PEMPAL TREASURY COMMUNITY OF PRACTICE (TCOP)
Thematic Group on Cash Management and Forecasting

Moving to More Active Cash Management

Videoconference, January 28, 2025

Introduction

1. On January 28, 2025, the PEMPAL Treasury community of practice held a videoconference on *Moving to More Active Cash Management*. The objective was to revisit in more detail the development of more active cash management, with a discussion of how the forecasts are used, of cash management instruments, and of country practices in applying them. The meeting was attended by 29 TCOP members from 14 PEMPAL countries (Albania, Azerbaijan, Bosnia and Herzegovina, Croatia, Georgia, Hungary, Kazakhstan, Kosovo, Kyrgyzstan, North Macedonia, Romania, Tajikistan, Türkiye, and Uzbekistan) as well as a representative of the Ministry of Finance of Indonesia. The meeting was facilitated by the World Bank resource team comprising Ms. Elena Nikulina (TCOP Resource Team Leader), Ms. Galina Kuznetsova and Ms. Elena Dobrolyubova (TCOP Resource Team Members), and Ms. Tetiana Shalkivska (TCOP Secretariat).

2. **Ms. Elena Nikulina** welcomed the participants and introduced the meeting objectives and the agenda. She highlighted that, during the recent thematic meeting in Tirana, a number of TCOP members showed a strong interest in how to implement active cash management, hence the VC was organized to revisit this issue and discuss it in more detail.

Moving to More Active Cash Management: Forecasts, Instruments and Country Practices

3. The main presentation was delivered by **Mr. Mike Williams,** TCOP Thematic Advisor. The presentation provided insights into the objectives of active cash management, highlighted the crucial role of cash forecasts, and elaborated on active cash management prerequisites, including the instruments, policy and legal framework, the need for coordination with public debt management and monetary policy, and capacity building.

4. Active cash management refers to smoothing cash flows by utilizing short-term borrowing and lending instruments targeting (a range for) the TSA balance in a manner designed to offset the impact on the banking sector of net cash flows in and out of government. It provides important benefits both to the treasury by reducing the cost of maintaining an unduly large cash buffer and protecting expenditure flows from cash volatility and to other policies, including monetary policy (by reducing volatility of banking sector flows), wider money market development, and debt management (by protecting the bond issuance programme). Implementing active cash management practices has several important prerequisites and is best taken forward as a gradual process of adopting new instruments and acquiring capacity (Fig. 1). Availability of reliable and frequent **forecasts of cash flows** over a sufficiently long time horizon is among the core prerequisites for actively managing cash.

