

Petroleum Fund of Timor-Leste

Quarterly Report

31 March 2021

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INTRODUCTION

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

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

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

EXECUTIVE SUMMARY

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

This report covers the period from 01 January to 31 March 2021.

Key statistics for the quarter include:

- The capital of the Fund at the end of the Current quarter was \$18.98 billion while the previous quarter was \$18.99 billion.
- Gross cash inflows to the fund from royalties and taxes were \$54.18 million.
- Outflow for the quarter were \$202.03 million, being transfers to the state budget of \$200 million while \$2.03 million was for management costs.
- The profit for the quarter was \$133.96 million, representing a gross of fees return of 0.77%. The return on financial market investments was 0.76% compared with the benchmark return of 0.46%.

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

Table 1

%	QTR	FYTD	1 Year	3 Years	5 years	Since Inc
Total Fund	0.77	0.77	17.03	7.31	6.72	4.82
International Fixed Interest	-1.86	-1.86	-0.83	3.10	1.90	2.67
International Equities	5.53	5.53	53.57	12.58	13.29	10.85
Private debt instrument for Petroleum Operations	1.10	1.10	4.50	n.a	n.a	4.50

Table 2

%	QTR	FYTD	1 Year	3 Years	5 years	Since Inc
Total Financial Market Investments	0.76	0.76	n.a	n.a	n.a	n.a
Benchmark	0.46	0.46	n.a	n.a	n.a	n.a
Excess	0.31	0.31	n.a	n.a	n.a	n.a
International Fixed Interest	-1.86	-1.86	-0.83	3.10	1.90	2.67
Benchmark	-1.94	-1.94	-0.85	3.21	1.91	2.67
Excess	0.08	0.08	0.02	-0.10	-0.01	-0.01
International Equities	5.53	5.53	53.57	12.58	13.29	10.85
Benchmark	4.92	4.92	54.03	12.81	13.36	10.51
Excess	0.61	0.61	-0.47	-0.24	-0.07	0.35

1. INVESTMENT MANDATE

A revised Management Agreement between Ministry of Finance and the Central Bank was signed on 25 June 2009. The Annexes of the Management Agreement has subsequently amended to reflect the actual investments. A revised Annex 1 was signed on 25 October 2020 where the Private Debt Instrument is separated from the financial market investments portfolio. The benchmarks as of March 2021 were as follows:

Table 3

	Jan-21	Feb-21	Mar-21
3 Month US Treasury Bills/Cash	5%	5%	5%
BOA Merrill Lynch 3-5 Years Treasury Bond Index	40%	40%	40%
BOA Merrill Lynch 5-10 Years Treasury Notes and Bond Index	10%	10%	10%
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped, Measured on a hedged basis	10%	10%	10%
Total Fixed Income	65%	65%	65%
Total equity (MSCI World Index Net Dividends Reinvested)	35%	35%	35%
Total Financial market Investments	100%	100%	100%

2. MARKET TRENDS DURING THE QUARTER

Global Macroeconomic Trend

The global economic outlook has improved in recent months supported by the world's effort to ramp up the Covid-19 vaccine manufacture and accelerate distributions. However, the trajectory of the recovery is varied among the regions and countries and depends on how fast their populations are inoculated against Covid-19. The first quarter of 2021 has seen vaccine rollouts do better than anticipated. The recent acceleration in vaccination rates and lower hospitalizations has instilled a sense of confidence amongst consumers and businesses regarding a quick return to normal. Moreover, fiscal stimulus and the easing monetary policy continue to support the economic recovery.

The U.S economy continued to rebound from the pandemic-induced crisis as the government ramps up the coronavirus vaccine distribution. The economy added over 1 million new jobs in the first three months of the year. The unemployment rate fell from 6.3% in January to 6.0% by the end of the quarter. The number of new jobs is expected to increase as the Covid-19 restrictions are scaled down due to rapid COVID-19 vaccine distributions in the country. On the fiscal front, the new administration presented another bill called "*The American Rescue Plan Act*", which totaled \$1.9 trillion and was subsequently approved by the U.S law makers. The U.S Federal Reserve stated during its meeting in March 2021 that the rise in inflation expectations is seen as a temporary phenomenon, and the Fed is committed to leaving the interest rate as it is now at least until 2023. The Fed's interest rate is at the range of 0.00 – 0.025%.

