



Puerto Rico Tax-Free Target Maturity Fund II, Inc.



2016 Annual Report

Dear Shareholder:

The Puerto Rico Tax Free Target Maturity Fund II, Inc. (the “Fund”) is pleased to present its Annual Report to Shareholders for the fiscal year ended May 31, 2016.

PUERTO RICO TAX-FREE TARGET MATURITY FUND II, INC.

The investment objectives of the Puerto Rico Tax-Free Target Maturity Fund II, Inc. are (1) to achieve a high level of current income that, for Puerto Rico Investors, is exempt from Federal and Puerto Rico income taxes, consistent with the preservation of capital, and (2) to distribute to shareholders during the period commencing January 1, 2008 and ending on December 31, 2028, an amount at least equal, in the aggregate, to the initial offering price of \$10 per Share.

FUND PERFORMANCE

There was no distribution of principal during the fiscal year.¹ The Fund's remaining principal for distribution as of the fiscal year-end amounts to \$1.80. Meanwhile, the average dividend yield for the 12-month period, computed over the original investment of \$10 per share, was 0.35%. At the end of the fiscal year, the market price of the shares was \$1.45. At the end of the same period, the weighted-average duration of the Fund's investment portfolio was 3.45 years and its average credit quality was AAA.

The accompanying Figure 1 shows the breakdown of the investment portfolio as of May 31, 2016.

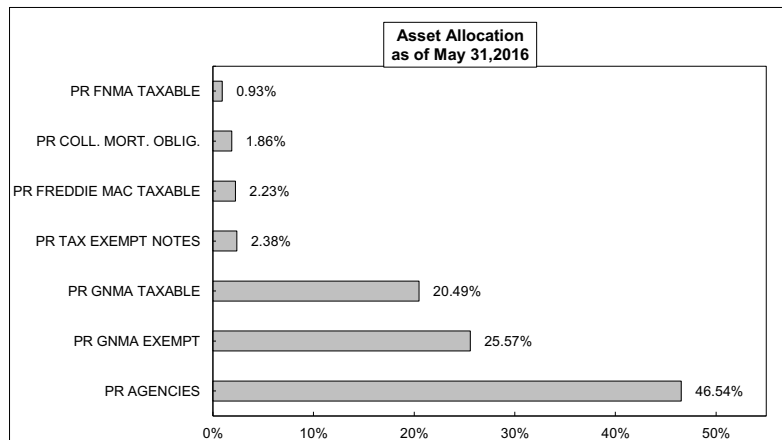


Figure 1. Asset Allocation as of May 31, 2016

¹ Principal distributions are derived from principal payments received by the Fund by reason of the maturity, prepayment, acceleration, redemption, sale, or other disposition of certain of its portfolio securities, as well as monies held in a reserve comprised of accumulated realized net capital gains and/or net investment income, established by Fund management in attempting to achieve its investment objective of distributing to shareholders an amount equal to the initial offering price of \$10 per share of Common Stock.

INVESTMENT STRATEGY

The Fund's investment advisers strive to select investment assets that maximize risk/return relationships, while adhering to the Fund's investment objectives.

The Fund is currently in its distribution period. Therefore, any maturities or prepayments in its investment portfolio are not reinvested in securities other than money market instruments.

ECONOMIC OVERVIEW

Puerto Rico Economy

The Puerto Rico Fiscal Agency and Financial Advisory Authority's Economic Activity Index (EAI) is an indicator of the general economic activity in Puerto Rico that is highly correlated with real GNP. The most recent EAI available, as of the end of May 2016, reflects a -1.8% year-over-year reduction.

Throughout the Fund's fiscal year, Puerto Rico bonds experienced high price volatility while continuing to trade at distressed levels. As measured by the Standard and Poor's Puerto Rico Municipal Bond Index, Puerto Rico bonds as a group fell 6.44% for the 12-month reporting period.

In late June 2015, Governor García Padilla surprised investors with his comments to The New York Times regarding the mathematical impossibility of Puerto Rico paying for all its \$72 billion in debt obligations. At the same time, the Government Development Bank released the Krueger report, prepared by three former IMF officials, which discusses the necessity for a comprehensive restructuring of all Puerto Rico debt, including General Obligations.

On August 3, 2015 Puerto Rico missed most of a \$58 million payment that was due on Public Finance Corporation bonds ("PFC"). This marked the first government default ever for the Island. The Fund does not own any PFC bonds.

On September 9, 2015 a working group appointed by the Governor publicly released the Puerto Rico Fiscal and Economic Growth Plan. The Plan outlines the scale of the challenges facing Puerto Rico, with an estimated \$28 billion fiscal gap over the next five years. In addition, it contains various recommended measures and reforms, which if fully implemented are expected to cut the fiscal gap in half by \$14 billion. The Plan states that the other half of the fiscal gap likely will need to be filled through a renegotiation of the debt.

On December 1, 2015 the Governor signed an executive order allowing the redirection of revenue budgeted for the Puerto Rico Highways and Transportation Authority, Convention Center, Infrastructure Financing Authority and other agencies in order to pay

for debt issued or guaranteed by the commonwealth. This claw-back measure allowed Puerto Rico to comply with all principal and interest payments that were due in December 2015.

In January 2016, Puerto Rico defaulted on about \$37 million in bond payments of the almost \$1 billion that were due. The missed payments were for \$35.9 million of non-commonwealth guaranteed Puerto Rico Infrastructure Financing Authority (“PRIFA”) debt and \$1.4 million of PFC bonds. The Fund does not own any bonds issued by either PRIFA or PFC.

Early in April 2016, Puerto Rico enacted the Emergency Moratorium and Financial Rehabilitation Act. The approved legislation allows Governor García Padilla to declare a fiscal emergency and implement a moratorium on a wide range of debt payments, including general-obligation bonds, through January 2017.

In May 2016, Puerto Rico defaulted on most of a \$422 million principal bond payment for its Government Development Bank, invoking the debt moratorium law approved in April 2016. The Fund does not own any GDB bonds.

Despite multiple discussions and intense lobbying, as of the end of May 2016 the U.S. Congress had not yet delivered on a comprehensive law to address Puerto Rico’s debt crisis. Significant debt-service payments are due in July 2016, so time is of the essence.

Credit Update

In June 2016, President Obama signed into law the Puerto Rico Oversight, Management and Economic Stability Act (“PROMESA”), which establishes an oversight board with broad authority to ensure that the Commonwealth implements and executes fiscal plans, balances the Commonwealth’s budget and enacts reforms if the Commonwealth fails to do so. PROMESA also seeks to promote a voluntary restructuring of the Commonwealth’s debts. It postpones creditor lawsuits seeking repayment and, if voluntary negotiations stall and certain conditions are met, provides for a court-ordered restructuring. It is expected that the oversight board created by PROMESA shall be in place by the end of September 2016.

In July 2016, Puerto Rico missed \$911 million in bond payments of the approximately \$2 billion that were due, again invoking the debt moratorium law. The skipped payments include \$780 million in payments of General Obligation bonds. The Fund does not own any bonds impacted by the default.

The United States Economy

Over the twelve-month reporting period, U.S. economic data continued to indicate modest growth in the 2.0% range. Labor markets were a tailwind for the economy during the Fund’s fiscal year. Job growth remained solid, with employers averaging 199,000 new jobs per month from June 2015 through May 2016. In addition, the national

unemployment rate fell to 4.7% in May 2016, compared to 5.5% the prior year. The unemployment rate is at its lowest level since 2007.

Influenced by a decline in commodity prices throughout the reporting period, inflation remained in check and continued to run below the 2% level, which is the Fed's longer-run goal. As measured by the U.S. Personal Consumption Expenditure Core Price Index, consumer prices rose 1.6% in the 12 months ended in May 2016.

Monetary policy was highly accommodative during most of the Fund's fiscal year. After much anticipation, in December 2015 the U.S. Federal Reserve took the long-awaited step of raising interest rates for the first time since 2006. The Federal Reserve approved a 0.25% increase in its target funds rate. The new target range will go from 0%-0.25% to 0.25%-0.50%.

In contrast to the Fed's tightening move, Central banks in Europe and Japan continued to embrace their easy monetary policies. In the U.S., Fed officials have said they will be cautious regarding further tightening due to concerns over global economic and financial conditions. Subsequent increases in interest rates are expected to be slow and gradual, subject of course to the direction of economic data.

Fixed-income markets were volatile throughout the Fund's fiscal year, with several zigzags during the period that reflected investors' anxiety about global growth and monetary policies. For the 12-month reporting period, U.S. Treasury yields moved generally lower, except for bonds with very short maturities which saw an increase in yield. Two-year U.S. Treasury yields, for example, rose from 0.61% at the beginning of the period to 0.88% at the end of the period. At the same time, the 10-year U.S. Treasury note went down 27 basis points in yield, from 2.12% to 1.85%. On the long end of the curve, 30-year U.S. Treasuries yielded 2.65% at the end of the Fund's fiscal year, compared to 2.88% at the beginning.

After five years without a single 10% correction, U.S. equity markets experienced two such corrections (August 2015 and January 2016) during the Fund's fiscal year. For the 12-month period, the Dow Jones Industrial, the S&P 500, and the NASDAQ posted returns of 1.39%, 1.71%, and -1.08% respectively.

OUTLOOK

The U.S. economic outlook indicates continued modest growth. For Puerto Rico, the fiscal situation remains uncertain as reflected by the Island's credit ratings. The combined scenario foreshadows a challenging investment environment for the management of the Fund. Notwithstanding, Banco Popular and UBS Puerto Rico remain committed to providing professional asset management services to the Fund for the benefit of its shareholders.

A handwritten signature in dark ink, consisting of a series of fluid, connected strokes that form a stylized, elongated shape.

