



AZƏRBAYCAN RESPUBLİKASININ  
**MƏRKƏZİ BANKI**



## Reserve Management: Trends and Challenges

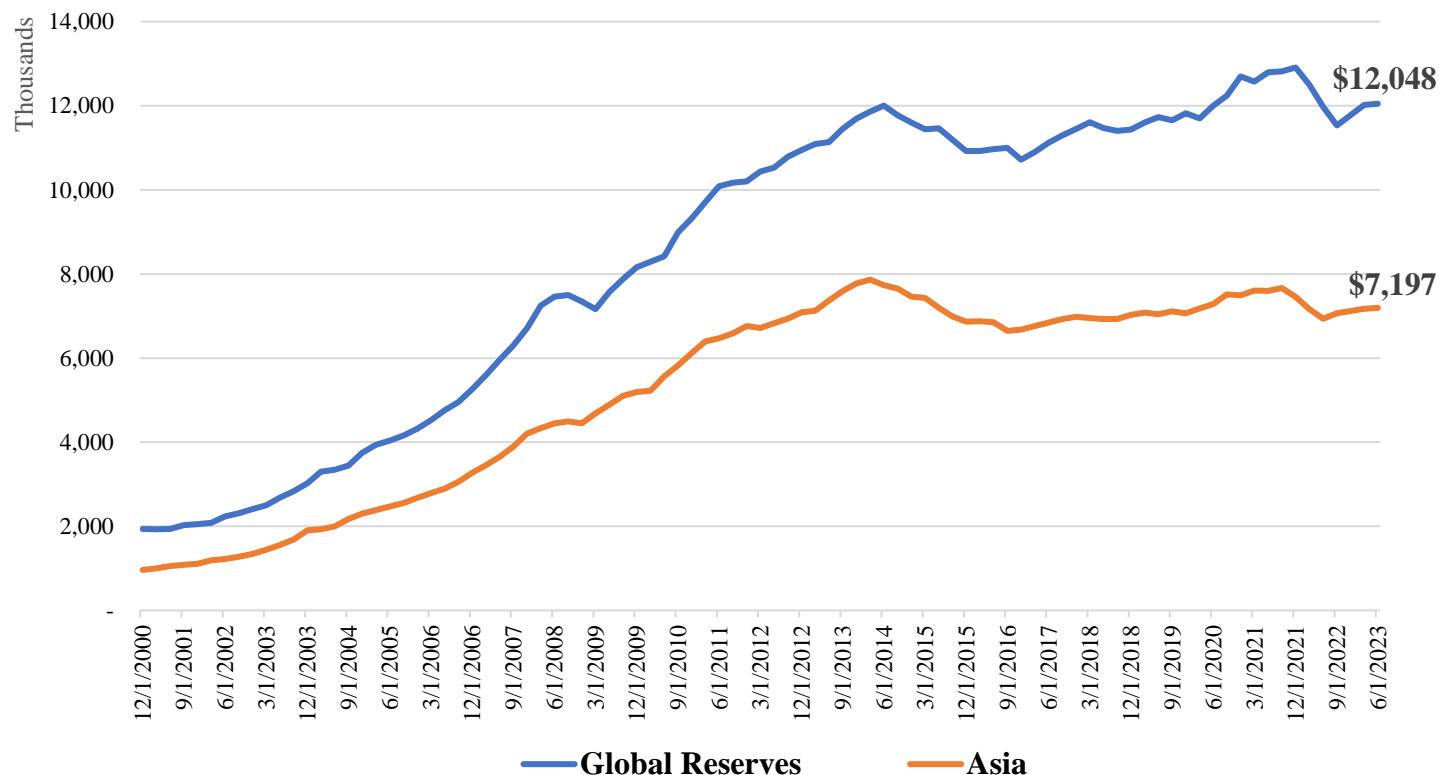
**Tarlan Rasulov**

**2023 Asian Regional Forum on Investment Management of  
Foreign Exchange Reserves,**

**October 25-27, 2023, Bali, Indonesia**

# Increasing FX reserves

## Global Foreign Currency Reserves



Source: IMF Statistics, Bloomberg

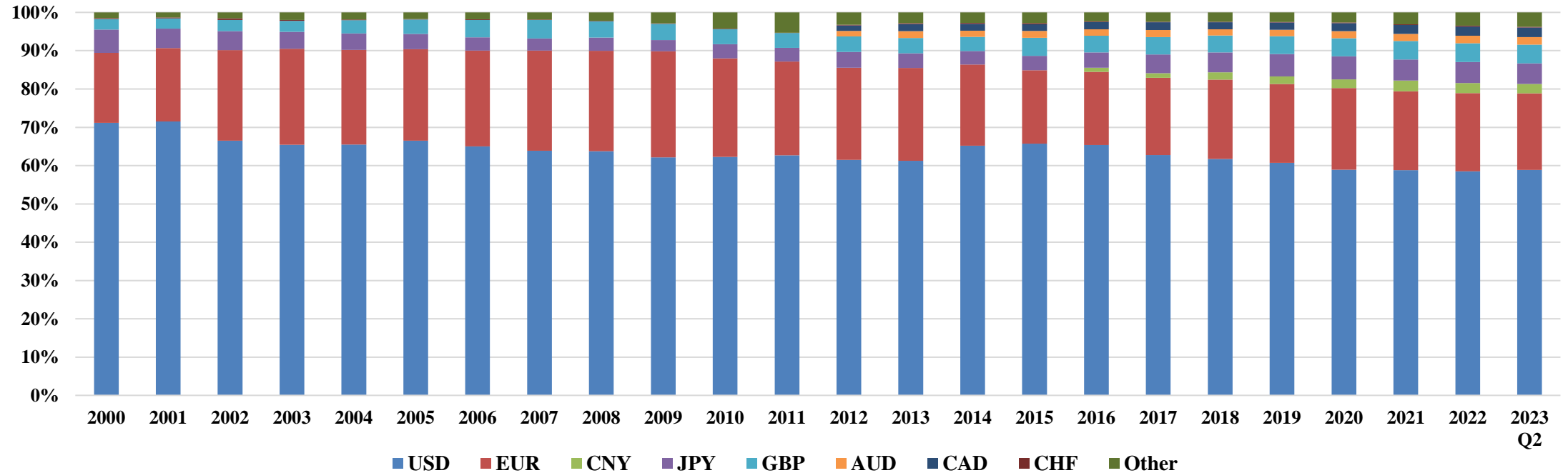
## Top 10 countries

No	Country	FX Reserves mln.\$	Δ 2023 YTD mln. \$
1	China	\$3,192,998	\$65,307
2	Japan	\$1,126,104	\$17,915
3	Switzerland	\$808,190	-\$40,320
4	Taiwan	\$564,830	\$9,900
5	India	\$527,979	\$29,957
6	Saudi Arabia	\$417,924	-\$16,956
