RESERVE BANK OF FIJI

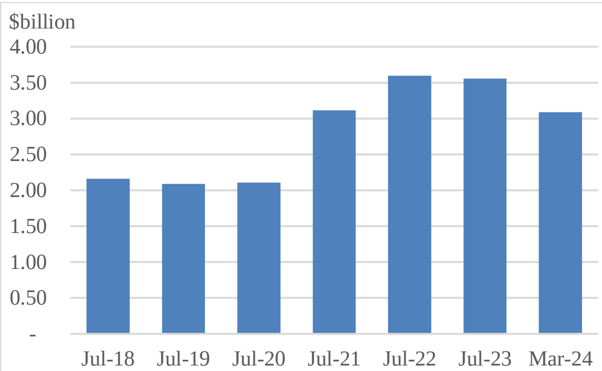
MANAGING FOREIGN RESERVES IN FIJI

Introduction

Most countries have to hold and manage foreign exchange reserves for various reasons. According to the International Monetary Fund, foreign reserves consist of official public sector foreign assets readily available to and controlled by the monetary authorities. Like most countries, the Reserve Bank of Fiji (RBF) maintains a portfolio of foreign reserves on behalf of the country to fund the international trade of goods and services, finance Fiji's external obligations, and serve its policy objectives. Foreign reserves are essential for preserving external stability, particularly maintaining our exchange rate peg.

Currently (28/03/24), the RBF holds the equivalent of F$3.1 billion in foreign reserves, comprising investible and non-investible reserves. Investible reserves are actively invested in the currencies of Fiji's major trading partner economies and are also readily available for immediate needs. RBF's non-investible reserves are earmarked for specific purposes, comprising the British Pound, IMF's Special Drawing Rights (SDR) and minimal portions of gold.

Figure 1: Foreign Reserves (RBF Holdings)



Acquiring Foreign Reserves

As a small and open economy that depends on other countries for goods and services and whose currency is not widely used internationally, Fiji needs to have an adequate supply of foreign currencies to pay for import and foreign debt commitments as well as fund other obligations, such as facilitating transactions by our people who need foreign currencies to send or travel abroad.

We can imagine what would happen if Fiji could not import essential items like medicine and food if no foreign reserves were available to pay for the imports. To ensure the orderly flow of goods and services and the movement of people across Fiji's borders, we need to have an adequate supply of foreign reserves readily available to fund amounts required for foreign payments.

The Reserve Bank accumulates the supply of foreign reserves from limited sources. These include funds received from Fiji's exports receipts from tourists who visit our shores, relatives and workers who live abroad (remittances), investments in Fiji made by foreign companies as well as countries and organisations that lend to Fiji. This is then netted off against payments for our imports, debts and other external obligations.

Foreign Reserves Management

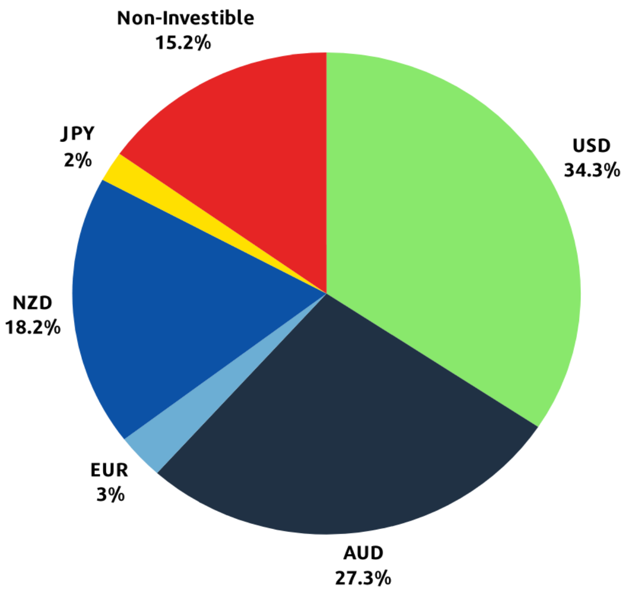
Given that Fiji's foreign reserves represent a major national asset and serve the RBF's policy objectives, managing these funds is an integral function of the Bank. Poor management of foreign reserves would risk major financial loss on the assets held and could cripple economic activity and cause financial instability. The process of reserves management is carried out across three units at the Bank to ensure strict separation of duties to manage risk and ensure compliance.

