

## Forex Reserves

Forex reserves' is an important term in economics and its understanding is necessary to understand how an economy functions with respect to international trade and commerce. In this article, we give you a brief about forex reserves for the [Civil Services Exam](#).

### What is Foreign Exchange Reserve or Forex Reserve?

Forex reserves or foreign exchange reserves (FX reserves) are assets that are held by a nation's central bank or monetary authority. It is generally held in reserve currencies usually the US Dollar and to a lesser degree the Euro, Japanese Yen, and Pound Sterling. It is used to back its liabilities – like the native currency issued and also reserves deposited by financial institutions or the government with the central bank.

### Objectives Behind Holding Forex Reserves:

- Supporting and maintaining confidence in the policies for monetary and exchange rate management
- Provides the capacity to intervene in support of the national or union currency.
- Limits external vulnerability by maintaining foreign currency liquidity to absorb shocks during times of crisis or when access to borrowing is curtailed.

In a conservative view, forex should only contain foreign banknotes, foreign treasury bills, foreign bank deposits, and long and short-term foreign government securities. But, in practice, it also contains gold reserves, IMF reserve positions, and SDRs, or special drawing rights. The latter figure is more easily available and is officially known as the international reserves.

This article will tell all you need to know about the topic 'Forex Reserves'. Economics is an important segment of the [IAS](#) exam and is also extensively linked to current affairs.

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## Forex Reserves Latest Updates

According to the Reserve Bank of India RBI Data, India's foreign exchange (Forex) reserves increased by \$3.074 billion in the week ended June 11. With this leap, the forex reserves have reached an all-time high of \$608.081 billion, on June 18, 2021.

Details on the [Reserve Bank of India](#) are available on the page link provided here.

The surge in forex reserves this week can be attributed to an increase in foreign currency assets (FCA), the largest component of a country's foreign exchange reserves.

### Foreign Currency Assets

- FCA are assets that are valued based on a currency other than the country's own currency.
- FCA is the largest component of the forex reserve. It is expressed in dollar terms.
- FCA includes the effect of appreciation or depreciation of non-US units like the euro, pound and yen held in the foreign exchange reserves.
  - Currency appreciation refers to the increase in value of one currency relative to another in the forex markets.
  - Currency depreciation is a fall in the value of a currency in a floating exchange rate system.
- In a floating exchange rate system, market forces (based on demand and supply of a currency) determine the value of a currency.

### Forex Reserves India

As of June 2021, India has USD \$608.081 billion forex reserves. India ranks fourth in the world in forex reserves. China is in first position, followed by Japan and Switzerland.



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## Purpose of keeping foreign exchange reserves

1. To keep the value of their currencies at a fixed rate.
2. Countries with a floating exchange rate system use forex reserves to keep the value of their currency lower than the US Dollar.
3. To maintain liquidity in case of an economic crisis.
4. The central bank (RBI) supplies foreign currency to keep markets steady.
5. To ensure that a country meets its foreign obligations and liabilities.

To know more about the [Foreign Exchange Management Act](#), visit the linked article.

### Reasons for High Forex Reserves

- Rise in investment by foreign portfolio investors and increased foreign direct investments (FDIs). Know in detail about the [Foreign Direct Investment – FDI](#) on the linked page.
  - The sharp jump in reserves started with the Finance Ministry's announcement in 2019, cutting corporate tax rates.
- Fall in crude oil prices has brought down the oil import bill, saving precious foreign exchange.
- Dollar outflow from overseas remittances and foreign travels have fallen steeply.

### Importance of foreign exchange reserves

According to a report by Goldman Sachs, stronger foreign currency reserves will allow developing market central banks to “buffer their currencies against sharp declines by supplying dollars to the market” at times of volatility.

### Importance of Increasing Foreign Exchange Reserves

- The government is in a comfortable position if there are rising forex reserves and the RBI in managing India's external and internal financial issues at a time of major contraction (23.9%) in economic growth.
- It Assist the government in meeting its foreign exchange needs and external debt obligations.
- Appreciation in Rupee – The rising foreign exchange reserves has helped the rupee to strengthen against the dollar.
- Crisis Management: Rising Forex Reserve serves as a cushion in the event of a Balance of Payment crisis on the economic front. It is enough to cover the import bill of the country for a year. Know more about the [Balance of Payment](#) on the linked page.
- Confidence in the Market: Forex Reserves will provide a level of confidence to markets and investors that a country can meet its external obligations