7	Hong Kong	\$417,153	-\$6,751
8	Russia	\$411,329	-\$6,477
9	South Korea	\$397,202	-\$1,841
10	Brazil	\$312,590	\$18,737
		<b>\$8,176,300</b>	<b>\$69,471</b>

- ❖ Global Foreign Exchange Reserves continues to accumulate after a drop from 2021 peak level.
- ❖ Reserves of Asia countries are in line with global trend.

# De-dollarization kicks in?

## Currency composition of Official Foreign Exchange Reserves

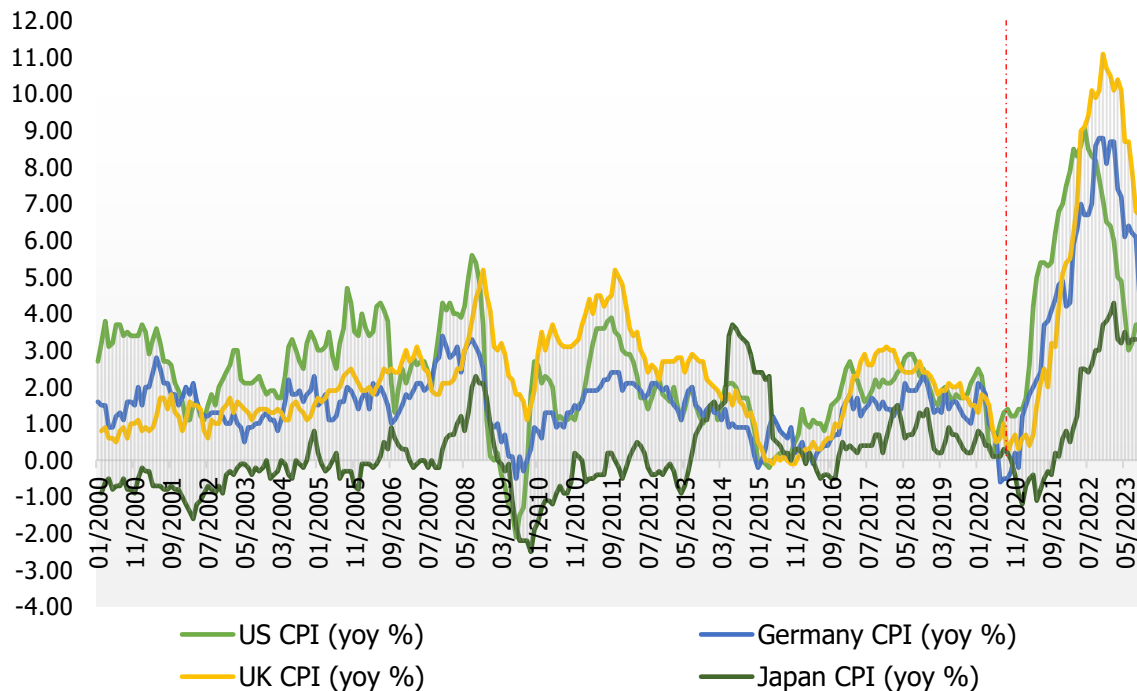


Source: IMF, Currency Composition of Official Foreign Exchange Reserves (COFER)

- ❖ For the last 3 years portion of US dollar fell below 60%.
- ❖ More currency diversification as a result of weaponization of finance?

