

# Ariff Ali: Reserve Bank of Fiji August 2016 – July 2017 Annual Report

Presentation by Mr Ariff Ali, Governor of the Reserve Bank of Fiji, to the Standing Committee on Economic Affairs, Suva, 5 April 2018.

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## 1. Introduction

Thank you Honourable Chair, and Honourable Members for the invitation to present the Reserve Bank of Fiji's Annual Report for the period 1 August 2016 to 31 July 2017, to the Standing Committee on Economic Affairs.

I had presented an extensive background to the Standing Committee last year on the role of central banks, and the functions of the RBF as stated in the RBF Act and the 2013 Constitution. However, I would wish to re-iterate as stated last year that central banking is not for the faint of heart as Alice Rivlin so aptly said, "**The job of the central banks is to worry**".

Honourable members, as I had highlighted in my presentation to you in 2017, the RBF is tasked to maintain:

- (i) Price stability – ensuring that inflation is low and stable;
- (ii) External (currency) stability – that foreign reserves level are comfortable; and
- (iii) Financial stability – that our financial system is strong and robust.

## 2. Key outcomes

Honourable Chair, please allow me to first provide highlights of the outcomes of our 2016/2017 operations, before I respond to the questions from the Standing Committee:

### (i) *Financial performance*

As we have highlighted previously, the objective of the central bank is not to maximise profit. While profit maximisation is not our goal, making losses is also not acceptable. As an important policy making institution, financial losses often results in reputational risk which then translates into loss of confidence from our key stakeholders.

Honourable Chair, for the financial year in review, the RBF made a profit of \$28.3 million and transferred to Government a total of \$29.4 million which included one-fifth or \$2.1 million of the revaluation reserve account (RRA). Of the \$28.3 million in profits, the RBF Board with the approval of the Minister transferred \$1.0 million to the General Reserve Account to strengthen the Reserve Bank's capital base. This is similar to how private companies retain dividends or earnings to strengthen their capital positions.

This compares with a transfer of \$16.9 million to Government (\$13.9 million profits and one-fifth RAA totalling \$3.0 million) for the seven month period ended 31 December 2015 with no transfers to the General Reserve Account.

Similar to past years, RBF's profit is underpinned by the income earned from our foreign reserves holdings which are invested in safe and liquid assets offshore. In the 2017 financial year, the Bank earned \$41.7 million in net foreign exchange income, boosted by elevated levels of foreign reserves.

I wish to further inform the Standing Committee that we again managed to sign off on the Bank's annual audited financial statements for the twelve months ending 31 July 2017, on 28 September 2017, within two months after the end of our financial year. Following the signing of the audited accounts and in line with the provisions of the RBF Act, the Bank provided to the Honourable Minister for Economy a certified auditor's copy of our financial accounts along with the operations report of the Bank, on 29 September 2017.

**(ii) Price stability**

Honourable Members, as you are well aware, Fiji was hit by Tropical Cyclone (TC) Winston in February 2016. It negatively impacted the supply and prices of fruits, vegetables, root crops and kava thereby placing upward pressure on domestic prices. Consequently, inflation averaged 5.2 percent in the first half of the fiscal year 2016-2017 and was something beyond our control.

However, supplies began to normalise in 2017 resulting in a decline in headline inflation from 6.8 percent in January 2017 to a low 2.0 percent by July 2017. The subdued global prices of key imports such as oil and food also contributed to this outcome.

**(iii) External stability**

As a small open economy dependent on imports of a variety of goods, we need to maintain a sufficient level of foreign reserves, otherwise there will be pressures on our exchange rate.

The International Monetary Fund (IMF) has set a benchmark on the level of foreign reserves which states that it should be sufficient to cover 3 months of imports. Given the external shocks and risk we face such as natural disasters like the one we experienced a few days ago, we built in an additional buffer above this benchmark.

I am therefore pleased to inform that Fiji's foreign reserves remained well above the benchmark throughout the review period. At the end of July 2017, our foreign reserves level stood at \$2,313.7 million and was sufficient to cover 5.5 months of retained imports. In addition, there was approximately \$591 million in foreign reserves held by non-bank financial institutions.