The positive news from the U.S also pushed the U.S dollar to appreciate against most of its peer developed countries' currencies during the first quarter. The value of the USD recovered from recent declines and analysts have attributed the upward movement to a few factors such as the positive economic outlook in the U.S and the disappointing vaccine rollout elsewhere.

The data showed the overall business activities in the Eurozone expanded for the first time in four months, with the manufacturing activities reaching an all-time high particularly in Germany and France. On the monetary front, the European Central Bank signaled an increase in pace of the pandemic emergency purchasing program (PEPP). The pace of vaccine distribution varied in the region as the U.K jumpstarted its program, while the European Union countries faced many logistical challenges which delayed the vaccine distribution to its member countries.

Global Equity Market Trends

The emergence of new strains of the Covid-19 in January rattled the market as many countries reintroduced restriction measures to curb the propagation of strains that are believed to be more contagious than the original one. As the quarter progressed, the global equity market returned to a positive path aided by the fast-paced Covid-19 vaccines distribution in some developed markets and the massive fiscal stimulus from the United States. Overall, Global equities advanced in Q1 and lowly-valued parts of the market fared well, as did smaller companies.

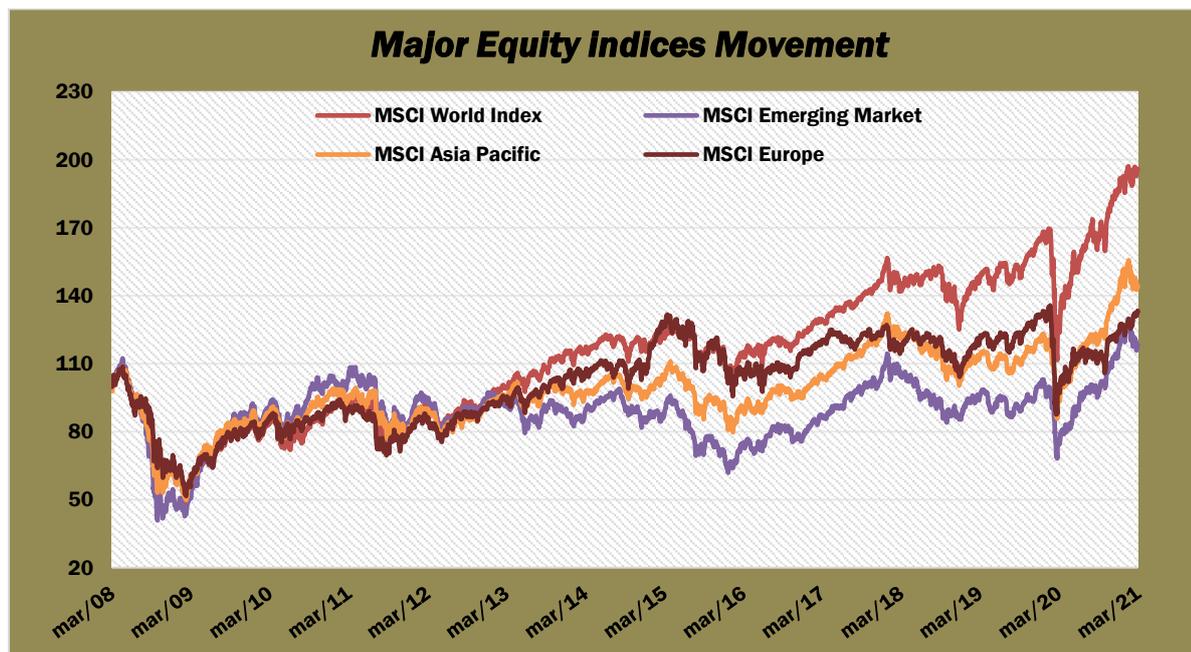
The improvement in vaccines distribution and new fiscal stimulus approved by the U.S lawmakers supported US equities performance during the quarter. As more people are inoculated, the number of infections declined which led to a decline in the number of people admitted to the hospitals and the death rate. By the end of the quarter, at least 37% of the U.S population has received at least one dose of the Covid-19 vaccine. The U.S President Joe Biden stated that the U.S is on track to achieve herd immunity by mid-year. This will allow the economic activities to gradually return to normal. The U.S equity market performance was led by the sectors that trailed during the COVID crisis. The U.S lawmakers have approved a fiscal stimulus worth around 9% of the U.S gross domestic product. The U.S Federal Reserve subsequently updated its economic growth outlook to 6.5% this year. This is an upgrade from the 4.2% projected in December 2020.