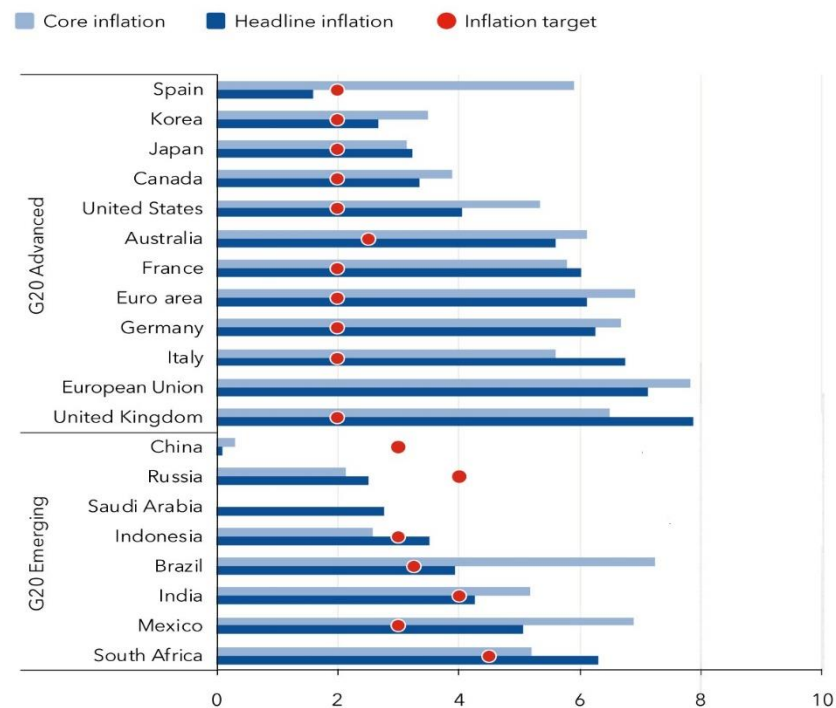
# Inflationary market environment – Regime change?

Global inflation rates



Source: Bloomberg

Headline and Core inflation (percent; yoy; as of May/June 2023)

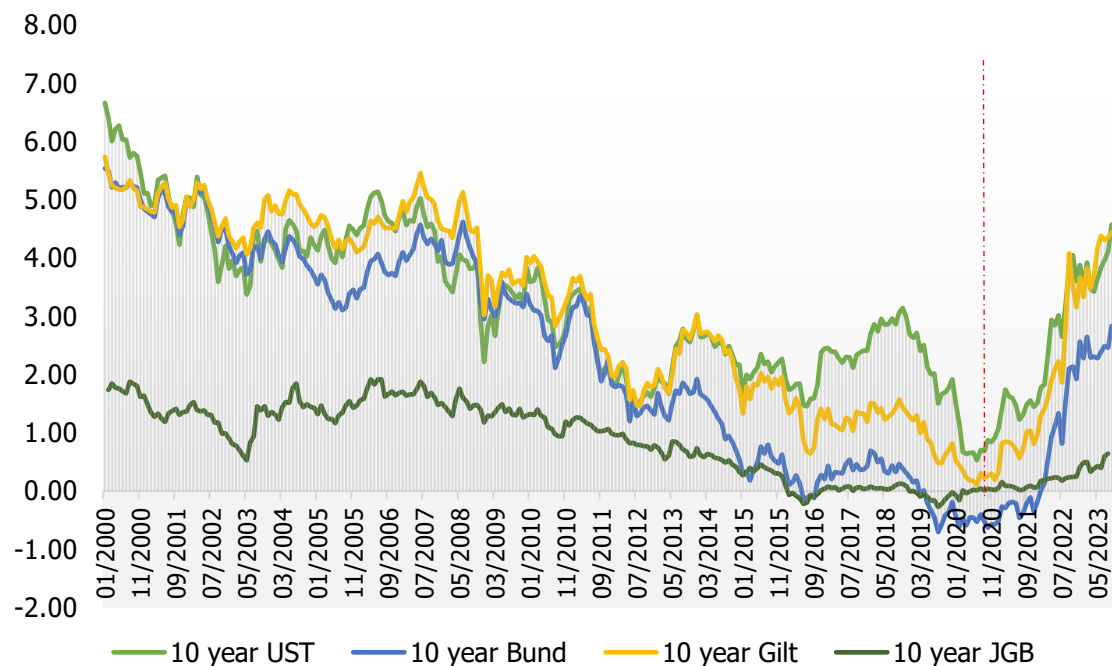


Source: IMF

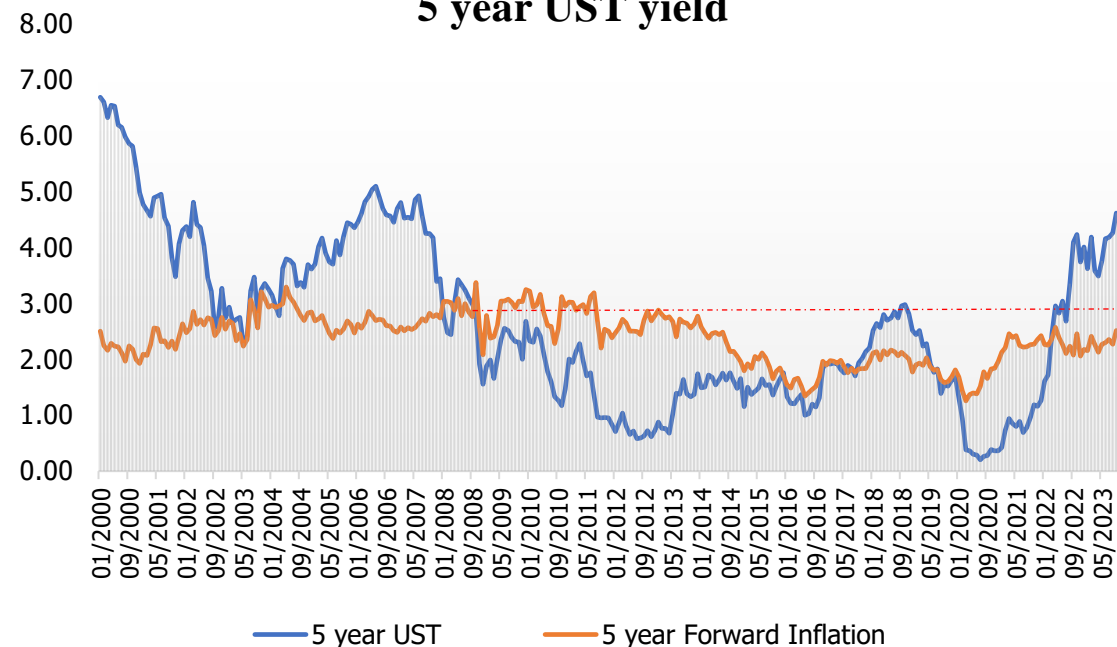
- ❖ In most G20 countries inflation remains well above central banks' targets.
- ❖ Inflation continues to fall, but it is not expected it to return to levels targeted by central banks until 2025.

