

GOVERNMENT CASH MANAGEMENT: AN OVERVIEW

Workshop Presentation
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Agenda

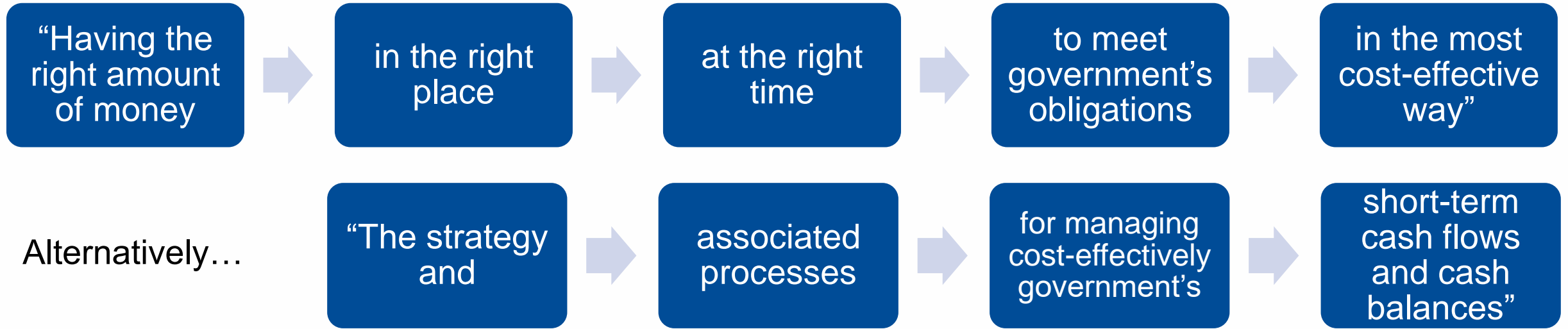


What cash
management is
and what it is not

The Three Pillars
of Modern Cash
Management

Getting from
here to there

What is Cash Management?



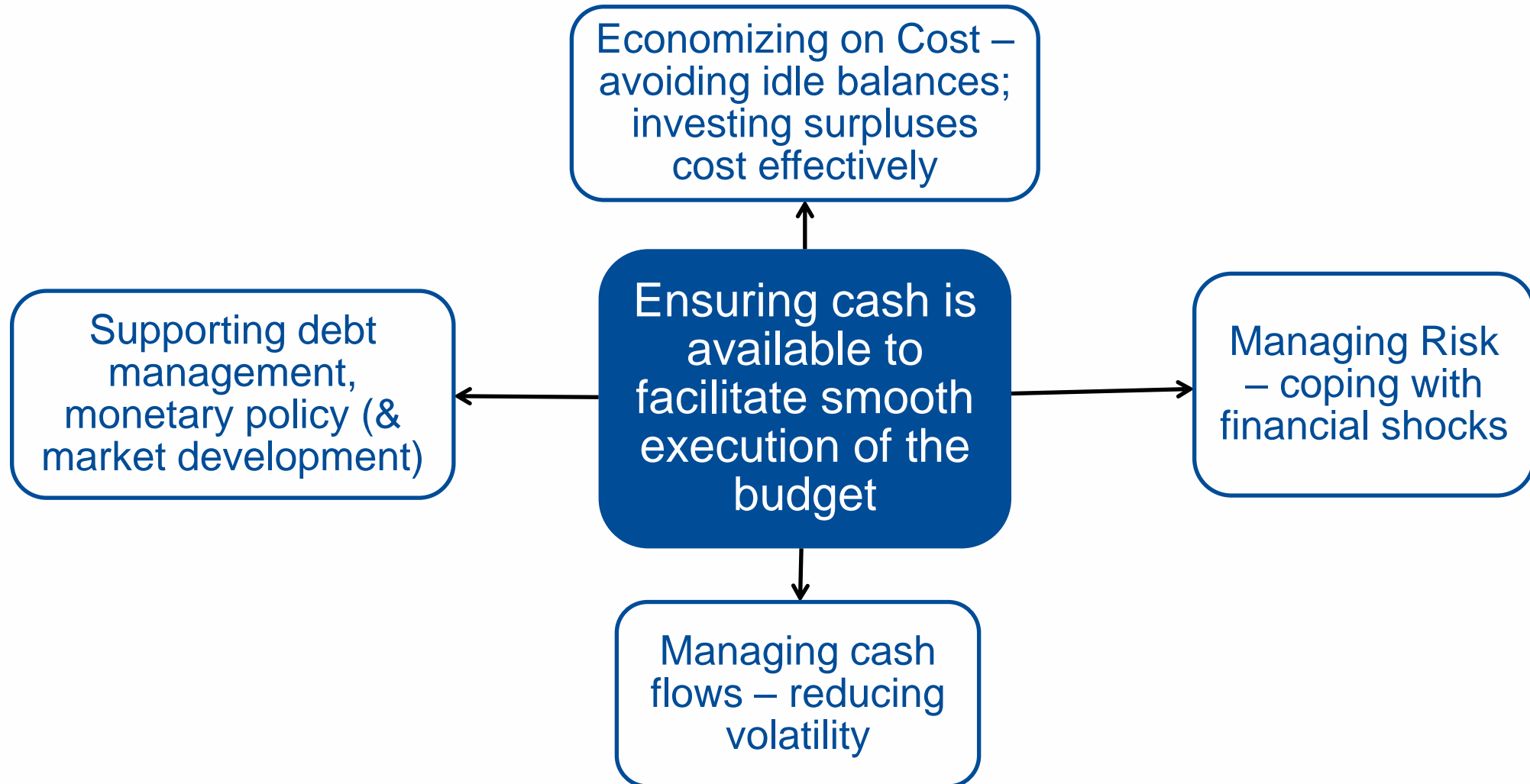
Cash management is distinct from budget management or budget execution