Enrique Vila del Corral, CPA
Chairman of the Board and President

THE BENEFITS AND RISKS OF LEVERAGING

The Puerto Rico Tax Free Target Maturity Fund II, Inc. is permitted to use leverage in an amount not to exceed 50% of the Fund's total assets. In addition, the Fund may also borrow for temporary or emergency purposes in an amount of up to an additional 5% of its total assets. The Fund obtains leverage by borrowing, using its investment portfolio as well as securities otherwise obtained as collateral.

Leverage can produce additional income when the income derived from investments financed with borrowed funds exceeds the cost of such funds. In such an event, the Fund's net income will be greater than it would be without leverage.

If, on the other hand, the income derived from securities purchased with borrowed funds is not sufficient to cover the cost of such funds, the Fund's net income will be less than it would be without leverage.

Leverage often increases the risk for shareholders of Common Stock. In addition, leverage may have a negative impact on net asset value. Leverage could also increase market price volatility, interest rate and market risk. On the other hand, adding leverage to the Fund could result in higher net income.

SHARE REPURCHASE PROGRAM

On January 31, 2014, the Board of Directors approved the implementation of a Share Repurchase Program for the acquisition of the Fund's shares of Common Stock (the "Shares"), in open-market transactions at share prices equal to or at a discount of the corresponding NAV per Share, of up to 25% of each Fund's total assets as of such date. The Fund's Share Repurchase Program is implemented on a discretionary basis, under the direction of the co-Investment Advisers. The Fund's repurchase activity for each fiscal year is disclosed in the Annual Report to Shareholders attached hereto (see Note 4), as well as the quarterly reports to shareholders.

The undertaking of a repurchase program does not obligate the Fund to purchase specific amounts of Shares. During the fiscal year, the Shares continued to experience a period of limited liquidity and/or trading at a discount to their net asset value. Although the holders of the Shares do not have the right to redeem their Shares inasmuch as the Fund is closed-ended, the Fund may, at its sole discretion, effect repurchases of Shares in the open market, in an attempt to increase the liquidity of the Shares as well as reduce any market discount from their corresponding net asset value. There is no assurance that, if such action is undertaken, it will result in the improvement of the Shares' liquidity or reducing any such market discount. Moreover, while such undertaking may have a favorable effect on the market price of the Shares, the repurchase of the Shares by the Fund will decrease the Fund's total assets and therefore, have the effect of increasing the Fund's expense ratio.

Repurchases by the Fund must be conducted in accordance with the terms and conditions contained in Article 10 of Regulation No. 8469 issued by the Puerto Rico Office of the Commissioner of Financial Institutions (the "PROCFI") and procedures adopted by the Fund's Board of Directors to address potential conflicts of interest with affiliated broker-dealers Popular Securities and UBS Financial Services Incorporated of Puerto Rico. Among other things, such regulation and procedures require that to the extent that various sellers indicate interest in selling shares of the Fund, it will purchase such shares starting with the lowest offered price and in the following order of priority for each price: (1) individual and corporate investors, irrespective of the broker-dealer that serves as record owner of the shares to be repurchased; (2) the trading desks of Puerto Rico broker-dealers which are unaffiliated with the Fund; and (3) the trading desks of Popular Securities and UBS Financial Services Incorporated of Puerto Rico. If sellers offer more shares for repurchase than the Fund is able to accept at any particular price for a particular level of priority, repurchase offers will be accepted on a pro-rata basis within that particular level of priority. Additionally, to the extent that Popular Securities or UBS Financial Services Incorporated of Puerto Rico elects to offer the Fund's shares of Common Stock for repurchase from its respective securities inventory, it must do so at its corresponding offer price per share reported to the public.

For the fiscal year ended May 31, 2016, the Fund repurchased 1,275,579 shares of its common stock in the open market. The total value of shares repurchased for the year ended May 31, 2016 amount to \$2,010,407 (at net asset value) and \$1,768,420 (at cost). Since the program's inception, the Fund has repurchased 2,379,683 shares of common stock in the open market with a net asset value of \$3,686,773 and a cost of \$3,290,087, which represent 15.95% of the total assets of the Fund as of May 31, 2014 (net of shares acquired for dividend reinvestment purposes and which remain outstanding).

GLOSSARY OF MUTUAL FUND TERMS

Bond - Security issued by a government or corporation to those from whom it has borrowed money. A bond usually promises to pay interest income to the bondholder at regular intervals and to repay the entire amount borrowed at maturity date.

Realized Gain (Loss) - The profit (loss) from the sale of securities. Realized gains are paid to fund shareholders on a per share basis. When a gain distribution is made, the fund's net asset value drops by the amount of the distribution because the distribution is no longer considered part of the fund's assets.

Dividend - A per share distribution of the income earned from the fund's portfolio holdings. When a dividend distribution is made, the fund's net asset value drops by the amount of the distribution because the distribution is no longer considered part of the fund's assets.

Interest Rate Swap - An agreement to exchange one interest rate stream for another. No principal changes hands.

Investment Adviser - An investment professional who is responsible for managing a portfolio's assets prudently and making appropriate investment decisions, such as which securities to buy, hold and sell, based on the investment objectives of the portfolio.

Leverage - Vehicle used by the Fund to increase the amounts available for investment through the issuance of commercial paper or repurchase agreements transactions.

Long-Term - An investment with a maturity greater than one year.

Mutual Fund - A company which combines the investment money of many people whose financial goals are similar, and invests that money in a variety of securities. A mutual fund allows the smaller investor the benefits of diversification, professional management and constant supervision usually available only to large investors.

Net Asset Value (NAV) Per Share - The NAV per share is determined by subtracting a fund's total liabilities from its total assets, and dividing that amount by the number of fund shares outstanding.

Offering Price - The offering price of a share of a mutual fund is the price at which the share is sold to the public.

Repurchase Agreements - Transactions in which the Fund sells securities to a bank or dealer, and agrees to repurchase them at a mutually agreed date and price.

Short-Term - An investment with a maturity of one year or less.

Total Investment Return - The change in value of a fund investment over a specified period of time, taking into account the change in a fund's market price and the reinvestment of all fund distributions.

Turnover Ratio - The turnover ratio represents the fund's level of trading activity. A fund divides the lesser of purchases or sales (expressed in dollars and excluding all securities with maturities of less than one year) by the fund's average monthly assets.

Yield - The annualized rate of income as measured against the current net asset value of fund shares.

FINANCIAL HIGHLIGHTS

The following table includes data for a share outstanding throughout each period and other performance information.

Increase (Decrease) in Net Asset Value:

	For the year ended May 31, 2016	For the year ended May 31, 2015	For the year ended May 31, 2014	For the year ended May 31, 2013	For the year ended May 31, 2012
Per Share Operating Performance:					
Net asset value, beginning of the year	\$1.55	\$1.46	\$1.64	\$1.95	\$1.97
(a) Net investment income	0.11	0.13	0.15	0.17	0.20
Net realized (loss)/gain and change in unrealized (depreciation)/appreciation on investments and derivatives	(0.02)	(0.02)	(0.23)	(0.07)	0.05
Total from investment operations	0.09	0.11	(0.08)	0.10	0.25
Less: dividends from net investment income to common shareholders	(0.01)	(0.04)	(0.08)	(0.10)	(0.14)
Less: return of capital	-	-	(0.02)	(0.31)	(0.13)
Total distributions	(0.01)	(0.04)	(0.10)	(0.41)	(0.27)
Discount on repurchase of common shares	0.04	0.02	-	-	-
Net asset value, end of the year	\$1.67	\$1.55	\$1.46	\$1.64	\$1.95
(b) Market value, end of the year	\$1.45	\$1.40	\$1.41	\$1.65	\$2.01

Total Investment

Return: (g)	3.98%	1.66%	(9.16%)	3.22%	4.81%
(b) Based on market price per share	8.17%	8.69%	(5.37%)	5.75%	14.07%
(g) Based on net asset value per share					

Ratios: (c)

(d) (f) Expenses to average net assets applicable to common shareholders - net of waived fees	1.93%	1.73%	1.20%	1.15%	0.86%
(e) (f) Operating expenses to average net assets applicable to common shareholders - net of waived fees	1.36%	1.38%	0.79%	0.71%	0.64%
Interest and leverage related expenses to average net assets applicable to common shareholders	0.57%	0.35%	0.41%	0.44%	0.32%
(f) Net investment income to average net assets applicable to common shareholders - net of waived fees	7.01%	8.30%	9.62%	10.03%	10.53%

Supplemental Data:

Net assets applicable to common shares, end of year (in thousands)	\$8,629	\$9,955	\$11,034	\$12,357	\$14,674
Portfolio turnover	0.00%	0.00%	0.00%	0.00%	0.00%
Portfolio turnover excluding the proceeds from calls and maturities of portfolio securities and the proceeds from mortgage backed securities paydowns	0.00%	0.00%	0.00%	0.00%	0.00%

(a) Based on weekly average outstanding shares of 5,519,001 and 6,848,808 for the years ended May 31, 2016 and 2015, respectively, and 7,555,000 for the years ended May 31, 2014, 2013, and 2012, respectively.

(b) The return is calculated based on market values provided by UBS Financial Services Incorporated of Puerto Rico, a dealer of the Funds shares and an affiliated party.

(c) The market values shown may reflect limited trading in the shares of the Fund in an over-the-counter market.

(d) Based on average net assets applicable to common shareholders of \$8,899,645, \$10,540,393, \$11,939,049, \$12,753,850, and \$14,351,437, for the years ended May 31, 2016, 2015, 2014, 2013, and 2012, respectively.

(e) "Expenses" include both operating and interest and leverage related expenses.

(f) "Operating expenses" represent total expenses excluding interest and leverage related expenses.

(g) The effect of the expenses waived for the years ended May 31, 2016, 2015, 2014, 2013, and 2012, was to decrease the expense ratios thus increasing the net investment income ratio to average net assets applicable to common shareholders by .95%, .96%, 1.01%, and .98%, respectively.