A similar market trend can be observed in the United Kingdom, as many people started to receive their Covid-19 vaccine shot, the government gradually rolled back the restrictions. As a result, the service sector related

activities have started to pick up according to the surveys. Equity markets across European Union countries performed well despite lagging on the vaccine rollout front. Consequently, Covid-19 infections have increased in many parts in the continent which triggered authorities to reintroduce the restriction measures.

Equity markets across the Asia Pacific region ended the quarter with gains led by the Japan and South Korea, boosted by the expectation of a strong rebound in global demand. On the vaccination front, the region has lagged other countries such as U.K and the U.S but due to the stricter control applied in these countries, the infections number is mostly under control.

Graph 01 Major Equity Indices Movement



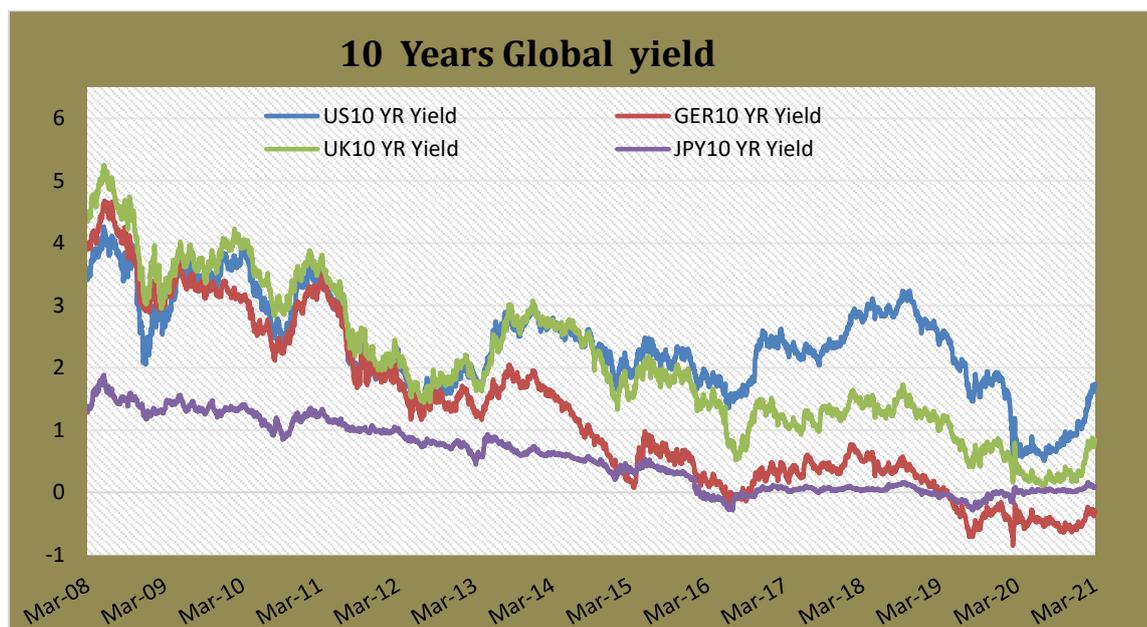
Global Treasury Bonds include U.S Treasuries

The yield of long-term global treasury bonds rose significantly for the quarter reflecting the prospect of positive economic growth and higher inflation expectation.

The U.S Treasury's yield curve has steepened as the yield of U.S short-term securities were muted while the long-term securities rose significantly during the quarter. The rise in yield in the long-end of the curve reflects the increase in expected growth and inflation. Higher inflation expectation is propelled by the Fed's new monetary policy framework that adopts an average inflation target along with the accelerating vaccine rollout, higher commodity prices and more fiscal stimulus.

