

TUVALU TRUST FUND

Annual Report 2012



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Abbreviations & Acronyms

A\$ - Australian Dollar

CIF - Consolidated Investment Fund

EDF - European Development Fund

EU - European Union

GoT - Government of Tuvalu

IC - Investment Committee

NZ - New Zealand

TTF - Tuvalu Trust Fund

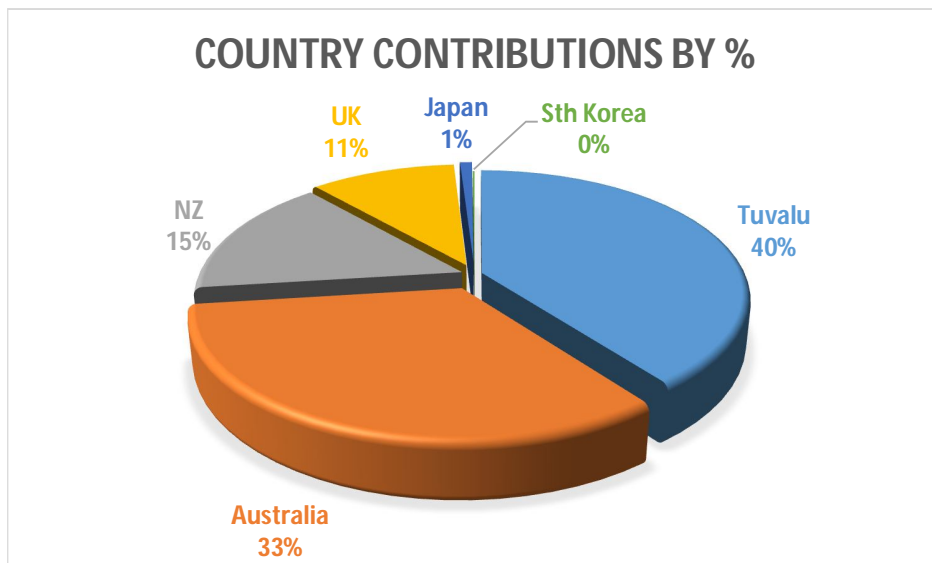
TTFAC - Tuvalu Trust Fund Advisory Committee

UK - United Kingdom

Historical Note

The Tuvalu Trust Fund was established in 1987 to provide a source of recurrent revenue to the Government of Tuvalu which has extremely limited alternative sources of revenue at its disposal when it achieved independence in 1978. Tuvalu started developing a case for a Trust Fund with its donor partners in 1982. After undergoing a series of negotiations with donors and further refinements of the proposed Fund, an agreement (The International Trust Fund Agreement) was signed on 16 June 1987 by Tuvalu, New Zealand, Australia and the United Kingdom as the original parties. The Fund itself was invested on 21 August 1987, with an initial value of A\$27.1 million of which A\$1.6 million was contributed by Tuvalu, A\$8 million by Australia, A\$8.3 million by New Zealand, \$8.5 million by United Kingdom, A\$0.7 million by Japan and A\$31,000 by South Korea. Since inception, the Fund has been receiving additional contributions from the parties to the Fund. The graph (figure 1) and the table below summarizes contributions by each country up to 30 September 2012, including the initial contributions at the establishment of the Fund:

Figure: 1 Contribution by Country into the Fund



Contributions into the Fund (A\$000's) up to 30 September 2012

TUVALU	AUSTRALIA	NZ	UK	JAPAN*	S. KOREA*	TOTAL
31,885	26,901	12,579	8,450	695	101	80,611

Purpose of the Fund

As set out in Part I, Article 2 of the agreement, the Fund has the following specific purpose:

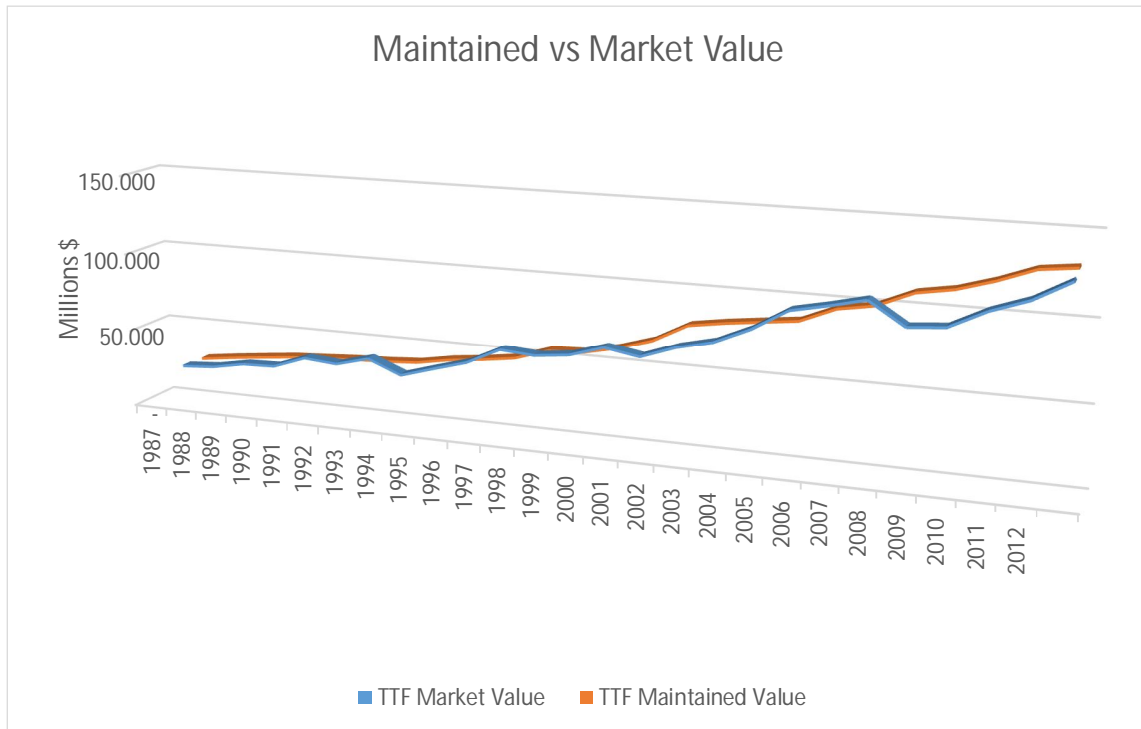
- a) assist the Government to achieve greater financial autonomy in the management of its recurrent budget;
- b) enable the Government to maintain, and if possible, improve existing levels of social infrastructure and services;
- c) enhance the capacity of the Government to receive and effectively utilize external capital development and technical assistance;
- d) enable the Government to meet long-term maintenance and operating costs of social and economic infrastructure and services; and
- e) assist the Government to develop the economy of Tuvalu

The Growth of the Tuvalu Trust Fund

As at 30 September 2012, the Fund's market value stood at A\$127.3m compared to A\$119.12 million at the end of 2011. This represents a dollar value increase of \$8.2m or 7%