(h) Distributions are assumed to be reinvested at the per share net asset value as defined in the dividend reinvestment plan.

(i) Market value as of May 31, 2016, 2015, 2014, 2013, and 2012 were estimated by UBS Financial Services Incorporated of Puerto Rico, as a result of limited trading activity due to commencement of Distribution of Principal period.

(j) The estimated value considers the limited trading activity near the fiscal year end. Refer to Note 1.

The accompanying notes are an integral part of these financial statements.

SCHEDULE OF INVESTMENTS

Face Amount		Issuer	Coupon	Maturity Date	Fair Value
Puerto Rico Agencies - 77.80% of net assets applicable to common shares, total cost of \$6,364,793					
\$370,000	#	(1) (3) PUERTO RICO HOUSING FINANCE CORPORATION SERIES A, CLASS Z-2	0.00%	07/01/19	\$336,622
3,060,000	#	(1) (3) PUERTO RICO HOUSING FINANCE CORPORATION SERIES A, CLASS Z-2	0.00%	01/01/20	2,731,938
1,470,000	#	(1) (3) PUERTO RICO HOUSING FINANCE CORPORATION SERIES A, CLASS Z-2	0.00%	07/01/20	1,288,161
1,000,000	#	(1) (3) PUERTO RICO HOUSING FINANCE CORPORATION SERIES A, CLASS Z-2	0.00%	01/01/21	855,670
552,249	@	(1) (4) PUERTO RICO HOUSING FINANCE AUTHORITY SERIES A, CLASS A-1	2.96%	06/29/26	522,753
367,224	@	(1) (4) PUERTO RICO HOUSING FINANCE AUTHORITY SERIES A, CLASS A-5	3.96%	06/29/26	361,525
609,799	@	(1) (4) PUERTO RICO HOUSING FINANCE AUTHORITY SERIES A, CLASS A-9	4.96%	09/29/26	616,604
					<u>6,713,273</u>
Principal Outstanding Amount					
Puerto Rico Tax Exempt Notes - 3.97% of net assets applicable to common shares, total cost of \$316,807					
160,771		(2) COMMUNITY ENDOWMENT, INC. (COLLATERALIZED BY FGD82665)	7.50%	03/01/27	179,390
56,714		(2) COMMUNITY ENDOWMENT, INC. (COLLATERALIZED BY FN378609)	7.50%	06/01/27	61,158
96,677		(2) COMMUNITY ENDOWMENT, INC. (COLLATERALIZED BY FN398488)	7.00%	09/01/27	102,321
					<u>342,869</u>
Puerto Rico GNMA Taxable* - 34.25% of net assets applicable to common shares, total cost of \$2,618,767					
277,081	#	GNMA P&I (POOL 636571)	6.00%	07/15/23	315,222
63,750	#	GNMA P&I (POOL 593787)	6.50%	12/15/23	66,078
316,487	#	GNMA P&I (POOL 593798)	5.00%	01/15/24	355,974
213,643	#	GNMA P&I (POOL 608543)	5.00%	02/15/24	240,311
299,537	#	GNMA P&I (POOL 608618)	5.00%	06/15/24	337,328
399,489	#	GNMA P&I (POOL 636538)	5.50%	06/15/25	453,055
104,650	#	GNMA P&I (POOL 636569)	5.00%	07/15/25	116,233
284,207	#	GNMA P&I (POOL 636563)	5.50%	07/15/25	326,902
329,751	#	GNMA P&I (POOL 636587)	5.00%	09/15/25	371,211
189,832	#	GNMA P&I (POOL 636539)	5.50%	06/15/27	212,586
143,187	#	GNMA P&I (POOL 636540)	5.50%	06/15/28	160,349
					<u>2,955,249</u>
Puerto Rico GNMA Exempt* - 42.73% of net assets applicable to common shares, total cost of \$3,346,499					
67,884		GNMA SERIAL (POOL 343018) UNITS 81-100	7.50%	01/15/23	74,564
82,578		GNMA SERIAL (POOL 332132) UNITS 81-100	7.50%	02/15/23	90,704
89,240		GNMA SERIAL (POOL 334281) UNITS 81-100	7.50%	02/15/23	98,021
94,285		GNMA SERIAL (POOL 401464) UNITS 60-100	7.00%	10/15/24	104,977
168,919		GNMA SERIAL (POOL 401469) UNITS 76-100	7.00%	12/15/24	188,075
72,554		GNMA SERIAL (POOL 417913) UNITS 61-100	7.50%	09/15/25	79,693
75,000		GNMA SERIAL (POOL 425579) UNITS 83-97	6.50%	10/15/25	85,708
123,046		GNMA SERIAL (POOL 425520) UNITS 40-100	7.00%	01/15/26	137,000
60,474		GNMA SERIAL (POOL 426794) UNITS 61-100	7.50%	03/15/26	66,425
114,554		GNMA SERIAL (POOL 425536) UNITS 84-100	6.50%	04/15/26	130,909
49,296		GNMA SERIAL (POOL 425579) UNIT 100	6.50%	06/15/26	56,334
58,091		GNMA SERIAL (POOL 426805) UNITS 74-100	7.50%	08/15/26	63,807
160,459		GNMA SERIAL (POOL 448416) UNITS 70-100	7.50%	02/15/27	176,248
112,515		GNMA SERIAL (POOL 448265) UNITS 1-100	7.00%	04/15/27	125,274
95,943		GNMA SERIAL (POOL 449346) UNITS 1-100	7.00%	08/15/27	106,823
317,244		GNMA SERIAL (POOL 449347) UNITS 1-100	7.00%	08/15/27	353,220
167,294		GNMA SERIAL (POOL 449348) UNITS 1-100	7.00%	08/15/27	186,265
141,034		GNMA SERIAL (POOL 453513) UNITS 1-100	7.00%	08/15/27	157,027
164,070		GNMA SERIAL (POOL 453516) UNITS 1-100	7.00%	08/15/27	182,675
161,419		GNMA SERIAL (POOL 453519) UNITS 1-100	7.00%	08/15/27	179,724
283,817		GNMA SERIAL (POOL 453523) UNITS 1-100	7.00%	08/15/27	316,002
140,761		GNMA SERIAL (POOL 298996) UNITS 1-100	7.00%	09/15/27	156,723
500,000		GNMA SERIAL (POOL 556254) UNITS 49-80	6.50%	11/15/28	571,385
					<u>3,687,583</u>

The accompanying notes are an integral part of these financial statements.

SCHEDULE OF INVESTMENTS

(concluded)

Principal Outstanding Amount	Issuer		Coupon	Maturity Date	Fair Value
Puerto Rico Fannie Mae Taxable+ - 1.56% of net assets applicable to common shares, total cost of \$129,030					
84,172		FNMA (POOL 592607)	7.00%	11/01/24	\$88,878
9,815		FNMA (POOL 401131)	7.50%	06/01/26	9,845
30,055		FNMA (POOL 372181)	7.00%	08/01/27	30,422
4,988		FNMA (POOL 394600)	7.50%	08/01/27	5,001
					<u>134,146</u>
Puerto Rico Freddie Mac Taxable ++ - 3.73% of net assets applicable to common shares, total cost of \$285,831					
5,078		FGLMC (POOL B70087)	7.00%	03/01/23	5,411
272,014	#	FGLMC (POOL D96310)	6.00%	10/01/23	308,150
8,645		FGLMC (POOL D81387)	7.50%	07/01/27	8,675
					<u>322,236</u>
Puerto Rico Collateralized Mortgage Obligations ** - 3.11% of net assets applicable to common shares, total cost of \$260,982					
3,163	@	LEHMAN BROTHERS 1993 GRANTOR TRUST 1G	6.25%	03/24/23	3,294
257,819	@	LEHMAN BROTHERS 1993 GRANTOR TRUST 3H	5.50%	10/24/23	264,952
					<u>268,246</u>
Total investments (167.15% of net assets applicable to common shares)					\$14,423,602
Interest rate swaps (-0.29% of net assets applicable to common shares)					(25,457)
Liabilities minus other assets (-66.86% of net assets applicable to common shares)					(5,769,009)
Net Assets applicable to common shares - 100%					<u>\$8,629,136</u>

* Puerto Rico GNMA - Represents mortgage-backed obligations guaranteed by the Government National Mortgage Association. They are subject to principal paydowns as a result of prepayments or refinancing of the underlying mortgage instruments. As a result, the average life may be substantially less than the original maturity.

** Puerto Rico Collateralized mortgage obligations - These obligations are subject to principal paydowns as a result of prepayments or refinancing of the underlying mortgage instruments. As a result, the average life may be substantially less than the original maturity.

+ Puerto Rico Fannie Mae Taxable - Represents mortgage-backed obligations guaranteed by the Federal National Mortgage Association. They are subject to principal paydowns as a result of prepayments or refinancing of the underlying mortgage instruments. As a result, the average life may be substantially less than the original maturity.

++ Puerto Rico Freddie Mac Taxable - Represents mortgage-backed obligations guaranteed by the Federal Home Loan Mortgage Corporation. They are subject to principal paydowns as a result of prepayments or refinancing of the underlying mortgage instruments. As a result, the average life may be substantially less than the original maturity.

A portion or all of the security has been pledged as collateral for securities sold under agreements to repurchase.

@ Security may be called before its maturity date.

(1) Revenue Bonds - Issued by agencies and payable from revenues and other sources of income of the agency as specified in the applicable prospectus. These Bonds are not an obligation of the Commonwealth of Puerto Rico.

(2) Community Endowment - These obligations are collateralized by Mortgage-Backed Securities and the only source of repayment is the collateral. They are subject to principal paydowns as a result of prepayments or refinancing of the underlying mortgage instruments. As a result, the average life may be substantially less than the original maturity.