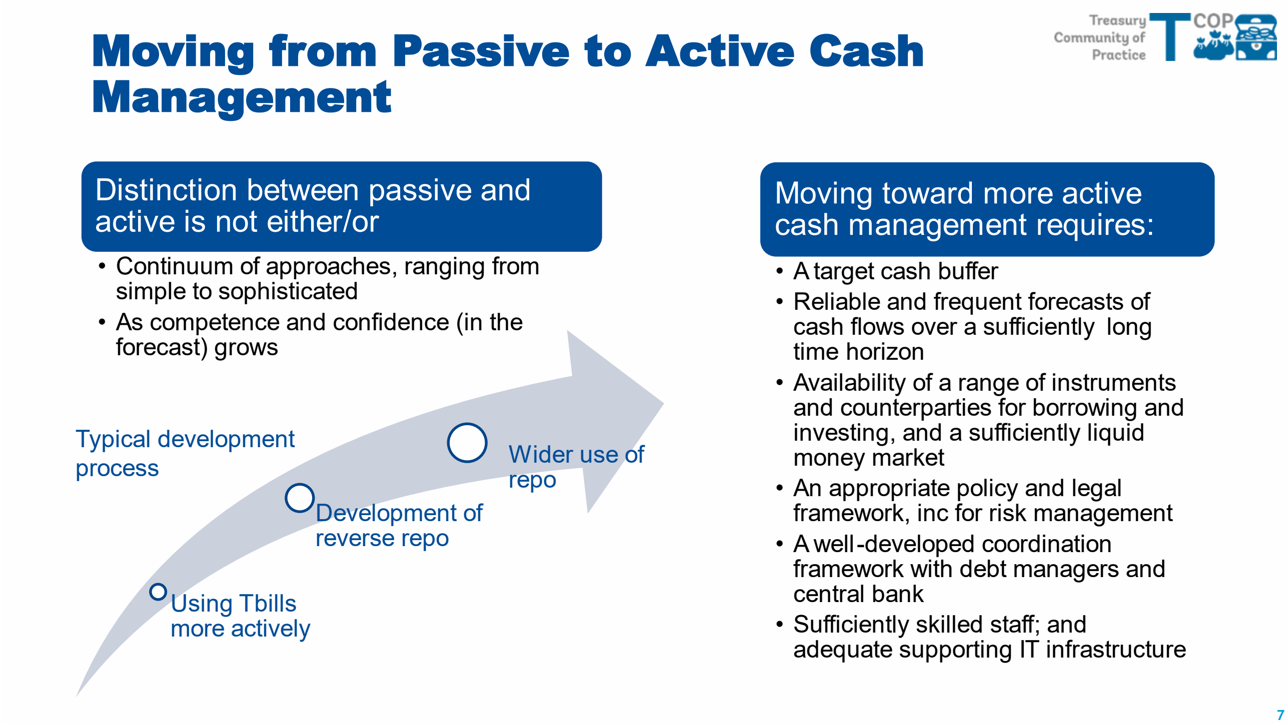

Fig. 1: Moving from Passive to Active Cash Management: Process and Pre-Requisites

5. Active cash management instruments for **short-term borrowing** include Treasury bills (Tbills), with an emphasis on short-term (e.g. 1-month) Tbills and Tbills with odd maturities, and Repo. The instruments used for **short-term investments** of temporary surpluses include reverse Repo, and deposits in commercial banks (which need to be collateralized to reduce the credit risk). Deposits in the Central Bank are also relevant, but only when there is a structural excess of liquidity in the market. The focus must be on short-term cash deficits and surpluses, as defined by the forecast; longer-term or structural deficits and surpluses call for other instruments (i.e., longer-term borrowing or investing structural surplus in stabilization, wealth or similar funds). Large foreign currency balances are not usually recommended, for both cost and risk reasons, but where some balances are maintained they could be drawn on (either directly or via SWAP operations) as part of the cash management safety net. The 2021 Cash Management Survey showed that while some PEMPAL countries use active cash management instruments, their application was limited. Thus, most countries had a possibility to issue short-term Tbills, eight countries were able to invest temporary surpluses in commercial banks, but only three countries had the capability to use repo for lending and borrowing.

6. Active cash management requires an adequate policy framework (Table 1) and legal framework. The policy framework should set objectives of cash management, specify acceptable instruments and risks, and establish performance criteria. The legal framework should set high-level objectives and provide adequate powers for the MoF to borrow to support the efficient management of the government's cash flows, and to invest surplus balances in the financial markets (or as term deposits in the central bank). However, the legislation should also allow flexibility in the use of various instruments and should not constrain maturities, the ability to borrow across the year end, or the central bank's ability to remunerate deposits.

Table 1: Policy Framework for Active Cash Management

Component	Issues Covered
Objectives	• Ensuring cash availability, smoothing cash flows • Cash buffer objectives • Risk, liquidity, yield objectives • Include build up of assets to meet end year expenditure surges
Clarity on acceptable instruments	• Including maturities (geared to cash flow profile; loans/deposits redeemed on days of cash outflow)
Specification of risks; policy towards market, credit, liquidity, legal and operational risks	• Identification of acceptable counterparties • Contractual requirements (GRMA) • Requirements for and handling of collateral • Mode of accessing market (tenders, bilateral price quotes, platforms, etc) • Market consultation
Establishing performance criteria	• Targeting a (range of) TSA balance

