Government Cash Management Relationship
Treasury and the Central Bank

Submitted by: AIPEG
Government Cash Management Relationship Treasury and the Central Bank

APEC Workshop on Treasury and Budget Reform
Agenda

- Workshop Session 1 goals
- Treasury perspective
- Central Bank perspective
- Treasury & Central Bank – shared interest in market development
- Managing the relationship
Session 1 Objectives

- “Identify best practices that may improve governance and achieve efficiency and effectiveness of government treasury functions and liquidity control”
- “Identify any measures that can be used to strengthen the coordination between Government and the central bank”
- “Choose measures that ensure the best option to deal with harmonizing the need of government and the need of the Central Bank”
Treasury perspective

Effective cash management
Effective cash management

- Cash management function arises from mismatch between the timing of payments and the availability of cash

- “The strategy and associated processes for managing cost-effectively the government's short term cash flows and cash balances, both within government, and between government and other sectors.”
Goals of cash management

- Adequate cash to pay for expenditures
- Borrow only when needed to minimize borrowing costs
- Maximize returns on idle cash
- Manage risk by investing temporary surpluses effectively against adequate collateral
Effective cash management – 9 Principles

- Centralizing government cash balances – TSA system
- Defining coverage of the cash management framework
- Accurately projecting short term cash inflows and outflows
- Adequate transaction processing and accounting framework
- Timely information sharing between the treasury, revenue collecting agencies, and spending ministries
- Appropriate institutional arrangements and clear responsibilities
Plus 3 desirable features

- Utilization of modern banking, payment, and settlement systems
- Use of short term financial market instruments for cash management
- Integration of debt and cash management
Cash Forecasting Framework

- A comprehensive framework that aligns expenditure planning and actual cash spending as well as incentivizes budget institutions to supply realistic plans
- Consistent with annual budget plans
- Concentrate on major inflows and outflows
- Identify past patterns of particular inflows and outflows
- Identify the timing of major flows
- Involve links between the treasury and revenue collecting agencies for the preferred timing of inflows
- Involve links between MoF and ministries at operational levels
- Ascertaining cash needs from expenditure commitments
- Distinguish information sharing from expenditure control
Responsibilities for Forecasting

Ministry of Finance  Treasury Department  Debt Office

Forecast Compiler (Above the Line)  Forecast Compiler (Below the Line)  Forecast Coordinator  Front Office

Forecast / Updates  Central Bank

Spending and Revenue Departments  Financial Market

TSA  Transactions
Links Cash and Debt Management

- Institutional arrangements - coordination/integration
- Cash manager a shorter term perspective with focus on timing
- Debt manager a perspective guided by a medium term debt strategy that is reflected in an orderly issuance plan.
- Debt manager choices on instruments, domestic/external, short/long, fixed/floating, retail/wholesale.

- Linkages
  - Issuance and redemption dates
  - Maturity dates versus other cash developments
  - Cooperative T bill and money market action can help smooth cash
Central Bank Perspective

Monetary policy with inflation target focus
Monetary policy objectives

- Anchoring the yield curve around the policy rate
Cash management and monetary policy – an evolution of challenges

- Early challenges of liquidity control
- Increasing coincidence of interests
- Managing risks to policy implementation
Challenges of liquidity control

- Excess idle cash either unremunerated or at below market rates
- Government cash flows source of short term volatility of liquidity and perhaps money markets
- Government actions conflict with monetary policy signals
- Central bank lending to finance government spending increases the monetary base
Increasing coincidence of policy interests

- Government related cash flows likely to remain the most volatile element of liquidity.
- But, if cash management is effective by targeting a low and stable level of cash then the central bank can conduct monetary policy effectively.
- Constraints may remain such as lack of adequate T bills that creates need for central bank to use own short term paper.
Managing risks to policy implementation

- With more sophisticated and effective cash management, new issues with central banks arise – largely in the nature of operational coordination.
- As Treasury becomes more active in the money market it should make sure that it does not undermine the central bank’s open market operations.
- Treasury should provide cash flow forecasts
- Central Bank should keep Treasury informed of flows and balances across the TSA, ideally in real time
- Arrangements of information exchange should include money market developments.
Financial market development

A shared interest
Financial Market Development

Interbank Market
- Clearing / settlement balances

Overnight Market
- Overnight funds
- Loans / Deposits (Repos)

Term Money Market
- Maturities 2 days to 1 year
- Tbills, CP, term deposits & Repos

Bond Market
- Securities > 1 year to maturity

Monetary policy

Cash Management

Primary T-Bill Market

Debt Management

Primary Government Bond Market

Money Market
- Maturities < 1 year

Foreign Exchange Market

Collateral
Managing the relationship
Relationship operates at different levels

Macroeconomic Policy

- Coherence of monetary policy with government financing and fiscal policy

Monetary Policy

- Interaction of govt debt and cash management interacts directly with monetary policy

Banking System

- Debt and cash management use the banking system for transaction services or as a counterparty

Central Bank

- Treasury’s banker providing services such as managing the TSA and serving as an agent for auctions, settlement and registration
Coordination – policy and operational

- Senior level meetings – ensuring policy coherence
- Standing committees such as a public debt committee and treasury liquidity or cash coordination committee
- Technical working groups
- Day-to-day operational interactions.
Cash Coordinating Committee

- Head of Treasury
- Head of Debt Management
- Head of Fiscal and/or Budget directorate
- Central Bank Representative
- As required representatives: revenue administration, customs, larger line ministries
- Secretary from Treasury
Agreements

- Policy Functions
  - Memoranda of Understanding and protocols

- Service Level Agreements
  - Services of a quasi contractual nature may find a SLA useful
Conclusions
Conclusions

- Principles of effective cash management – a necessary condition for sound collaboration with Central Bank

- Effective coordination of cash and debt management – serves monetary policy and market development

- Financial and money market development can be at the center of Treasury and Central Bank collaboration

- Treasury and Central Bank building an effective relationship based on clear foundation of MoU and SLAs