(3) Puerto Rico Housing Finance Authority Corporation (the "Corporation") issues these revenue bonds payable from and secured by certain mortgage-backed securities guaranteed by GNMA or issued by FNMA.

(4) Puerto Rico Housing Finance Corporation Series A, Class Z-2 are economically defeased to maturity with US Treasury Obligations, US Agencies and REFCORP Strips.

The accompanying notes are an integral part of these financial statements.

STATEMENT OF ASSETS AND LIABILITIES

Assets:			
	Investments in securities:		
	Securities pledged as collateral under repurchase agreements, at fair value (cost - \$7,726,302)	\$8,475,790	
	Other securities, at fair value (cost - \$5,596,407)	<u>5,947,812</u>	\$14,423,602
	Cash and cash equivalents		347,179
	Interest and other receivables		36,568
	Other assets		<u>1,133</u>
	Total assets		<u>14,808,482</u>
Liabilities:			
	Securities sold under agreements to repurchase		6,091,000
	Interest rate swaps, at fair value		25,457
	Payables:		
	Interest	5,634	
	Investment advisory fees	127	
	Administration fees	634	
	Dividend payable	<u>387</u>	6,782
	Accrued expenses and other liabilities		<u>56,107</u>
	Total liabilities		<u>6,179,346</u>
Net Assets Applicable to Common Shares:			<u>\$8,629,136</u>
Net Assets			
Consist of:			
	<u>Common Stock</u>		
	Capital Stock, \$0.01 par value, 100,000,000 shares authorized, 5,155,317 issued and outstanding		\$51,553
	Paid-in capital		16,472,098
	Undistributed net investment income		635,828
	Accumulated net realized loss from investments and derivatives		(9,605,779)
	Unrealized net appreciation on investments		1,100,893
	Unrealized net depreciation on derivatives		<u>(25,457)</u>
	Net assets applicable to common shares		<u>\$8,629,136</u>
	Net asset value applicable to common shares - per share; 5,155,317 shares outstanding		<u>\$1.67</u>

The accompanying notes are an integral part of these financial statements.

Puerto Rico Tax-Free Target Maturity Fund II, Inc.

STATEMENT OF OPERATIONS

		For the year ended May 31, 2016
Investment income:	Interest	\$794,931
Expenses:	Interest and leverage related expenses	50,573
	Investment advisory fees	64,098
	Administration fees	16,025
	Custodian and transfer agent fees	16,025
	Professional fees	50,683
	Insurance expense	13,510
	Directors' fees and expenses	28,000
	Printing and shareholder reports	9,620
	Other	9,269
	Total expenses	257,803
	Waived investment advisory, administration, custodian, and transfer agent fees	(86,533)
	Net expenses after waived fees	171,270
Net investment income:		623,661
Realized Gain (Loss) & Unrealized Appreciation (Depreciation) on Investments and Derivatives:	Net realized gain on investments	74,423
	Net realized loss on derivatives	(94,198)
	Unrealized depreciation on investments	(214,829)
	Unrealized appreciation on derivatives	90,859
	Net loss on investments and derivatives	(143,745)
	Net increase in net assets resulting from operations	\$479,916

The accompanying notes are an integral part of these financial statements.

Puerto Rico Tax-Free Target Maturity Fund II, Inc.

STATEMENTS OF CHANGES IN NET ASSETS

		For the year ended May 31, 2016	For the year ended May 31, 2015
Increase (Decrease) in Net Assets:			
Operations:	Net investment income	\$623,661	\$874,638
	Net realized gain (loss) on investments	74,423	(2,281,552)
	Net realized loss on derivatives	(94,198)	(1,201,548)
	Unrealized (depreciation) appreciation on investments	(214,829)	2,146,044
	Unrealized appreciation on derivatives	90,859	1,152,879
	Net increase in net assets resulting from operations	479,916	690,461
Distributions to Common Shareholders From:	Dividends from net investment income	(37,048)	(248,410)
	Repurchase of common shares	(1,768,420)	(1,521,667)
	Decrease in net assets derived from common shares transactions	(1,805,468)	(1,770,077)
Net Assets:	Net decrease in net assets attributable to common shares	(1,325,552)	(1,079,616)
	Balance at beginning of year	9,954,688	11,034,304
	Balance at end of year	\$8,629,136	\$9,954,688

The accompanying notes are an integral part of these financial statements.

Puerto Rico Tax-Free Target Maturity Fund II, Inc.

STATEMENT OF CASH FLOWS

		For the year ended May 31, 2016
Increase (Decrease) in Cash:		
Cash Provided by	Net increase in net assets from operations	\$479,916
Operating Activities:	Adjusted by:	
	Sales of portfolio securities	1,636,392
	Proceeds from mortgage-backed securities paydowns	1,324,486
	Net realized loss on paydowns	4,658
	Net realized gain on investments	(74,423)
	Unrealized depreciation on investments	214,829
	Unrealized appreciation on derivatives	(90,859)
	Accretion of discounts on investments	(244,720)
	Amortization of premiums on investments	4,645
	Decrease in interest and other receivables	12,471
	Increase in other assets	(328)
	Increase in interest payable	213
	Decrease in administration fees payable	(116)
	Decrease in investment advisory fees payable	(23)
	Increase in accrued expenses and other liabilities	5,142
	Total cash provided by operating activities	<u>3,272,283</u>
Cash Used in	Repurchase related repayments; net of issuances of \$94,590,120	(1,516,000)
Financing Activities:	Dividends to common shareholders paid in cash	(48,719)
	Repurchase of common shares	<u>(1,768,420)</u>
	Total cash used in financing activities	<u>(3,333,139)</u>
Cash:	Net decrease in cash and cash equivalents	(60,856)
	Cash and cash equivalents at beginning of year	<u>408,035</u>
	Cash and cash equivalents at end of year	<u><u>\$347,179</u></u>
Cash Flow	Cash paid for interest and leverage related expenses	<u><u>\$49,026</u></u>
Information:		

The accompanying notes are an integral part of these financial statements.

NOTES TO FINANCIAL STATEMENTS

Note 1 - Reporting Entity and Significant Accounting Policies:

Puerto Rico Tax-Free Target Maturity Fund II, Inc. (the "Fund") is a non-diversified, closed-end management investment company. The Fund is a corporation organized under the laws of the Commonwealth of Puerto Rico and is registered as an investment company under the Puerto Rico Investment Companies Act. The Fund was incorporated on June 12, 1997 and started operations on July 31, 1997.

Commencing on January 1, 2008 and up to December 31, 2028 (the "Target Date"), the Fund will distribute on a pro rata basis to its Shareholders (after deducting any amounts utilized by the Fund to repay outstanding leverage), in addition to the regular monthly distributions of net investment income and any annual distributions of net capital gains, the principal payments received by the Fund on the Fund's portfolio securities whether by maturity, prepayments, acceleration, redemption, sale or otherwise ("Distribution of Principal"). The Fund may be liquidated early depending on market conditions. The Fund intends to distribute an amount at least equal, in the aggregate, to the initial offering price of \$10 per share through Distribution of Principal. However, to the extent necessary, the Fund may use realized net capital gains, and/or the net investment income (in that order) to achieve this investment objective. Any amounts distributed by the Fund during this period will be separately designated to indicate the sources of such distribution. During this period, UBS Asset Managers of Puerto Rico and Banco Popular de Puerto Rico (collectively, "the Investment Advisers"), will not reinvest any principal payment received by the Fund on its portfolio securities, except in temporary investments pending Distribution of Principal to shareholders. There is no assurance that the Fund will be able to effect the Distributions of Principal in accordance with its objective or otherwise return an amount at least equal, in the aggregate, to the initial offering price of \$10 per share. As a fundamental policy, the Fund will not hold investments with a maturity date subsequent to December 31, 2023, except for mortgage-backed securities which will have an assumed final distribution date no later than December 31, 2028. The assumed final distribution date for mortgage-backed securities is the last date required under contractual terms.

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The following is a summary of the Fund's most significant accounting policies:

(a) Cash and Cash Equivalents - Cash and cash equivalents consist of all demand deposits and funds invested in short-term investments with original maturities of 90 days or less. Cash and cash equivalents are valued at amortized cost, which approximates fair value. At May 31, 2016, cash and cash equivalents consisted of a time deposit open account amounting to \$347,179 with Banco Popular de Puerto Rico, which is an affiliated entity.

(b) Valuation of Investments - Investments included in the Fund's financial statements have been stated at fair values as determined by Banco Popular de Puerto Rico, as the Fund's administrator, with the assistance of the Investment Advisers (Refer to Note 3), on the basis of valuations provided by dealers or by pricing services, which are approved by the Fund's management and the Board of Directors, in accordance with the valuation methods set forth in the Governing Documents and related policies and procedures. See Note 2 for further discussions regarding fair value disclosures.

(c) Taxation - The Fund has elected to be treated as a registered investment company under the Puerto Rico Internal Revenue Code of 2011, as amended, and the regulations and administrative pronouncements promulgated thereunder. As a registered investment company, the Fund will be treated as a conduit or pass-through entity that will be disregarded for Puerto Rico income tax purposes. Accordingly, the income earned by the Fund is not subject to Puerto Rico income tax at the Fund level if it distributes to its shareholders at least 90% of its taxable net investment income for the taxable year, among other requirements. The Fund has never been subject to taxation.

In addition, fixed income and equity investments of the Fund are exempt from Puerto Rico personal property taxes. The Fund is exempt from United States income taxes, except for dividends received from United States sources, which are subject to a 10% United States withholding tax, if certain requirements are met. Dividend income is recorded net of taxes.

NOTES TO FINANCIAL STATEMENTS

In the opinion of the Fund's legal counsel, the Fund is not required to file a U.S. federal income tax return.

