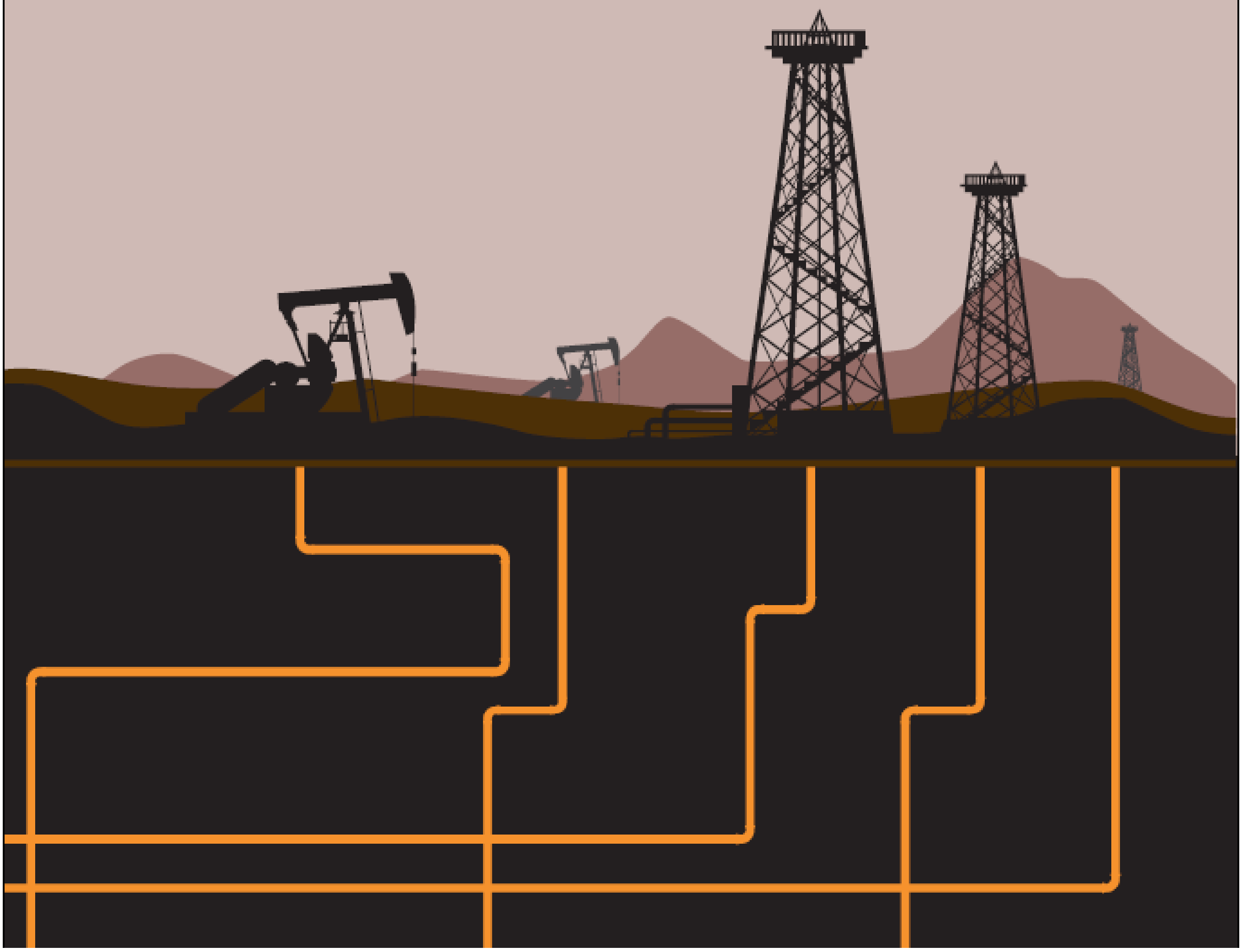
Trinidad and Tobago

Heritage & Stabilisation Fund

QUARTERLY INVESTMENT REPORT
APRIL - JUNE 2012



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EXECUTIVE SUMMARY

Prospects for the global economic recovery weakened during the second quarter of 2012 amid heightened political and financial uncertainty in Greece, increased banking system strains in Spain and the resurfacing of the sovereign debt stress in the Euro area periphery. Growth also slowed in several emerging market countries including Brazil, China and India. These developments adversely impacted the economic and financial environment resulting in a less optimistic outlook for the global economy.

In the **United States (US),** growth decelerated to an annualised rate of 1.5 per cent in the second quarter of 2012, compared with growth of 2 per cent in the previous quarter. Manufacturing activity contracted in June 2012 for the first time since July 2009 as the Purchasing Managers Index[1] (PMI) fell to 49.7 from 53.4 in March 2012. Meanwhile, gains in nonfarm payroll employment waned significantly to 75,000 jobs per month in the second quarter of 2012, well below the average of 226,000 jobs per month in the first quarter of 2012.

The economic picture in the **Euro zone** weakened further in the second quarter of 2012, as the manufacturing sector contracted while labour market conditions worsened. On July 05 2012, the Governing Council of the European Central Bank (ECB) cut its benchmark policy rate by 25 basis points in an effort to stimulate activity in the Euro area.

In the **United Kingdom (UK),** preliminary GDP estimates revealed that the economy contracted for a third consecutive quarter in the three months to June 2012. Real GDP declined by 0.7 per cent as output in the production, construction and services industries fell. In **Japan**, the economy gained momentum during the first quarter of 2012 and this

[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.

was expected to strengthen further in the second quarter with on-going public investment related primarily to post earthquake reconstruction efforts.

Over the second quarter of 2012, financial markets were characterized by increased risk aversion as investors became wary of a double dip recession in Europe, while the slowdown in growth in China and weak economic data from the US failed to boost investor confidence. As a result, most equity markets posted losses with the US S&P 500 index falling 3.3 per cent during the quarter, the Nikkei 225 Index declining 10.7 per cent and the MSCI EAFE index giving up 8.4 per cent.

Bond markets benefitted from the heightened uncertainty, which caused investors to increase their demand for US Treasury securities. Within the Barclays Capital US Aggregate Bond index, US Treasury securities was the best performing sector returning 2.8 per cent in the second quarter of 2012, compared with 2.1 per cent for the overall Bond index. In general, US Treasury yields declined over the quarter with the ten-year Government bond yield reaching 1.6 per cent at the end of June 2012, down from 2.2 per cent three months earlier.

For the quarter ended June 2012, the HSF investment portfolio generated a negative return of 0.9 per cent, compared with a negative return of 0.6 per cent for the Strategic Asset Allocation (SAA) benchmark. The relatively subdued mood in the market over the period depressed stock prices causing the equity portion of the Fund to return losses which dampened the gains generated by the fixed income segments. The equity portion of the Fund posted a negative weighted return of 2 per cent, while the fixed income segment added a weighted return of 1.1 per cent. At a more disaggregated level, all the mandates outperformed their respective benchmarks with the exception of the US Core Domestic Equity mandate which underperformed by 1.3 per cent.