7. Active cash management is closely linked with debt management and monetary policy which requires continuous coordination across the functions. In some countries, such coordination is ensured by integrating the functions of public debt and cash management in one department. Cash Coordination (Liquidity) Committees with participation of Cash Management Department, Debt Management Department, the Central Bank and other relevant departments present another form of such coordination. Whatever the institutional structure, the same front office should execute both borrowing and lending transactions. Memorandums of Understanding and Service Level Agreements are also useful tools providing a sound basis for coordinating cash management and monetary policy operations. Finally, moving to more active cash management calls for developing internal procedures and building institutional capacity (Fig. 2).

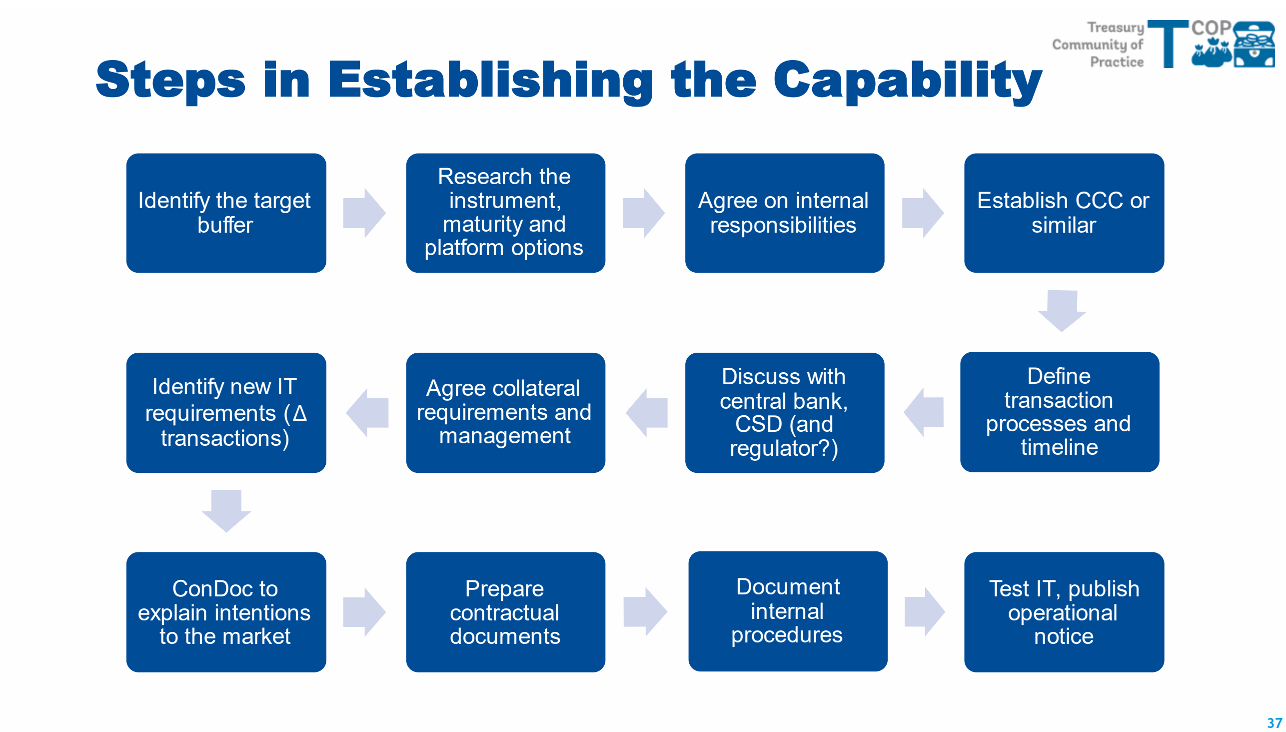

Fig. 2: Operational Steps in Introducing Active Cash Management

8. **Ms. Nikulina** thanked Mr. Williams for a comprehensive presentation and noted that, since the 2021 Thematic Survey on cash management some more countries, including Uzbekistan, have adopted such instruments. She invited representatives of two PEMPAL countries, Romania and Georgia, to share their experience in active cash management.