GAAP requires the evaluation of tax positions taken or expected to be taken in the course of preparing the Fund's tax return to determine whether the tax positions are "more-likely-than-not" of being sustained by the applicable tax authority. Tax positions not deemed to meet the "more-likely-than-not" threshold are recorded as a tax benefit or expense in the current year. Management has analyzed the Fund's tax positions taken on its Puerto Rico income tax returns for all open tax years (the current and prior three tax years) and has concluded that no liability should be recorded related to uncertain tax positions taken on returns filed for the current and prior three tax years. On an ongoing basis, management will monitor the Fund's tax position to determine if adjustments to this conclusion are necessary.

The balance of undistributed net investment income, if any, and of accumulated net realized loss on investments and derivatives reflect the reclassification of permanent differences and of temporary differences between book and tax balances that become permanent. As a result of the reclassifications, these amounts shown in the Statement of Assets and Liabilities reflect the amounts for tax purposes, except for remaining temporary differences, if any (See Note 11).

(d) Statement of Cash Flows - The Fund invests in securities and distributes dividends from net investment income, which are paid in cash. These activities are reported in the Statement of Changes in Net Assets. Additional information on cash receipts and payments is presented in the Statement of Cash Flows. Accounting practices that do not affect the reporting of activities on a cash basis include carrying investments at fair value and amortizing premiums or discounts on debt obligations.

(e) Dividends and Distributions to Shareholders - Dividends from substantially all of the Fund's net investment income are declared and paid monthly. The Fund may at times pay out more or less than the entire amount of net investment income earned in any particular period and may at times pay out such accumulated undistributed income earned. The Fund records dividends and distributions to its shareholders on the ex-dividend date.

(f) Derivatives Instruments - In order to attempt to hedge various portfolio positions, to manage its cost of funds or to enhance its return, the Fund invests in certain instruments which are considered derivatives. Derivative instruments, because of their increased volatility and potential leveraging effect, may adversely affect the Fund. The use of these instruments for income enhancement purposes subjects the Fund to risk of loss which would not be offset by gains on other portfolio assets or acquisitions. There is no assurance that the Investment Advisers will employ any hedging strategy, and even where such derivatives instruments are used for hedging purposes, there can be no assurance that the hedging transactions will be successful or will not result in losses.

Specifically, the Fund enters into interest rate swap agreements that involve an agreement between two parties to exchange fixed-and-variable-rate interest rate payments that are calculated based on a specified amount of principal (the "notional principal amount") for a specified period of time. The Fund usually enters into interest rate swaps on a net basis, *i.e.*, the two payment streams are netted out), with the Fund receiving or paying, as the case may be, only the net amount of the two payments.

These types of transactions subject the Fund to the risk that a counterparty will default on its obligation to the Fund. The Fund attempts to control such risk by entering into these transactions only with banks and recognized securities dealers believed by the Fund's Investment Advisers to present minimal risk in accordance with the guidelines of the Board of Directors. These types of transactions are also subject to market risk as interest rates and market prices fluctuate. Risks may exceed related amounts recognized in the Statement of Assets and Liabilities. The credit exposure may change as the fair value of the instrument changes. The Fund's management entered into these transactions in an attempt to improve its funding costs. The Fund is currently in its distribution window, therefore Fund's management could either cancel its interest rate swaps prior to maturity or let them expire. Also, the Fund may enter into additional transactions to mitigate the cost of existing interest rate swaps as market conditions change.

NOTES TO FINANCIAL STATEMENTS

The Fund is a party to ISDA (International Swap and Derivatives Association, Inc.) Master Agreements (“Master Agreements”) with certain counterparties that govern over the counter derivative contracts entered into from time to time. The Master Agreements may contain provisions regarding, among other things, the parties’ general obligations, representations, agreements, collateral requirements, events of default, and early termination. Generally, collateral can be in the form of cash or debt securities issued by the U.S. Government or related agencies or other securities as agreed to by the Fund and the applicable counterparty. Collateral requirements are determined based on the Fund’s net position with each such counterparty. Termination events applicable to the Fund may occur in certain instances specified in the Master Agreements, which may include, among other things, a specified decline in the Fund’s net asset value or the termination of the Fund’s Investment Advisers. In each case, upon occurrence, the counterparty may elect to terminate early and cause settlement of all or some of the derivative contracts outstanding, including the payment of any losses and costs resulting from such early termination, as reasonably determined by the terminating party. Any decision by one or more of the Fund’s counterparties to elect early termination could impact the Fund’s future derivative activity.

At May 31, 2016, the Fund held derivatives in a total liability position of \$25,457 on derivative contracts subject to the Master Netting Agreements. The Fund did not receive or deliver any collateral from swap counterparties related to market valuations on the open derivative contracts at May 31, 2016.

Certain of the Fund’s derivative instruments contain provisions that require the Fund to maintain minimum net asset value levels. If the Fund’s net asset value were to decline below certain specified net asset value levels, the counterparties may declare an early termination event on any or all transactions with the Fund. If the Fund failed to maintain minimum net asset value levels on such date, the Fund’s transactions with any such counterparties may be terminated prior to their respective term. To the extent such termination resulted in a net liability to the Fund, the collateral held by any such counterparty may be liquidated and netted against the amounts owed by the Fund to such counterparty.

The Fund manages the credit component of the swaps through various mechanisms. Counterparties must have a minimum credit rating (the higher of S&P, Moody’s, and/or Fitch), or credit support from another entity. The swaps are executed pursuant to signed Master ISDA Agreements that may include a Credit Support Annex (CSA). The economic terms of each swap transaction is documented in a written confirmation. In the event the counterparty is downgraded below A, the swap must either be transferred to another A or better counterparty or the credit exposure must be collateralized with eligible collateral as defined in the CSA. Based on management’s evaluation, at May 31, 2016, no adjustment for non-performing risk is necessary.

Changes in the value of swap agreements are reported separately in the Statement of Assets and Liabilities and as unrealized net appreciation (depreciation) on derivatives in the Statement of Operations.

The Fund records periodic payments to or collections from derivative contracts as a component of net realized gain or loss on derivatives in the Statement of Operations. For the fiscal year ended May 31, 2016, the Fund made periodic payments aggregating to \$94,198 to swap counterparties. However, for purposes of dividend distributions, the Fund’s periodic swap payments are included as a component of net investment income (See Note 11).

(g) Securities Sold Under Agreements to Repurchase - Under these agreements, the Fund sells securities, receives cash in exchange and agrees to repurchase the securities at a mutually agreed date and price. Ordinarily, those counterparties with which the Fund enters into these agreements require delivery of collateral, nevertheless, the Fund retains ownership of the collateral through the agreement that requires the repurchase and return of such collateral. These transactions are treated as financings and recorded as liabilities. Therefore, no gain or loss is recognized on the transaction and the securities pledged as collateral remain recorded as assets of the Fund (See Note 6).

(h) Paydowns - Realized gains and losses on mortgage-backed securities paydowns are recorded as an adjustment to interest income as required by GAAP. For the year ended May 31, 2016, the Fund decreased interest income in the amount of \$4,658 related to realized losses on mortgage-backed securities paydowns. The Fund declares and pays

NOTES TO FINANCIAL STATEMENTS

monthly dividends from the net investment income. For purposes of dividend distributions, net investment income excludes the effect of mortgage-backed securities paydowns gains and losses (See Note 11).

(i) *Use of Estimates in the Preparation of Financial Statements* - The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

(j) *Other* - Security transactions are accounted for on the trade date (the date the order to buy or sell is executed). Realized gains and losses on security transactions are determined based on the identified cost method. Premiums and discounts on securities purchased are amortized over the life or the expected life of the respective securities using the effective interest method. Interest income is accrued daily except when collection is not expected.

(k) *Recent Accounting Pronouncements* – During fiscal year 2015, the following pronouncements were issued by the Financial Accounting Standards Board (FASB):

Accounting Standards Update No. 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent): This standard removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. It also removes the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. The standard is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. The Fund does not believe this would have a material effect on the financial statements.

Note 2 – Fair Value Measurements:

Under GAAP, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability.

GAAP establishes a fair value hierarchy that prioritizes the inputs and valuation techniques used to measure fair value into three levels in order to increase consistency and comparability in fair value measurements and disclosures. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for the fair value measurement are observable or unobservable. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect the Fund's estimates about assumptions that market participants would use in pricing the asset or liability based on the best information available. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date. Valuation on these instruments does not need a significant degree of judgment since valuations are based on quoted prices that are readily available in an active market.

Level 2 – Quoted prices other than those included in Level 1 that are observable either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or that can be corroborated by observable market data for substantially the full term of the financial instrument.

NOTES TO FINANCIAL STATEMENTS

Level 3 – Unobservable inputs are significant to the fair value measurement. Unobservable inputs reflect the Fund’s own assumptions about assumptions that market participants would use in pricing the asset or liability.

The Fund maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. The inputs or methodologies used for valuing securities are not necessarily an indication of the risk associated with investing on those securities. Fair value is based upon quoted market prices when available. If listed price or quotes are not available, the Fund employs internally developed models that primarily use market-based inputs including yield curves, interest rates, volatilities, and credit curves, among others. Valuation adjustments are limited to those necessary to ensure that the financial instrument’s fair value is adequately representative of the price that would be received or paid in the marketplace. These adjustments include amounts that reflect counterparty credit quality, constraints on liquidity and unobservable parameters that are applied consistently.

The estimated fair value may be subjective in nature and may involve uncertainties and matters of significant judgment for certain financial instruments. Changes in the underlying assumptions used in calculating fair value could significantly affect the results. In addition, the fair value estimates are based on outstanding balances without attempting to estimate the value of anticipated future business. Therefore, the estimated fair value may materially differ from the value that could actually be realized on a sale.

