



2013

CARIBBEAN COURT OF JUSTICE TRUST FUND

ANNUAL REPORT

**GROWTH**

**STABILITY**

**PROTECTION**

**LONGEVITY**

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## REPORT OF THE BOARD OF TRUSTEES

The Board of Trustees is comprised of nominees from the following institutions as defined in the “Revised Agreement Establishing the Caribbean Court of Justice Trust Fund.” The composition is as follows:

<b>INSTITUTION</b>	<b>REPRESENTATIVE TRUSTEE</b>	<b>BOARD AND COMMITTEE POSITION</b>
Caribbean Congress of Labour	Dr. Linton Lewis	Chairman
University of the West Indies	Mrs. Christine Sahadeo	Vice-Chairman; Member, Finance & Investment Committee
Organisation of Commonwealth Caribbean Bar Association	Mr. Wilfred Abrahams	Member, Audit Committee
Conference of Heads of the Judiciary of Member States of the Caribbean Community	Chief Justice Ivor Archie	
CARICOM Secretariat	Mr. Oswald Barnes	Member, Audit Committee
Caribbean Association of Industry and Commerce	Dr. Rollin Bertrand	
Insurance Association of the Caribbean	Mr. Gerry Brooks	Chairman, Finance and Investment Committee
Caribbean Association of Banks Inc.	Mrs. Carole Eleuthere-Jn Marie	Member, Finance & Investment Committee
Institute of Chartered Accountants of the Caribbean	Mr. Harryram Parmesar	Chairman, Audit Committee

# REPORT OF THE BOARD OF TRUSTEES



Top: **Dr. Linton Lewis**; Chairman, Top Row (l-r): **Mrs. Christine Sahadeo**; Vice Chairman; Member, Finance and Investment Committee, **Mr. Wilfred Abrahams**; Member, Audit Committee, **Chief Justice Ivor Archie**; **Mr. Oswald Barnes**; Member, Audit Committee.

Bottom Row (l-r): **Dr. Rollin Bertrand**; **Mr. Gerry Brooks**; Chairman, Finance and Investment Committee, **Mrs. Carole Eleuthere-Jn Marie**; Member, Finance and Investment Committee, **Mr. Harryram Parmesar**; Chairman, Audit Committee.

## REPORT OF THE BOARD OF TRUSTEES

I am pleased to report, on behalf of the Board of Trustees, on the positive performance of the Caribbean Court of Justice Trust Fund for the year ended December 31, 2013. The year 2013 marked the beginning of the end of the quantitative easing programme in the US, an economic stimulus programme introduced after the 2008 financial crisis in order to stimulate growth in the US economy. The year was also marked by the resurgence of fiscal crises in Italy and Cyprus, despite the improving economic picture in the Eurozone and continued commitment to accommodative monetary policy by the region's policy makers. 2013 was also noteworthy for increased signs of slowing growth in emerging markets, and emerging market equity prices struggled at the same time that there was a significant rally in developed equity market prices.

### Background

The Caribbean Court of Justice Trust Fund ("the Trust Fund") was endowed with its initial capital in April 2005 with the mandate to provide the financial resources necessary to fund the Caribbean Court of Justice ("the Court") and the Regional Judicial Legal Services Commission ("the Commission") in perpetuity. The Board of Trustees manages the resources of the Trust Fund in accordance with the following philosophy:

*"The fund will be invested prudently with a long-term investment horizon in a wide range of tax-efficient international instruments so as to produce an optimal gross rate of return with reasonable security of its capital."*

Accordingly, the Board has developed Investment Guidelines for the Fund, which were approved by the CARICOM Heads of Government. In order to have a reasonable likelihood of satisfying the funding requirements of the Court and the Commission, these approved Guidelines permit a significant exposure to growth assets, such as public and private equity, within a diversified portfolio complemented by allocations to risk-reducing and inflation protection assets.

The Board of Trustees continues to uphold its fiduciary responsibility to manage the assets of the Trust Fund

prudently to fulfill its long-term objective. During the course of the year, the Board met six times, and the Finance & Investment Committee and the Audit Committee each met twice.

At the start of the financial year under review, the Trust Fund had produced annual rates of return of +10.4%, +9.2%, -19.5%, +15.9%, +10.3%, -1.8% and +10.1% for the complete calendar years 2006 to 2012 respectively. All returns in this report are stated net of investment management expenses, consistent with industry standards.

### Overview of Performance

The balance of the Fund as at December 31, 2012 was US\$93,693,618 and increased to US\$100,449,670 as at the end of the financial year 2013. This increase in market value reflected a net annual return of +12.2% for 2013, bringing the annualised and cumulative net returns since inception (April 2005) to +5.4% p.a. and +56.4% respectively.