# Inflation expectations and real return opportunities

## Global sovereign rates



## Fed's 5 year inflation expectations and 5 year UST yield

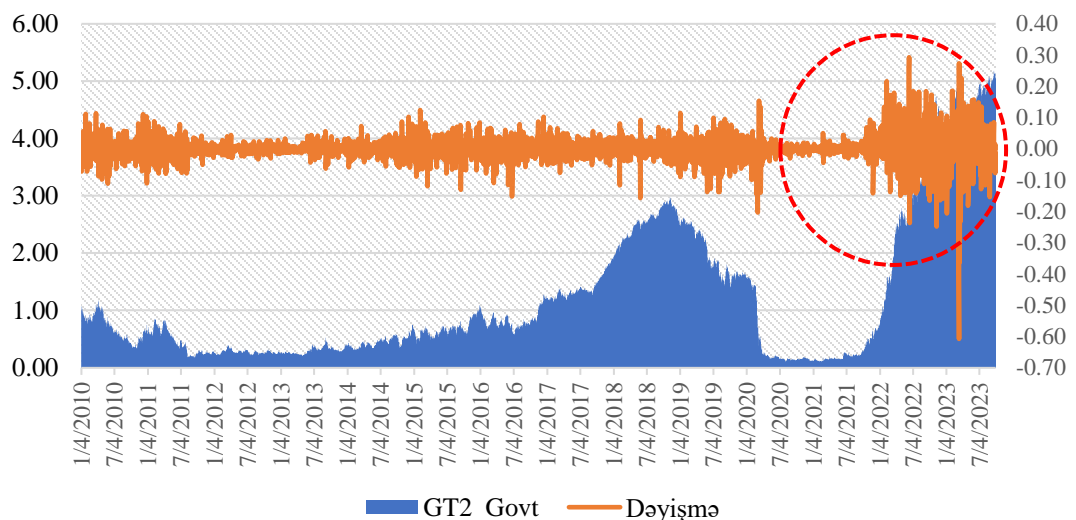


Source: Bloomberg

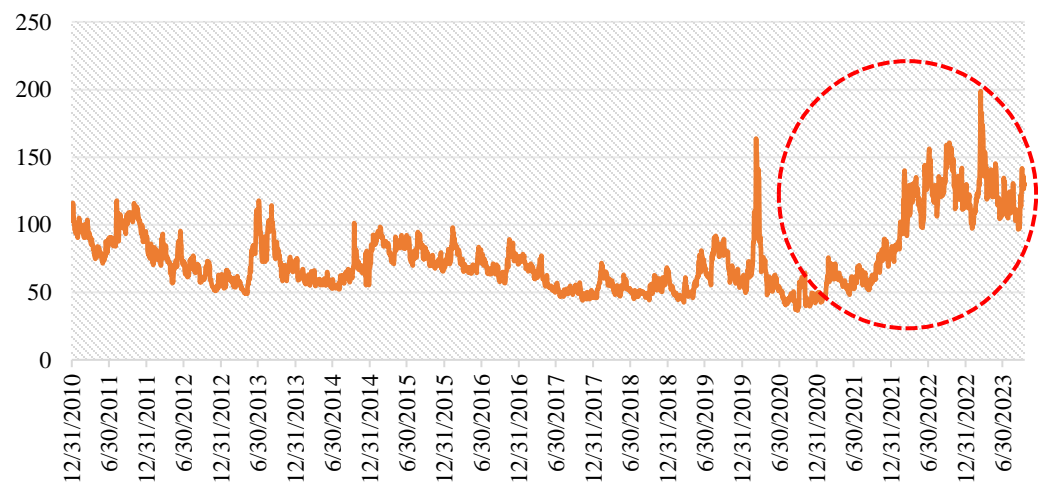
- ❖ Based on inflation expectations, global sovereign rates continues to rise.
- ❖ The situation where the nominal market interest rate on a 5-year U.S. government bond exceeds the Federal Reserve's 5-year forward inflation expectation opens up opportunities for real return that is rare after 2008.