On November 8, 2013, the Board of Directors of the Fund delegated to the Valuation Committee, comprised of voting members of Popular Asset Management, a division of Banco Popular, and UBS Asset Managers of PR, a division of UBS Trust Company of PR, certain procedures and functions related to the valuation of portfolio securities for the purpose of determining the Net Asset Value of the Fund. The Valuation Committee is generally responsible for determining the fair value of the following types of portfolio securities:

- Portfolio instruments for which no price or value is available at the time the Fund’s NAV is calculated on a particular day;
- Portfolio instruments for which the prices or values available do not, in the judgment of the Investment Advisers, represent the fair value of the portfolio instruments;
- A price of a portfolio instrument that has not changed for four consecutive weekly pricing periods, except for Puerto Rico taxable securities and U.S. portfolio instruments;
- Any PR taxable securities and the U.S. portfolio instruments whose value has not changed from the previous weekly pricing period.

Following is a description of the Fund’s valuation methodologies used for assets and liabilities measured at fair value:

Obligations of Puerto Rico, States, and political subdivisions: Obligations of Puerto Rico, States, and political subdivisions are segregated and the like characteristics divided into specific sectors. Market inputs used in the evaluation process include all or some of the following: trades, bid price or spread, quotes, benchmark curves including but not limited to Treasury benchmarks, LIBOR and swap curves, and discount and capital rates. These bonds are generally classified as Level 2.

Puerto Rico Tax-Exempt Notes: Prices for these securities are obtained from broker quotes. These securities trade in over-the-counter markets. Quoted prices are based on recent trading activity for similar instruments and do not trade in highly liquid markets. Community Endowments are generally classified as Level 2 and the pricing is based on their collateral.

Mortgage and other asset-backed securities: Certain agency mortgage-backed securities (“MBS”) are priced based on a bond’s theoretical value from similar bonds; “similar” being defined by credit quality and market sector. Their fair value incorporates an option adjusted spread. GNMA Puerto Rico Serials are priced using a pricing matrix with quoted

NOTES TO FINANCIAL STATEMENTS

prices from local broker dealers, based on trade activity in local markets and is compared with data from exchange platforms where similar instruments regularly trade. The agency MBS and GNMA Puerto Rico Serials are generally classified as Level 2.

Collateralized mortgage obligations: Agency and private collateralized mortgage obligations (“CMOs”) are priced based on a bond’s theoretical value from similar bonds; “similar” being defined by credit quality and market sector. Their fair value incorporates an option adjusted spread. The option adjusted spread includes prepayment and volatility assumptions, ratings (whole loans collateral) and spread adjustments. The CMOs are generally classified as Level 2. CMOs that include a significant adjustment based on assumptions important to market participants, such as credit risk, source of payment, etc., are classified as Level 3.

Derivatives: The fair value of derivative instruments is based on observable market parameters and takes into consideration the credit risk component, when appropriate. The “Hull-White Interest Rate Tree” approach is used to value the option components of derivative instruments, and discounting of the cash flows is performed using US dollar LIBOR-based discount rates or yield curves that account for the industry sector and the credit rating of the counterparty and/or the Fund. Derivatives are mainly composed of interest rate swaps. As part of the determination of fair value of interest rate swaps a credit component is considered as required by GAAP. Interest rate swaps are classified as Level 2.

The following is a summary of the levels within the fair value hierarchy in which the Fund invests based on inputs used to determine the fair value of such securities:

	Hierarchy			
	Level 1	Level 2	Level 3	Balance 5/31/2016
Assets:				
Puerto Rico Agencies	\$ -	\$ 6,713,273	\$ -	\$ 6,713,273
Puerto Rico Tax Exempt Notes	-	342,869	-	342,869
Mortgage Backed Securities:				
Puerto Rico GNMA Taxable	-	2,955,249	-	2,955,249
Puerto Rico GNMA Exempt	-	3,687,583	-	3,687,583
Puerto Rico Fannie Mae Taxable	-	134,146	-	134,146
Puerto Rico Freddie Mac Taxable	-	322,236	-	322,236
Puerto Rico Collateralized Mortgage Obligations	-	-	268,246	268,246
Total	\$ -	\$ 14,155,356	\$ 268,246	\$ 14,423,602
Liabilities:				
Derivatives	\$ -	\$ 25,457	\$ -	\$ 25,457
Total	\$ -	\$ 25,457	\$ -	\$ 25,457

Temporary cash investments, if any, are valued at amortized cost, which approximates market value.

NOTES TO FINANCIAL STATEMENTS

The following is a reconciliation of assets for which Level 3 inputs were used in determining fair value:

	Balance as of 5/31/15	Change in Unrealized (depreciation)/ appreciation	Paydowns	Transfers in (out) to Level 3	Balance as of 5/31/16
Lehman Brothers Grantor Trust 1993-1G	\$ 4,332	\$ (56)	\$ (982)	\$ -	\$ 3,294
Lehman Brothers Grantor Trust 1993-3H	312,278	(1,944)	(45,382)	-	264,952
Total	\$ 316,610	\$ (2,000)	\$ (46,364)	\$ -	\$ 268,246

Quantitative Information about Level 3 Fair Value Measurements:

	Fair Value at May 31, 2016	Valuation Technique	Unobservable Inputs	Price
Lehman Brothers Grantor Trust 1993-1G	\$ 3,294	Broker Quotes	Evaluated Quotes	\$104.14
Lehman Brothers Grantor Trust 1993-3H	264,952	Broker Quotes	Evaluated Quotes	102.77

At May 31, 2016, Level 3 securities were valued based on broker-dealer indicative quotes determined using pricing models, discounted cash flows methodologies, or similar techniques, for which the determination of fair value is based on significant unobservable inputs that require significant judgment or estimation.

Changes in unrealized gains and losses included in the Statement of Operations relating to investments classified as Level 3 that are still held at May 31, 2016 amounted to a net unrealized depreciation of \$2,000.

Note 3 - Investment Advisory, Administrative, Custodian, Transfer Agency Arrangements, and Other Transactions with Affiliates:

Pursuant to separate Investment Advisory Agreements with UBS Asset Managers of Puerto Rico, a division of UBS Trust Company of Puerto Rico, and Banco Popular de Puerto Rico ("Banco Popular"), the Fund receives advisory services in exchange for a fee. The investment advisory fee is calculated at an annual rate of .40% of the Fund's average weekly net assets, as defined in the agreement. For the year ended May 31, 2016, the gross investment advisory fees amounted to \$64,098. For this calculation, average net assets include the liquidation value of all outstanding debt securities of the Fund. Total waived fees amounted to \$62,496 for a net fee of \$1,602.

Banco Popular also provides administrative, custody and transfer agency services pursuant to Administration, Custodian and Transfer Agency Agreements. Under the terms of the Administration Agreement, Banco Popular provides facilities and personnel to the Fund for the performance of the administrator duties. The fees related to these services are calculated at an annual rate of .10% of the Fund's average weekly net assets, as defined above. For the year ended May 31, 2016, the gross fees for such services amounted to \$16,025. Total waived fees amounted to \$8,012 for a net fee of \$8,013. The fees related to Custody and Transfer Agency are calculated at an annual rate of .10% of the Fund's average weekly net assets and amounted to \$16,025 for the year ended May 31, 2016. These fees were waived in their entirety.

The Fund is not registered under the U.S. Investment Company Act of 1940, as amended, and therefore is not subject to the restrictions contained therein regarding, among other things, transactions between the Fund, Banco Popular and UBS

NOTES TO FINANCIAL STATEMENTS

Financial Services Incorporated of Puerto Rico ("UBS Puerto Rico") or their affiliates ("Affiliated Transactions"). In that regard, the Board of Directors of the Fund adopted a set of procedures ("Procedures") for Affiliated Transactions in an effort to address potential conflicts of interest that may arise.

It is anticipated that Affiliated Transactions will continue to take place in the future and that any Affiliated Transactions will be subject to the Procedures adopted by the Board of Directors.

Certain officers and directors of the Fund are also officers and directors of the Investment Advisers and/or their affiliates. The six independent directors of the Fund's Board are paid based upon an agreed fee of \$1,000 per meeting. Three of the independent directors of the Fund also serve on the Fund's audit committee and are paid based upon an agreed fee of \$1,000 per committee meeting. In addition to the meetings at \$1,000 which amounted to \$27,000, the directors also met once for an audit committee meeting and once for a director committee meeting at an agreed fee of \$111 per director per meeting. For the year ended May 31, 2016, the compensation expense for the six independent directors of the Fund was \$28,000.

The affiliates of the Fund may have lending, banking, brokerage, underwriting, or other business relationships with the issuers of the securities in which the Fund invests.

The total amount (in thousands) of other affiliated and unaffiliated transactions, listed by counterparty, during the year were as follows:

	Sales of Portfolio		Securities sold under	
	Securities	%	Agreements to Repurchase	%
UBS Puerto Rico	\$ 802	49%	\$ 31,085	33%
Popular Securities, LLC	-	-	17,598	19%
Unaffiliated	834	51%	45,907	48%
Total	\$ 1,636	100%	\$ 94,590	100%

Note 4 – Capital Share Transactions:

Currently, the Fund's shares are experiencing a period of limited liquidity and/or trading at a discount to its net asset value. Although the holders of the shares do not have the right to redeem their shares inasmuch as the Fund is closed-ended, the Fund may offer a repurchase of shares in the open market, in an attempt to increase the liquidity of the shares as well as reduce any market discount from its corresponding net asset value. There is no assurance that, if such action is undertaken, it will result in the improvement of the shares' liquidity or reducing any such market discount. The Fund's policies require that repurchase of shares from an affiliated party be effected in accordance with procedures to address any conflicts of interest which may arise.

On January 31, 2014, the Board of Directors authorized the repurchase by the Fund of outstanding shares of Common Stock (the "Shares") in open-market transactions up to an aggregate dollar amount of shares to be repurchased of up to 25% of the Fund's total assets, at share prices equal to or at a discount of the corresponding net asset value ("NAV") per share. As of May 31, 2016, 9.05% of total assets are still available to be repurchased.