During the financial year to December 31, 2013, the Trust Fund disbursed US\$5,719,315 to cover the funding requests of the Court and the Commission. The Trust Fund also received from the Court, a return of funds previously disbursed, in the sum of US\$1,356,424, which primarily represented a repayment of pension monies previously invested with a third party. This brought the net amount disbursed for the year to the Court and the Commission to US\$4,362,891. The Trust Fund also received the amount of US\$1,017,778 which represented the eighth of nine instalments of a third party contribution from the Government of the Commonwealth of the Bahamas.

### The Markets in 2013

The year 2013 was largely highlighted by the US Federal Reserve's announcement of the beginning of the end of their quantitative easing (QE) programme, the 16-day US Government shutdown, echoes of a fiscal crisis in Italy and Cyprus despite general economic improvements in the Eurozone, and slowing growth forecasts globally, including in emerging markets. Despite these events, the year was noteworthy for the impressive run up in developed market equity prices, while bond prices fell,

## REPORT OF THE BOARD OF TRUSTEES

in an investment environment characterised by lower volatility, low inflation and modest economic growth. The VIX, a measure of market volatility, reached a 5-year low in March 2013 of 11.30 before ending the year at 12.46, well below its 20-year monthly average of 20.43 (Bloomberg).

Globally, equity markets, with the exception of emerging markets, ended the year with double digit positive returns as shown in Table 1 below, which highlights the quarterly and annual returns on major indices for 2013. In US equity markets, the broad DJ US Total Stock Market Index and the S&P 500 posted gains of +33.5% and +32.4% respectively, whilst the Dow Jones Industrial Average, which measures the performance of 30 blue-chip stocks, posted a +29.7%

return for 2013. Similarly, non-US developed market equities provided investors with double digit positive returns as the benchmark index, MSCI EAFE, ended the year with a return of +22.8%. Despite the recovery in the second half of the year, emerging market equities ultimately provided investors with a negative return, -2.6%, for the year.

Natural resources also provided investors with double digit positive returns, with the benchmark S&P Natural Resources index posting a gain of +16.5% in 2013. Global fixed income came under pressure in the face of the global equity rally, and provided investors with a -2.0% return, as measured by the Barclays Aggregate index.

**Table 1: Major Indices - Quarterly and Annual Returns 2013**

Index	Q1 2013	Q2 2013	Q3 2013	Q4 2013	2013
<b>DJ US Total</b>	+ 11.07%	+ 2.79%	+ 6.16%	+ 10.11%	+ 33.47%
<b>S&amp;P 500</b>	+ 10.61%	+ 2.91%	+ 5.25%	+ 10.51%	+ 32.39%
<b>DJIA</b>	+ 11.93%	+ 2.92%	+ 2.12%	+ 10.22%	+ 29.65%
<b>MSCI EAFE</b>	+ 5.13%	- 0.98%	+ 11.56%	+ 5.71%	+ 22.78%
<b>MSCI Emerging Markets</b>	- 1.62%	- 8.08%	+ 5.77%	+ 1.83%	- 2.60%
<b>S&amp;P Natural Resources</b>	+ 7.17%	- 4.95%	+ 8.63%	+ 5.27%	+ 16.49%
<b>Barclays Aggregate</b>	- 0.12%	- 2.33%	+ 0.58%	- 0.14%	- 2.02%

Source: Mercer Hammond Monthly Market Updates

## REPORT OF THE BOARD OF TRUSTEES

### Management of the Portfolio

The Trust Fund is an institutional endowment fund that, assisted through the services provided by its investment advisor, Mercer Hammond Investment Consulting, manages the portfolio with the long-term focus necessary to achieve the mandate of funding the Court and the Commission in perpetuity. The portfolio has been structured to attain its target rate of return over the long-term, within acceptable risk parameters, and is diversified across a selection of growth, risk-reducing and inflation-protection asset classes.

The benefits of maintaining a diversified strategic long-term asset allocation have been proven throughout the varying market conditions experienced since inception. The continuing commitment to its diversified long-term strategic asset allocation has rewarded the Trust Fund with a positive return in 2013 of +12.2%, which exceeded the annualised long-term target rate of return.

The total rates of return earned by the portfolio for the complete calendar years since inception are shown in Table 2.