- Budget execution is about ensuring that the budget is managed consistently within agreed limits
- Cash management is about ensuring that the government has the liquidity to execute its payments

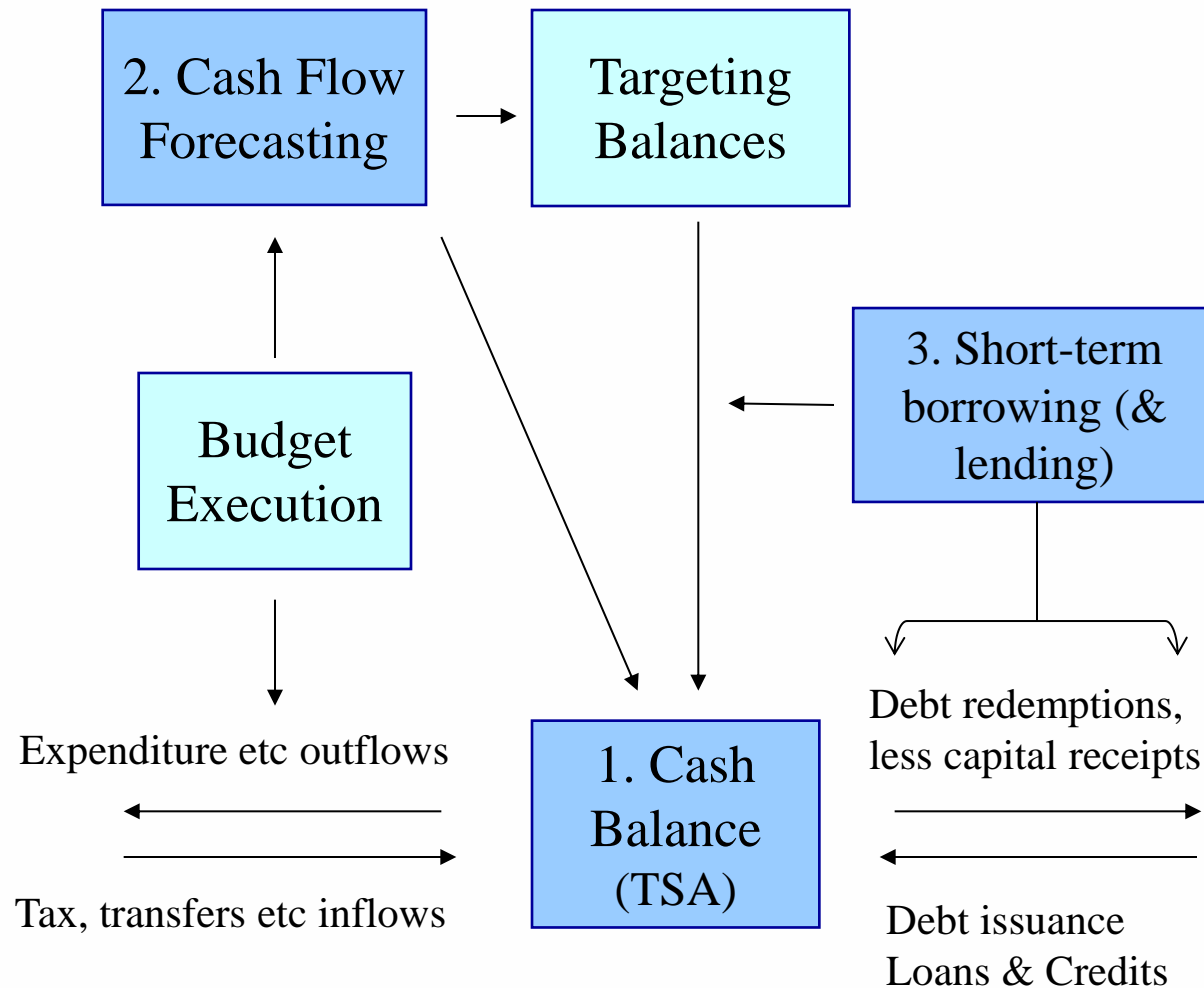
Cutting expenditure plans for lack of cash is cash rationing, not cash management

- Effective cash management removes the need for cash rationing

