. Seven out of ten sectors recorded gains for the index in the second quarter of 2013, with the Financials and Consumer Discretionary sectors posting the highest returns. Japan was the leader in the non-US equity market, with the Nikkei 225 index posting returns of 10.32 per cent over the quarter. Prime Minister Shinzo Abe's pledge to end deflation has resulted in an increase in the demand for Japanese equities, as he released the "third arrow" of "Abenomics", which includes structural reforms. In the Euro zone, the French CAC index advanced 0.20 per cent, whilst Germany's DAX 30 index returned 2.10 per cent over the three months ending June 30, 2013. The MSCI EAFE index however lost 2.11 per cent as equity markets in Australia, New Zealand and Greece were heavy detractors from the overall return of the index as a result of local currency weakness and amid concerns that the tapering of the Fed's asset purchase program would negatively impact asset prices and growth. Additionally, in the UK the FTSE 100 declined 3.06 per cent over the period.

Figure 4
Price Returns on Equity Indices
/Per cent/



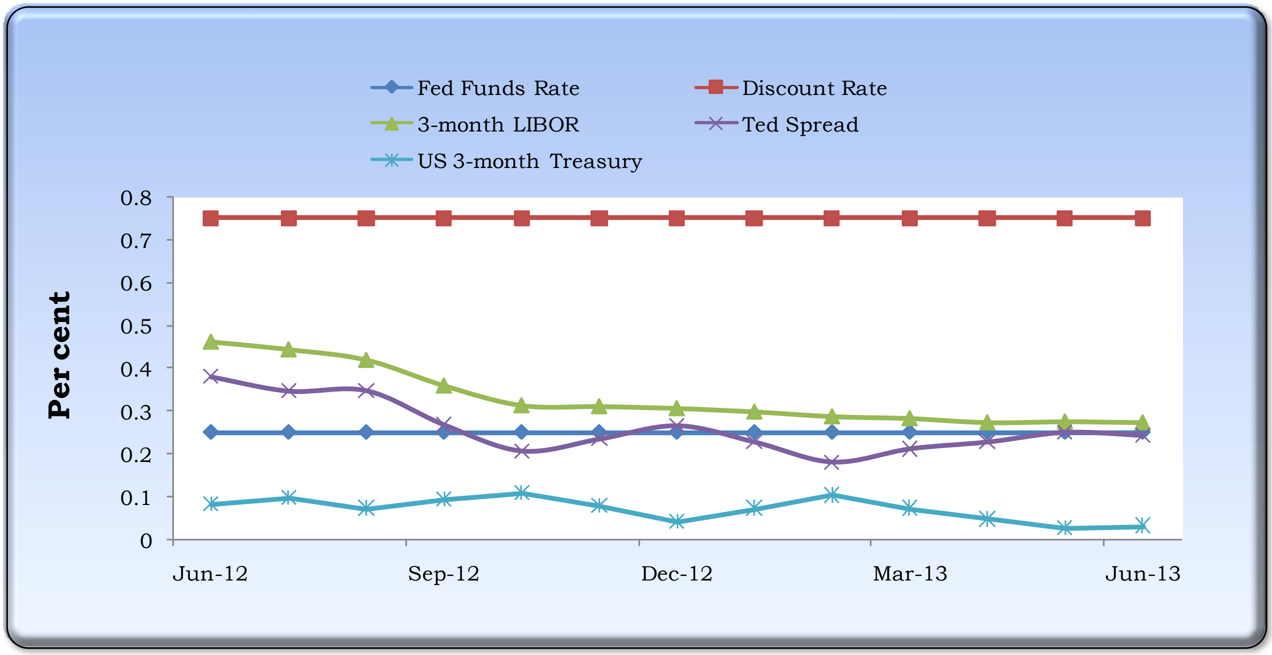
	QTR ended Jun-13	QTR ended Mar-13	QTR ended Dec-12	QTR ended Sep-12	QTR ended Jun-12	QTR ended Mar-12	FY 11/12
Russell 3000	2.17	10.53	-0.34	5.68	-3.65	12.32	27.53
S&P 500	2.36	10.03	-1.01	5.76	-3.29	12.00	27.33
FTSE 100 - UK	-3.06	8.71	2.71	3.07	-3.42	3.52	11.96
CAC 40 - France	0.20	2.48	8.53	4.95	-6.63	8.35	12.50
DAX 30 - Germany	2.10	2.40	5.49	12.47	-7.64	17.78	31.15
Nikkei 225 - Japan	10.32	19.27	17.19	-1.52	-10.68	19.26	1.95
MSCI EAFE	-2.11	4.38	6.17	6.14	-8.37	9.98	10.01

Source: Bloomberg.