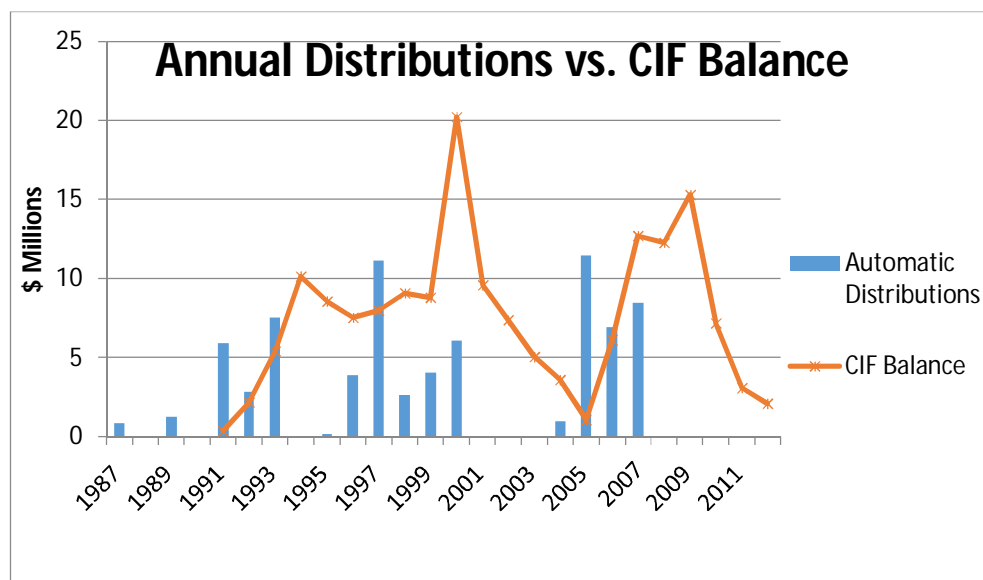
The chart below shows the Funds Market value compared to its maintained value since inception to 30 September 2012.

* not a party to the Agreement



Creation of the Consolidated Investment Account – the Buffer Account

In November 1993, the TTF Board of Directors endorsed the initiative of the Tuvalu government to create a buffer account, the Consolidated Investment Fund (CIF). The CIF was created upon the need to provide a mechanism for holding distributions from the TTF (the A account) until such time as they were required. The CIF belongs entirely to the Government of Tuvalu as opposed to the TTF which is managed by the Board in trust for the people of Tuvalu and governed by the Agreement.



Governance of the Fund

The Fund is governed by the provisions set out in the International Agreement. The Parties to the Agreement - the Government of Tuvalu, Australia, New Zealand and the United Kingdom – are the members of, and those responsible for, the Tuvalu Trust Fund. Following its regional program review, the United Kingdom withdrew its membership of the Tuvalu Trust Fund Board and the Advisory Committee in 2004.

Board of Directors

In accordance with Part II, Article 6 of the Agreement, the Fund has a Board of Directors, in which all powers of the Fund are vested in, and exercised by the Board. The Directors of the Fund are:

- a) a Director appointed by the Government of Tuvalu, who is Chairman of the Board;
- b) one Director appointed by each other original Party to the Agreement.

Since the UK's withdrawal, the Board now consists of representatives from Tuvalu (Chair), Australia and New Zealand.

Annual Reports

In accordance with Part VIII, Article 23 of the Agreement, within six months of the end of each financial year, the Board shall publish and submit to each Party, an Annual Report on the activities and management of the Fund, including the annual accounts of the Fund Managers, and the reports of Fund Monitor, Auditor, and Advisory Committee.

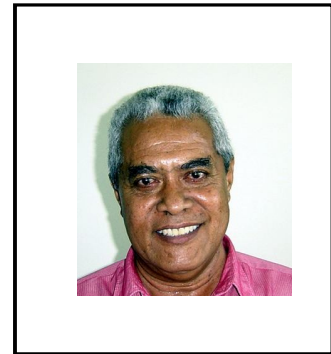
Board of Directors

Hon Lotoala Metia

Chairman

Minister of Finance and Economic

Development for the Government of Tuvalu



Mr Brian Bell

Director

for the Government of New Zealand

Ms Sarah Goulding

Director

for the Government of Australia

Service Providers

Fund Managers

Ms Jessica Howe, Client Services,-Aberdeen Asset Management Limited

Ms Belinda Gorgievski, Client Services-Deutsche Asset Management (RREEF Global Property Securities Fund)

Mr Le Tao, Relationship Associate,-State Street Global Advisors

Ms Joel Connell, Relationship Manager,-Bell Asset Management Fund (Bridgewater Fund)

Mr Jo White, Head of Client Services, BT Investment Management Limited

Ms Clare Marlow, Portfolio Administrator, JF Capital Partners Limited

Ms Susan Miller, Client Services, Blackrock Global Investors

Ms Clare Offwood, Client Services, Schroders Investments.