Cash Management: the Objectives



The Three Pillars



Phase 1: Treasury Single Account

- Integration of government accounts
- Minimising any overnight balances outside the TSA

Phase 2: Forecasting Capability

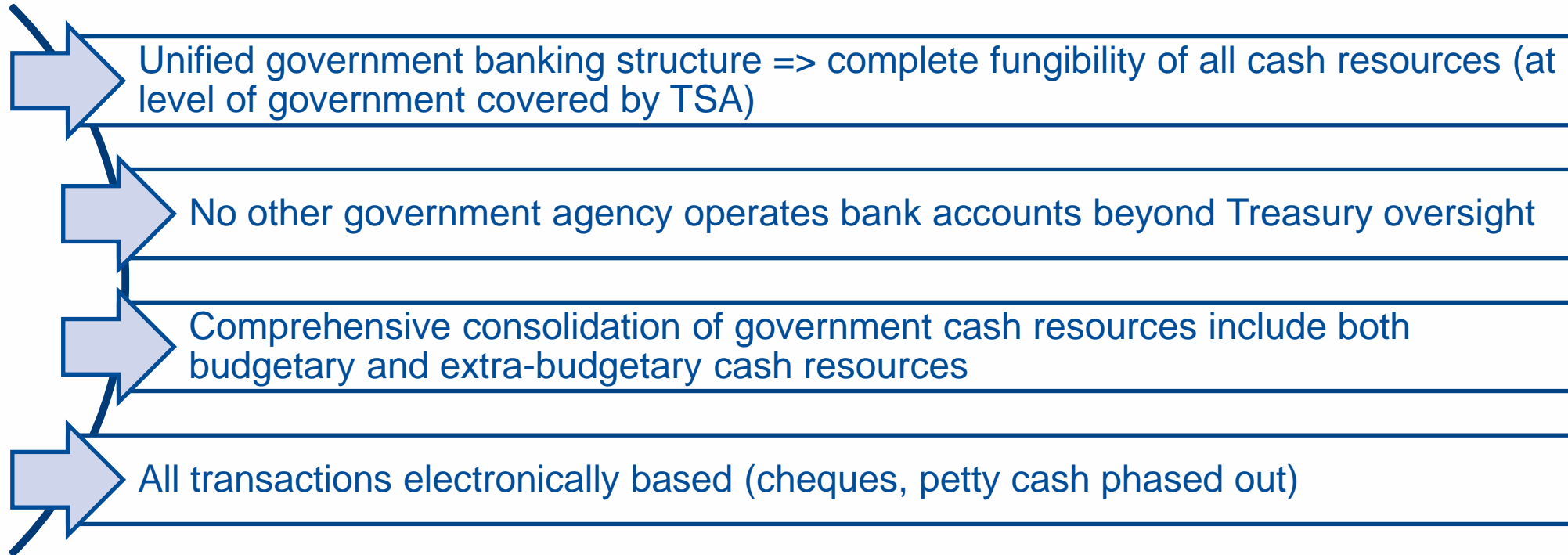
- Development of capability to monitor and forecast (at least 3 months ahead) changes in cash balances in TSA