Contribution to Quarterly Return,
For the period April 2012 – June 2012
/per cent/

	SAA Weights	Portfolio Weights as at 30-Jun- 2012	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	100.00	-0.90	-0.60
US Core Domestic Fixed Income	40.00	40.16	0.92	0.82
US Core Domestic Equity	17.50	18.99	-0.77	-0.44
Non US Core International Equity	17.50	16.59	-1.18	-1.12
US Short Duration Fixed Income	25.00	24.26	0.14	0.15

NB: Differences in totals are due to rounding.

As at the end of June 2012, the **net asset value of the HSF was US$4,378.9 million**, down slightly from US$4,397.3 million at the end of March 2012. In April 2012, the Government deposited approximately US$26.2 million to the Fund in respect of the first quarter of 2012. An additional deposit of US$69.4 million was made in July 2012 in respect of the second quarter of 2012. In the three months to June 2012, both the fixed income and equity segments of the Fund remained relatively close to their respective SAA weights.

SECTION 1 – INTERNATIONAL ECONOMIC ENVIRONMENT

United States

The International Monetary Fund (IMF) lowered its growth forecast for the United States (US) to 2 per cent in 2012 and 2.3 per cent in 2013 on concerns of the intensifying euro area debt crisis and the uncertainty of reaching agreements to avoid a "fiscal cliff" in the US. Preliminary GDP data indicated that the US economy expanded at an annualised rate of 1.5 per cent in the second quarter of 2012 compared with growth of 2 per cent in the previous quarter. Other economic indicators also suggest that the US economy slowed in the second quarter.

According to the Manufacturing Institute of Supply Management's Purchasing Managers Index[2] (PMI), activity in the manufacturing sector declined in June 2012 to 49.7 for the first time since July 2009, from 53.5 one month earlier and 53.4 in March 2012. Most of the decline was attributable to a falloff in new orders. Further, economic activity in the services sector decelerated during this period as the non-manufacturing ISM PMI weakened to 52.1 points. Data on industrial production was more positive and revealed that industrial output grew by 4.7 per cent in June 2012.

Meanwhile, nonfarm payroll employment slowed significantly in the second quarter of 2012, increasing by a monthly average of 75,000 jobs compared with a monthly average of 226,000 jobs in the first quarter of 2012. Slower job growth occurred in most of the major industries. As a result, the unemployment rate remained unchanged at 8.2 per cent at the end of June 2012.

[2] 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.

In the housing market, the S&P Case-Schiller indices which are the leading measures of US home prices, pointed towards some improvements as house prices rose by 2.2 per cent and 1.3 per cent in April and May 2012, respectively following declines in the first quarter of 2012. Other housing market data also signalled improvements as sales on new residential houses rose in May and new residential construction grew by 6.9 per cent in June 2012.

Headline inflation, as measured by the consumer price index, decelerated during the second quarter of 2012, falling to 1.7 per cent in the twelve months to June 2012 from 2.7 per cent three months earlier. However, the core inflation rate which excludes the volatile components of energy and food measured 2.2 per cent in June 2012 compared with 2.3 per cent in March 2012. The relatively higher core inflation rate can be attributed to the energy index which decreased for the third consecutive month in June 2012 as gasoline prices continued to decline.

Nevertheless, the Federal Open Market Committee at its June 20, 2012 meeting indicated that a highly accommodative monetary policy stance will be maintained and decided to keep the target range for the Federal Funds rate unchanged at 0.00 to 0.25 per cent until late 2014. The Committee also decided to maintain its "Operation Twist" program to the end of 2012, while indicating that they are prepared to take further action if needed to promote stronger economic recovery and sustained improvement in labour market conditions.

Euro zone

Following a contraction in real GDP of 0.3 per cent in the fourth quarter of 2011, growth in the Euro Zone was flat in the first quarter of 2012. The economic picture in the euro area is expected to weaken further in the second quarter of 2012 amid heightened concerns for recapitalization of the banking system and the ongoing sovereign debt crisis.

The euro zone manufacturing Purchasing Managers' Index fell to 45.1 in June 2012, the lowest level in three years, reflecting a deterioration in manufacturing activity as production and orders in the sector dropped. The effects of the euro zone crisis widened to Germany as the PMI for that country reached a 36 month low of 45. After declining by 1.4 per cent in April 2012, the retail sales index decreased by 1.7 per cent in May 2012

On the labour market front, conditions worsened as unemployment rose slightly to 11.1 per cent in May 2012 from 11 per cent in April and March 2012. The lowest unemployment rates were recorded in Austria (4.1 per cent), Netherlands (5.1 per cent), and Germany (5.6 per cent), while the highest were in Spain (24.6 per cent) and Greece (21.9 per cent). Meanwhile, euro area inflation measured year-on-year to June 2012 decelerated to 2.4 per cent from 2.7 per cent at the end of March 2012.

The European Central Bank (ECB), following it Governing Council meeting on 5 July 2012, decided to cut its benchmark policy rate by 25 basis points in an effort to support the weakening economy. The Governing Council also took measures in June 2012 to increase collateral availability for counterparties.

Financial stress re-emerged in Spain in the second quarter of 2012 as the Spanish government formally requested Euro area financial assistance of up to EUR 100 billion for the recapitalization of its banking sector. Following a diagnostic exercise, some EUR 19 billion of capital was injected into "Bankia", one of Spain's largest banks, which was on the brink of collapsing due to its significant exposure to Spain's real estate crash. In addition, Moody's credit rating agency downgraded 28 of the country's lenders (including Bankia), on account of an unprecedented double-dip recession and the government's limited resources to provide support.

United Kingdom

Following two consecutive quarters of negative growth, the UK economy entered a technical recession in the first quarter 2012. This trend continued into the second quarter as real GDP contracted by 0.7 per cent reflecting a decline in output in the production, construction and services industries.

Further, the UK manufacturing PMI fell to 48.6 at the end of June 2012 compared with a reading of 52.1 at the end of the previous quarter. Although this reading is higher than that observed in the previous month it still remains below 50 indicating that manufacturing sector contracted. According to the services PMI, growth in the services sector softened as the PMI reached an eight month low of 51.3 at the end of June compared to 55.3 in March 2012. The extra Jubilee Holiday and weak demand are accountable for this softening in activity. However, the index of domestic production pointed to an increase in manufacturing to May 2012.

Labour market conditions improved slightly, as the unemployment rate declined to 8.1 per cent in May 2012 from 8.2 per cent March 2012. Meanwhile, inflation slowed to 2.8 per cent in May 2012, down from 3 per cent in April. This is the lowest annual inflation rate since November 2009 when it reached 1.9 per cent.