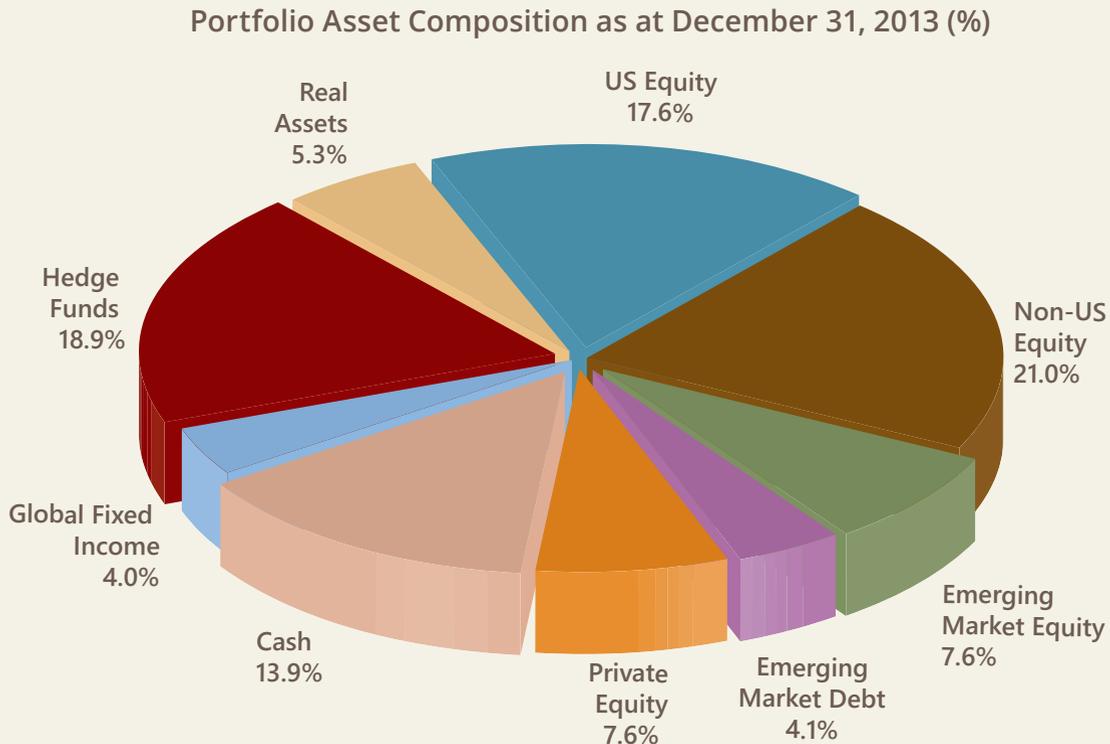
**Table 2: Fund Returns**

	<b>Period Return</b>	<b>Annualised Rate from Inception</b>
January 1, 2006 to December 31, 2006	+ 10.4%	+ 9.3%
January 1, 2007 to December 31, 2007	+ 9.2%	+ 9.3%
January 1, 2008 to December 31, 2008	- 19.5%	+ 0.7%
January 1, 2009 to December 31, 2009	+ 15.9%	+ 3.5%
January 1, 2010 to December 31, 2010	+ 10.3%	+ 4.7%
January 1, 2011 to December 31, 2011	- 1.8%	+ 3.7%
January 1, 2012 to December 31, 2012	+ 10.1%	+ 4.5%
January 1, 2013 to December 31, 2013	+ 12.2%	+ 5.4%

The portfolio allocation as at December 31, 2013 is provided in Chart 1:

## REPORT OF THE BOARD OF TRUSTEES

Chart 1: Portfolio Asset Composition as at December 31, 2013 (%)



The Trust Fund has consistently adopted a disciplined approach to rebalancing the portfolio in scenarios of increasing asset prices, while maintaining the long-term focus of the Fund. Accordingly, while the overall exposure to US and non-US equities was retained at a level consistent with the long-term strategic asset allocation of the portfolio, rebalancing actions were undertaken in 2013 which benefitted the portfolio significantly as profits were realised and reinvested. This disciplined approach will continue to crystallise unrealised gains, whilst potentially reducing volatility in the Fund's returns. Correspondingly, by reinvesting proceeds in underperforming asset classes, which are attractively valued for future performance, the Trust Fund may be able to enhance its long-term return potential.

The phased investment in private equity continued into 2013. This sector is expected to continue to contribute positively to return, as a diversified portfolio of private

equity fund of funds investments is built to its full allocation.

Hedge fund of funds investments are expected to continue to fulfil a vital role in risk reduction without significantly sacrificing return in the long run, and can create value through active management across different sectors. The Trust Fund increased its holdings in hedge fund of funds in 2010, relative to its long term strategic asset allocation, in preference to other risk-reducing assets (cash, fixed income) for which the return outlook was comparatively low. This tactical overweight was removed at the end of 2013 based on the expectation that the reduced volatility currently prevailing in the investment markets would continue in the near term. The resultant inflow of cash at the end of the year was reinvested in early 2014 in growth assets, for which there was a positive medium-term return outlook.