# Higher volatility – main characteristic of post pandemic era?

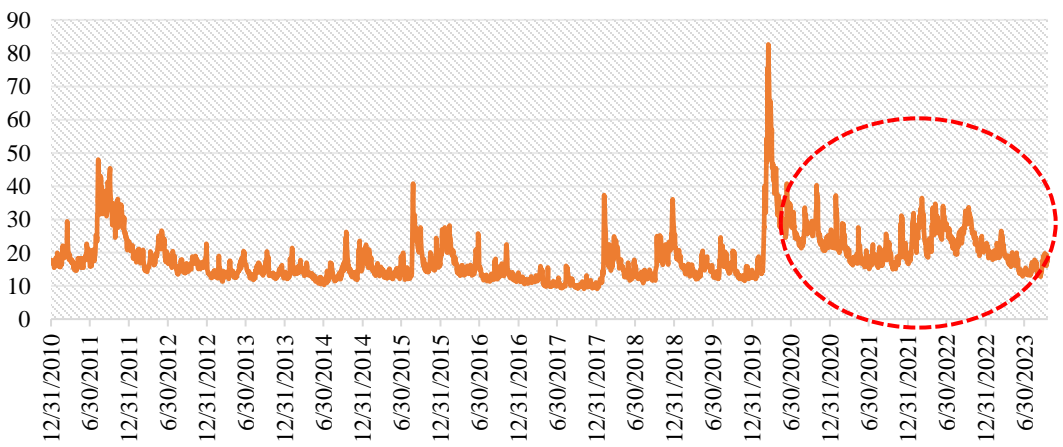
### 2 year UST volatility



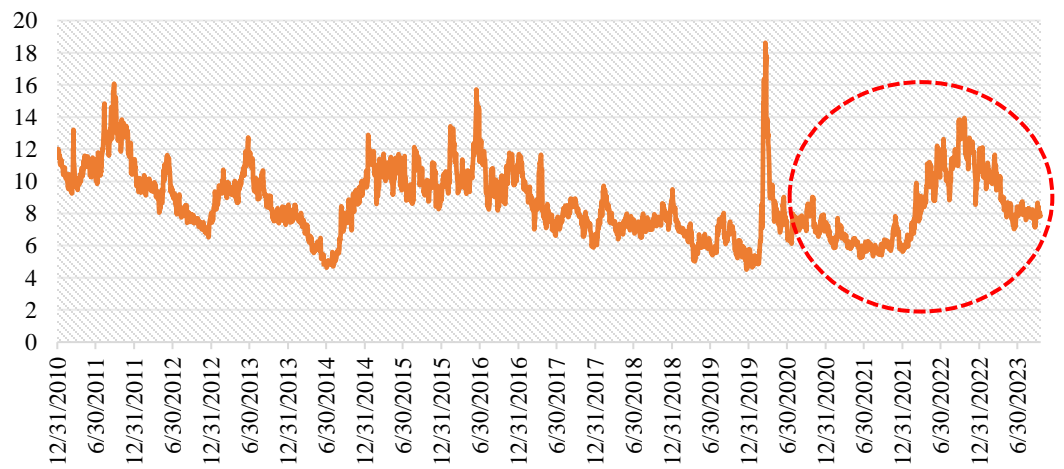
### Move index



### VIX index



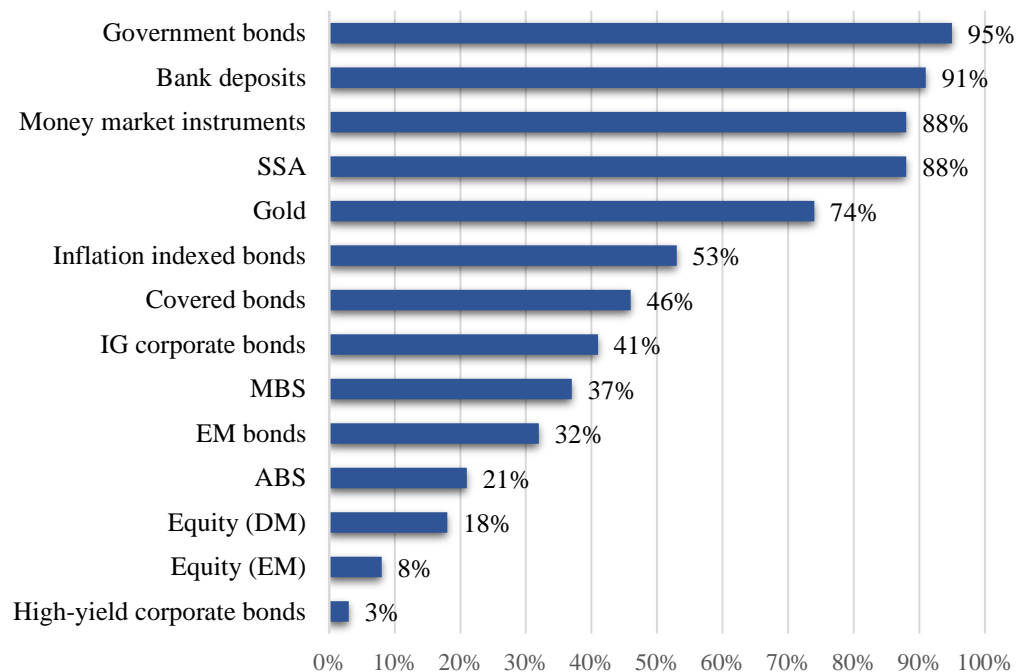
### JP Morgan G10 FX volatility 1M index