Money Market

Short-term interest rates remained at relatively low levels as the major central banks continued their accommodative monetary policy stance. The 3-month US Treasury bill rate declined 4 basis points to 0.03 per cent at the end of the quarter. Meanwhile, the 3-month London Inter-Bank Offered Rate (LIBOR) fell less than 1 basis point to 0.27 per cent.

Figure 5
US Money Market Rates
/per cent/

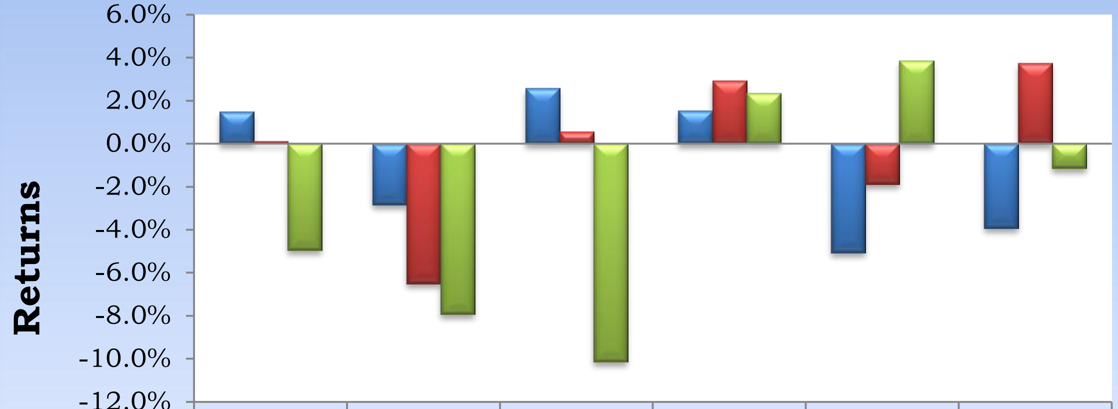


Source: Bloomberg.

Currency Markets

The US dollar strengthened against some of the major currencies across the globe, with the exception of the British pound, the Euro and the Swiss franc. The Japanese Yen was the worst performing G10 currency, depreciating by 4.97 per cent vis-à-vis the US dollar over the quarter. The fall in the value of the yen was primarily driven by the release of the 'third arrow' of Abenomics in Japan, which is meant to stimulate growth in the economy through monetary, fiscal and structural policies. The British Pound rose by 0.1 per cent in the quarter, mainly on an improved growth story in the UK economy. The Euro also appreciated over the quarter by 1.5 per cent amidst political uncertainty and a deepening recession in the Euro area, as the Fed continued to pump currency into its financial markets.

Figure 6
Foreign Exchange Returns for Major Currencies vis-à-vis the US Dollar
/per cent/



	QTR ended Jun-13	QTR ended Mar-13	QTR ended Dec-12	QTR ended Sep-12	QTR ended Jun-12	FY 11/12
EUR	1.49%	-2.83%	2.59%	1.52%	-5.07%	-3.94%
GBP	0.10%	-6.50%	0.54%	2.93%	-1.88%	3.74%
JPY	-4.96%	-7.93%	-10.13%	2.35%	3.86%	-1.15%

Source: Bloomberg.

SECTION 3 – PORTFOLIO PERFORMANCE

Strategic Asset Allocation

Over the period April to June 2013, the asset classes of the Fund deviated from their Strategic Asset Allocation (SAA) but their weights were all within the permitted (+/- 5 per cent) range. 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 two equity mandates carried overweight allocations relative to their SAA weights and these resulted from their stronger performance when compared with their fixed income counterparts. By the end of the quarter, the asset class with the largest overweight was the US Core Domestic Equity mandate while the US Core Fixed Income mandate had the largest underweight position.