The yield of 10-year treasuries bonds in key economic countries in the European Union also increased during the quarter but to a lesser magnitude seen in the U.S. A relatively smooth resolution to Brexit in the end of the year has narrowed the sovereign spread across the EU countries. However, the yields of those sovereign bonds have fluctuated due to the setback in the region's vaccine distribution and the political risk from Italy.

Graph 02. 10 Years Global Yield



3. MANAGEMENT DURING THE QUARTER

Objectives

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

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

Table 4

Mandate	Management Style	Authorised Managers	Tracking Error	Outperformance Target	Commencement date
3 Month USD Treasury Bills/Cash	Passive	BCTL	n/a	Nil	14-Aug-18
BOA Merrill Lynch 3-5 Years US Treasury Bond Index	Passive	BCTL	0.25%	Nil	19-Jan-12
BOA Merrill Lynch 5-10 Years US Treasury Bond Index	Passive	BCTL	0.50%	Nil	29-May-20
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped Measured on a hedged basis	Enhanced Passive	Bank for International Settlements	0.50%	0.15%	30-Apr-20
MSCI World Index ex Australia Net Dividends Reinvested	Equity Factor	Schroders Equity Factor	3.00%	Nil	2-Aug-19
	Equity Factor	SSgA Equity Factor	3.00%	Nil	2-Aug-19
MSCI World Index ex Australia Net Dividends Reinvested	Passive	SSgA International Equity	0.35%	Nil	18-Jan-12
	Passive	BlackRock International Equity	0.35%	Nil	21-Feb-13
MSCI Australia	Passive	BCTL	0.50%	Nil	4-Jul-16
Private debt instrument for Petroleum Operations	Passive	BCTL	n/a	Nil	10-Apr-19

Operational Implementation

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

Table 5

Mandate	Managers	Target Benchmark	Tolerance	Actual	Lower Boundary	Upper Boundary
3 Month US Treasury Bills/Cash	BCTL	5.00%	± 2.5%	5.79%	2.50%	7.50%
BOA Merrill Lynch 3-5 Years Treasury Bond Index	BCTL	40.00%		38.12%		
BOA Merrill Lynch 5-10 Years Treasury Notes and Bond Index	BCTL	10.00%		9.18%		
Barclays Global Treasury Developed Market ex US, 30% Eurozone and 10% Country Capped measured on a hedged basis	Bank for International Settlements	10.00%		9.64%		
Total Fixed Income		65.00%		62.73%		
MSCI Index ex Australia Net Dividends Reinvested	Schroders Investment Management	8.75%		9.46%		
	SSgA Equity Factor					
MSCI Index ex Australia Net Dividends Reinvested	SSgA International Equity	25.38%		26.47%		
	BlacRock					
MSCI Australia Index	BCTL	0.88%		1.34%		
Total Equities		35.00%	± 5%	37.27%	30.00%	40.00%
Total Financial Market Investments		100.00%		100.00%		
Total Private debt Instrument for Petroleum Operations	BCTL			3.73%		

4. PORTFOLIO PERFORMANCE

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

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

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

GLOBAL PORTFOLIO

In the course of the quarter the Petroleum Fund balance was \$18.98 billion as follows:

Table 6

Capital Account	\$'000
Opening book value (01 January 2021)	18,990,614
Receipts during the period	54,177
Transfer to General State Budget	-200,000
Investment Return	133,965
Closing book value (31 March 2021)	18,978,757

The Fund was invested as follows:

Table 7

Assets	\$'000
Cash and Cash Equivalents	1,298,467
Other Receivables	13,077
Financial assets held at fair value through profit or loss	16,965,389
Financial assets held at amortised cost	708,663
Less:	
Payable for Securities Purchased	-5,806
Accounts Payable	-1,033
Total	18,978,757

The income for the quarter was as follows:

Table 8

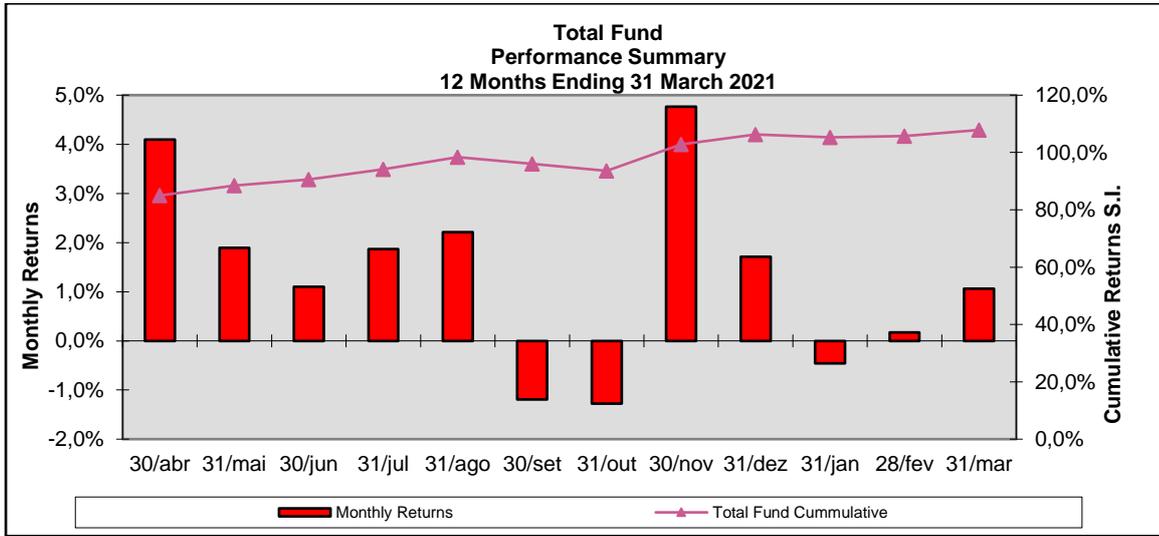
Income	\$'000
Interest income	40,463
Dividend income	34,645
Unit Trust distributions	982
Other Investment income	22
Net gains/(losses) on Financial Assets at fair value	75,306
Net foreign exchange gains/(losses)	-665
Less:	
External manager, custody fees	-613
Central Bank management expenses	-1,226
IAB Expenses	-36
Other expenses	-153
Withholding taxes	-14,760
Total Investment Income	133,965

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

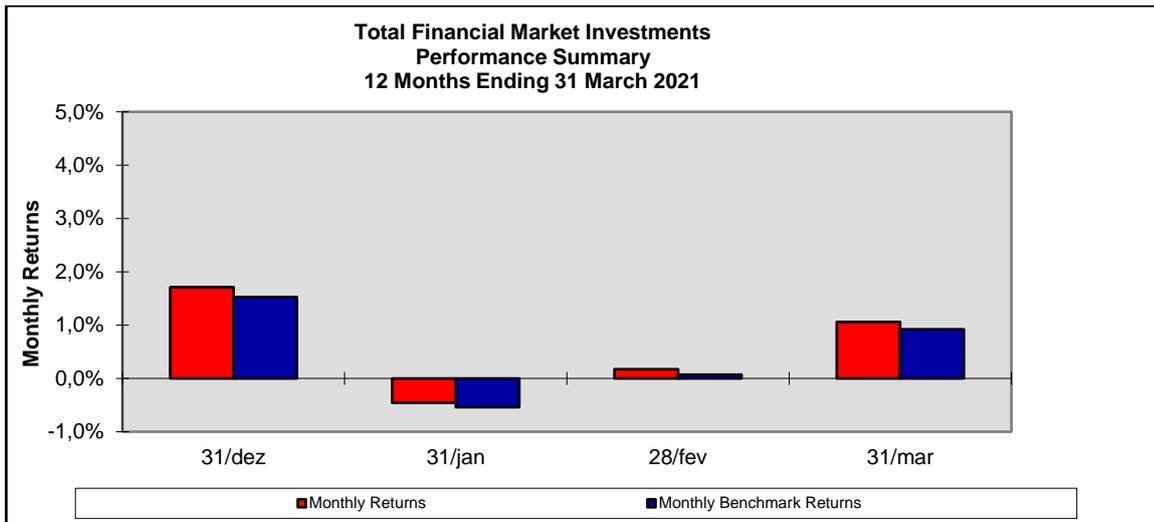
- Unit trust distribution is the income received from listed property investment entities.
- Other expenses relate to derivative trading costs which are deducted directly from the Fund.