Phase 3: Active Cash Management

- Short-term borrowing (and investing surplus cash) in a pattern designed to offset fluctuations in cash flows, i.e. to smooth the change in the balance in the TSA

The Treasury Single Account

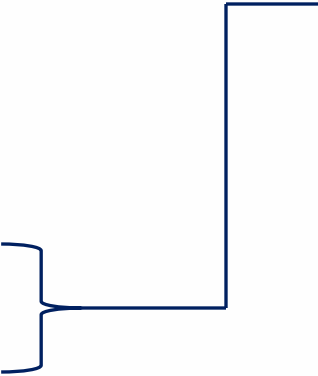
- **TSA = unified structure of government bank accounts to give a consolidated view of government cash resources**
- A fully-fledged TSA shares essential features:



[Treasury “Single” Account is misleading - typically a sub-account structure or network of linked accounts]

Cash Flow Forecasting

- Efficient cash management requires ability to forecast daily cash flows across the TSA
 1. To facilitate orderly achievement of budget targets; to ensure that budgeted expenditure is smoothly financed avoiding delays; and to give early warning of any problems
 2. To devise the strategies for active cash management

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- A smoother cash flow means:
 - ▶ Lower average cash balances
 - ▶ Reduced net borrowing costs
 - ◆ Interest on cash balances always less than interest on marginal borrowing
 - ◆ Interest can be earned on any temporary cash surpluses (structural cash surplus invested separately)
 - ▶ Less pressure on central banks' monetary policy operations

- **Characteristic of all modern government cash management systems**

Forecasting Sound Practice: Main Characteristics

■ Preparing the Forecasts

- Annual cash plans supporting budget execution
- Forecasts, extending at least 3 months ahead
 - ▶ Daily or weekly, rolled forward regularly
 - ▶ Making good use of inputs from (larger) spending units (MDAs) and (especially) the Revenue Authorities
 - ▶ Focussing on what will happen, not what should happen
- Additional support from:
 - ▶ Linkages between days of inflow and outflow; and notice of large payments

■ Using the Forecasts

- Integration or close coordination between debt and cash management
 - ▶ Issuance linked to cash profile of deficit/surplus
- Active cash management
 - ▶ Borrowing (Tbills)
 - ▶ Lending (repo or deposits)
- Decision-making process/ structures
 - ▶ E.g. Cash Coordination Committee
 - ▶ Information flows with central bank

Coordination between Debt & Cash Management

Integration of (or close coordination between) cash and debt management functions ensures:

