



## Special Series on Fiscal Policies to Respond to COVID-19

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# Government Cash Management Under Fiscal Stress<sup>1</sup>

Faced with decreasing revenues and constrained access to financial markets, governments must address the challenge of meeting extended cash needs to finance COVID-19-related emergency spending. A multi-pronged approach to cash management is required to ensure that liquidity is adequate to satisfy the government's payment obligations.

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## I. KEY CHALLENGES

**The role of cash management is to support the smooth execution of the government's budget, even in times of crisis.** The government's cash plans should be adjusted to reflect increased emergency spending, concurrent drops in revenues, and the financing of the crisis-related spending measures. The main task of the government's cash managers<sup>2</sup> is to ensure there is adequate liquidity to meet the government's payment obligations as they fall due. In performing this task, the crisis poses several challenges, notably:<sup>3</sup>

- How to identify and estimate the impact of the crisis and the various emergency policy responses on the government's cash operations?
- How to forecast the government's daily cash balance position and its cash flow requirements?

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<sup>2</sup> This note discusses the government's cash management function and the unit which executes this function. This function is often located in the treasury department of the finance ministry or the accountant general's department, but sometimes elsewhere, e.g., in the debt management department.

<sup>3</sup> For implications of the COVID-19 crisis on wider PFM systems, see S. Saxena and M. Stone, "Preparing PFM Systems for Emergency Response," *IMF Special Series on Fiscal Policies to Respond to COVID-19*. For implications of the COVID-19 crisis on debt management, see *IMF Special Series* note on "Debt Management Response During the Pandemic."

- How to find enough cash resources to meet increased liquidity needs while financial markets are highly stressed?

**A response to these challenges should be centered around the 4 main pillars of modern cash management:** (i) cash consolidation; (ii) cash forecasting; (iii) management of cash balances; and (iv) institutional and organizational arrangements. The objective should be for cash managers to utilize all available sources of liquidity in the best way possible.

**The following sections provides a suite of measures that countries could take to address these challenges.** Countries should focus on the measures that are most relevant and feasible given their capacities and the local context. Those with a relatively well-developed cash management function will not only be better positioned to manage the impact of the crisis but also have a wider range of available instruments to safeguard their liquidity position. Countries that are at an earlier stage of development can still take steps to improve their cash management. The crisis also creates an opportunity for countries to initiate structural reforms that could bring lasting benefits over the medium term.<sup>4</sup>

## II. CASH MANAGEMENT: SUGGESTED MEASURES

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**Cash consolidation will help in pooling all the cash at the disposal of the treasury, facilitating its best possible use under highly stressed fiscal conditions.** Governments that have a functional Treasury Single Account (TSA) structure in place will find it easier to monitor and control their cash flows and balances during the crisis. Such countries could look for any available opportunities to further expand the TSA coverage and to improve the speed with which cash flows through the system. Many governments, however, hold numerous accounts for government ministries, agencies and extra-budgetary entities (EBEs) that are outside the treasury's control.

**Relevant short-term cash consolidation measures include the following:**

- Empower the treasury to take the actions required to consolidate the cash held by government ministries, agencies and EBEs into the TSA or the government's main account.
- Focus on identifying any significant central government cash balances currently held outside the TSA or the main account. A treasury directive to banks to share information on such balances may be an efficient way of identifying potential candidates for consolidation.
- Countries without a TSA should still aim to monitor the overall level of consolidated cash balances. This information will be useful in identifying the resources and needs of government entities. Entities with adequate cash resources in their own bank accounts can be directed to use their own cash first.
- Where feasible, in consultation with the central bank, such countries should take steps to consolidate commercial bank account balances within their main account. For example, sweeping arrangements can be established to transfer overnight balances in commercial bank accounts to the treasury's main account at the central bank. Sweeping does not require the closure of individual bank accounts which are still needed for transactional purposes. The central bank should consider the impact of such arrangements on the banking system's liquidity position.

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<sup>4</sup> Many South East Asian countries, for example, pursued TSA reforms in the aftermath of the Asian financial crisis of the 1990s. As a first step, a main government account can be designated as the seed of a TSA system which serves as the basis for cash consolidation.