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

Graph 03 Total Fund Performance



Graph 04 Total Financial market Investments Performance



FIXED INTEREST

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

Table 9

%	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
International Fixed Interest	-1.86	-1.86	-0.83	3.10	1.90	2.67
Benchmark	-1.94	-1.94	-0.85	3.21	1.91	2.67
<i>Excess</i>	0.08	0.08	0.02	-0.10	-0.01	-0.01
BCTL Cash Management (TLCM)	0.00	0.00	0.00	1.33	n.a	1.27
Three Month US Treasury bills	0.03	0.03	0.12	1.60	n.a	1.59
<i>Excess</i>	-0.03	-0.03	-0.12	-0.27	n.a	-0.32
BCTL 3-5 yr US Treasury Bond	-1.23	-1.23	-0.58	3.96	2.19	1.93
BoA Merrill Lynch 3-5 Years US Treasury Passive	-1.27	-1.27	-0.62	4.03	2.22	1.92
<i>Excess</i>	0.04	0.04	0.04	-0.08	-0.02	0.00
BCTL ML 5-10 Years US Treasury Notes & Bonds	-4.44	-4.44	n.a	n.a	n.a	-5.00
BoA Merrill Lynch 5-10 Years US Treasury Passive	-4.48	-4.48	n.a	n.a	n.a	-4.81
<i>Excess</i>	0.04	0.04	n.a	n.a	n.a	-0.19
BIS FI - Global Treasury Developed Market - Hedged	-3.01	-3.01	n.a	n.a	n.a	-1.60
Benchmark6	-3.00	-3.00	n.a	n.a	n.a	-1.71
<i>Excess</i>	-0.01	-0.01	n.a	n.a	n.a	0.11

INTERNATIONAL EQUITIES

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

Table 10

	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
International Equities	5.53	5.53	53.57	12.58	13.29	10.85
Benchmark	4.92	4.92	54.03	12.81	13.36	10.51
<i>Excess</i>	0.61	0.61	-0.47	-0.24	-0.07	0.35
Schroders Investment Management*	8.14	8.14	52.57	n.a	n.a	18.04
MSCI World Index ex Net Australia dividends Reinvested	4.95	4.95	53.75	n.a	n.a	18.85
<i>Excess</i>	3.19	3.19	-1.18	n.a	n.a	-0.81
SSgA Equity Factor**	6.47	6.47	48.42	n.a	n.a	15.31
MSCI World Index ex Net Australia dividends Reinvested	4.95	4.95	53.75	n.a	n.a	18.85
<i>Excess</i>	1.51	1.51	-5.32	n.a	n.a	-3.54
SSgA International Equity	5.01	5.01	53.95	12.92	13.56	11.87
MSCI World index ex Australia Passive	4.95	4.95	53.75	12.90	13.44	11.61
<i>Excess</i>	0.06	0.06	0.21	0.02	0.12	0.26
BlackRock Investment Management	5.02	5.02	54.24	13.04	13.67	11.39
MSCI World index ex Australia Passive	4.95	4.95	53.75	12.90	13.44	11.12
<i>Excess</i>	0.07	0.07	0.49	0.15	0.24	0.27
BCTL Australia Equity	3.56	3.56	68.81	8.63	n.a	9.49
MXAU AU Index Passive	3.41	3.41	68.44	9.03	n.a	9.73
<i>Excess</i>	0.15	0.15	0.37	-0.40	n.a	-0.24

*The Performance number of Schroder reflects the reclassification of Schroder's mandate to be factor mandate effectively implemented on 2 August 2019.