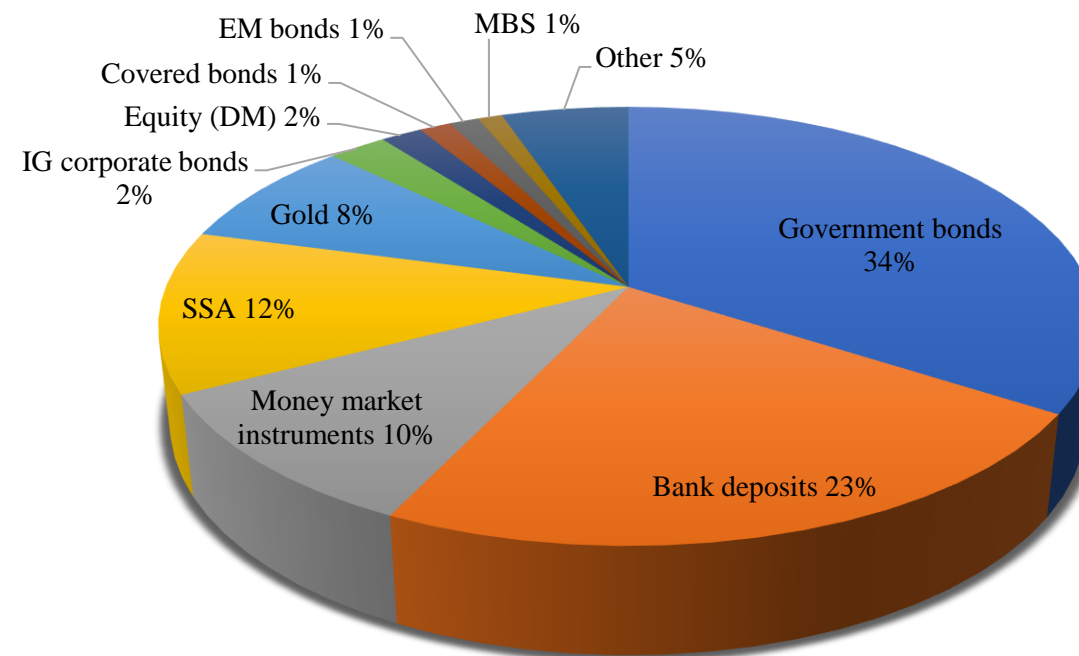
Source: Bloomberg

# More diversified asset classes

## Eligible asset classes - central banks



## Average actual asset allocation - central banks

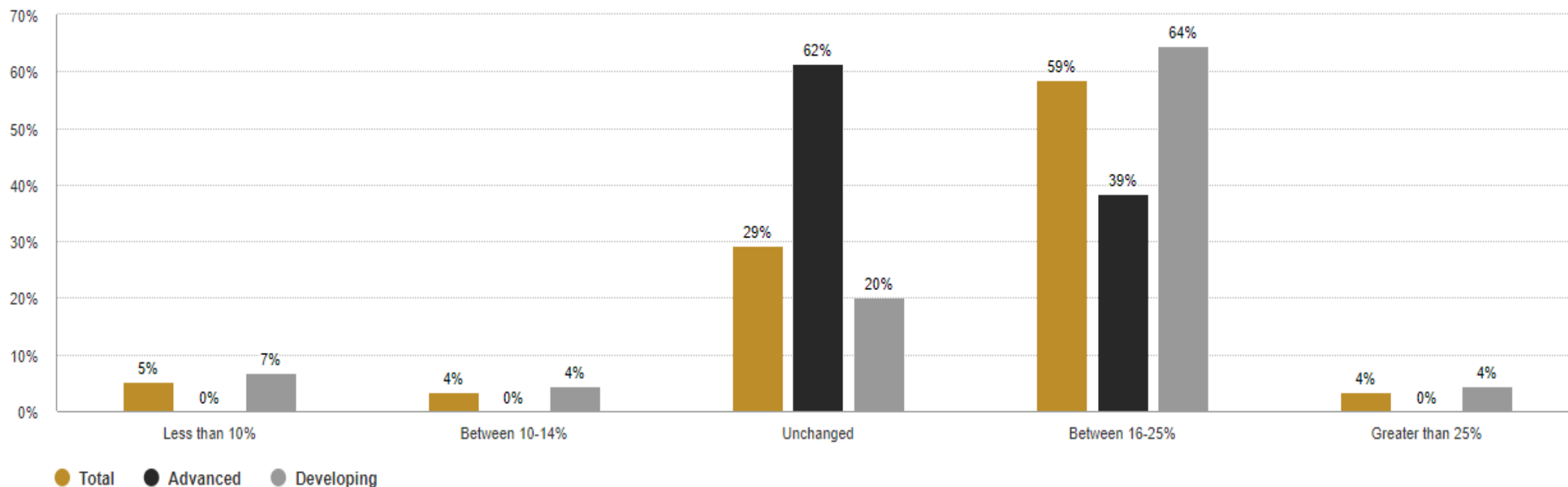


Source: Central Bank Reserve Management Practices, Third RAMP Survey, The World Bank Treasury 2021

- ❖ Almost 75% of central banks were allowed to invest in nontraditional asset classes such as corporate bonds, emerging market bonds, covered bonds, mortgage-backed securities, and equities.
- ❖ On average, nontraditional asset classes still only make up a small portion of reserve portfolios, with an average allocation of 8.2 percent across all respondent banks.

# Gold remains an important asset class

What proportion of total reserves do you think will be denominated in gold 5 years from now?