- Countries that rely on cash distribution—due to constraints on cash pooling from a lack of modern banking technology—can explore options for establishing credit lines with banks to ensure uninterrupted delivery of critical public services.
- The treasury should consult public corporations, pension funds and EBEs that hold large idle cash deposits and explore options for establishing on-demand short-term borrowing arrangements with these entities.<sup>5</sup>
- In the current crisis, several countries have established emergency response funds that accept donations and earmark the resources for specific spending needs (e.g., Gabon, Ghana, Nigeria, Kenya). These funds should ideally be set-up as sub-accounts of the TSA under the oversight of the treasury who can monitor the government's overall cash availability. In any case, accounting for all receipts and donations and their utilization should comply with public financial management laws and rules and be subject to strict governance control and reporting requirements.
- Opening new bank accounts outside the TSA to manage funds dedicated to crisis-related expenditures is best avoided. Doing so entails the risk of fragmenting the cash management function and hampering the oversight of cash balances.
- Where needed, banks which receive deposits of taxes and other government revenues should be instructed to transfer these revenues into the TSA (or the designated main account) as soon as possible, so that the cash becomes available for utilization by the treasury.
- The treasury should closely monitor movements in the TSA balances on a real time (or at least daily) basis. If needed, it should require the central bank to provide online access to their account(s) or, alternatively, to make available end-of-the-day balance reports.

**Reliable and timely cash forecasts are critical for decisions on managing the government's cash flows and balances.** Given the heightened volatility in revenue and expenditure and the uncertainty associated with the disbursements of emergency spending, maintaining the reliability of cash forecasts will be challenging. Top-down forecasts may suffer from a lack of credible assumptions, and past patterns of spending and revenue may no longer be a good predictor of future cash flows. The government's strategy should be to gather high-frequency (ideally daily or weekly) bottom-up information that is needed to prepare reliable forecasts. Delays in official communications between agencies may, however, challenge efficient data collection.

**Relevant short-term measures for reliable and timely cash forecasts include the following:**

- Focus on the short-term cash flow impact of fiscal policy measures and macro-economic developments in coordination with the finance ministry's budget and macro-fiscal analysis departments and the revenue collection authority.
- Identify key points of contact (e.g., the finance ministry, or the office of the president or prime minister) to get timely updates on any emergency funding (e.g., from development partners) and/or debt relief to help improve the accuracy of top-down forecasts.
- Establish direct (and, if needed, informal) communication channels with major spending agencies—especially the health ministry and other sectors managing emergency spending—and the revenue collection

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<sup>5</sup> For example, the Argentinian treasury has an arrangement with the *Banco de la Nación*—where all government agencies hold their bank accounts—for interest-free overdrafts against the cumulative balances of these accounts. In Greece, the Treasury Accounts System allows the central government to monitor idle cash balances of entities outside the central government, which may be accessed through repo arrangements if there is a need. In Turkey, in the 1990s following a financial crisis, a Common Public Sector Treasury Account was established to allow the Central Government Treasury to monitor financial resources/cash of public sector institutions. The Treasury used this information in its cash management operations.

authority and seek high frequency updates to the cash plans or forecasts. Cash forecasters in the treasury should reach out to their counterparts in these agencies every day or week. The focus should be on identifying larger cash flow items, including those related to the emergency, and getting them right.

- If necessary, cash managers should shorten the cash forecasting horizon to the bare minimum required for conducting auctions of T-Bills and other instruments that are required to maintain an adequate cash balance. In most cases, a forecasting horizon of 4–6 weeks should suffice for immediate needs, but cash managers should take account of pressures that may arise over a longer period.
- Update aggregate cash forecasts daily based on movements in the TSA (or the treasury's main account balance) and fresh bottom-up information.
- Develop scenarios to inform decision making. In an environment of uncertainty, in addition to a baseline forecast, a worst-case scenario accounting for delays in financing and disruptions in revenue collection should be developed to analyze their potential effects and develop options to respond.
- Cash flow scenarios should also include the possibility that contingent liabilities will be realized. Debt managers should seek information about the payment schedule for guaranteed loans in the near-term and the likelihood of beneficiary agencies asking for government support. Major public-private partnership contracts should be reviewed to identify likely materialization of contingent obligations. Likewise, exchange rate fluctuations will have to be factored into the forecasts of debt repayments that are denominated in foreign currency.
- Share and discuss every day (or week) the cash forecasts with the budget office, debt managers and the central bank, along with a brief explanation of major changes since the previous forecast.
- Closely monitor actual cash outturns, investigate the reasons for forecast errors and feed the results of this analysis back into the forecasts for the next period. Where needed, consult counterparts in line ministries. Understanding the underlying causes of deviations (whether there is a permanent change in the pattern of spending or a change in the timing of cash flows) is necessary under stress conditions so that forecasts can be realistically updated. Informality in consultations could be useful in ensuring timely information.

**The government's management of cash balances should be geared to maintaining the required balance in the TSA.** The strategy should be to tap all available sources, with due regard to costs and risks.