In July 2012, the Bank of England announced that it would keep the official Bank rate at 0.5 per cent but would increase the size of its programme of asset purchases by GBP 50 billion in the next four months to GBP 375 billion in an effort stimulate the UK economy.

Japan

Economic activity in Japan is gaining momentum, driven chiefly by domestic demand. The Japanese economy realized growth of 1.2 per cent in the first quarter of 2012, which is anticipated to strengthen further in the second quarter as public investment related primarily to post earthquake reconstruction continues to increase and business fixed investment trend upwards.

Nonetheless, Japan's industrial production fell in April and May with the decline in the latter month more severe as output across transport equipment, precision machinery and chemical products were significantly reduced. Meanwhile, there was some improvement on the labour market front as the unemployment rate declined to 4.4 per cent in May 2012, down from 4.6 per cent in April 2012.

Japan's inflation rate measured 0.2 per cent at the end of June 2012. At the monetary policy meeting held on July 12, 2012, the Policy Board of the BOJ decided to keep its benchmark interest rate unchanged at the range of 0 to 0.1 per cent.

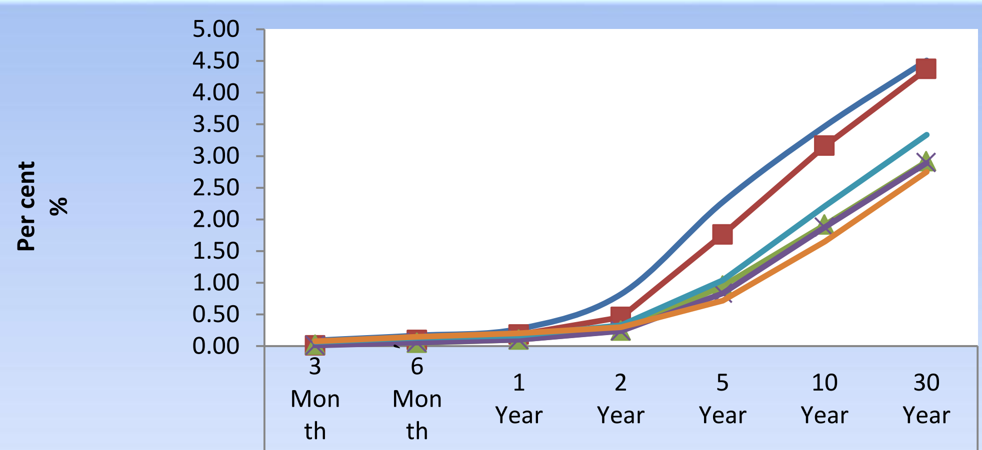
SECTION 2 – CAPITAL AND MONEY MARKET REVIEW

Financial market volatility increased during the second quarter of 2012 amidst waning momentum in the global economy and the resurgence of the fiscal and banking crisis in Europe. Investors also became increasingly concerned about the fiscal uncertainty in the US which further dampened their appetite for risk. The Chicago Board Options Exchange Volatility Index (VIX), which is a widely used measure of market risk and is often referred to as the "investor fear gauge", averaged 20 points for the second quarter of 2012, up from an average of 18.2 points for the previous quarter. Over the review period, the VIX peaked at 26.7 points, which is much lower than the levels experienced in the third quarter of 2011 when stock markets experienced double-digit declines. With trading volumes being relatively lower and investors becoming more cautious, the mood in the market had been more of a subdued one which was in stark contrast to that of the previous three months. For the second quarter of 2012, the Standard and Poor's (S&P) 500 index lost 3.3 per cent compared with a gain of 12 per cent in the first quarter, while the MSCI EAFE index which gauges the performance of non-US Developed equity markets lost 8.4 per cent compared with a return of 10 per cent in the prior quarter. In the fixed income market, US Treasury yields in the 2-year to 30-year segment of the yield curve declined while yields at the shorter end continued to trend upwards.

Fixed Income

After trending upwards during the previous quarter, US Treasury yields particularly in the 2-year to 30-year section of the curve, declined in the second quarter of 2012. These lower yields reflected in part heightened investor uncertainty about the prospects for the US economy where the pace of economic growth has slowed. As a result, investors increased their demand for US Treasury securities. Further downward pressure was placed on long-term interest rates when the Federal Open Market Committee (FOMC) on June 20 announced that it would continue its programme through the end of 2012 to extend the average maturity of the Federal Reserve's holdings of Treasury securities ('Operation Twist'). The Operation Twist involves the simultaneous sale of shorter dated Treasuries and the purchase of longer-dated issues. The 10-year benchmark US Treasury yield decreased 56 basis points to 1.6 per cent in the second quarter of 2012.

Figure 1
US Treasury Yield Curve
/per cent /

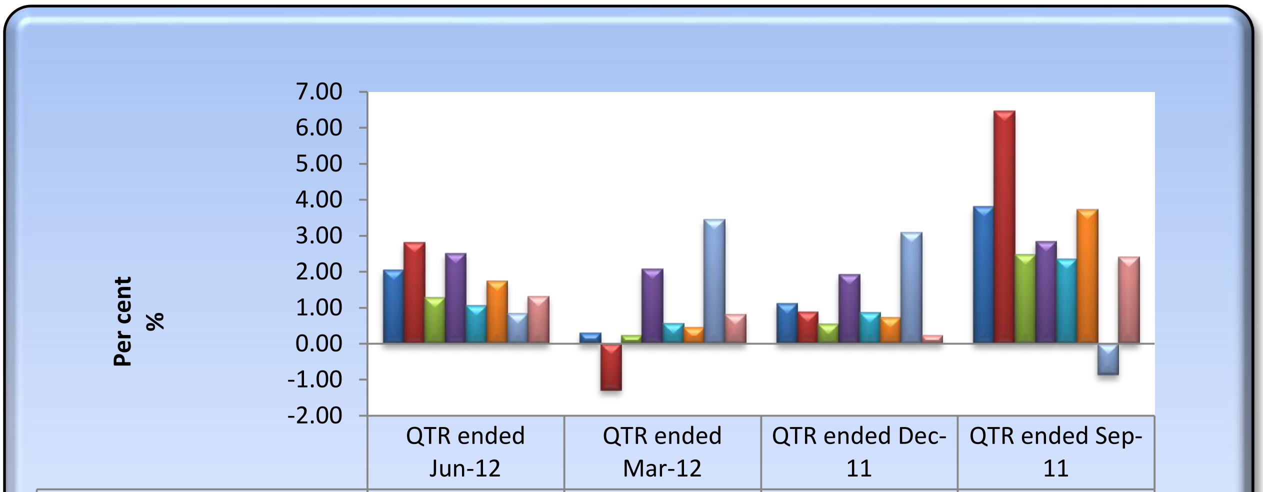


	3 Month	6 Month	1 Year	2 Year	5 Year	10 Year	30 Year
March 31, 2011	0.09	0.17	0.27	0.82	2.28	3.47	4.51
June 30, 2011	0.01	0.10	0.18	0.46	1.76	3.16	4.37
September 30, 2011	0.02	0.05	0.10	0.24	0.95	1.92	2.91
December 30, 2011	0.01	0.06	0.10	0.24	0.83	1.88	2.89
March 31, 2012	0.07	0.13	0.17	0.33	1.04	2.21	3.34
June 30, 2012	0.08	0.15	0.20	0.30	0.72	1.65	2.75

Source: Bloomberg.