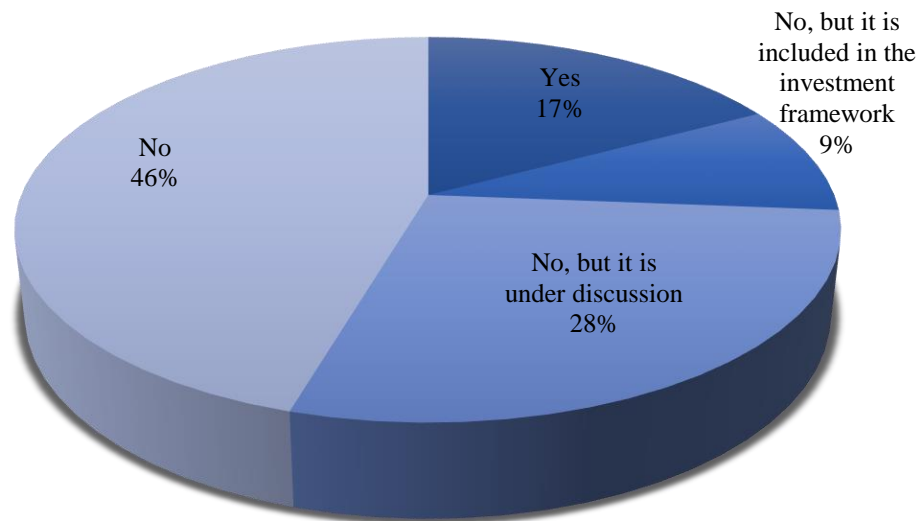
Source: World Gold Council, 2023 Central Bank Gold Reserves Survey

- ❖ Gold is viewed favorably by central banks amid a high level of uncertainty even though actual allocation of central bank reserves to gold is 8% on average.
- ❖ A majority of central banks expect a slight increase in the proportion of total reserves being denominated in gold over the next five years, with developing economies primarily driving this view