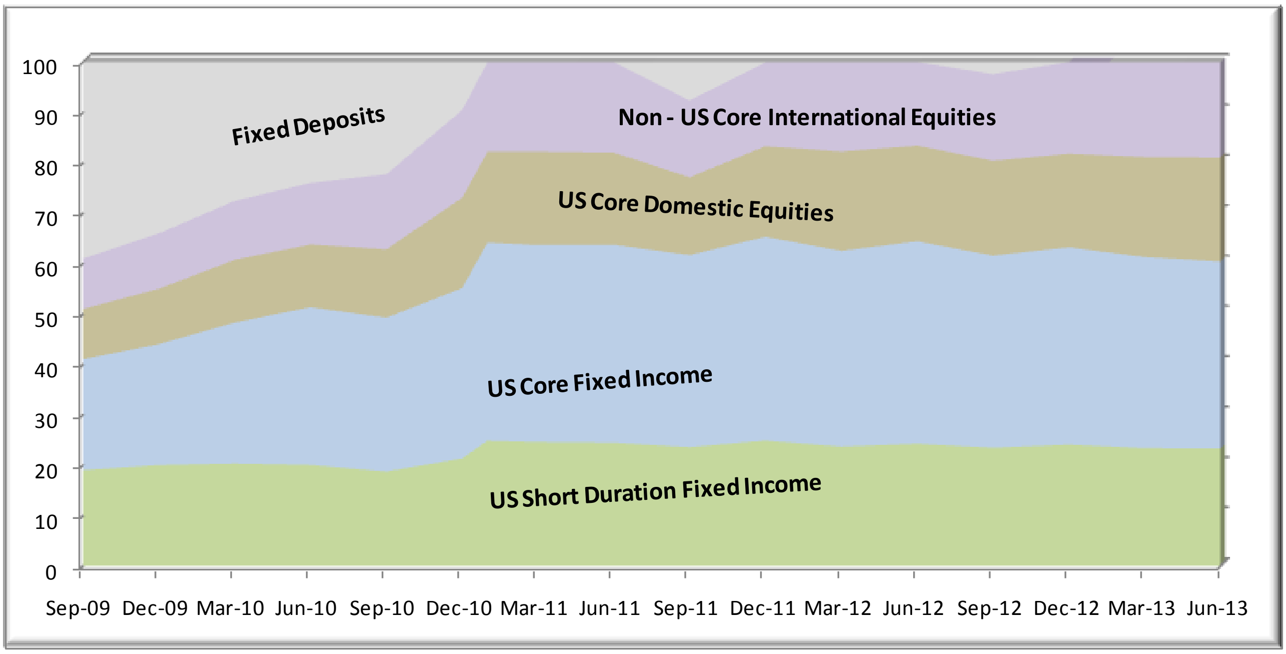
The total net asset value of the Fund as at the end of June 2013 totaled US$4,914.4 million, compared with US$4,933.3 million at the end of the previous quarter. Of this total, the investment portfolio was valued at US$4,913.6 million, while the remaining portion (US$0.8 million) was held in cash to 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 June 30 2012 to June 30 2013 are shown in Table 1, overleaf.

Table 1
Portfolio Composition relative to the Approved SAA
/per cent/

	Asset Class		***Jun-12***	***Sep-12***	***Dec-12***	***Mar-13***	***Jun-13***
		Target Weight SAA	***Actual % of Fund***	***Actual % of Fund***	***Actual % of Fund***	***Actual % of Fund***	***Actual % of Fund***
Portfolio Weights	Cash	0.00	0.00	2.37*	0.00	0.00	0.00
	US Short Duration Fixed Income	25.00	24.26	23.46	24.09	23.38	23.30
	US Core Domestic Fixed Income	40.00	40.16	38.13	39.14	37.92	37.11
	US Core Domestic Equity	17.50	18.99	18.82	18.57	19.86	20.64
	Non-US Core International Equity	17.50	16.59	17.22	18.20	18.84	18.95

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

Figure 7
Asset Composition of the HSF Portfolio
/per cent/



Performance of the Investment Portfolio

For the second quarter of 2013, the HSF investment portfolio declined 0.3 per cent, compared with a return of -0.7 per cent for the SAA benchmark[2]. This outperformance by 39 basis points can be attributed to favourable security selection as well as the deviation between the portfolio and SAA weighting composition. Most of the HSF portfolio's returns were generated by the equity portion of the Fund which contributed 0.8 per cent to the overall performance, while the fixed income mandates detracted 1.1 per cent from the overall return.