Since March 2012

Mathew Hopkins & Chris Wildman - AMP Capital, Sydney

Simon Doyle & Clare Offwood - Schroder Investments, Sydney

TTF Investment Committee

Mr Brian Bell, NZ Adviser and Chairman

Mr Tim Henaghan, Australian Adviser and Member (up to June 2012)

Mr David Hutton ,Australian Adviser (since July 2012)

TTF Advisory Committee

Mr Michael Hyndman- Consultant for the Government of Australia

Mr Chris Chamberlin - Consultant for the Government of New Zealand

Mrs Nicky Wrighton- Consultant for the Government of Tuvalu

Fund Monitor

Mr Maroun Younes - Investment Adviser, Towers Watson (up to June 2012)

Ms Amy The – Investment Consultant, Towers Watson (up to June 2012)

Mr. Jonathan Eriksen - Eriksen & Associates (since July 2012)

Fund Auditor

Mr Sikeli Tuinanuma- Partner, Ernst & Young

Secretariat

Mr Lee Faiva Moresi - Secretary

Ms Salai Sualo – Assistant Secretary

Chairman's Report

It gives me great pleasure to present the Annual Report of the Tuvalu Trust Fund (TTF) for the financial year ending 30 September 2012. Before I go into details of the TTF's activities I would first like to pay tribute to and acknowledge my former colleague, the late Hon. Lotoala Metia who we all know has been the Chairman of the TTF Board of Directors since 2006 until his passing away in December 2012. I thank him for his stewardship and chairmanship of the Tuvalu Trust Fund.

I am pleased to report that the affairs, activities and management of the Tuvalu Trust Fund during the 2012 financial year were in accordance with the International Agreement.

The year 2012 saw the Fund adopt a new investment strategy based upon the recommendations of the Investment Committee and the recommendations of an independent consultant. The strategy changed from the traditional Static Asset Allocation (SAA) where the Board stipulated an asset allocation mix between growth and defensive assets to Objective Based Asset Allocation, (OBAA). The objective of the TTF remains that of obtaining a return of CPI + 4.5% with the Fund managers tasked with managing the investments to achieve that performance target or better. I am pleased to report that thus far it appears that the new strategy is paying dividends. Given that 2012 saw a continuation of uncertainty in the world markets characterized by flat growth and market volatilities, it is prudent to remain cautious. It will take a little bit longer before a true picture of the new strategy can be drawn.

With the market value of the TTF below its maintained value as at the end of the 2012 financial year (30 September 2012), there was no distribution for this year. Fortunately for the Government of Tuvalu, the large distributions from the better

years saw some funds remain in the Consolidated Investment Fund, CIF, from which it was able to access and utilize for its pressing financial needs. The Fund would have been badly affected by the continuing downturn in world markets, but thanks to the hard working efforts and professional skills of the Fund Managers, Investment Consultant, the TTF Investment Committee, TTFAC, the Board of Directors and the secretariat for the successful management of the fund.

Tuvalu mo te Atua

Highlights of the Year

Change in Investment Strategy, Managers and Fund Monitor.

The year 2012 saw a few personnel changes within the different structures of the Trust Fund starting with the change in New Zealand's Board representative with H.E. Gareth Smith taking over from Dr Brian Bell. The Trust Fund acknowledges Dr Bell's contribution to the Tuvalu Trust Fund not only as a Board Director but also through his various roles with the TTF over the years. TTF is pleased to see that he continues his long association with the Fund and Tuvalu by remaining on the Investment Committee. On the Advisory Committee Mr Chris Chamberlin came in to replace another stalwart of the Tuvalu Trust Fund Mr David Abbot as New Zealand's representative on the TTFAC. Mr Abbot's involvement with Tuvalu through various roles goes back to the early days of Tuvalu as an independent nation. During the year 2012 Towers Watson ceased to be the Fund Monitor and Consultant for the Trust Fund and they were replaced by Eriksen & Associates with Jonathan Eriksen taking on the role of lead Consultant.