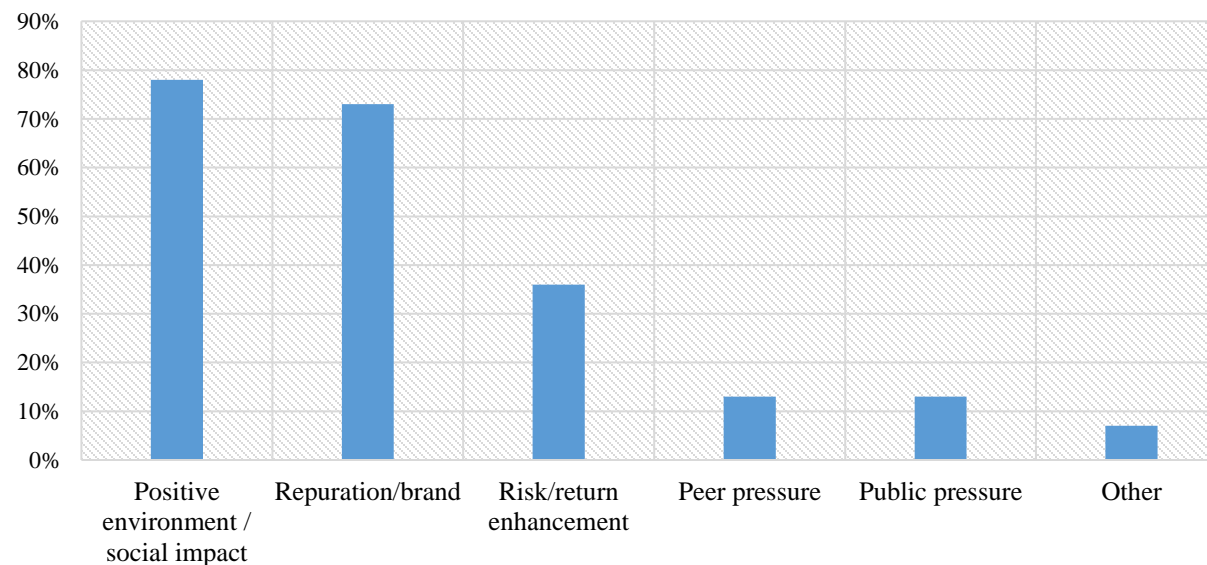


# Incorporation of ESG

## Inclusion of ESG factors in the investment policy



## Motivating factors to incorporate ESG

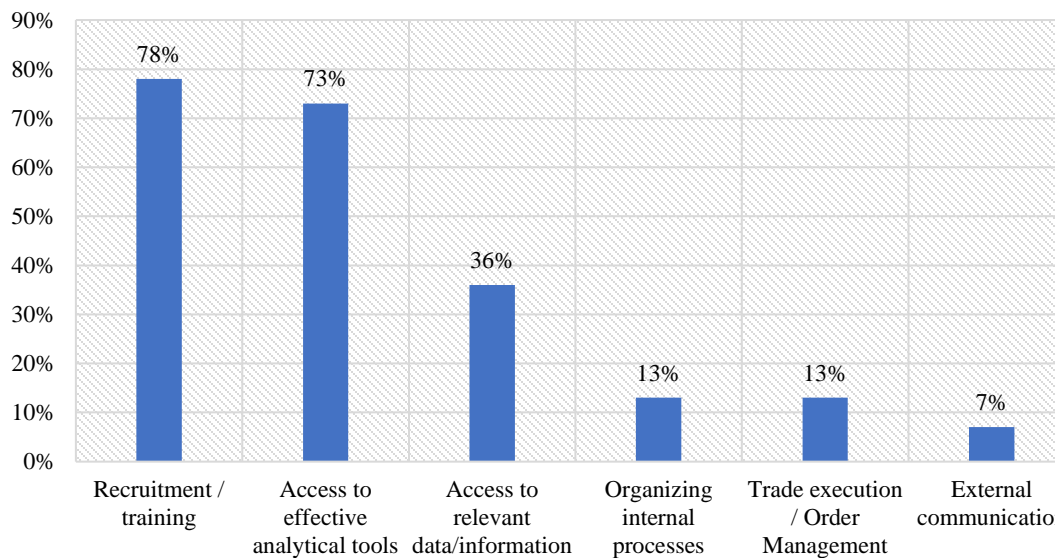


Source: Central Bank Reserve Management Practices, Third RAMP Survey, The World Bank Treasury 2021

- ❖ The low adoption rate of ESG is attributable to the fact that central banks concentrate on high-quality fixed-income assets, where the availability of ESG instruments and strategies is limited.
- ❖ Having a positive impact and maintaining their reputation are the main drivers of ESG implementation in central banks.

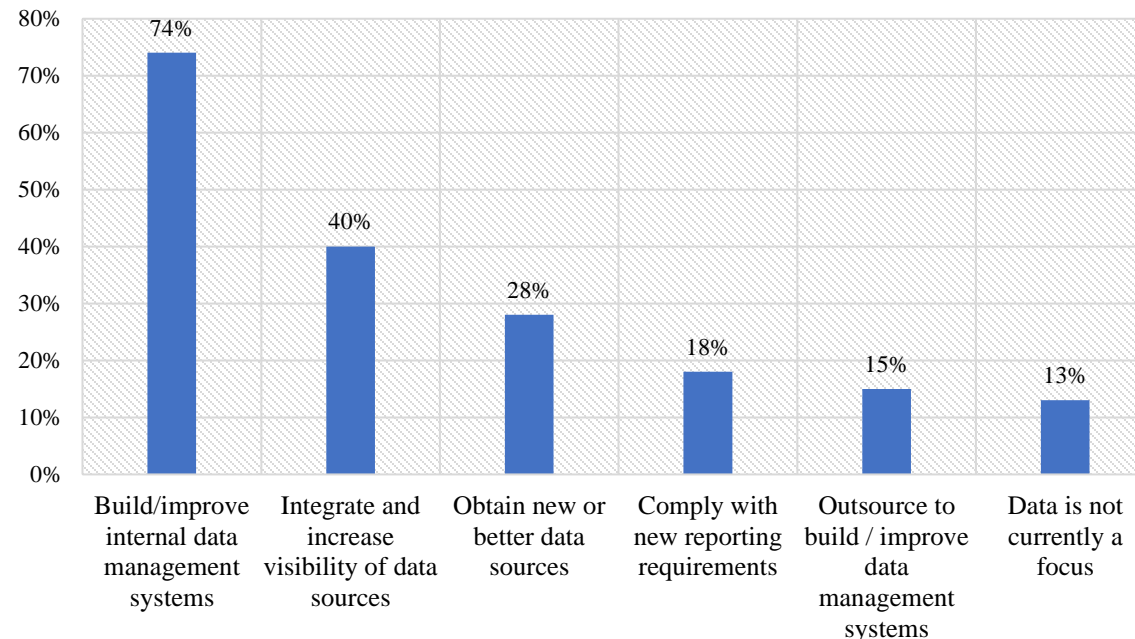
# Operating & technological challenges

## Operating challenges for central banks



Source: OMFIF Global Public Survey 2023

## Data priorities of central banks for the next 12-24 months



- ❖ Accessing to effective analytical tools and relevant information are the two main operating challenges after filling in talent gaps.
- ❖ Data rapidly becoming more important for reserve management as 87% of respondents expressed that data is a focus for the next 12-24 months.

# Global economic challenges

- ❑ Inflation
- ❑ Global economic slowdown
- ❑ Geopolitical tensions
- ❑ Volatile exchange rates
- ❑ Rising policy rates
- ❑ High public debt level



Capital preservation and liquidity have become more important for central banks

- ✓ highly liquid and safe assets like short-term government bonds
- ✓ longer-duration global government bonds as deflation hedge
- ✓ inflation-linked bonds as inflation hedge.

Stagflation concerns are growing

# Global risks

## 2 years

1	Cost of living crisis
2	Natural disasters and extreme weather events
3	Geo economic confrontation
4	Failure to mitigate climate change
5	Erosion of social cohesion and societal polarization
6	Large scale environmental damage incidents
7	Failure of climate-change adaption
8	Widespread cybercrime and cyber insecurity
9	Natural resource crisis
10	Large scale involuntary migration

Environmental

Social

## 10 years

1	Failure to mitigate climate change
2	Failure of climate-change adaption
3	Natural disasters and extreme weather events
4	Biodiversity loss and ecosystem collapse
5	Large scale involuntary migration
6	Natural resource crisis
7	Erosion of social cohesion and societal polarization
8	Widespread cybercrime and cyber insecurity
9	Geo economic confrontation
10	Large scale environmental damage incidents

Technological

Geopolitical

Source: World Economic Forum, Global Risks Perception Survey 2022-2023

❖ People think environmental risks will have more fierce impacts in a long run.

Thank you!