On an asset class level, all the mandates outperformed their respective benchmarks during the quarter ended June 30 2013.

The **US Short Duration Fixed Income** portfolio posted an absolute return of -0.67 per cent during the second quarter of 2013, outperforming its benchmark, the Bank of America Merrill Lynch US Treasury 1-5 year index, by 2 basis points. This ouperformance was attributed to the portfolio's exposure to German 3-year bonds and its relative duration positioning of US and German bonds over the quarter. Detracting from performance was the portfolio's exposure to spread products as spreads in agencies and supranational securities widened. The net asset value of this mandate as at June 30 2013 was **US$1,145.0 million,** compared with US$1,153.1 million at the end of the previous quarter. For the financial year to June 2013, this mandate portfolio returned -0.40 per cent compared with a return of -0.50 per cent for the benchmark.

[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 longer duration fixed income mandate which consists of **US Core Fixed Income** securities**,** posted a return of -2.43 per cent during the second quarter of 2013, underperforming its benchmark, the Barclays Capital US Aggregate Bond index which lost 2.32 per cent. The under-performance of this portfolio relative to the benchmark resulted from its overweight allocation to commercial mortgage backed securities, collateralized mortgage obligations and treasury inflation protected securities (TIPS). Favourable security selection within the investment grade credit sector along with an overweight to student loans within the consumer asset backed security sector helped to limit the under-performance of the portfolio. The net asset value of this mandate as at June 30 2013 declined in comparison to the previous quarter, totaling **US$1,823.5 million** compared with US$1,870.0 million in March 2013. For the financial year to June 2013, the US Core Fixed Income mandate returned -1.95 per cent compared with a benchmark's return of -2.23 per cent.

The **Non-US International Equities** mandate generated a gain of 0.33 per cent for the second quarter of 2013, compared with a return of -0.81 per cent for its benchmark, the MSCI EAFE ex Energy index. This outperformance was mainly on account of the managers' stock selection decisions which were favourable in Japan, Hong Kong, the U.K., France and Belgium. In addition, the portfolio benefitted from a currency hedge on the yen, which gained in value as the yen depreciated vis-à-vis the US dollar during the quarter. The net asset value of the Non-US Core International Equity mandate as at June 30, 2013 grew to **US$931.1 million**, from US$929.3 million at the end of March 2013. For the financial year to June 2013, this mandate returned 15.14 per cent, compared with a benchmark's return of 12.44 per cent.