**SSgA Equity factor performance numbers commence on 2 August 2019.

PRIVATE DEBT INSTRUMENT FOR PETROLEUM OPERATIONS

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

Table 11

	Qtr	FYTD	1 Year	3 Years	5 Years	Since Inc
Private debt instrument for Petroleum Operations	1.10	1.10	4.50	n.a	n.a	4.50
<i>Benchmark</i>	1.10	1.10	4.50	n.a	n.a	4.50
<i>Excess</i>	0.00	0.00	0.00	n.a	n.a	0.00

5. MANAGEMENT COSTS

A management fee of \$2.03 million for operational management costs was charged to the fund during the quarter. The fee covered the following services (in thousands \$):

Table 12

External Management and Custody expenses	613
Central Bank management expenses	1,226
IAB expenses	36
Other Expenses	153
Total Cost	2,028

6. TRANSFERS TO STATE BUDGET

According to Article 7.1 of the Petroleum Fund Law transfers from the Fund may only be made to the credit of a single State Budget account. An amount of \$200 million was transferred to the State Budget account during the quarter.

Table 13

In Thousand (\$)

Transfer January 2021	0
Transfer February 2021	-200,000
Transfer March 2021	0
Transfer for this Quarter	-200,000
Total transfers this fiscal year to March 2021	-200,000

7. COMPLIANCE STATEMENT

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

Qualifying Instruments

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

Modified Duration

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

Tracking Error

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

External Managers

External managers' investments were within their mandates during the quarter.

Internal Audit

The provisions of Article 22 of the Petroleum Fund law no. 9/2005 require the Central Bank's Internal Auditor to perform an audit of the Fund every six months. The Internal Auditor has performed an audit up to quarter ended 31 December 2020.

8. FINANCIAL INFORMATION

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

Table 14

BALANCE SHEET	March-21	March-20
In thousands of USD		
ASSETS		
Cash and Cash Equivalents	1,298,467	1,126,225
Receivables	13,077	47,008
Financial assets held at fair value through profit or loss	16,965,389	15,196,916
Financial assets held at Amortized Cost	708,663	679,010
TOTAL ASSETS	18,985,596	17,049,158
LIABILITIES		
Payables for securities purchased	-5,806	-12,524
Accounts payable	-1,033	-7,701
TOTAL LIABILITIES	-6,839	-20,224
NET ASSETS	18,978,757	17,028,934
CAPITAL		
Opening Balance (January)	18,990,614	17,691,816
PF Law Art. 6.1 (a) Revenue receipts	31,765	70,691
PF Law Art. 6.1 (b) DA receipts	22,411	105,035
PF Law Art. 6.1 (e) Other receipts	0	5,386
PF Law Art 7.1 Transfers to State Budget	-200,000	0
Income for the period	133,965	-843,994
CAPITAL	18,978,757	17,028,934

Table 15

STATEMENT OF PROFIT OR LOSS In thousands of USD	QUARTER		YEAR TO DATE	
	Mar-21	Mar-20	Mar-21	Mar-20
INVESTMENT INCOME				
Interest income	40,463	61,746	40,463	61,746
Dividend income	34,645	38,938	34,645	38,938
Trust income	982	1,525	982	1,525
Other investment income	22	0	22	0
Net gains/(losses) on Financial Assets at fair value	75,306	-938,077	75,306	-938,077
Net foreign exchange gains/(losses)	-665	-2,832	-665	-2,832
Total Investment Income	150,753	-838,700	150,753	-838,700
EXPENSES				
External management, fees	613	864	613	864
Internal operational management fees	1,226	1,758	1,226	1,758
IAB Expenses	36	13	36	13
Other expenses	153	894	153	894
Total expenses	2,028	3,529	2,028	3,529
Profit before tax	148,725	-842,229	148,725	-842,229
Withholding taxes on investments	14,760	1,764	14,760	1,764
Profit/loss for the period	133,965	-843,994	133,965	-843,994
Other comprehensive income	0	0	0	0
Total comprehensive income for the period	133,965	-843,994	133,965	-843,994

Note:

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

Dili, 19 April 2021



Venancio Alves Maria
Deputy Governor



Abraão de Vasconcelos
Governor