Honourable Members, it may be worth noting that our foreign reserves level broke a number of records last year and reached a high of \$2.445 billion on 18 September 2017.

**(iv) Financial stability**

It is paramount that we continue to have a sound, stable and healthy financial system to ensure confidence, and the efficient allocation of resources, and distribution of risks across the economy. You may recall that the Minister for Economy made a Ministerial Statement on the importance of safeguarding the stability of Fiji's financial system in the recent sitting of Parliament and therefore, I will be brief on this outcome.

I am pleased to inform the Standing Committee that the Fijian financial system remains safe and sound supported by a growing asset portfolio which rose from \$16.8 billion in August 2016 to \$18.5 billion in July 2017 and a further increase to \$19.4 billion by the end of 2017. This is almost twice our GDP.

The growth and importance of our financial system was validated by the recent findings of the Financial Sector Stability Review (FSSR) for Fiji which was undertaken by the IMF. It is important for me to highlight that Fiji was only the fifth country in the world and the first in the Pacific region to undergo a financial sector stability review. The 7-member mission team was here from 14-27 February 2018.

Honourable Members, the IMF has concluded the 2018 FSSR for Fiji with its stress test assessment indicating that the banking system in Fiji as a whole appears to be resilient to shocks similar to those experienced in the last 15 years. However, to further ensure the ongoing safety and soundness of our financial system, the 2018 FSSR mission has made some key recommendations for the continued strengthening of the RBF's regulatory role on which we will commence work shortly.

**3. Responses to questions by the standing committee**

Let me now respond to the list of questions posed by the Standing Committee.

***[i] We note that the Housing Facility to assist low income first time home owners has increased to \$60 million from \$25 million. Can we be given a number of how many have benefitted from this facility? Will this facility progressively increase in line with demand?***

Honourable Members, please allow me to preface my response by saying that the Reserve Bank grants special lending facilities to address specific areas that may be impeding economic development and growth. From a national or macro perspective, these facilities do provide positive benefits. We have our National Disaster Recovery facility which we reactivated recently in light of the recent floods, and the Import and Export Substitution Facility. The Housing Facility was introduced to help address the housing affordability issue.

Funds for the initial \$25.0 million Housing Facility for low income households was channeled through the Housing Authority (HA). The amount was increased to \$60.0 million given the need to assist first home buyers, and broaden the coverage to include commercial banks, licensed credit institutions and the Fiji Development Bank. To date, the Reserve Bank has approved a total of 142 first home applications with a total value of \$12.5 million in addition to the 635 that benefitted initially from the Facility through HA. The maximum interest rate charged on this Facility for home owners is 5.00 percent, and financial institutions borrow funds from the RBF at 1.00 percent. Therefore, a total of \$22.8 million remain available for lending to new first home buyers and we expect this to be utilised in the next 12-18 months.

In line with the expected buoyant economic activity and rising need for housing, the Reserve Bank will continue to review the demand for funds in meeting the objective of the Housing Facility.

***[ii] Please provide an update on the status of Fiji's Green Bond?***

Fiji floated its first Green Bond on 1 November 2017 attracting interest from both local and foreign investors. The participation rate recorded was three times more than were normally associated with the Fiji Government Infrastructure Bonds.

Of the total of \$40.0 million floated on 1 November, a sum of \$87.7 million was received in tenders, for the two tenors of 5 and 13 years. A second issuance of \$20.0 million was made on 28 December which was also oversubscribed with \$31.5 million received in tenders, for the 13 year tenor. A total of \$100.0 million is targeted to be raised for this financial year for which we have received \$60.0 million with the remaining \$40.0 million expected to be raised in April and June this year.

In line with the Green Bond Principles, these Green Bond proceeds are being channeled towards eligible projects such as the maintenance of drainage and flood protection, the construction of the new Labasa weather office and the rehabilitation and construction of schools destroyed by Tropical Cyclone Winston.

Fiji's Green Bond Framework is guided by the Green Bond Principles which sets out process guidelines for best practices: which include the Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds and Reporting. An external independent verifier had confirmed that Fiji's Green Bond Framework is credible, transparent and aligns with the core principles. In addition, we are developing reporting and monitoring guidelines to ensure compliance with the Green Bond Framework and any environmental and social risk assessments. A key outcome would be the release of periodical reports on both the use of green bond proceeds and expected climate and/or environmental impacts of eligible projects.