## REPORT OF THE BOARD OF TRUSTEES

### Movement in Fund Balance

The Fund experienced an increase in market value from US\$93,693,618 at the start of the year to end 2013 at US\$100,449,670.

**Table 3: Statement of Movement in Fund Balance – 2013, 2012 and From Inception (April 2005)**

	2013	2012	April 2005 to December 2013
<b>Opening Fund Balance</b>	<b>93,693,618</b>	<b>90,839,149</b>	<b>100,946,142</b>
Additional Contributions	1,017,778	1,017,778	12,103,742
	<u>94,711,396</u>	<u>91,856,927</u>	<u>113,049,884</u>
Interest & Dividends <sup>1</sup>	961,761	1,056,804	16,637,396
Realised Gains/(Losses)	1,279,544	650,234	15,235,717
	<u>2,241,305</u>	<u>1,707,038</u>	<u>31,873,113</u>
Investment Management Expenses	(313,103)	(293,900)	(3,183,377)
Net Investment Income	1,928,202	1,413,138	28,689,736
Trust Fund Administrative Expenses (including Depreciation)	(672,158)	(646,158)	(5,723,351)
Net Income	1,256,044	766,980	22,966,385
Net Gain/(Loss) in Fair Value on Investments	8,845,121	7,350,457	10,150,066
<b>Net Gain/(Loss) in Fund Before Disbursements</b>	<b>10,101,165</b>	<b>8,117,437</b>	<b>33,116,451</b>
Net Disbursements to Court & Commission	(4,362,891)	(6,280,746)	(45,716,665)
Net Change in Fund Balance (excluding Additional Contributions)	5,738,274	1,836,691	(12,600,214)
<b>Closing Fund Balance @ December 31</b>	<b>100,449,670</b>	<b>93,693,618</b>	<b>100,449,670</b>

During the financial year 2013, a third party capital contribution of US\$1,017,778 was received from the Government of the Commonwealth of the Bahamas.

Realised Gains were recorded within the financial year 2013, as in the two prior years, as the Fund executed its rebalancing strategy and crystallised mark to market gains on assets for which there had been a significant increase in market value.

<sup>1</sup> Net of Foreign Exchange Gains/(Losses)

Investment management expenses increased by approximately US\$19,000 or 6.5%, as a result of the increased asset values. The Trust Fund continued its trend of prudent management of administrative expenses, showing a minor increase of US\$26,000 (4.0%) in expenditure in the current financial year. The ratio of investment management expenses plus administrative expenses of the Trust Fund, expressed as a percentage of the average fund balance, was

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1.0%, in line with the average maintained in the previous years since inception of the portfolio in 2005.

The Fund experienced a Net Gain in Fair Value on investments of US\$8,845,121 in 2013, bringing the cumulative Net Gain in the Fund Before Disbursements since inception to US\$33,116,451. Disbursements to fund the expenses of the Court and the Commission, net of the one-off return of funding previously disbursed, amounted to US\$4,362,891 in the financial year ended December 31, 2013 bringing cumulative disbursements since inception to US\$45,716,665. The Fund experienced a positive net change in 2013, after disbursements and total expenses and before additional contributions, of US\$5,738,274.

The fund balance, after net disbursements to the Court and the Commission of US\$4,362,891 and total expenses of the Trust Fund of US\$985,261 in 2013, amounted to US\$100,449,670 at the end of the financial year.

### Outlook for 2014

The major themes emerging for the year are:

- Reduced economic growth
- Continued recovery in developed markets
- A potential return to higher volatility

A reduced economic growth story may unfold in 2014 with each of the major regions logging positive GDP growth in 2013, and most forecasting more modest increases in 2014. The US economy shows signs of being strong enough to withstand the effect of the Fed's tapering of QE, and its potential impact on interest rates. Continued economic growth is contingent on the corporate response to an improved economic outlook. US companies have resisted capital investment so far, and cash and short-term investments as a percent of total corporate assets are high. Increased and steadier corporate spending may be a big driver in the next phase of US economic growth.