Active Cash Management in Romania and Georgia

9. **Mr. Romeo Dumitru,** General Directorate of Treasury, Ministry of Finance of Romania, shared the experience of Romania in using active cash management instruments. Overall, the legislation in Romania provides for the possibility of using both temporary investment and temporary borrowing instruments. However, the current cash deficit meant that only borrowing instruments are currently used in practice. There are three instruments that could be used for temporary borrowing:

- Government bonds **(Tbills)** for a period of *1 month, 3 months, 6 months* (although the banks tended not to be interested in such short-term securities; in 2024, the treasury had 8 operations with a maturity of 7 months, 6% of total CTN and DBN issues, the total amount representing 9% of total issuance);
- **Sale of foreign currency** from the buffer (using direct transactions with the Central Bank, potentially also SWAPs although they have yet to be used); and
- <u>**Loans**</u> **from commercial banks (deposits received from banks),** which represent the most frequently used instrument, with overnight, 1 week, 2-3 weeks, and 1 month maturities (the loans are attracted from large or in some cases also medium sized-banks; these loans may be bilateral or multilateral – the latter being attracted by auctions).

10. In some cases, a mix of instruments (for instance loans from commercial banks and foreign currency operations) are used on the same day to ensure an adequate balance on the TSA.

11. **Mr. Erekle Gvaladze,** Treasury of Georgia, shared the experience of Georgia in temporarily investing cash surpluses. Since 2017, Georgia has been using auctions to place temporarily available funds in commercial banks. The deposit maturities vary from 1 to 6 months, and 99% of all auctions require collateral to reduce risks (the auctions without collateral target smaller banks). The procedure involves three steps, including a preparatory stage, when the amount, date, maturity, and auction type are defined and the auction is announced; the auction itself; and post-auction when the collateral is received and payment made. The Central Bank reference rate is used as a minimum rate for auctions.

12. Mr. Gvaladze highlighted the positive outcomes of the auction practice, including additional revenues to the budget, effective management of public resources, additional sources of liquidity for the banking sector, and institutional development of the treasury.

Discussion

13. **Ms. Nikulina** thanked Mr. Dumitru and Mr. Gvaladze for their insightful presentations and welcomed all participants to join the discussion.

14. **Mr. Williams** commented on a question from the Ministry of Finance of Indonesia related to the need for differentiating cash management bills. He noted that some countries differentiate Tbills used

for cash management, but the need for that depended on communication with the market. The objectives of short-term borrowing should be made clear so that the market did not conclude that the government's borrowing reflected a structural fiscal shortage.

15. **Ms. Mimoza Pilkati,** Head of Treasury Operations Department, Albania, thanked the Resource Team for the opportunity to learn about the experience of Romania and Georgia and noted that in Albania the Central Bank is a fiscal agent of the government. Notably, some years previously treasury and debt management functions were performed by the same directorate within the Ministry of Finance. Currently, there are two General Directorates for these functions, but a Coordinating Committee is meeting monthly to ensure proper coordination of cash management and debt management. **Ms. Nikulina** thanked Ms. Pilkati and noted that representatives of both directorates participated in the recent thematic meeting in Tirana, where the approaches to coordinating debt and cash management were discussed in detail[1].

16. **Mr. Gvaladze** asked Mr. Williams whether the functions of debt and cash management can be divided into rough-tuning (done by debt managers for a longer horizon, for instance by issuing Tbonds) and fine-tuning (implemented by cash managers for a shorter horizon). **Mr. Williams** stressed that, to minimize the risk of confusing signals coming from the Ministry of Finance, the same front office should transact Tbonds, Tbills, and surplus investment. There were sometimes policy differences; for example, in some countries debt managers were reluctant to issue short-term securities because of the impact on the portfolio average term to maturity and refinancing risks (although in practice the use of Tbills for cash management purposes usually had a limited impact on such indicators).