Given Fiji's success story and experience on its green bonds, the International Finance Corporation has released a report titled "*Guidance for Sovereign Green Bond Issuers*" which focuses on lessons from Fiji's example as the first emerging economy to issue a sovereign green bond, and which can be applied by any future green bond issuer. In addition, Fiji was also awarded a prestigious Green Bond Pioneer Award at the recent Climate Bonds Initiative's Conference in London. To further leverage our position on the global scale and bolster

awareness and interest from foreign investors and stock exchanges, Fiji Green Bonds will be listed on the International Securities Market of the London Stock Exchange on 18 April 2018.

***[iii] On page 50 under 'Reserve' we note that \$1.0 million was transferred to General Reserve whereas no such transfer was made in 2016. Can this be explained?***

In accordance with the RBF Act, all the profits of the Reserve Bank are distributed annually to Government together with one-fifth of the foreign currency revaluation reserve account. Over the years, the total capital and reserves of the Bank have been declining and stood at around \$82.0 million as at the end of July 2017.

As explained earlier, it is prudent to set aside a small portion of the profits to the General Reserves to strengthen the Bank's capital base similar to what is practiced by private companies. The Reserve Bank had written to the Minister for Economy on 17 August 2017 recommending the transfer of \$1.0 million from the 2016-17 financial year profits to the General Reserve Account.

The request for the transfer of profits is in line with the provision of section 8 of the RBF Act. The last transfer to the General Reserve Account was made for the financial year ended 31 December 2007 when the Minister approved that \$1.0 million be set aside from the profits distributable to Government.

***[iv] On page 33 relating to the development of the economy; we note that these are not the core functions of the RBF and we would like to know how much resources are devoted to these areas.***

Honorable Members, the definition of 'core role' of central banking has blurred over time. Central Banking has evolved quite significantly, but we continue to refer to the conduct of monetary policy to achieve price stability as well as financial stability, as the heart or 'core' of what a central bank does. Other functions such as the development role we play complement our core functions and contribute to our overall vision of "**Leading Fiji to Economic Success**".

The development function of the Reserve Bank is driven by the Financial System Development Group. The Group was established in 2009 to drive sustainable and inclusive economic growth initiatives. This Group is headed by a Chief Manager with a total staff complement of 21. In the 2018 financial year, the Group has a budget allocation of \$1.9 million or 7.4 percent of the Bank's Total Operating Budget.

***[v] Page 8 outlines the roles played by the Governor, some of which are outside the core responsibilities within RBF. Can we be given the assurance that these extra roles are not in conflict with what is expected of the Governor and that they do not impact on the performance of his core duties?***

Thank you for this question as I had actually planned to address this issue to clear what appears to be mis-information that has been raised both inside and outside Parliament.

Under section 15 of the RBF Act, the Duties of the Governor are stated accordingly. In particular, section 15(2) states:

The Governor shall devote the whole of his or her professional services to the Reserve Bank and shall not, without the approval of the Minister –

- (a) Receive any salary or supplement thereto from any other source other than the Reserve Bank;
- (b) Occupy any other office or employment, whether remunerated or not except as nominee of the Reserve Bank except that he or she may –
  - (i) Act as a member of any statutory, committee or commission established by the Government;

- (ii) Become a governor, director or member of the board of any international financial institution of which Fiji is a member.

In the Reserve Bank of Fiji August 2016-July 2017 Report, you will note on Page 8 that I am also the:

- Alternate Governor for Fiji at the International Monetary Fund;
- Alternate Governor for Fiji at the Asian Development Bank;
- Chairman of the Monetary Policy Committee;
- Chairman of the Macroeconomic Committee;
- Chairman of the Capital Markets Advisory and Development Taskforce;
- Chairman of the National Financial Inclusion Taskforce;
- Chairman of the Government Tender Board;
- Chairman of the Sugar Cane Growers Fund; and
- Board Director of the Fiji Sugar Corporation Limited.