NOTES TO FINANCIAL STATEMENTS

For the year ended May 31, 2016, the total value of repurchase of common stock by the Fund was as follows:

Counterparty	Shares	Net Asset Value	Cost
Affiliates	1,219,913	\$ 1,923,363	\$ 1,694,307
Unaffiliated	55,666	87,044	74,113
Total	1,275,579	\$ 2,010,407	\$1,768,420

The shares repurchased from affiliates include shares held by clients in such affiliate.

The repurchase of shares resulted in a NAV increase of \$0.04.

Capital share transactions for the years ended May 31, 2016 and 2015, were as follows:

	Dollar Amount	
	2016	2015
<u>Common shares:</u>		
Dividends declared	\$ (37,048)	\$ (248,410)
Repurchase of common shares	(1,768,420)	(1,521,667)
Decrease in net assets derived from common shares transactions	<u>\$(1,805,468)</u>	<u>\$(1,770,077)</u>

The Fund is authorized to issue up to 100,000,000 shares of common stock, par value \$0.01 per share.

Common share transactions for the years ended May 31, 2016 and 2015, were as follows:

	Number of Shares	
	2016	2015
<u>Common shares:</u>		
Beginning balance	6,430,896	7,535,000
Repurchase of common shares	(1,275,579)	(1,104,104)
Ending balance	<u>5,155,317</u>	<u>6,430,896</u>

NOTES TO FINANCIAL STATEMENTS

Note 5 - Investment Transactions:

The proceeds from sales and paydowns of portfolio securities (in thousands), excluding short-term transactions, for the year ended May 31, 2016 were as follows:

	Sales	Paydowns
Puerto Rico Agencies	\$ -	\$ 136
Puerto Rico Tax-Exempt Notes	-	30
Puerto Rico GNMA Taxable	-	426
Puerto Rico GNMA Exempt	-	467
Puerto Rico Fannie Mae Taxable	1,636	184
Puerto Rico Freddie Mac Taxable	-	35
Puerto Rico Collateralized Mortgage Obligations	-	46
Total	\$ 1,636	\$ 1,324

The following table presents the value of the swap agreements held as of May 31, 2016, detailed by primary risk exposure and their respective location on the Statement of Assets and Liabilities:

Counterparty	Notional Amount (#)	Fund to Receive		Fund to Pay		Expiration Date	Fair Value
		Rate at 5/31/16	Type	Rate at 5/31/16	Type		
Interest Rate Contracts:							
Barclays Bank PLC, UK	\$2,400	0.43%	V##	4.23%	F	09/15/2016*	\$ (25,457)

F Fixed

V Variable, applicable for period 5/16/16 to 6/15/16.

1 month LIBOR BBA, fixing date 5/12/16.

Amount in thousands of dollars.

* Counterparties have the option to terminate the swaps on a quarterly basis on the date specified in the swap agreement.

The Fund's average notional balance of interest rate swaps during the period was \$2,400,000 for pay fixed-rate swaps.

Interest payable on swap agreements amounted to \$2,247 at May 31, 2016.

The following tables present the effect of swap agreements on the Statement of Operations for the year ended May 31, 2016, by primary underlying risk exposure:

Amount of realized loss on swap agreements recognized in income (1):

Derivative contract:	Realized loss
Interest rate contracts	\$ (94,198)

(1) Refer to Note 11 for a reconciliation of the accounting treatment of realized gain (loss) for tax purposes.

NOTES TO FINANCIAL STATEMENTS

Unrealized appreciation on swap agreements recognized in income:

Derivative contract:	<u>Unrealized appreciation</u>
Interest rate contracts	\$ 90,859

The following table presents the Fund's swaps by counterparty and the related collateral pledged by the Fund at May 31, 2016:

Counterparty	Gross Amount of Swap Presented in the Statement of Assets and Liabilities	Swap Available for Offset	Collateral Posted (a)	Net Amount Due to Counterparty (not less than zero)
Barclays Bank PLC, UK	\$ 25,457	\$ -	\$ -	\$ 25,457

(a) Collateral received or posted is limited to the net swap liability amount.

Note 6 - Securities Sold under Agreements to Repurchase:

Weighted average interest rate at end of year	<u>0.71%</u>
Maximum aggregate balance outstanding at any time during the year	<u>\$7,683,848</u>
Average balance outstanding during the year	<u>\$7,011,037</u>
Average interest rate during the year	<u>0.71%</u>

At May 31, 2016, the interest rates on securities sold under agreements to repurchase ranged from 0.63% to 0.85% with maturities up to June 2, 2016. Some of the outstanding agreements to repurchase as of year end may be called by the counterparty before their maturity date.

At May 31, 2016, investment securities amounting to \$8,475,790 are pledged as collateral for securities sold under agreements to repurchase. The counterparties have the right to sell or repledge the assets during the term of the repurchase agreement with the Fund. Interest payable on securities sold under agreements to repurchase amounted to \$3,387 at May 31, 2016.

At May 31, 2016, the total amounts (in thousands) of affiliated and unaffiliated securities sold under agreements to repurchase were as follows:

Counterparty	Amount	%
Puerto Rico Short-Term Investments Fund, Inc. (1)	\$ 3,085	51%
Unaffiliated	3,006	49%
Total	\$ 6,091	100%

(1)A Fund managed by UBS Asset Managers of Puerto Rico.

NOTES TO FINANCIAL STATEMENTS

U.S. GAAP requires an entity to disclose information about offsetting and related arrangements to enable users of that entity's financial statements to understand the effect of those arrangements on its financial position. The Fund is subject to master netting agreements or similar arrangements that allow for amounts owed between the Fund and a counterparty to be netted upon an early termination. The party that has the larger payable pays the excess of the larger amount over the smaller amount to the other party. The master netting agreements or similar arrangements do not apply to amounts owed to/from different counterparties.

The following table presents the Fund's repurchase agreements by counterparty and the related collateral pledged by the Fund at May 31, 2016:

Counterparty	Gross Amount of Securities Sold Under Repurchase Agreements	Securities Sold Under Repurchase Agreements Available for Offset	Net amount of Repurchase Agreements presented in the Statement of Assets and Liabilities	Collateral Posted (a)	Net Amount Due to Counterparty (not less than zero)
PR Short-Term Investments Fund, Inc.	\$ 3,085	\$ -	\$ 3,085	\$ 3,085	\$ -
Goldman Sachs, NY	3,006	-	3,006	3,006	-
Total	\$ 6,091	\$ -	\$ 6,091	\$ 6,091	\$ -

(a) Collateral received or posted is limited to the net securities sold under repurchase agreements liability amounts.

Note 7 – Short-Term Financial Instruments:

The fair market value of short-term financial instruments, which include \$6,091,000 in securities sold under agreements to repurchase, are substantially the same as the carrying amounts reflected in the Statement of Assets and Liabilities as these are reasonable estimates of fair values, given the relatively short period of time between origination of the instrument and their expected realization. There were no long-term financial instruments outstanding at May 31, 2016.

Note 8 – Credit Facility:

The Fund has available with Banco Popular de Puerto Rico (an affiliate of one of the Investment Advisers) an uncommitted line of credit that is part of a credit facility extended to the Puerto Rico Investors Family of Funds and the Popular Family of Funds. The proceeds of the credit advances will be exclusively used by the Borrower for short term funding needs arising from failed repurchase agreement transactions or cash shortfalls due to the non-receipt by the Borrower of payments in the settlement process of transactions to which the Borrower is a party. During the year ended May 31, 2016, the Fund borrowed from the line of credit as follows:

Weighted average interest rate at end of year	<u>N/A</u>
Maximum aggregate balance outstanding at any time during the year	<u>\$403,000</u>
Average balance during the period outstanding	<u>\$403,000</u>
Average interest rate during the period outstanding	<u>2.78%</u>

The Fund can obtain credit advances not to exceed the lesser of \$8,000,000 or ten percent (10%) of Banco Popular's capital stock and surplus, provided that the aggregate sum of all outstanding balances under all credit facilities never exceeds \$200,000,000. Interest on the unpaid balance of each credit advance accrues at a rate of 2.25% over the one week LIBOR Rate and will be payable on the dates set forth in each credit facility note. As of May 31, 2016, the Fund had no outstanding balance and had the complete credit facility available for drawing, subject to the limitations described above.

NOTES TO FINANCIAL STATEMENTS

Note 9 - Concentration of Credit Risk:

Concentrations of credit risk (whether on or off balance sheet) that arise from financial instruments exist for groups of customers or counterparties when they have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

The major concentration of credit risk arises from the Fund's investment securities in relation to the location of issuers. For calculation of concentration, all fixed-income securities guaranteed by the U.S. Government are excluded. At May 31, 2016, the Fund had investments with an aggregate market value of \$7,780,770 which were issued by entities located in the Commonwealth of Puerto Rico and are not guaranteed by the U.S. Government. In addition, at May 31, 2016, the Fund had investments with market values amounting to \$5,212,391 and \$1,500,882, respectively, which were each issued by one issuer located in the Commonwealth of Puerto Rico and are not guaranteed by the Puerto Rico Government.

As stated in the Prospectus, the Fund will ordinarily invest at least 67% of its total assets in Puerto Rico obligations (the "67% Investment Requirement"). Therefore, to the extent the securities are not guaranteed by the U.S. Government or any of its subdivisions, the Fund is more susceptible to factors adversely affecting issuers of Puerto Rico obligations than an investment company that is not concentrated in Puerto Rico obligations to such degree.

Note 10 - Investment and Other Requirements and Limitations:

The Fund is subject to certain requirements and limitations related to investments and leverage. Some of these requirements and limitations are imposed statutorily or by regulation while others are imposed by procedures established by the Board of Directors. The most significant requirements and limitations are discussed below.