- Debt issuance decisions are taken in the context of the seasonal nature of government's cash flows
- Single unit has overview of whole market – important when taking decisions about the future balance of short- and long-term debt, including Treasury bills

Other day-to-day coordination requirements include:

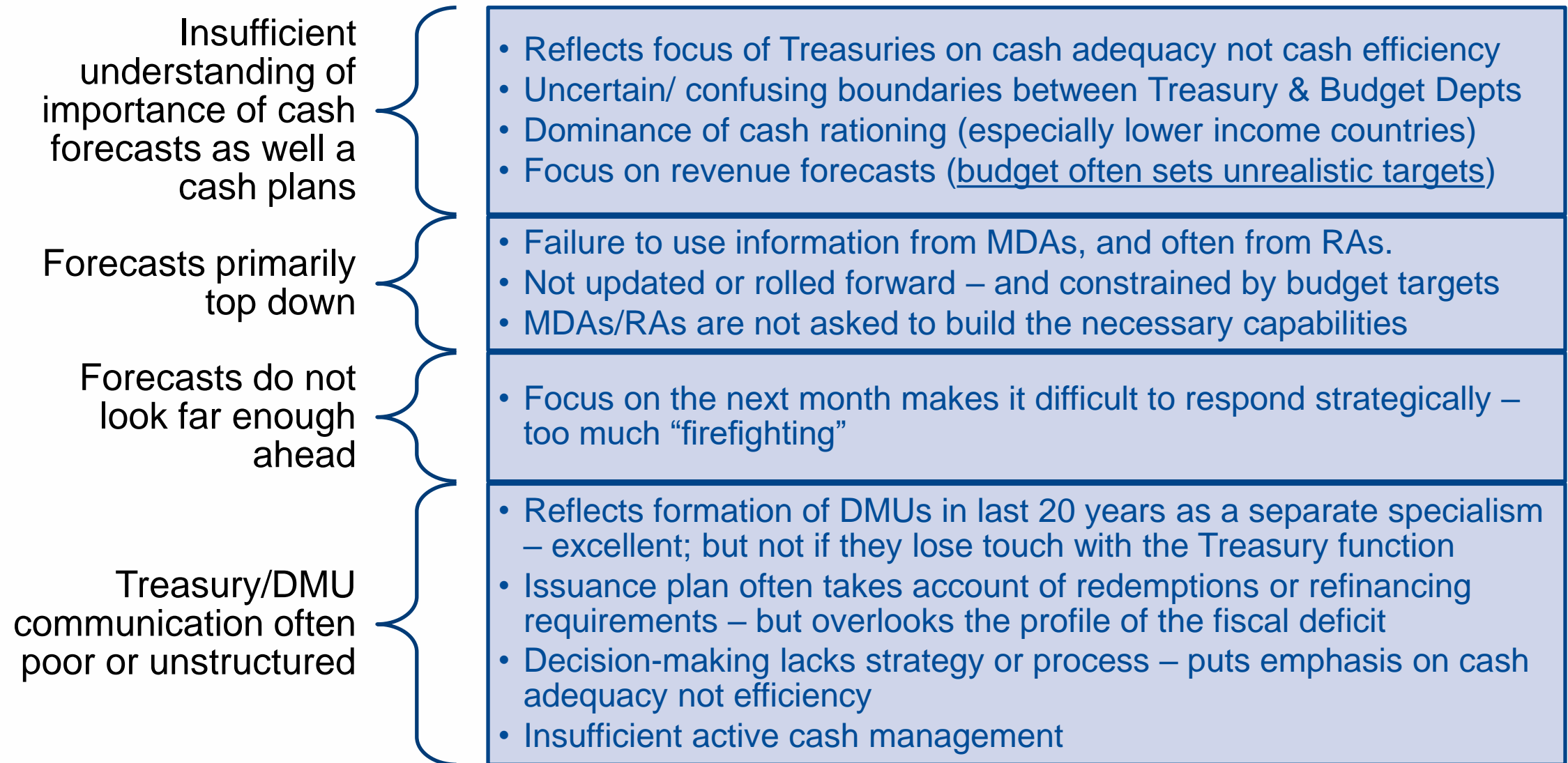
- Linkage of issuance dates with redemption dates
- Maturity dates chosen to avoid weeks, especially days, of heavy cash outflow (eg salary payments): instead target days of cash inflow (due date for tax payments)
- Debt managers can mitigate the cash management problems that potentially arise when large bonds come to maturity
- Debt managers can also correct repo market distortions or disruptions