**Relevant short-term measures to manage cash balances include the following:**

- Explore the possibility of establishing (or expanding) credit lines with banks and overdraft facilities with the central bank.<sup>6</sup> Such arrangements can substantially reduce pressures on cash managers, but their use should be regulated to bridge temporary cash shortages, not to provide another source of deficit financing. Such facilities should come with a ceiling and a time limit and be interest bearing.
- Recalibrate the cash buffer levels. A cash buffer is the government's safety net against cash flow volatility. Several governments set up or increased these buffers in the aftermath of the Global Financial Crisis (GFC). Increased volatility in cash flows and tighter market conditions may require a review of the cash buffer levels. Cash managers should calibrate the likely impact of the current crisis on the government's cash position to guide decisions on what would be an appropriate level of the buffer, and how much to draw down

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<sup>6</sup> For example, the Sri Lankan treasury has established credit lines with selected commercial banks. Countries such as Bangladesh and India have a 'ways and means' (W&M) facility from their respective central bank, which allows the TSA balance to go temporarily into deficit. The UK Treasury and the Bank of England have recently agreed to extend temporarily the use of the W&M facility to provide an additional source of liquidity to the government.

or top up, as part of the government's overall fiscal policy response. Enhancing the use of the cash buffer is especially useful for governments that have weaker forecasting capacity and poorer access to money markets. The buffer should be part of the TSA or invested in call deposits with the central bank.

- Countries with cash reserve funds can explore how much these resources should be drawn down and over what period, so the government can decide on their utilization. Some countries maintain foreign exchange (forex) reserve funds, which may be tapped into, if necessary and where feasible. Sinking funds reserved for future debt service can also provide temporary relief to meet immediate cash needs.
- In some countries, it may still be possible to invest temporary liquidity surpluses. The strategy should be to invest in low credit risk and shorter maturity instruments to guard against credit quality, liquidity and interest rate volatility. Governments must be able to break their deposits on call, with a penalty.

**Institutional arrangements should be strengthened to undertake the required cash management actions.**

These arrangements should be anchored in the government's overall plan for managing the fiscal crisis, led by the finance minister. Enhanced coordination among departments within the ministry of finance and key counterparts, including spending and revenue collection agencies and the central bank, is crucial in periods of severe liquidity pressure.

**Relevant short-term measures to strengthen organizational arrangements include the following:**

- Empower the Cash Management Unit (CMU).<sup>7</sup> If a CMU is not already in place, a small dedicated team could be formed as a Cash Management Working Group (CMWG) comprising cash managers and representatives from other departments of the finance ministry. The CMWG should be responsible for making cash flow forecasts—reaching out to counterparts in ministries and agencies—and advising on the management of cash balances. International experiences suggest a team of 2-3 staff can suffice for these tasks. The CMU (or CMWG) should closely coordinate its forecasts and actions with the central bank. There should be regular exchanges of information among all concerned departments and agencies on cash forecasts, cash balances, and the timing of market interventions.
- Set up a high-level Cash (Treasury) Coordination Group (CCG) to meet frequently and act as a decision-making body on cash management operations (Box 1). This group could be a part of or report to a broader Fiscal Crisis Management Group chaired by the finance minister which is responsible for the overall management of fiscal responses to the crisis. It should be recognized that the scenarios discussed in this note cannot (and should not) be handled by cash managers alone: for example, revisions to the budget may be required, or changes in the fiscal strategy. The CCG should inform policy makers based on the availability of cash resources and financing options. It should be chaired at a sufficiently high level such as the deputy finance minister or the principal secretary, and include heads of departments of budget, debt management, macro-fiscal analysis and representatives of the revenue authority and major spending agencies. If necessary these arrangements can be established informally during the crisis and formalized later.

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<sup>7</sup> In many countries, a CMU is a designated unit responsible for compiling cash flow forecasts, monitoring cash balances and projecting cash availability.

### Box 1. Main Tasks of the Cash Coordination Group (CCG)

- Analyze the cash flow forecasts. In periods of fiscal stress, these forecasts can be critical to inform decision making on fiscal policy.
- Identify the availability of financial resources and any potential gaps. The projections of cash balances, financing options and other resources should be compiled by the CMU and presented to the CCG to assess the availability of resources for financing emergency spending measures over the next 4-6 weeks. This assessment will be a major input for the Fiscal Crisis Management Group to take decisions on spending priorities.
- Analyze and decide on policy options for possible adverse scenarios.
- Develop instructions and guidelines for spending agencies to ensure that their cash plans are in line with the CMU's cash forecasts and the priorities of the government. Such guidelines are especially needed if the payment process is decentralized, namely if spending agencies can initiate payments without going through the central treasury.
- Take measures, such as timely reporting requirements, to enhance the monitoring of cash flows and cash balances, especially if payment processes are decentralized and cash balances are fragmented.
- Take steps for business continuity in critical cash management processes. Cash management is typically a core function included in a government's business continuity plan. However, if this function is not included in these plans, or the plans have not foreseen a crisis on the scale of COVID-19, some simple measures can be undertaken, including the identification of key staff who will work on critical processes, and the reporting structure with their back-up responsibilities.<sup>1</sup>