Transition and Overlay Management.

Following a review of the Fund and its investment strategies, the Board decided in its November 2011 meeting to adopt the new OBAA strategy as per the recommendation of the review report. As part of the change, the number of Fund managers was also reduced from 7 to 2.

Managing the transition was carried out by Goldman Sachs's Sydney office and this was carried out over the months of February and March 2012. With Goldman Sachs's expertise, the fund profited by \$202,000AUD over the transition. All Funds were invested with the two new Fund managers, AMP Capital and Schroder, by the end of March 2012.

Global Markets Overview.

The year started well with continuing moderate growth from the previous year appearing to indicate recovery from the global financial crisis of 2008. However, towards the end of 2012 the markets showed signs of nervousness with the looming US "fiscal cliff". As it turned out the US were able to avoid this eventuality by agreeing a bi-partisan solution and the resultant continuation of quantitative easing, (QE).

The year 2012 also saw continuing sovereign debt issues with some EU countries causing uncertainty in the markets. This uncertainty was further fueled by changes in political ideologies as reflected in some European elections, especially in France.

China's predicted declining growth also loomed as a global growth and recovery inhibitor with flow on effects to economies that heavily depend on China's growth for their own growth.

Perhaps a positive was in the emerging markets and the Australian economy. Australia's mining industries, despite having a few jitters, appeared to have propped up their economy. Emerging markets also experienced growth in 2012 allowing for some opportunities in the investment markets.

Fund Performance

Tuvalu Trust Fund status

The Tuvalu Trust Fund returned 10.6% (gross of fees) for the 12 months to 30 September 2012. This equates to a relative performance of 3.7% against the benchmark of CPI + 4.5%. Most of the returns were attributable to the new Fund Managers with Schroder contributing 2.8% and AMP 0.9% to the overall fund's performance. As at the end of the 2012 financial year the managers' holdings and weightings were 50.6% with Schroder, AMP 49.2% and BT Global the remaining 0.2%

Market Value

As at the end of 30 September 2012, the market value of the Tuvalu Trust Fund's investments stood at A\$127.3 million compared to A\$115 million on 30 September 2011, representing a \$12.3million increase or 10.6%.

Maintained Value

The Tuvalu Trust Fund maintained value as at end of 30 September 2012 was A\$129,987,221 compared to \$127,481,925.00 the previous year.

CIF Closing Value

The value of the Tuvalu Consolidated Investment Fund as at end of 30 September 2012 was A\$4.43 million compared to A\$3.12 million on 30 September 2011. This included budget support contributions from Australia (\$4m) and NZ (\$188,016) during the 2012 financial. Over the same period the Government of Tuvalu drew down \$3m from the CIF. All of the investment was in cash, held by Craigs Investment Partners.

Automatic Distribution

In 2012, there was no automatic distribution from TTF into CIF as the TTF market value was below its maintained value.

Directors Report

The Directors of the Tuvalu Trust Fund during the period covered in this report are:

Hon. Lotoala Metia (Tuvalu - Chairman) now replaced by

Hon. Kausea Natano.

H.E. Gareth Smith (New Zealand)

Ms Sarah Goulding (Australia)

Statement of the Directors

In the opinion of the Directors, in accordance with Part VIII, Article of the Trust agreement, the Annual Report has been properly prepared from the financial statements set out in the report, the monitoring statements set out in the report, the advisory statements set out in the report , and is properly drawn up and based on the full and complete reports of the Fund managers, monitor, audit, advisory committee and other relevant source materials so as to give a true and fair view of the affairs , activities and management of the Fund as at 30 September 2012, and of the transactions and results of the year ended on that date.

The FUND has been conducted in accordance with the constituent agreement of the parties to the Tuvalu Trust Fund.

SIGNED in accordance with resolution from and approval of the Board of Directors of the Tuvalu Trust Fund.

Hon. Kausea Natano

Chairman

H.E. Gareth Smith

Director

Ms Sarah Goulding

Director

Financial Statements