17. **Mr. Gvaladze** also asked Mr. Dumitru if the Romania Treasury had preferred banks from which to borrow. **Mr. Dumitru** noted that working with large commercial banks was the preferred option. He also commented that, to coordinate debt and cash management policy, a Financial Committee meets monthly and discusses Tbills and Tbonds issuance as well as other methods to cover cash gaps.

18. **Ms. Nikulina** noted that the cash buffer in Romania was kept in foreign currency and asked Mr. Dumitru about the reasons for such approach. **Mr. Dumitru** noted that the funds borrowed from the external market in EUR or USD are not converted and instead provide a buffer in circumstances when market conditions are unfavorable for issuing new debt externally (or refinancing public debt). For instance, since the Romanian budget for 2025 has not been yet approved, the Ministry of Finance cannot issue new securities in EUR but can draw on the foreign currency buffer. Moreover, as it is not always possible to borrow sufficiently from the commercial banks, the foreign currency balances provide additional flexibility for cash management. **Mr. Williams** noted it was very unusual to rely entirely on a foreign currency, rather than a domestic currency, buffer, although he acknowledged that some countries maintain buffers in foreign currency to cover the upcoming foreign currency payments.

19. **Ms. Nikulina** thanked everyone for participating in the videoconference and noted that cash management remained an important subject on TCOP's agenda. To support the further development of cash management practices in the PEMPAL region, the TCOP Executive Committee asked the Resource Team to prepare a paper on liquidity committees. She informed the participants that the next TCOP

[1] For more information, please see the Event Report for the Thematic Meeting in Tirana, available at: https://www.pempal.org/events/pempal-tcop-thematic-meeting

thematic VC is planned for late February. It will follow up on the experience of the Treasury of Indonesia in data analytics and provide an opportunity to learn about the results of the recent data analytics readiness assessment (DARA) conducted in the Ministry of Finance of Indonesia. The next face-to-face TCOP event will be organized on March 27 in Vienna, back-to-back with the Whole-of-Network Plenary. **Mr. Erekle Gvaladze** invited the participants to join the Extended Study Visit to Georgia which would be held on May 28-30.

Conclusions

20. **More active cash management brings important benefits both to treasuries but also to debt management and monetary policy**. It allows a lower average cash buffer and reduces associated costs, reduces volatility of banking sector flows, supports money market development and adds to financial resilience. Attaining these benefits calls for several important prerequisites, including high-quality cash forecasts, adequate policy and legal framework, risk management, effective coordination with debt management and monetary policy, and continuous capacity building.

21. **Implementing active cash management is not a one-off project, but rather a gradual process of institutional development and capacity building, and adoption of more sophisticated instruments**. At the early stages countries are mostly engaged in 'rough tuning' cash imbalances using Tbills; as the treasury institutions and markets mature, more sophisticated instruments such as repo and reverse repo are being introduced to 'fine-tune' cash flaws and further reduce carry on costs.

22. **As illustrated by the practices shared by the treasuries of Romania and Georgia, active cash management instruments should be tailored to specific country contexts and needs**. Although one country (Romania) focuses on short-term borrowing and another country (Georgia) on short-term investment, both approaches bring benefits and reduce financial risks (by adopting a mix of instruments and as necessary requiring collateral) and emphasize the efficiency concerns (by minimizing borrowing and maximizing lending rates). Thus, the optimal set of active cash management instruments depends not only on treasury capability, but also on the market conditions and the fiscal context.

23. **Effective coordination between cash management, public debt management, and monetary policy** is an important prerequisite for implementing active cash management practices. Liquidity Committees present one of the approaches to ensure such coordination. Since there is high interest in active cash management in PEMPAL countries, a knowledge product on Liquidity Committees will be prepared.