The broader US fixed income market, as represented by the Barclays Capital US Aggregate Bond index, generated a total return of 2.1 per cent for the second quarter of 2012 compared with a return of 0.3 per cent in the previous quarter. Within the Barclays Index, the US Treasury sector was the best performer returning 2.8 per cent to rebound from the decline of 1.3 per cent in the quarter ending March 2012. Meanwhile, the Investment Grade Corporate sector continued to enjoy robust gains returning 2.5 per cent following a gain of 2.1 per cent in the quarter ending March 2012. Conversely, the worst performing sector was the Commercial Mortgage Backed Securities (CMBS) sector which returned 0.9 per cent. This sector posted the strongest performances in the prior two quarters gaining 3.5 per cent and 3.1 per cent in the March 2012 and December 2011 quarters, respectively.

Figure 2
Returns on Fixed Income Indices
/per cent/



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

Source: Barclays Capital.

In the Euro Zone, sovereign bond spreads for some countries widened in the second quarter of 2012. In particular, those for Spain, Italy and Greece rose as their bond yields appeared the most volatile over the period. In Greece, political turmoil and increasing disaffection with austerity measures threatened the future of its bailout programme. In April 2012, Standard and Poor's downgraded Spain's long-term debt rating by two notches to BBB+ while Italy's sovereign debt credit rating was downgraded by Moody's Investors

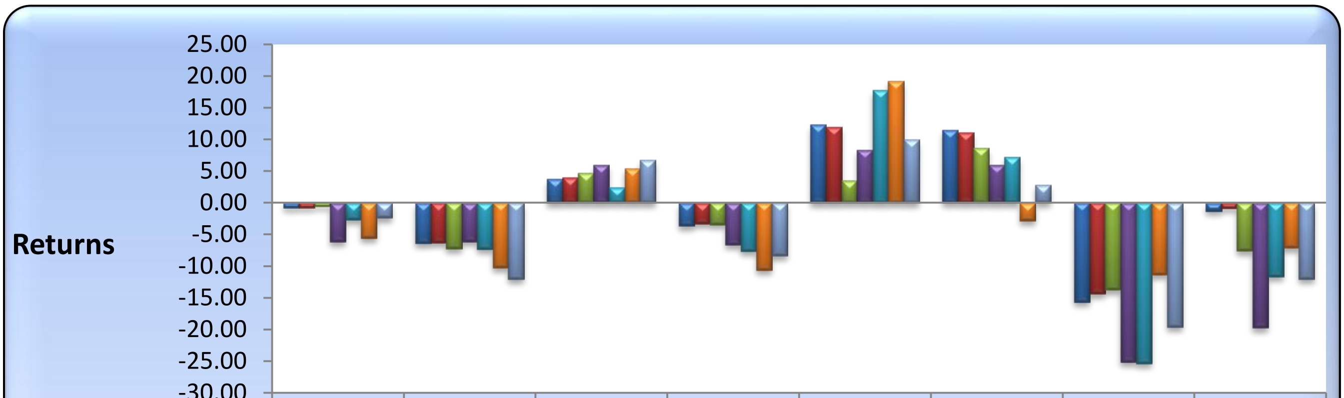
Service by two notches to Baa2 on July 13, 2012. The yield on the Spanish Government ten-year bond rose to 6.3 per cent at the end of June 2012 from 5.4 per cent at the end of March 2012. Whilst the yield on the Italian Government ten-year bond increased to 5.8 per cent from 5.1 per cent in March 2012 and the yield on Greek bonds reached 25.8 per cent, up from 21.1 per cent three months earlier. In contrast, the German bunds and Danish bonds which are perceived as safer investments saw their ten-year yields decline by 21 basis points and 39 basis points, respectively.

Equity Markets

After exhibiting strong performances during the first quarter of 2012, equity markets gave back some of the returns in the second quarter as investors became wary of a double dip recession in Europe, while the slowdown in growth in China and weak economic data from the US failed to boost investor confidence. Most of the losses occurred in May when investor uncertainty intensified as the possibility of Greece exiting the Euro zone resurfaced, political uncertainty in France and Greece heightened and a number of Spanish and Italian banks were downgraded. The market produced solid gains in June but these were insufficient to offset the sharp losses made over the prior two months.

Among the major equity markets, US stocks returned a smaller loss relative to those in other developed markets. The S&P 500 index fell 3.3 per cent during the second quarter of 2012 following a gain of 12 per cent in the previous quarter. In Japan, the Nikkei 225 Index declined 10.7 per cent in the quarter ending June 2012 compared with a gain of 19.3 per cent in the prior three months. Meanwhile, the MSCI EAFE index fell 8.4 per cent in the second quarter after increasing 10 per cent in the first quarter of 2012.

