# SCOPE AND FUNCTIONS OF TREASURY MANAGEMENT

## OBJECTIVES OF THE TREASURY

- **Cash Management:** Local government finance professionals need **a understanding of cash management** and investments that produces the greatest yield.
- **Maintain banking relation-** Treasury managers are challenged to keep their **banking relationships strong** and professional while many internal and external factors could potentially impact those relationships
- **Forecasting:** Cash flow forecasting is critical for a treasury manager. **Without proper cash flow forecasting**, it is impossible to know what amounts can be invested and for what period of time.
- **Collections:** The object of collections is to increase the amount of funds available for investing by **speeding collections into the government's bank account.**
- **Disbursements:** Disbursements should **be used to remove cash from the local government's treasury** only at the last possible moment.
- **Investments:** The investment function can only take place after all of the other important activities of establishing banking relationships, understanding the inflow and outflow of revenues and disbursements and constructing a cash flow forecast. Once the investment process begins, investments become one of the most important responsibilities of the treasury managers job.

## ORGANISATIONAL STRUCTURE

In view of the voluminous and complex nature of transactions handled by a treasury, various functions are segregated as under.

## Treasury Organization

| | |
|---|---|
| **Front-Office** | Dealing and investment - Risk Taking |
| **Mid-Office** | Risk Management, Policy compliances and Management Information |
| **Back-Office** | Deal Confirmations, Settlements, Accounting and Reconciliation, Marking to Market and revaluations |

### Front-office
The front office of a treasury has a **responsibility to manage investment and market risks** in accordance with guidance received from the bank's ALCO.

### Mid-Office
Mid-office is responsible for onsite risk measurement, monitoring and management reporting. The other functions of Mid-Office are:

- Assessing likely market movements based on internal assessments and external / internal research.
- Interacting with the bank's Risk Management Department on liquidity and market risk.
- Monitoring currency positions.
- Calculating and reporting VAR.
- Stress testing and back testing of investment and trading portfolios.
- Risk-return analysis.
- Marking open positions to market to assess unrealised gain and losses.

### Back-Office Functions
The key functions of back-office are:

- Deal slip verification.
- Generation and dispatch of interbank confirmations.

- Monitoring receipt of confirmations from counterparty banks
- Monitoring receipt of confirmations of forward contracts.
- Receiving payments.
- Monitoring receipt of forex funds in interbank contracts
- Statutory reports to the RBI.
- Reconciliation of accounts.
- Monitoring approved exposure and position limits;
- Accounting.

## FUNCTIONS OF A TREASURER

Treasury operations of a commercial bank consist mainly of two vital functions viz:

- Maintaining the stipulated **Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)**
- Ensuring the optimum **utilization of the residual resources through investments**
- Raising additional resources required for meeting credit demands at an affordable cost and
- Managing market and **liquidity risks** in the transactions.

## RESPONSIBILITIES OF A TREASURER

- **Balance Sheet Management**

The financial sector reforms have provided the banks freedom to price most of their assets and liabilities by themselves, with the exception of pricing of loans under Differential Interest Rate scheme. The pricing of treasury assets and liabilities which form a critical mass of the balance sheet, is therefore, very crucial to the balance sheet management. It is well known that the balance sheet management is a dynamic process. It **requires continuous monitoring, analysis of market changes and**

**controls. Demand and supply forces will impact the optimal balance sheet size and its growth rate.**

- **Transfer Pricing**

The treasury not only provides the interface between the bank and the external market, The treasurer has to ensure that the funds of the bank are deployed in **the most appropriate manner without sacrificing either yield or liquidity.** This is done very effectively through the means of a transfer pricing mechanism administered by the treasury . **Benchmarking of rates provides forecast about the expected rate movements in the future.** Depending on the signals provided by the treasury in the form of benchmark rates for assets and liabilities, focus of the individual **business groups can be shifted from asset growth to liability growth or vice-versa.**

- **Reserve Management and Investments**

Since significant proportion of funds is deployed in reserves, management of these reserves is a very important factor in the overall profitability of the bank. It should ideally **take into account both liquidity as well as yield considerations.** Even though the longer maturity securities could offer the higher yields, but there may be fall in price due to changes in the yield curve. On the other hand, short dated securities have low price risk but they could offer only lower returns. Therefore, the choice of an appropriate mix of reserve and investment is a very important function of the treasury manager.

- **Customer Focus**

In the present-day competitive environment, treasury cannot afford to lose its customer focus. There is **bound to be a pressure on the treasury**

**to offer various rupee-based and cross currency hedge** products to their clients who have foreign currency exposures on their balance sheets.

- **Risk Management**

Treasury risk management is a separate topic in its own right. One of the major responsibilities of a successful treasury is **to manage the risks arising out of the financial transactions entered into by the treasury.** The most important risks which it has to manage are liquidity risk and price risk in addition to counterparty risk and issuer risk.