As interaction with the market develops, integration becomes especially important

- In time, active management of the short-term cash position helps to weaken the link between the timing of cash flows and of bond issuance. Allows pattern of bond sales to be announced in advance
- Ensures that the government presents a consistent face to the market

Overview of International Experience

Based on work in 39 countries, including several LI, LMI



The Move to More Active Cash Management

Internationally there is a move from passive cash management

- Monitoring cash balances, maintaining cash buffer to handle volatility and unanticipated outflows
- If necessary, restraining expenditures / delaying payments - cash “rationing” not cash management

To more active management

- Smoothing weekly or daily cash flow by more active borrowing and lending in money market
- Allows lower average cash buffer – with benefits to other policies
- Gives tools to protect expenditure plans from cash flow volatility

Distinction between passive and active is not either/or
But active cash management is more demanding

Requires

- Reliable & high-frequency cash flow forecasts over a sufficiently long horizon
- A well-developed coordination framework with debt managers & central bank
- A range of available instruments in a money market with some liquidity

The Objective: Characteristics of Modern Cash Management (1/2)

1. A Treasury Single Account (TSA) for pooling liquidity, held preferably at the central bank (there are only a few exceptions)

2. A government direct payments system, centralized through a Treasury-managed TSA, or decentralized payment by ministries and agencies through zero-balanced bank accounts (ZBAs) linked to the TSA

3. Immediate transfer of all government revenues to TSA, including of “own-revenues” of line ministries and agencies

4. Policies for matching expenditure and revenue flows, including fixed timing of central government grants to provinces, linking tax payment days to salary payment days etc

5. Ability to make reliable projections of short-term cash inflows and outflows

Characteristics of Modern Cash Management (2/2)

6. Timely information sharing between the Treasury, revenue-collecting agencies, spending ministries; and between Treasury and the central bank


7. Clear responsibilities and institutional arrangements between Treasury and line ministries/agencies, inc. submitting cash plans

8. Targeting a remunerated TSA balance or target zone (if money markets are deep and liquid, usually a very small positive balance)

9. Use of short-term financial instruments, both on the liability and on the asset side, to borrow cash as needed and invest temporary surplus cash

10. Close interaction with the debt management department; and understandings with the central bank on the interaction with monetary policy operations

Cash Management is a Project

- Most of the actions are for the Treasury to take forward, with support as necessary from others in the MoF
- But effective cash management also needs:
 - A supportive central bank.
 - Competent finance functions in spending units and the tax departments to supply good cash flow forecasts - and see it as part of their responsibility to do so.
 - A flexible banking system and a developed money market.
- Development of cash management therefore best thought of as a project
 - Dependencies, bottlenecks and a need to prioritise
 - Needs also to link with money market development
- Four streams of work 

Within the Treasury or MoF

- Develop policies and systems for TSA, forecasts, instruments
- Build capacity: systems, people, training
- Legislation and regulations

