



Publications

## Report on the Investment of Israel's Foreign Exchange Reserves in 2020

22/03/2021

[Foreign exchange reserves, foreign currency market](#)

[Regular publications and reports](#)

[To view this press release as a file](#)

Press Releases

Regular Publications



[Full report](#)

Monetary Committee Publications

Speeches and Presentations

About the Spokesperson's Office

Legislation and Regulations

The annual report on the investment of Israel's foreign exchange reserves for 2020 was published today. Following are the main points in the report:

**The COVID-19 crisis**

Due to the outbreak of the coronavirus pandemic, in 2020 there was a sharp slowdown in real activity and an increase in risks worldwide. In financial markets, this was reflected in steep declines in equity and corporate bond prices and in a sharp decline in yields on government bonds around the world, particularly in the US and Germany in the first quarter of the year. However, over the course of the rest of the year, risk assets increased in value and most ended 2020 with positive rates of return. During the year, a sharp increase in volatility was seen in all financial assets.

The Bank of Israel, as a long-term investor, maintained the share of investment in risk assets in the reserves portfolio while taking various steps intended to minimize the financial risks to which it is exposed through the investment in such assets. In addition, in view of a marked deterioration in economic conditions in the domestic economy due to the spread of the COVID-19 pandemic and the steps taken to halt it, the Bank of Israel used a range of tools to aid in handling the crisis. Among other things, the foreign exchange reserves were used for the first time and the Bank began to execute swap transactions in the foreign exchange market with the goal of supplying dollar liquidity to the domestic banks.

**Level of the reserves**

Israel's foreign exchange reserves were \$173.3 billion at the end of 2020, an increase of \$47.3 billion over the course of the year, compared with the preceding year. The level of the reserves relative to GDP increased from 31.9 percent to 43.3 percent.

**Sources of the change in the reserves**

The increase in the reserves derived from foreign exchange purchases totaling \$21 billion by the Bank of Israel as part of the implementation of the monetary policy, from the government's deposits totaling \$14.6 billion, and from profits, revenue, and exchange rate and price differentials (mark to market) totaling \$11 billion.

**Composition of assets in the reserves**

At the end of 2020, 64 percent of the reserves were invested in government assets, 15 percent in equities, 14 percent in spread assets, and 7 percent in corporate bonds.

**Financial conditions**

From a full year perspective, financial markets were supportive of the portfolio's performance. The decline in yields to maturity on government bonds, in parallel with an increase in the prices of risk assets, equities, and corporate bonds, contributed to the return, while at the same time an increase in risk was reflected in a sharp increase in financial asset volatility.

**Return on the portfolio** The rate of return on the reserves portfolio in 2020 was 4 percent in terms of the numeraire, which is a basket of currencies, primarily comprised of the dollar and euro. Over the past three years, the rate of return has averaged 3.4 percent per year, and over the past five years, it has averaged 3 percent per year (Table 1a).

**Table 1a**

**Rate of return on the foreign exchange reserves portfolio, annual and multiyear perspectives, in terms of the numeraire, annual terms**

|                                  | 2020 | 3 years | 5 years |
|----------------------------------|------|---------|---------|
| <b>Reserves Portfolio return</b> | 4.0  | 3.4     | 3.0     |
| <b>Benchmark return</b>          | 0.6  | 1.1     | 0.7     |
| <b>Excess return</b>             | 3.4  | 2.3     | 2.2     |

**Contribution of active management** The contribution of active portfolio management, measured by comparing the portfolio return with the risk-free portfolio (the basic benchmark) return, was 3.4 percent in 2020. The main contribution to this was from equities—1.8 percent, primarily through the investment in US equities—1.76 percent, as well as from duration—1.5 percent.

**Risk level in the portfolio** The portfolio's volatility, which represents its risk level, rose to a record this year. Due to the high volatility in equity indices and due to their high share in the portfolio compared to previous years, the standard deviation of the portfolio's return, which measures such volatility, reached 3.35 percent in 2020, compared to a level of approximately 1 percent, on average, in the past decade.

**Review of investment policy objectives** The marked increase in the level of the reserves, which derives from the Bank of Israel's foreign exchange purchases as part of the implementation of the monetary policy, led the Bank to examine the objectives on which the reserves investment policy is based and the policy's characteristics, such as the investment horizon, risk profile, share of investment in risk assets, as well as the currency for measuring the return on the reserves. Subject to achieving the safety and liquidity objectives, it is important that the investment policy of the reserves portfolio achieve a return in shekel terms that in the long term will at least cover the financing cost of holding the reserves (the cost of the liabilities on the Bank's balance sheet). In view of this, the holding rate of return on the reserves portfolio is reported in shekel terms as well (Table 1b).

In 2020, the return in shekel terms is negative, due to the appreciation of the shekel vis-à-vis the main currencies in which the reserves are held, particularly against the dollar. Despite the prolonged appreciation of the shekel vis-à-vis the investment currencies, the return is only slightly negative in the 1-year and 5-year terms, and is even positive in the 3-year term.

**Table 1b**

**Rate of return on the foreign exchange reserves portfolio, annual and multiyear perspectives, in shekel terms, percent, annual and cumulative terms**

|  | 2020 | 3 years | 5 years |
|--|------|---------|---------|
|  |      |         |         |



|  |      |      |       |
|--|------|------|-------|
| <b>Reserves portfolio return – annual terms</b>    | -0.5 | 1.1  | -0.3  |
| <b>Reserves portfolio return – cumulative</b>      | -0.5 | 3.4  | -1.4  |
| <b>Numeraire/NIS rate of change – annual terms</b> | -4.3 | -2.2 | -3.1  |
| <b>Numeraire/NIS rate of change – cumulative</b>   | -4.3 | -6.5 | -14.8 |
| <b>\$/NIS rate of change</b>                       | -7.0 | -2.5 | -3.8  |

A negative sign in the rate of change in the exchange rate means depreciation of the shekel.

 [Print Page](#)



[Site Map](#) | [Disclaimer](#)