Reserves management is undertaken with the objectives of preserving safety and value, ensuring adequate availability and optimising income in order of priority. This presents the Bank with the complex task of managing the trade-off between risk and return by investing in low-risk assets that can be readily liquidated with a reasonable rate of return.

The RBF monitors global financial markets, economic trends, and geopolitical developments to guide investment decisions. Market analysis includes assessing factors such as interest rate movements, inflation expectations, and credit conditions to identify opportunities and risks in the investment environment.

To minimise losses against currency fluctuation in the international market, our reserve holdings are aligned closely to the composition of the Fiji dollar basket weights. As a result, most of Fiji's foreign reserves are held in the US currency, followed by the AUD, NZD, JPY and the Euro currencies.

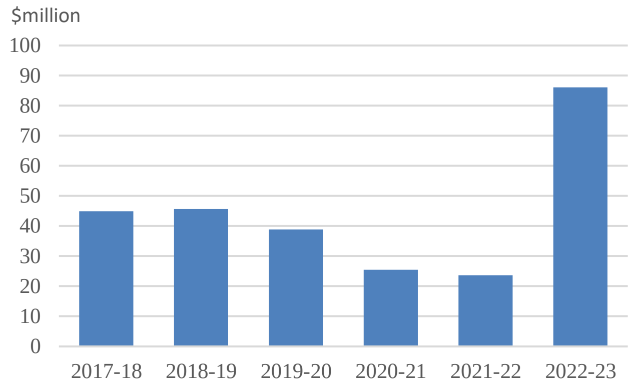
Figure 2: Currency Composition of Fiji's Foreign Reserves as at end of December 2023



To ensure that reserves are safe, funds are invested in high-quality assets with a wide range of issuers. Like other central banks, the RBF monitors credit ratings to manage the risk of loss from counterparty defaults and uses a robust daily process to monitor eligible issuers and exposures. Strong considerations are also placed on highly liquid instruments with an optimal level of duration or maturity to manage market risk.

Once the Bank is content with the safety and liquidity of foreign reserves, the focus is tilted to maximising return and income, which also adds to the accumulation of foreign reserves. To gauge how well the investment portfolio performs, the RBF compares its actual reserve holdings against a hypothetical portfolio called the benchmark, which represents the best passive strategy for the Bank given the level of risks. Over the years, the RBF reserves portfolio has generally outperformed the benchmark. At the end of the last fiscal year (2022-23), net foreign exchange income rose to an all-time high of $86.1 million, from $23.7 million in the previous year. This formed a significant portion of the $103.4 million in profits transferred to the Government last year. The notable increase in income reflected prudent management of foreign reserves and investments executed at high yields amidst the period of global central banks' monetary tightening. Moving forward, the RBF is on track to achieve another record year in income in this financial year, given the current level of reserves and elevated interest rates.

Figure 3: RBF Net Foreign Reserves Income



In recent years, Environmental, Social and Governance (ESG) factors have gained prominence in foreign reserves management. The Bank recognises the importance of aligning its investments with sustainable practices and sets a minimum threshold of 4.0 percent of investible reserves towards ESG investments. Currently, the RBF's exposure to ESG fixedincome bonds stands at around 12.0 percent of investible reserves.

The Bank's management of foreign reserves is continually evolving, and processes are reviewed periodically while new strategies are adopted.

Reserve Bank of Fiji
04 April 2024