I assumed all positions except for the last three by virtue of being the Governor of the Reserve Bank of Fiji. The Hon Attorney-General and Minister for Economy appointed me to serve on those boards when I was the Deputy Governor. Since the Report was published, I have also been appointed Chairman of the Accident Compensation Commission Fiji by the Hon Attorney-General and Minister for Economy.

The Standing Committee on Economic Affairs can be rest assured that the role of the Governor remains intact in serving the priorities of the Reserve Bank and also meeting the expectations of stakeholders. Issues of conflict of interest have been highlighted in some circles and I wish to clarify that contrary to such statements; none of these institutions that I serve on as a board member or chair are licensed or regulated by the RBF.

Notwithstanding the assurance I have given, I further wish to reflect on the vision of the Reserve Bank of Fiji of Leading Fiji to Economic Success and one of our key mission statements to “Enhance our role in the development of the economy”. This mandate calls for the Governor to play a wider role in the economy and the community allowing for knowledge and expertise sharing. I also wish to highlight that the RBF has an approved policy on external board appointments which supports the conduct of a transparent process in approving staff participation in external boards.

***[vi] We note that since the report was published Mr. Esala Masitabua has been appointed the new Deputy Governor, making RBF an institution that has fully localised all its positions from Governor, senior managers, etc. We also note that of your 8 Executive Managers 5 are female and 3 are male – this is highly commendable. In your opinion, how can other institutions follow suit and possibly learn from RBF’s example?***

Thank you for noting our fully localised management team and the high composition of female members in this regard. I wish to add that the RBF have a long history of fully localised management team.

We take pride in developing a corporate culture that rewards our people on merit. This drives us to ensure that our leaders are those who have the capacity to lead with integrity and commitment to our vision and missions. Having more females in our leadership team was not made a special consideration as sometimes promoted by some gender based propositions. The female members of our team have made it to the senior positions that they hold, through merit, and they are supported the same way as we support our male members.

However, like many other organisations, we also have our share of challenges and continue to invest in empowered and accountable leadership through tailor made leadership training programmes, as well as receiving regular guidance from the board and the Governors.

We also wish to highlight that the RBF continues to promote merit based individuals into its leadership team while ensuring gender diversity in its key roles. In line with this, the RBF had issued a press release on 3 February 2017 on a call to action for greater participation and representation by women of merit on the boards of listed companies of the South Pacific Stock Exchange. We believe that gender diversity is a key indicator for good corporate governance, and the Bank will continue to collaborate with stakeholders in support of Fiji's National Gender Policy and the achievement of SDG 5 of Gender Equality.

For other local institutions, it would be of immense benefit if a merit based culture is inculcated in the organisation, and fairness and honesty guide decision making on leadership positions. Institutions will also need to invest in high-quality leadership training and be specific with leadership qualities they wish to have. The top echelon of the organisation structure will have to show interest in the continuous development of their senior and middle management, and ensure that effective succession planning is in place.

***[vii] On page 60 – Statement of Cash flows – there seems to be a lot of movement between the figures of the seven month period ended 31 July 2016 and Year ended 31 July 2017 i.e. Net movement in Short Term Commercial Paper, Net movement of Domestic Securities, Net movement in Demand Deposits. We realise that one report is just a 7 month period and the other covers 12 months, however, the differences are still large. Please give us some insight into why the big differences.***

The movements noted in the statement of cash flow reflect the changes (increases/decreases) in the Bank's financial position as at 31 July 2017 compared to the same period in 2016. The underlying reason for the movement in cash flow is the increase in total external reserves which rose from \$1,982 million to \$2,314 million (Page 68 Note 5).

The reduction in short term commercial papers from \$376.2 million to \$257.8 million can be explained by a rise in the current account (\$124.4 million to \$241.3 million).

On the other hand, domestic securities declined by \$8.4 million as RBF holdings of Government bonds matured (Page 68 Note 6).

Unlike short-term papers and domestic securities which are assets of the Bank, demand deposits are a liability and rose significantly over the year directly correlating to the level of foreign reserves. The demand deposits are commercial bank's settlement balances placed with the RBF and they are paid equivalent Fiji dollar when they sell their surplus foreign currency to RBF.