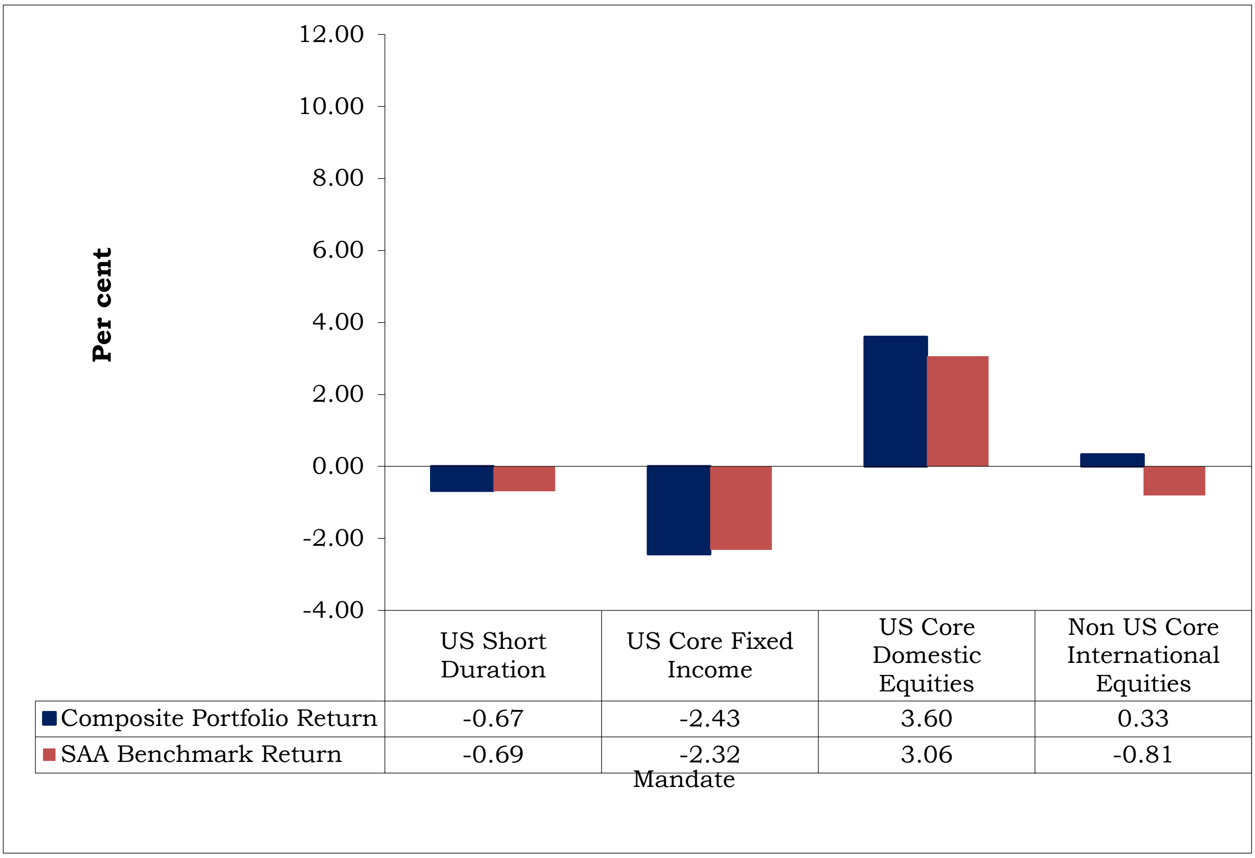
The **US Core Domestic Equities** mandate returned 3.60 per cent, compared with a benchmark return of 3.06 per cent. This outperformance was on account of the managers' favourable stock selection decisions which resulted in a combination of stocks that generated a higher return relative to those stocks in the benchmark. On a sector level, the holdings in the Technology, Financial Services and Health Care sectors added the most to excess returns. The net asset value of this mandate, as at June 30 2013, was **US$1,014.0 million**, compared with US$979.7 million at the end of March 2013. For the financial year to June 2013, this mandate returned 14.76 per cent compared with a return of 15.17 per cent for the benchmark.

Table 2
Contribution to Quarterly Return,
For the period April 2013 – June 2013
/per cent/

	SAA Weights	Portfolio Weights as at 30-Jun-2013	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	100.00	-0.30	-0.69
US Core Domestic Fixed Income	40.00	37.11	-0.90	-0.93
US Core Domestic Equity	17.50	20.64	0.71	0.54
Non US Core International Equity	17.50	18.95	0.07	-0.11
US Short Duration Fixed Income	25.00	23.30	-0.15	-0.17

NB: Differences in totals are due to rounding.

Figure 8
Absolute Returns by Asset Class
For the period April 2013 – June 2013
/per cent/



SECTION 4 –COMPLIANCE AND PORTFOLIO RISKS

Compliance

During the quarter ended June 30 2013, there was no breach of the Investment Guidelines.

Portfolio Risks

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

Credit 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 June 30, 2013.

Table 3
Average Credit Rating

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

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. The Asset classes in which the Fund invests react differently under a given market condition. As such, it is likely that 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. In addition, Concentration Risk is minimised within asset groups. For the **equity portfolios**, this 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.

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 June 30, 2013.