Figure 3
Returns on Equity Indices
/Per cent/



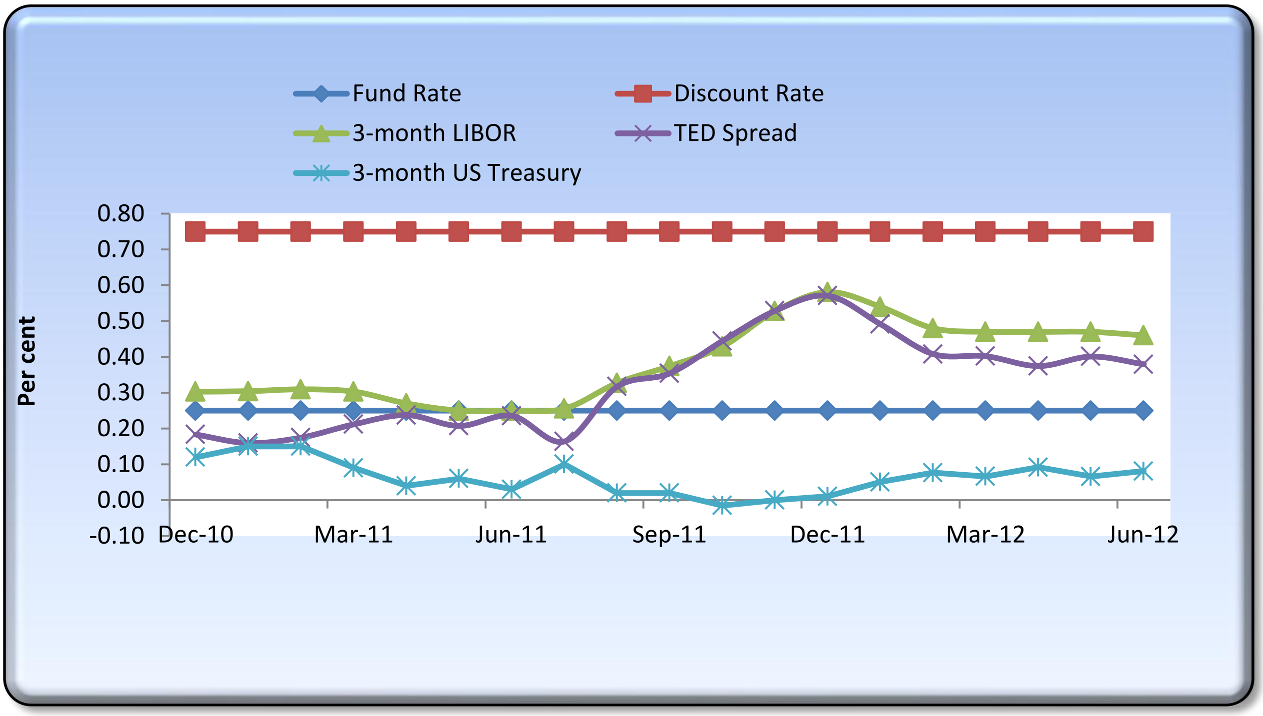
	Apr-12	May-12	Jun-12	QTR ended Jun-12	QTR ended Mar-12	QTR ended Dec-11	QTR ended Sep-11	FY 10/11
Russell 3000	-0.77	-6.41	3.75	-3.65	12.32	11.50	-15.70	-1.30
S&P 500	-0.75	-6.27	3.96	-3.29	12.00	11.15	-14.33	-0.86
FTSE 100 - UK	-0.53	-7.27	4.70	-3.42	3.52	8.65	-13.74	-7.57
CAC 40 - France	-6.16	-6.09	5.95	-6.63	8.35	5.96	-25.12	-19.74
DAX 30 - Germany	-2.67	-7.35	2.42	-7.64	17.78	7.20	-25.41	-11.67
Nikkei 225 - Japan	-5.58	-10.27	5.43	-10.68	19.26	-2.82	-11.37	-7.14
MSCI EAFE	-2.40	-12.09	6.79	-8.37	9.98	2.86	-19.60	-12.02

Source: Bloomberg.

Money Market

Money market yields remained relatively flat during the quarter. The accommodative monetary policy stance by the major central banks helped to keep these short-term rates at the current low levels. The 3-month London Inter-Bank Rate (LIBOR) declined to 46 basis points at the end of June 2012 compared with 47 basis points three months earlier. While the 3-month US Treasury bill rose to 8 basis points at the end of June 2012 from 6 basis points in March 2012. The TED spread, which represents the difference between the 3-month Treasury bill rate and 3-month LIBOR, tightened by 2 basis points to 38 basis points in June 2012 compared with 40 basis points three months earlier.

Figure 4
US Money Market Rates
/per cent/

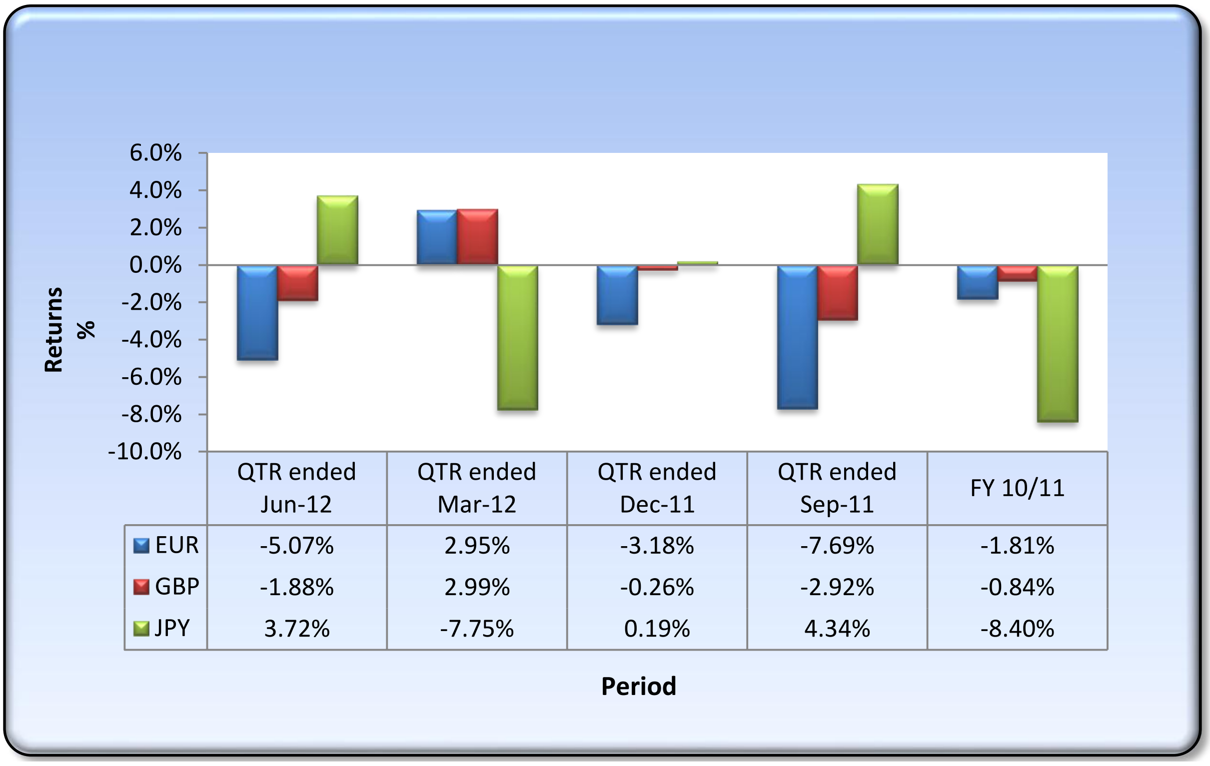


Source: Bloomberg.

Currency Markets

The risk aversion in Europe contributed to high levels of volatility in currency markets over the second quarter of 2012. The Euro and GBP depreciated relative to the US dollar by 5.1 per cent and 1.9 per cent, respectively. These movements represented a reversal in trend as both currencies appreciated by 3 per cent in the previous quarter. The flight to safety trades also benefitted the Yen as there was an increased demand for the currency. The Yen appreciated 3.7 per cent vis-à-vis the US dollar over the quarter closing June at JPY 79.79. The US dollar index which indicates the general international value of the US dollar against major world currencies strengthened 3.3 per cent to 81.63 during the three months ending June 2012.

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



Source: Bloomberg.