1/ See S. Saxena and M. Stone, "Preparing PFM Systems for Emergency Response," *IMF Special Series on Fiscal Policies to Respond to COVID-19*; and E. Balibek, "Covid-19 Rethinking Treasury Business Continuity Plans," *IMF PFM Blog*, March 30, 2020.

### III. COORDINATION WITH DEBT MANAGEMENT

**Coordination between cash and debt managers should be strengthened to ensure timely access to financing and mitigate refinancing risk for existing debt.** In several countries, there is an integrated framework for managing cash and debt, which facilitates efficient decision making. In other settings, the debt management department should consider the cash flow forecasts in updating their issuance strategy and borrowing plans and inform the CMU and CCG about the available resource envelope.

**Relevant short-term measures to address additional financing needs include the following:**<sup>8</sup>

- Explore the possibility of external (concessional) financing, including from the extended set of financing options provided by international financial institutions. In many developing countries, the absorption capacity of domestic markets to finance additional spending requirements is limited. In advanced economies, central banks have stepped in to purchase additional amounts of government securities from markets, indirectly financing the government. This option should be considered with caution in emerging market and developing countries, where additional liquidity in the financial system may generate inflationary and/or

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<sup>8</sup> See *IMF Special Series note on Debt Management Responses During the Pandemic* for further information on measures related to debt management.

devaluation pressures. Where available, developing country governments may prefer to use concessional financing, grants and market-based financing to extend their resource envelope.

- Explore options for temporary debt relief. The IMF's Catastrophe Containment and Relief Trust (CCRT), for example, has already provided debt service relief for a significant number of qualifying countries. Such relief would free up resources for other expenditure. Depending on the expenditure profile, a part of the additional available space can be used to ramp up cash buffers for later use.
- Revise borrowing programs based on cash flow forecasts. Countries that are active in domestic debt markets, including many emerging market and developing countries, should revise their annual and/or quarterly calendars to inform market participants about increased borrowing requirements and any changes to the available debt instruments. Such communication is important to allow sufficient time for potential lenders to adjust their portfolios. Several countries (including Belgium, France, Hungary, the Netherlands, and the United Kingdom have already done so.
- Adopt a flexible approach to debt management. Experience from the GFC suggests that flexibility may need to be adopted to mitigate funding risks. Issuance techniques and pricing systems may also need to be adapted to market conditions (e.g., auctions announced with a shorter lag, uniform price auctions, and syndications). The set of offered instruments can also be amended to explore financing options in non-traditional (or not-frequently-relied-upon) markets.<sup>9</sup>
- Examine liability management operations. Bond exchanges can be a way to switch instruments maturing in the near-term for longer-term instruments without cash movements, helping mitigate refinancing risk. Cash buybacks should be avoided where possible to make better use of available cash (Belgium, for example has stopped the practice of buying back securities maturing in 2022).
- It is important for public entities not to compete for funds in the market. Subnational governments (especially in some federal countries such as Brazil and the U.S.), public corporations, and EBEs may also have increased financing requirements. If possible, the central government can take measures to relieve financing pressure on these entities by lending directly or providing cash.<sup>10</sup> These actions can also help mitigate pressure on interest rates in financial markets and reduce risk perception. Improved coordination with the debt management department may be required to ensure that such operations taken place smoothly and there is no overlapping of borrowing calendars.
- For the medium-term, keep track of risks particularly for foreign currency and short-term debt and contingent liabilities, considering their long-term impact on fiscal space and debt sustainability.

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<sup>9</sup> Ireland, Italy and Portugal are examples of countries that increased the issuance of retail debt in the aftermath of the GFC.

<sup>10</sup> A recent example is the Municipal Liquidity Facility in the U.S., which was established to help state and local governments better manage cash flow pressures. In India, in addition to the enhanced Ways and Means Scheme of the Reserve Bank, the Ministry of Finance also took measures to relieve liquidity pressures on States by advance payments of their entitlements, and advances under the Ways and Means facility of the Central (Union) Government.