Table 4
Weighted Average Duration
/Years/

Mandate	Portfolio	Benchmark
US Short Duration	**2.63**	**2.64**
US Core Domestic Fixed Income	**5.33**	**5.23**

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 June 2013, the currency exposure for this portfolio was 99 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			Financial YTD			Annualised Return Since Inception		
	Portfolio	Benchmark	Excess	Portfolio	Benchmark	Excess	Portfolio	Benchmark	Excess
	%	%	bps	%	%	bps	%	%	bps
FY 2010									
December	0.96	0.89	6.65	0.96	0.89	6.65	3.72	3.78	-6.16
March	1.61	1.68	-6.20	2.59	2.58	0.49	3.95	4.03	-7.76
June	-1.83	-1.89	6.05	0.71	0.64	6.69	3.07	3.12	-5.18
September	5.33	5.08	24.73	6.07	5.75	31.93	4.37	4.35	2.06
FY 2011									
December	2.29	2.21	8.15	2.29	2.21	8.15	4.70	4.65	4.13
March	1.62	1.54	7.24	3.94	3.79	15.68	4.81	4.76	5.72
June	1.88	1.81	6.68	5.89	5.67	22.91	4.98	4.91	7.00
September	-4.82	-4.28	-53.66	0.79	1.14	-34.89	3.57	3.63	-6.29
FY 2012									
December	2.74	3.03	-28.52	2.74	3.03	-28.52	3.97	4.08	-12.00
March	5.04	4.46	57.50	7.92	7.63	29.29	4.78	4.78	-0.08
June	-0.90	-0.60	-30.42	6.95	6.98	-3.72	4.37	4.43	-6.13
September	3.53	2.98	55.03	10.73	10.18	55.02	4.68	4.65	2.07
FY 2013									
December	1.49	1.45	4.11	1.49	1.45	4.11	4.88	4.83	4.76
March	3.29	2.90	39.19	4.82	4.38	44.01	5.23	5.12	11.20
June	-0.30	-0.69	39.05	4.51	3.66	84.64	4.97	4.80	17.26

Notes:

(1) Differences in totals are due to rounding.

(2) 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.

(3) 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).

(4) With effect from the quarter ended December 2012, the Annualised Returns Since Inception were computed using a geometric average and not the previously used arithmetic average. For comparative purposes, prior period annualised returns since inception shown above were computing using a geometric average.

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, 2012	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
December 31, 2012	4,780,065,524	42,243,928	861,557,777	-
March 31, 2013	4,933,344,741	70,726,991	1,015,212,703	-
June 30, 2013	4,914,375,234	56,685,027	996,411,094	-

Appendix III
Summary Characteristics of Composite Benchmarks
Fixed Income Benchmarks

Key Characteristics	Barclays US Aggregate Index	Merrill Lynch 1-5 Index
Total Holdings	8,394	137
Coupon (%)	3.47	1.85
Duration (Years)	5.23	2.64
Average Life (Years)	6.92	2.73
Yield to Maturity (%)	2.26	0.64
Option Adjusted Spread (bps)	51	0
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	2,733	854
Earnings Per Share (EPS Growth 3-5y fwd)	10.20	10.53
Price Earnings (P/E fwd)	14.1	12.70
Price / Book (P/B)	2.40	1.59
Weighted Average Market Capitalization* (Bn)	$77.5	$54.4

