

Governance and Organisational Development

OVERVIEW

During 2007, the Bank's governance and organisational development practices continued to focus on building a performance-driven culture to ensure that the Bank is able to deliver its core mandates of ensuring monetary and financial system stability, as well as supporting sustained medium and long-term growth. The Bank increased investments in human capital, learning and knowledge, work space and physical facilities, and technology. Attention was also given to changes in governance structure. New policies, practices, processes and systems were also introduced to enhance the potential for the Bank to strengthen performance. These improvements were reinforced by the promotion of new sets of role-based behavioural competencies and value-based corporate codes designed to ensure the organisation continues to effectively contribute to the nation's economic and financial agenda.

The organisational development strategies and practices to support the Bank's role have yielded demonstrable results. Performance improvement was visible across the organisation, reflected by greater capacity to respond to the higher performance expectations, and achievements of goals set for the operating units and the institution during the year. The Bank made a conscious effort during the year to reprioritise organisational development initiatives and programmes, and importantly to enhance the focus on areas directly related to the Bank's strategic results. Project-based collaborative work among line departments, which had become a norm within the Bank, contributed towards optimising the utilisation and sharing of resources, leading to higher level of performance in these priority areas. Roles of leadership at all levels were given greater emphasis, with augmented commitment and efforts to enhance talent management practices, in particular, mobilisation of talent, talent development, succession management and reward management. The Bank's planned programmes under its "knowledge-based and learning organisation" initiatives were continued, with positive results on the staff, in particular, with respect to self-directed learning. Given the growing importance of regional integration, the Bank addressed its capabilities to build more effective regional and international networks.

Governance

The Board of Directors, which functions as an oversight board, comprises of the Governor as the Chairman, three Deputy Governors and five other non-executive members from the industry and public sector. The Board is responsible for policy and the general administration of the affairs and business of the Bank. In performing these roles, the Board is guided by three key pillars of governance, namely **independence** based on its given roles; **accountability** based on the need for operational effectiveness and efficiency in performing the given roles through optimising the use of available resources, as well as monitoring performance and managing the associated risks; and **transparency** in ensuring clarity of its actions as they impact the Bank's multiple stakeholders. In furthering its roles, the Board is assisted by the Board Audit Committee to supervise the Bank's financial and non-financial compliance to the internal controls. The Board Audit Committee is chaired by an independent director. The Board convened 12 monthly meetings and four Board Audit Committee meetings in 2007.

The Management Committee, which is the highest executive entity within the Bank and chaired by the Governor, meets weekly to deliberate on policy matters pertaining to the Bank's core functions as well as the general operations of the Bank. The practice of cross-functional committees which over time had become increasingly effective in the Bank's decision making process had been institutionalised to become a critical component in the Bank's decision management framework. The Management Committee is complemented by several other policy committees, which are also chaired by the Governor. These committees include, the Monetary Policy Committee, Financial Sector Policy Committee, Reserve Management Committee, Financial Liberalisation Committee and Risk Management Committee. These policy committees provide for balanced participation of staff across the line departments, as well as depth and breadth in inputs and more effective implementation of decisions, in addition to enhancing ownership and accountability. Collectively the Management Committee and the policy committees provide the executive leadership, to steer the Bank in fulfilling its statutory mandates.

Various measures to enhance governance were introduced during 2007. The orientation of enhancing time-to-market required focus on efficiency of decision making processes as well as effectiveness of execution of decision at the operating level. In particular, there was a realignment of the supervisory and regulatory functions which was initiated in 2006 and implemented in 2007. The realignment was to provide sector-wide functional focus and foster a holistic approach to the management of the challenges of the sector. The new structures put in place enabled effective sharing of knowledge, experience, information and data and promoted greater cross-functional consultations and in-depth deliberations across business units for a more timely detection and resolution of emerging issues.

Department reviews were also undertaken to enhance the governance of three departments of the Bank. A review of the Economics Department was undertaken to ensure that the Bank continues to have in place capability to identify, assess and respond to emerging macroeconomic developments. The review aimed at further strengthening macro economic surveillance and assessment as well as research capability to support the Bank's core mandates of monetary and financial stability, as well as the Bank's role as an economic adviser to the government. The Bank, in 2007, established a new unit known as Central Banking Services to share knowledge and best practices with other central banks and regulatory authorities. The primary role is to foster mutual learning and to strengthen relations and interlinkages with the central banking fraternity.

During the year, the Bank also initiated a strategic review of the Internal Audit and Currency Management and Operations departments which is due to be completed in 2008. Further changes were also made in the area of sound management of the Bank's finances. The Bank actively focused on the issue of more effective cost management taking into account the risks, costs and benefits in the conduct of central banking business. In 2007, the Bank's Procurement Management Policies and Procedures were further enhanced with respect to risk management and cost effectiveness in procurement. As part of the on-going Cost Conscious Culture initiative, various measures were implemented by the departments in 2007 ranging from more efficient office administration,

handling of external meetings and events, training, travelling, currency operations, e-payment and improved work processes to enhance effective resource management in the conduct of routine operations.