Upon reaching its corresponding Distribution Commencement Date (January 1, 2008), the 67% Investment Requirement ceased to apply to the Fund, provided it distributes all principal payments, whether by maturity, prepayments, acceleration, redemption, sale or otherwise, to its Common Stockholders as described in the Fund's offering document.

The Fund's leverage, as measured by the ratio of total assets, may not exceed 50%. Should this ratio be exceeded, the Fund is precluded from payment of dividends and further leverage transactions until the maximum 50% ratio is restored.

Note 11 - Reconciliation between Net Investment Income and Distributable Net Investment Income for Tax Purposes and Net Realized Gain on Investments and Derivatives and Net Realized Gain on Investments and Derivatives for Income Tax Purposes:

As a result of certain reclassifications made for financial statement presentation, the Fund's net investment income and net realized gain on investments and derivatives reflected in the financial statements differ from distributable net investment income and net realized gain on investments and derivatives for income tax purposes, respectively, as follows:

Net investment income	\$ 623,661
Reclassification of realized loss on securities' paydowns	4,658
Reclassification of swap net periodic payments	(94,198)
Distributable net investment income for tax purposes	<u>\$ 534,121</u>

NOTES TO FINANCIAL STATEMENTS

Net realized loss on investments and derivatives	\$ (19,775)
Reclassification of realized loss on securities' paydowns	(4,658)
Reclassification of swap net periodic payments	94,198
Net realized gain on investments and derivatives, for tax purposes	<u>\$ 69,765</u>

The undistributed net investment income and accumulated net realized loss on investments and derivatives (for tax purposes) at May 31, 2016 were as follows:

Undistributed net investment income, beginning of the year	\$ 138,755
Distributable net investment income for the year	534,121
Dividends	<u>(37,048)</u>
Undistributed net investment income, end of the year	<u>\$ 635,828</u>
Accumulated net realized loss on investments and derivatives, beginning of the year	\$ (9,675,544)
Net realized gain on investments and derivatives, for the year	<u>69,765</u>
Accumulated net realized loss on investments and derivatives, end of the year	<u>\$ (9,605,779)</u>

Note 12 - Indemnification:

In the normal course of business, the Fund enters into contracts that contain a variety of indemnifications. The Fund's maximum exposure under these agreements is unknown. However, the Fund has not incurred or paid prior claims or losses pursuant to these contracts and expects the risk of losses to be remote.

Note 13 – Risks and Uncertainties:

The Fund is exposed to various types of risks, such as geographic concentration, industry concentration, non-diversification, interest rate, and credit risks, among others. This list is qualified in its entirety by reference to the more detailed information provided in the offering documentation for the securities issued by the Fund.

The Fund is exposed to certain risks resulting from the reduced geographic diversification of its portfolio. The Fund's assets are invested primarily in securities of Puerto Rico issuers. Consequently, the Fund in general is more susceptible to economic, political, regulatory, or other factors adversely affecting issuers in Puerto Rico than an investment company that is not so concentrated in Puerto Rico issuers.

A relatively high percentage of the Fund's assets may be invested in obligations of a limited number of Puerto Rico issuers. Consequently, the Fund's net asset value and its yield may increase or decrease more than that of a more diversified investment company as a result of changes in the market's assessment of the financial condition and prospects of such Puerto Rico issuers. The Fund may also be more susceptible to any single economic, political, or regulatory occurrence in Puerto Rico than a more widely diversified investment company.

Interest rate risk is the risk that interest rates will rise so that the value of existing fixed rate securities will fall. The current low long-term rates present the risk that interest rates may rise and that as a result the Fund's investments will decline in value. Also, the Fund's yield will tend to lag behind changes in prevailing short-term interest rates. In addition, during periods of rising interest rates, the average life of certain types of securities may be extended because of the right of the issuer to defer payments or make slower than expected principal payments. This may lock-in a below market interest rate, increase the security's duration (the estimated period until the security is paid in full), and reduce the value of the security. This is known as extension risk, which the Fund is also subject to. Conversely, during periods

NOTES TO FINANCIAL STATEMENTS

of declining interest rates, the issuer of a security may exercise its option to prepay principal earlier than scheduled in order to refinance at lower interest rates, forcing the Fund to reinvest in lower yielding securities. This is known as prepayment risk, which the Fund is also subject to.

Credit risk is the risk that debt securities in the Fund's portfolio will decline in price or fail to make dividend or interest payments when due because the issuer of the security experiences a decline in its financial condition. The risk is greater in the case of securities rated below investment grade, or rated in the lowest investment grade category.

The Fund may engage in repurchase agreements, which are transactions in which the Fund sells a security to a counterparty and agrees to buy it back at a specified time and price in a specified currency. Repurchase agreements involve the risk that the buyer of the securities sold by the Fund might be unable to deliver the securities when the Fund seeks to repurchase them and may be unable to replace the securities or only at a higher cost.

Mortgage-backed securities in which the Fund may invest have many of the risks of traditional debt securities but, in general, differ from investments in traditional debt securities in that, among other things, principal may be prepaid at any time due to prepayments by the obligors on the underlying obligations. As a result, the Fund may receive principal repayments on these securities earlier or later than anticipated by the Fund. In the event of prepayments that are received earlier than anticipated, the Fund may be required to reinvest such prepayments at rates that are lower than the anticipated yield of the prepaid obligation. The rate of prepayments is influenced by a variety of economic, geographic, demographic, and other factors, including, among others, prevailing mortgage interest rates, local and regional economic conditions, and home owner mobility. Since a substantial portion of the assets of the Fund may be invested in mortgage-backed securities at any time, the Fund may be subject to these risks and other risks related to such securities to a significant degree, which might cause the market value of the Fund's investments to fluctuate more than otherwise would be the case. Collateralized mortgage obligations or "CMOs" exhibit similar risks to those of mortgage-backed securities but also present certain special risks. CMO classes may be specially structured in a manner that provides a variety of investment characteristics, such as yield, effective maturity, and interest rate sensitivity. As market conditions change, however, particularly during periods of rapid or unanticipated changes in interest rates, the ability of a CMO class to provide the anticipated investment characteristics and performance may be significantly reduced. These changes may result in volatility in the market value, and in some instances, reduced liquidity of the CMO class.

The Fund may also invest in illiquid securities which are securities that cannot be sold within a reasonable period of time, not to exceed seven days, in the ordinary course of business at approximately the amount at which the Fund has valued the securities. There presently are a limited number of participants in the market for certain Puerto Rico securities or other securities or assets that the Fund may own. That and other factors may cause certain securities to have periods of illiquidity. Illiquid securities may trade at a discount from comparable, more liquid investments.

There may be few or no dealers making a market in certain securities owned by the Fund, particularly with respect to securities of Puerto Rico issuers including, but not limited to, investment companies. Dealers making a market in those securities may not be willing to provide quotations on a regular basis to the Investment Adviser. It may, therefore, be particularly difficult to value those securities.

In order to attempt to hedge various portfolio positions or to enhance its return, the Fund may invest a portion of its total assets in certain instruments which are or may be considered derivatives. Because of their increased volatility and potential leveraging effect (without being subject to the Fund's leverage limitations), derivative instruments may adversely affect the Fund. For example, investments in indexed securities, including, among other things, securities linked to an equities or commodities index and inverse floating rate securities, may subject the Fund to the risks associated with changes in the particular indices, which may include reduced or eliminated interest payments and losses of invested principal. Such investments, in effect, may also be leveraged, thereby magnifying the risk of loss.

NOTES TO FINANCIAL STATEMENTS

Note 14 - Subsequent events:

On June 30, 2016, the Board of Directors declared an ordinary net investment income dividend of \$0.000075 per common share, totaling \$387 which was paid on July 11, 2016 to common shareholders of record as of June 30, 2016.

On July 28, 2016, the Board of Directors declared an ordinary net investment income dividend of \$0.000075 per common share, totaling \$387 which was paid on August 10, 2016 to common shareholders of record as of July 29, 2016.

The Fund has performed an evaluation of events occurring subsequent to May 31, 2016 through August 19, 2016, which is the date the financial statements were available to be issued. Management has determined that there were no events occurring in this period that required disclosure in or adjustment to the accompanying financial statements, other than those disclosed above.



Independent Auditor's Report

To the Board of Directors and Stockholders of
Puerto Rico Tax-Free Target Maturity Fund II, Inc.

We have audited the accompanying financial statements of the Puerto Rico Tax-Free Target Maturity Fund II, Inc. (the "Fund"), which comprise the statement of assets and liabilities, including the schedule of investments, as of May 31, 2016 and the related statements of operations and of cash flows for the year then ended, of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the five years in the period then ended. These financial statements and financial highlights are hereafter collectively referred to as "financial statements."

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Fund's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Puerto Rico Tax-Free Target Maturity Fund II, Inc. at May 31, 2016, and the results of its operations and its cash flows for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the five years in the period then ended, in accordance with accounting principles generally accepted in the United States of America.

San Juan, Puerto Rico
August 19, 2016

CERTIFIED PUBLIC ACCOUNTANTS
(OF PUERTO RICO)
License No. LLP-216 Expires Dec. 1, 2016
Stamp E246253 of the P.R. Society of
Certified Public Accountants has been
affixed to the file copy of this report

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Luis M. Pellot
Director

Leslie Highley, Jr.
Senior Vice President

Carlos V. Ubiñas
Executive Vice President

Héctor Rivera Rivera
Treasurer

Illich Colón
Secretary

Remember that:

- *Mutual Funds Shares are not bank deposits or FDIC insured.*
- *Mutual Funds Shares are not obligations of or guaranteed by Banco Popular de Puerto Rico or UBS Financial Services Incorporated of Puerto Rico or any of their affiliates.*
- *Mutual Funds Shares are subject to investment risks, including possible loss of the principal amount invested.*