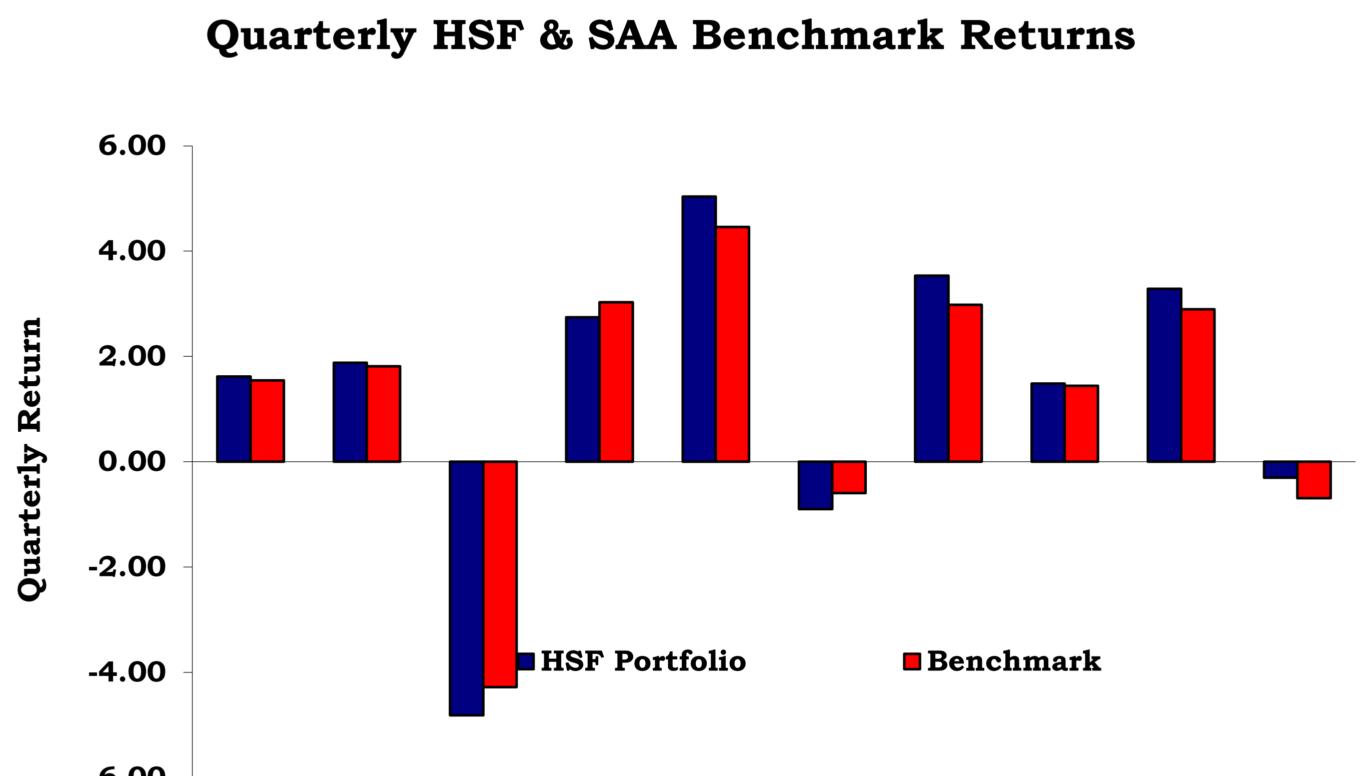
*Market capitalization is a measurement of the size of a company (share price x the number of outstanding shares). The weighted average market capitalization of a stock market index represents the average size of the firms comprising the index where each is weighted according to its market capitalization.

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

	June 2012	September 2012	December 2012	March 2013	June 2013
Total Fund Value	**4,379**	**4,712**	**4,780**	**4,933**	**4,914**
Total Value of Equity	**1,557**	**1,697**	**1,757**	**1,909**	**1,945**
US Core Domestic Equity	831	886	887	980	1,013
Non-US Core International Equity	726	811	869	929	931
Total Value of Fixed Income	**2,820**	**2,901**	**3,021**	**3,023**	**2,969**
US Short Duration Fixed Income	1,062	1,105	1,151	1,153	1,145
US Core Domestic Fixed Income	1,758	1,796	1,870	1,870	1,823
Total Value of Cash or Cash Equivalents	**2**	**114***	**2**	**1**	**1**

NB: Differences in totals are due to rounding.
*This mainly represented the cash contribution (US$111.9million) made by the Government on September 28, 2012.

Appendix V
HSF Portfolio Quarterly Returns
/per cent/



	FY2011 Q2	FY2011 Q3	FY2011 Q4	FY2012 Q1	FY2012 Q2	FY2012 Q3	FY2012 Q4	FY2013 Q1	FY2013 Q2	FY2013 Q3
HSF Portfolio	1.62	1.88	-4.82	2.74	5.04	-0.90	3.53	1.49	3.29	-0.30
Benchmark	1.54	1.81	-4.28	3.03	4.46	-0.60	2.98	1.44	2.90	-0.69