SECTION 3 – PORTFOLIO PERFORMANCE

Strategic Asset Allocation

Over the period April to June 2012, deviations of the Fund's asset classes from their target Strategic Asset Allocation (SAA) were all within the (+/- 5 per cent) range in which they are allowed to vary. At the end of June 2012, the US Core Domestic Equity mandate had an overweight allocation by 1.5 per cent, causing the HSF investment portfolio to have an overweight exposure to equities amounting to 35.6 per cent versus 35 per cent in the SAA. The corresponding underweight was borne by the fixed income portion of the portfolio which accounted for the remaining 64.4 per cent. (Table 1 below refers). 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%*

During the second quarter of 2012, the Government made a deposit of US$26.2 million to the Fund in respect of the first quarter of 2012. On May 7 2012, US$25 million was transferred to the external asset managers in proportions such that the mandates would be closer to their approved SAA weight. Also in July 2012, a deposit of US$69.4 million was made to the Fund in respect of the second quarter of 2012.

At the end of June 2012, the total net asset value of the Fund was US$4,378.9 million, down from US$4,397.3 million at the end of March 2012. Of this total, the investment portfolio was valued US$4,376.8 million while the remaining US$2.1 million was held in cash to meet the day-to-day expenses that are incurred in management of the Fund. The

Fund's portfolio weighting relative to its strategic asset allocation is shown below in Table 1 and Figure 6.

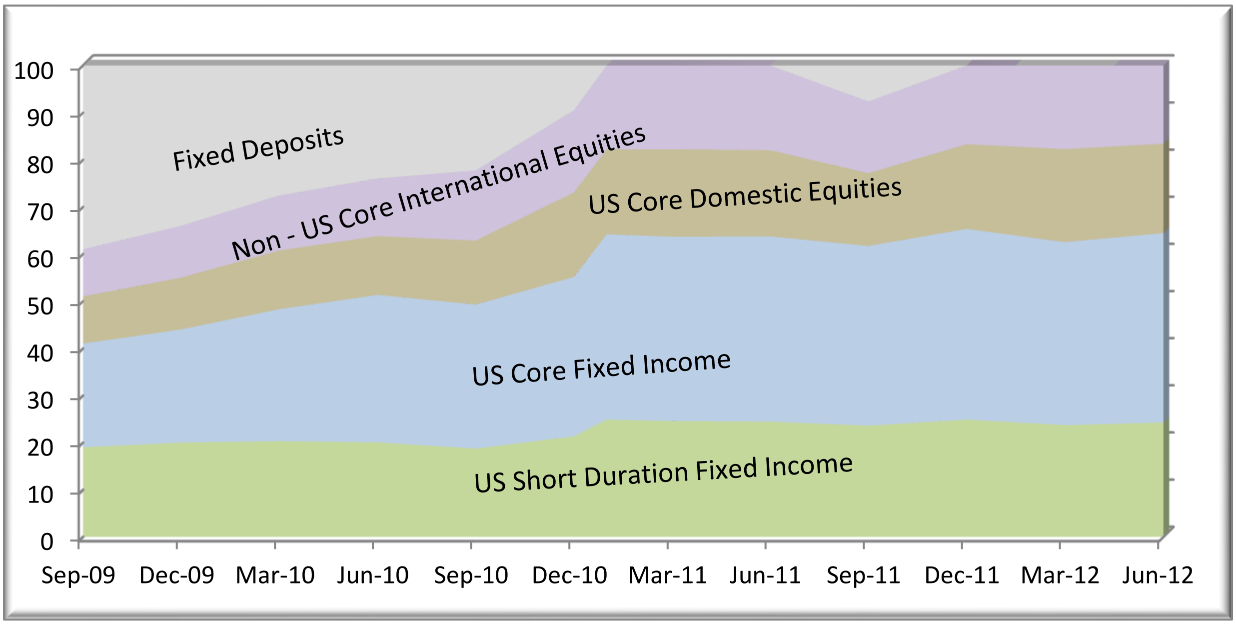
Table 1

Portfolio Composition relative to the Approved SAA
/per cent/

Portfolio Weights	Asset Class		Sep-11	Dec-11	Mar-12	Jun-12
		Target Weight SAA	*Actual % of Fund*	*Actual % of Fund*	*Actual % of Fund*	*Actual % of Fund*
	US Deposits	0.00	7.63*	0.00	0.00	0.00
	US Short Duration Fixed Income	25.00	23.59	24.86	23.70	24.26
	US Core Domestic Fixed Income	40.00	38.11	40.46	38.83	40.16
	US Core Domestic Equity	17.50	15.45	17.98	19.72	18.99
	Non-US Core International Equity	17.50	15.22	16.70	17.75	16.59

*These deposits represent the cash contribution made by the Government on September 30, 2011.

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



Performance of the Investment Portfolio

During the second quarter of 2012, the HSF investment portfolio generated a negative return of 0.9 per cent compared with a negative return of 0.6 per cent for the SAA benchmark[3]. The relatively subdued mood in the market over the period depressed stock prices causing the equity portion of the Fund to post losses which more than outweighed the gains generated by the fixed income mandates. The equity mandates detracted 2 per cent from overall performance while the fixed income portion of the Fund added 1.1 per cent. At a more disaggregated level, all the mandates outperformed their respective benchmarks, with the exception of the US Core Domestic Equity mandate.

The **US Short Duration Fixed Income** portfolio returned 0.6 per cent, marginally outperforming its benchmark, the Bank of America Merrill Lynch US Treasury 1-5 Year index by 1 basis point. This slightly better performance reflected positive contributions from the portfolio's holding of agency mortgages and foreign government guaranteed bonds that outperformed short duration US Treasuries. Partially offsetting these gains was a flattening of the US yield curve in response to increased volatility in Europe. For the financial year to June 2012, this mandate gained 1 per cent compared with 0.8 per cent for the benchmark. The mandate's net asset value as at June 30 2012 was **US$1,061.7 million** compared with **US$1,041.7 million** at the end of March 2012. This increase in value partly reflected the transfer of US$14 million to this mandate on May 7 2011.

The other fixed income mandate, the **US Core Fixed Income**, returned 2.4 per cent compared with 2.1 per cent for the benchmark, the Barclays Capital US Aggregate Bond

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[3] 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%).

index. The outperformance of this mandate can be mainly attributed to its exposure to corporate bonds which generated higher gains than similar bonds in the benchmark. In particular, security selection within the industrial sector contributed the most to excess returns. Complementing the positive performance was the portfolio's exposure to asset-backed securities and agency mortgage-backed securities, which outperformed most fixed income spread sectors. For the financial year to June 2012, this mandate gained 4.4 per cent compared with 3.5 per cent for the benchmark. The net asset value of this mandate at June 30 2012 was **US$1,757.6 million**, compared with US$1,706.9 million at the end of March 2012. This increase in value partly reflected the transfer of US$11 million to this mandate on May 7 2011.