Between the Treasury and spending agencies & revenue authorities

- Ensure effective TSA; build cash flow forecasting and flow of information

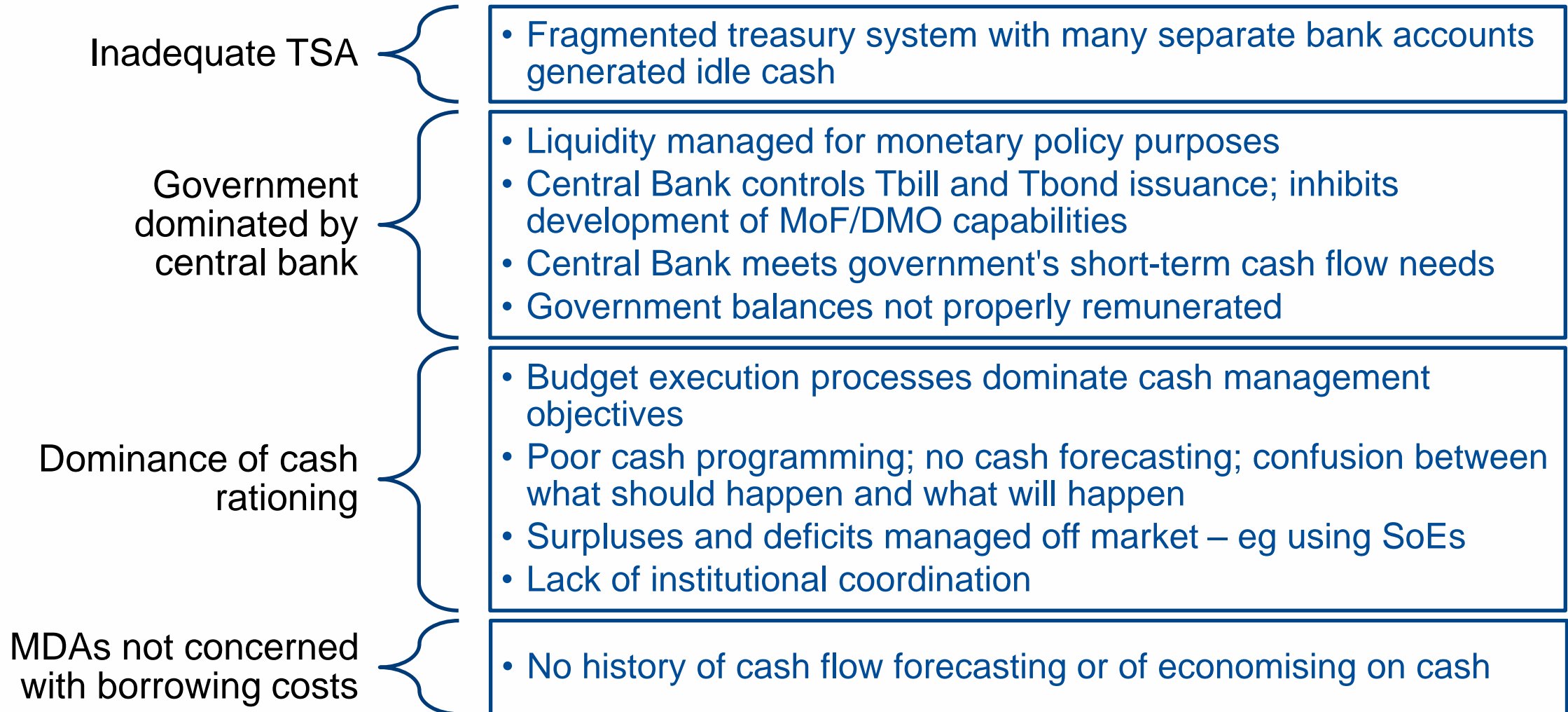
Between the Treasury and Central Bank

- Establish high level policy; agree MoU and SLA
- Money market development programme

Between the Treasury and the financial market

- Money market development
- Policy communication & consultation

Some Common Problems



The Development Process



Active Cash Management

- Rough tuning = the issue of Treasury bills (or other bills) in a pattern designed to offset liquidity impact of net daily cash flows
- Fine tuning = more active policies, with a wider range of instruments, to smooth more fully MoF's balance at central bank

The Way Forward (for most countries)

- Move to rough tuning (fine tuning more demanding)
- Develop capabilities incrementally – but as steps on a route to an understood objective
- Work on different phases can proceed in parallel

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