***[viii] Also along the same lines – Page 67 – Interest Expense 'International Monetary Fund' 66 against 604 for 2017.***

All central banks have an account with the International Monetary Fund (IMF). The RBF receives interest on Special Drawing Rights (Asset) and in the year received \$579,000 compared with \$53,000 in the previous financial year (page 67). Central Banks also have Liability – SDR Allocation where we pay interest to IMF. In the latest financial year, the RBF paid \$604,000 compared with \$66,000 in the previous year. The RBF tries to maintain its SDR Assets and Liabilities in a similar amount so that the interest received and paid are netted off.

The SDR is a basket of currency used by IMF and includes the US dollar, Euro and Japanese Yen. The interest paid/received is the weighted average short-term market interest rate in the three currencies and the increase in interest paid/received is due to two main factors:

- On 1 October 2016, the IMF announced the inclusion of the Chinese renminbi in the SDR basket of currencies. With the renminbi rate higher than the other currencies, this pushed the average interest rate higher; and

- Over the course of 2017, the short-term US interest rates have risen reflecting the interest rate hike by the US Federal Reserve as well as the tightening bias by the financial market.

***[ix] We notice that there is a lot of emphasis on financial inclusion. Can we be given an update on how we are reaching out to the section of our population that does not have access to the banking system?***

Work on financial inclusion is guided by the National Financial Inclusion Strategic Plan (2016 -2020). The overall target of this Strategic Plan is to increase access and usage of formal financial services from 64 percent to 85 percent (an additional 130,000 adults), of which 50 percent are women. In terms of geographical distribution, it is anticipated that 6 percent will be from the Eastern Division, 22 percent from the Northern Division, 40 percent from the Western Division and 32 percent from the Central Division.

These 2020 targets are based on findings from the 2015 Fiji Financial Services Demand Side Survey which highlighted that around 221,077 (36%) of the adult population are underserved.

This Strategic Plan focuses on 7 key areas: Empowerment of Women, Youth and those living with disabilities; Financial Infrastructure; Digital Finance; Services and Products; Financial Literacy and Consumer Protection; Public and Private Sector partnership and Data Measurement.

The RBF closely monitors the financial inclusion core set of indicators which include the following:

- Number of cash-in cash-out financial access points per 10,000 adults;
- Percentage of new account(s) at a formal financial institution;
- Percentage of adults that have an active mobile money account (used in the last 90 days);
- Percentage of adults using formal credit products;
- Percentage of adults with an insurance product; and
- Percentage of adults with a FNPF membership account.

Some achievements made to date include the launch of a bundled insurance product that has enabled 12,500 sugar cane farmers to be insured. An alternative affordable low cost life and health insurance product was launched in 2016 which customers can purchase using their mobile phones. A survey of the subscribers to this product showed 80 percent previously never had any form of insurance.

Financial inclusion has been achieved through the collaboration of public and private sector partners working together to remove the barriers that deter people from engaging with the formal financial system. Hence financial education is now embedded into the school curriculum and free community financial literacy training and media awareness programmes are some of the initiatives that have been made widely available to the public to assist them in making informed financial decisions.

#### **4. Summary**

Honourable Members, before I end, I wish to highlight a few key points for your noting:

- [1] The inflation rate has been below 3.0 percent since August 2017 and was 2.6 percent in March 2018. While we expect the end year inflation to be around 3.0 percent, we anticipate a rise in inflation over the next few months due to the impact of TC Josie on the supply of fresh fruits and vegetables;

- [2] Foreign reserves are currently just below \$2.2 billion, sufficient to cover 4.9 months of retained imports and reflect the seasonal outflow as well as venting of reserves to non-bank financial institutions; and
- [3] We had projected the economy to grow by 3.6 percent in 2018, and this is currently being reviewed. This will be our 9th consecutive year of growth – a record not achieved since independence.

Finally Honourable Members, I would like to acknowledge the great team that we have at the Bank and I wish to thank them, including our former Governor Whiteside who also contributed towards the 2016/2017 financial year, and the RBF Board for their leadership and guidance.

I hope these remarks are helpful background for the Committee's review of the Reserve Bank of Fiji's August 2016-July 2017 Report and we would be happy to answer any further questions.