Various investor sentiment indicators were depressed during the second quarter of 2012 causing an increase in flight-to-quality trades. This contributed to the relatively poor performance of most equity markets. The **US Core Domestic Equity** mandate lost 4 per cent for the quarter, compared with a loss of 2.7 per cent for the Russell 3000 ex Energy benchmark. This underperformance was due to managers' unfavourable stock selection decisions where those stocks chosen for the portfolio generated greater losses than the stocks in the benchmark. Some of the individual stocks that detracted the most from performance were in the producer durables, consumer staples and financial services sectors. In the case of the financial services sector, despite the portfolio's underweight exposure relative to the benchmark, the specific companies held in the portfolio experienced declines in their share prices causing these positions to lose relatively more than those in the benchmark. During the second quarter of 2012, financial companies in the Russell 3000 Index lost 5.1 per cent but remained one of the top performing sectors with a return of 25.1 per cent for the first nine months of the financial year. In addition, the portfolio's performance was negatively impacted by its overweight allocations to stocks which had low price-to-earnings (P/E) ratios in comparison to other stocks in the same industry. These attractively valued stocks underperformed the Russell 3000 ex Energy benchmark over the quarter. For the financial year to June 2012, this mandate returned 23.1 per cent compared with 23.5 per cent for the benchmark. The net asset value of this mandate as at June 30 2012 was **US$831.3 million**, compared with US$867 million at the end of March 2012.

Increased anxiety in Europe led to the poor performance of the region's equity markets. As a result, the **Non-US International Equity** mandate which has exposure to the Australian, New Zealand, European and Far East Asian stock markets lost 6.8 per cent compared with a loss of 6.9 per cent for its benchmark, the MSCI EAFE ex Energy index. The smaller negative return by the portfolio was attributed to country allocation, stock selection and currency hedging decisions. The greatest contributions to excess returns, however, came from country allocation choices where underweight positions in developed Europe benefitted the portfolio since these markets were down on average by 12 per cent. The corresponding overweight to Asia ex-Japan markets was also beneficial for the portfolio given the better performance of these markets relative to other non-US developed ones. For the financial year to June 2012, this mandate returned 14.2 per cent compared with 14.1 per cent for the benchmark. The net asset value of this mandate as at June 30, 2012 was **US$726.2 million**, compared with US$780.3 million at the end of March 2012.

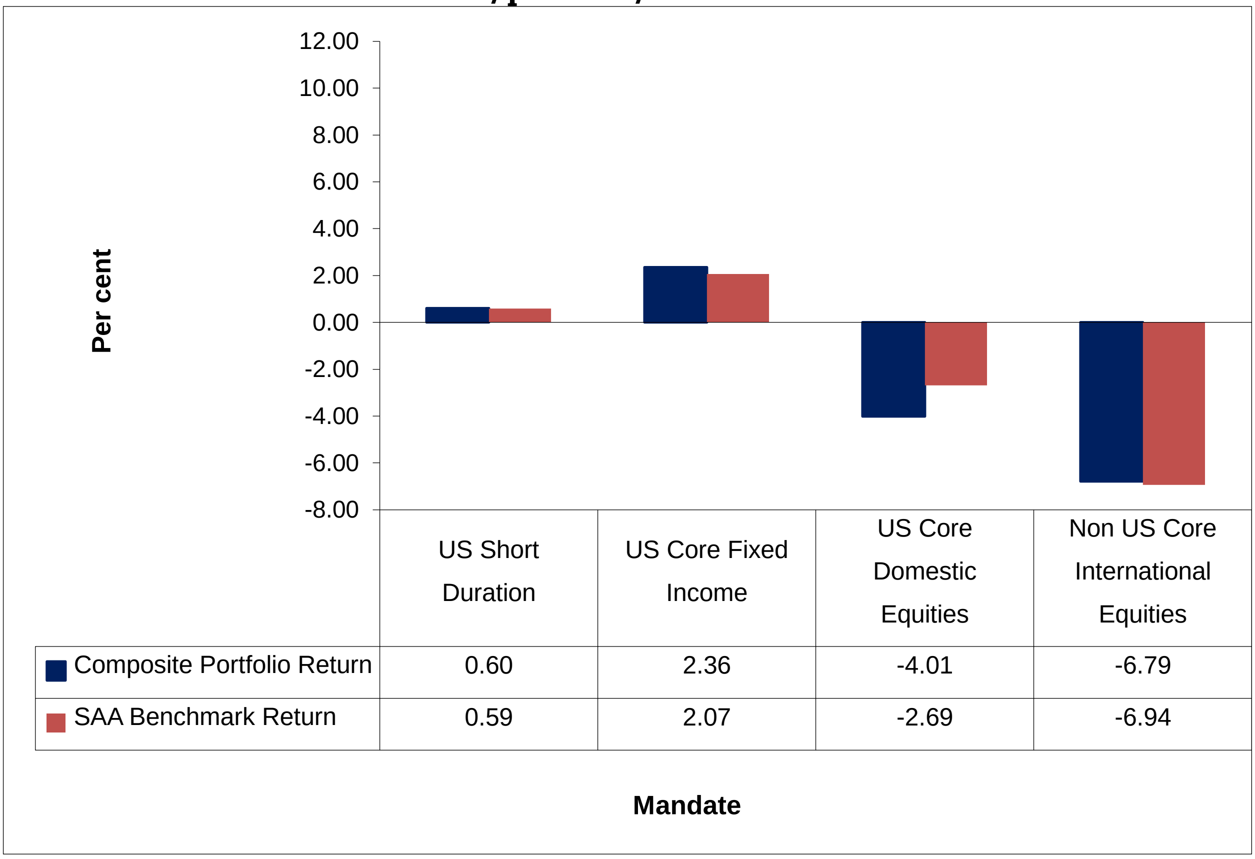
For the remainder of 2012, global fixed income and equity markets are expected to remain volatile as uncertainty about Europe's unresolved sovereign debt and banking sector challenges are likely to add to market tension. In addition, investors will focus on the upcoming US elections, and how issues surrounding the "fiscal cliff" will be addressed. Accordingly, investment managers can be expected to take tactical decisions in an effort to outperform their respective benchmarks.

Table 2
Contribution to Quarterly Return,
For the period April 2012 – June 2012
/per cent/

	Portfolio Weights as at 30-Jun- 2012	Weighted Return HSF	Weighted Return Benchmark
Composite Portfolio	100.00	-0.90	-0.60
US Core Domestic Fixed Income	40.16	0.92	0.82
US Core Domestic Equity	18.99	-0.77	-0.44
Non US Core International Equity	16.59	-1.18	-1.12
US Short Duration Fixed Income	24.26	0.14	0.15

NB: Differences in totals are due to rounding.

Figure 7
Absolute Returns by Asset Class
For the period April 2012 – June 2012
/per cent/



SECTION 4 –COMPLIANCE AND PORTFOLIO RISKS

Compliance

During the quarter ended June 30 2012, 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 2012.