Europe and Japan continue to stimulate their way to growth. Private sector resilience, reduced fiscal drag and a possible upturn in exports underpin the positive outlook for European growth in 2014. The troublesome PIIGS (Portugal, Italy, Ireland, Greece and Spain) now hold positive current account balances, indicating a firmer fiscal base. The Bank of England and the European Central Bank (ECB) have consistently shown their commitment to economic stimulus and price stability. There is still room for the ECB to employ monetary easing strategies to continue to stimulate their economies through further interest rate cuts and additional LTRO<sup>2</sup> programmes, with restrictions on early repayment. While the outlook is still uncertain with high unemployment, low growth and a relatively strong Euro, the Central Banks' commitment and an improved fiscal base in most countries within the Eurozone provide a relatively strong argument for positive return potential.

Emerging market economic growth may likely be highly differentiated in the face of higher US interest rates, as countries whose trade imbalances have been supported by investment inflows flocking to higher interest rates, adjust to reduced inflows and the consequent tightening of liquidity. Inflation is under control in most of the region (with the exception of India and Indonesia), giving local central banks the ability to keep rates steady and even stimulate the economy if necessary, depending on their current account status. While China, a major commodity-demand economy, expects growth to decline significantly from its pre-2011 +10% level, officials are still targeting an average growth rate of +7% in 2014, which is still considerable particularly on a much larger economic base. The structural advantages of China and other emerging economies over the developed world remain compelling, with typically low levels of public and private debt, adequate currency reserves and generally favourable demographics. The macroeconomic growth outlook for these economies remains relatively positive.

With the exception of the US, stocks remain relatively inexpensive in comparison to long term normalised fair valuations, even after rallying significantly in 2013. Within the US, robust corporate earnings figures were reported

<sup>2</sup> Long Term Refinancing Operation – an ECB loan programme for Eurozone banks, which aims to stimulate interbank lending and other loan origination.

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throughout 2013. Nevertheless, the potential for further upside remains, and there remains a cautiously positive outlook for US equities on the basis of strong corporate earnings expectations and improving economic data. The outlook for global equities remains positive overall, and therefore equities are likely to offer an attractive risk premium.

Uncertainty over the timing of interest rate increases and the current relative attractiveness of riskier assets are not optimal conditions for outperformance in credit markets. The outlook remains difficult to predict under these conditions.

Active management may continue to play an increased role in generating return in 2014 as managers seek to derive alpha in markets which present such opportunities. A consistently employed rebalancing strategy will assist in maintaining discipline around the asset allocation strategy in the face of investor exuberance.

While the economic landscape seems more positive than the prior year, risks remain in investment markets arising from:

- Continued pressure on fixed income prices as QE is unwound, and interest rates normalise;
- A resurgence of US political risk as Congress addresses the debt ceiling in 2014;
- The varying economic statuses of the Eurozone countries and the possible resurgence of political risk; and
- Continued stress on emerging market economies as US interest rates normalise, drawing capital away.

The Trust Fund's portfolio is managed prudently with a long-term focus, with a strategic asset allocation designed to weather normal market cycles whilst seeking to protect existing capital. Despite this strategic positioning, the benefits of which have been proven in periods of market uncertainty, the portfolio is not immune to the impact of short-term market conditions, and negative fluctuations in value and return may occur.

### Summary

The Trustees continue to manage the assets of the Trust Fund in keeping with its stated investment philosophy and the long-term objective of funding the Court and the Commission in perpetuity. In 2013, the Trustees made several pro-active rebalancing decisions, in addition to repositioning the portfolio whilst remaining cognizant of the long-term goal.

Contributions received from the participating Member Governments and the Government of the Commonwealth of the Bahamas have amounted to US\$113,049,884 since inception. After total disbursements to the Court and the Commission of US\$45,716,665 and total expenses of the Trust Fund of US\$8,906,728 since inception, the balance of the Fund as at December 31, 2013 is US\$100,449,670.

The Trust Fund recorded a return of +12.2% for 2013, which brought the annualised and cumulative net returns since inception (April 2005) to +5.4% p.a. and +56.4% respectively.

The importance of a maintaining a diversified long-term strategic asset allocation has been proven throughout the varying market conditions experienced since the Trust Fund's inception in 2005. The Trust Fund's portfolio is appropriately spread across different asset classes, and the resultant diversification effect reduces the inherent risk of the portfolio. The Board of Trustees remains confident that the strategic asset allocation of the portfolio will enable the achievement of the Trust Fund's long-term objectives, despite potential variability in annual returns.

### Appreciation

I would like to thank the Board of Trustees, and its various Committees, for continuing to employ a prudent and proactive approach in guiding the Trust Fund along the path of fulfilling its long-term objective. The Board would like to record appreciation for the continued contribution of our independent investment adviser, Mercer Hammond Investment Consulting. The Board would also like to extend appreciation to the Management Team for their continued diligence and professional commitment throughout the year.

**Dr. Linton Lewis**  
Chairman