Table 3
Average Credit Rating

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

For the **equity portfolios**, Credit Risk is managed by imposing a maximum percentage holding of 3.00 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 June 30, 2012.

Table 4
Weighted Average Duration
/Years/

Mandate	Portfolio	Benchmark
US Short Duration	**2.71**	**2.66**
US Core Domestic Fixed Income	**4.78**	**4.68**

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 2012, the currency exposure for this portfolio was 94.7 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 2009									
December	0.76	0.99	-22.49	0.76	0.99	-22.49	4.19	4.24	-5.25
March	0.08	0.07	0.62	0.84	1.06	-21.88	3.72	3.76	-4.30
June	0.02	0.03	-0.69	0.87	1.09	-22.60	3.33	3.37	-4.15
September	1.92	2.06	-14.62	**2.80**	**3.18**	**-37.81**	**3.81**	**3.91**	**-10.01**
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	4.88	-7.37

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

Appendix III
Summary Characteristics of Composite Benchmarks

Fixed Income Benchmarks

Key Characteristics	Barclays US Aggregate Index	Merrill Lynch 1-5 Index
Total Holdings	7,873	123
Coupon (%)	3.82	2.07
Duration (Years)	4.68	2.66
Average Life (Years)	6.62	2.76
Yield to Maturity (%)	1.86	0.44
Option Adjusted Spread (bps)	71	0
Average Rating (S&P)	AA	AA+
Minimum Rating (S&P)	BBB-	AA+

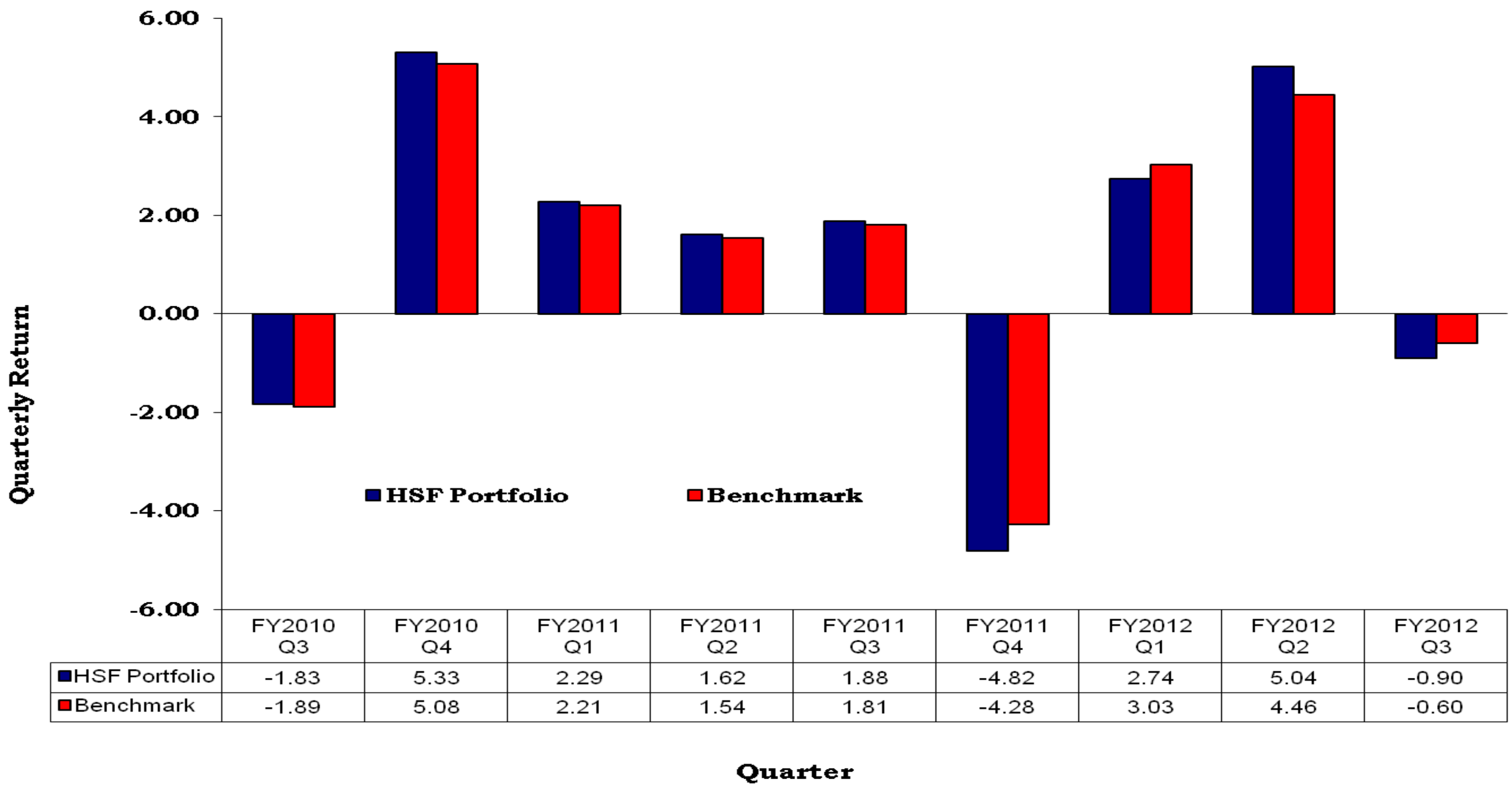
Equity Benchmarks

Key Characteristics	Russell 3000 (ex energy)	MSCI EAFE (ex energy)
Total Holdings	2,796	870
Earnings Per Share (EPS Growth 3-5y fwd) (%)	11.90	10.25
Price Earnings (P/E fwd)	13.1	11.24
Price / Book (P/B)	2.20	1.27
Market Capitalization (Bn)	$81.9	$44.5

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

	September 2011	December 2011	March 2012	June 2012
Total Fund Value	**4,084**	**4,191**	**4,397**	**4,379**
Total Value of Equity	**1,251**	**1,453**	**1,647**	**1,557**
US Core Domestic Equity	630	753	867	831
Non-US Core International Equity	621	700	780	726
Total Value of Fixed Income	**2,519**	**2,736**	**2,749**	**2,820**
US Short Duration Fixed Income	963	1,041	1,042	1,062
US Core Domestic Fixed Income	1,556	1,695	1,707	1,758
Total Value of Cash or Cash Equivalents	**314**	**2**	**1**	**2**

Appendix V
HSF Portfolio Quarterly Returns
/per cent/



	FY2010 Q3	FY2010 Q4	FY2011 Q1	FY2011 Q2	FY2011 Q3	FY2011 Q4	FY2012 Q1	FY2012 Q2	FY2012 Q3
HSF Portfolio	-1.83	5.33	2.29	1.62	1.88	-4.82	2.74	5.04	-0.90
Benchmark	-1.89	5.08	2.21	1.54	1.81	-4.28	3.03	4.46	-0.60