Corporate Social Responsibility

The Bank established a BNM Volunteers team for community service in 2007 to provide another channel for staff to contribute to society. The establishment of the BNM Volunteers team enables the Bank and the staff to fulfill corporate social responsibility and contribute towards the advancement of disadvantaged and under-served communities. This is done through hands-on voluntary community service projects and financial contributions.

The Bank had also initiated a project to create greater awareness and formulate initiatives to implement and monitor strategies to address global warming. An Engine Group has been established to drive this project including creating awareness among staff to actively recycle, reuse and reduce the utilisation of depletable resources. Efforts have also been undertaken to embed and implement environmentally friendly initiatives within the Bank's systems and work processes. As the staff voluntary movement gathers momentum, nation-wide initiatives partnering with other agencies championing this cause will also be undertaken by volunteers from the Bank.

The Bank continued with its programme of early engagement with deserving and talented students from the lower income groups in particular those from the rural areas. The programme is part of the Bank's initiative to develop human capital to broaden the talent supply for the Bank and the nation and involves the identification of young Malaysian talent in upper secondary classes. Their academic, physical and social developments are facilitated with financial support for learning materials as well as equipment for extra curricular activities.

Talent Management

During 2007, various new human capital management practices were introduced to further enhance the Bank's ability to meet the challenges in the area of talent management. The Bank adopted a Workforce Planning Framework which focuses on the overall talent requirements of the Bank over the medium and long term, addressing

issues such as the number of employees, the required skill sets and competencies for the respective functional areas of the Bank. The framework forms a guideline in the determination of jobs, manpower levels and structures within the Bank that would deliver the Bank's desired outcomes in the most efficient, effective and sustainable manner.

In terms of Talent Demand, the Bank redefined the job families and its structure to improve alignment with the Bank's business strategy. This process led to a re-assessment of manpower for certain critical functions. The Talent Supply processes which were also introduced in 2007, have led to more effective and efficient assessment of the availability and readiness of talents to assume jobs across all levels. The talent supply process ensures that greater job-person fit is maintained, while enabling greater flexibility in moving talent within the Bank. This framework is also used for succession planning for mission critical positions in the Bank.

Performance differentiated practices continued to be an integral part of the Bank's talent management strategy, underpinning major human capital policies and processes. Despite raising the performance standards and more stringent evaluations and assessments in 2007, the average performance of the Bank's staff has continued to improve. The Bank reviewed the reward system, focusing on variable components of the remuneration in order to ensure that it remains relevant and competitive.

Talent management has also involved the strengthening of staff values and commitment to improve their level of attachment and engagement with the organisation. By understanding positive values that are intrinsic to the Bank and common to its members, the staff will be better able to internalise these values and have greater appreciation of their roles within the Bank. In 2007, the Bank revised the core shared values introduced in the mid-90s to be more reflective of its current roles and environment. The core shared values are represented by the acronym "i-ACTED" which stands for Integrity, Authoritative, Collaborative, Trust, Excellence and Diversity.

In terms of capacity, the total staff strength of the Bank increased by four percent to 2,597 as at end-2007. The attrition rate due to retirement and

resignations reduced to four percent. With a ratio of Executive and Non-Executive of 3:2, the Bank continues to emphasise the increase in its professional talent pool.

As part of the Bank's efforts to build its talent pipeline, as well as contribute to the nation's human capital development, 165 scholarships were awarded to candidates pursuing pre-university programmes at local colleges and first degree programmes at local and overseas universities in 2007. To provide opportunities for the Bank's staff to enhance their knowledge and expertise, 47 of them were offered scholarships to pursue first degree programmes at local universities and post graduate studies at local and overseas universities. The distribution of the scholarship awards focused on disciplines relating to central banking areas such as Economics, Actuarial Science, Law, Accountancy, Financial Engineering and Mathematics. Other areas included Islamic Banking and Economics, Corporate Finance and Shariah.

As part of the Bank's contribution towards nation building, the Bank started the Special Scholarship Award for top Sijil Pelajaran Malaysia achievers in 2005. In line with the Bank's aspiration to develop top potentials in the country, the awards have given young Malaysians opportunities to acquire the best learning experience at world class learning institutions. A total of 12 students have been awarded this special scholarship since it was introduced in 2005. For the year 2005 and 2006, the Bank awarded three Special Scholarships for each year. However, the number was increased to six in 2007.

Knowledge Management

In 2007, the focus with respect to knowledge management related to improving content management, including visibility and leveraging on accumulated corporate information and research, as well as improving knowledge acquisition, knowledge sharing and collaboration with both internal and external stakeholders.

In terms of content management, the Bank introduced a new Enterprise Content Management policy, setting out guiding principles and broad policies that supports the entire lifecycle of content in the Bank. The Enterprise Content Management policy introduces a uniform set of

best practices to preserve the Bank's intellectual capital. As part of this on-going agenda, there were concerted efforts to identify knowledge gaps so that the Bank's knowledge management systems will be able to ensure that the gaps are addressed, and thus, ensure greater alignment of knowledge management processes with the Bank's business requirements.

Work on the Bank's Enterprise Portal progressed further in 2007 with the deployment of two key functions, namely the Knowledge-Hub (which provides a means for seeking and sharing of information as well as collaboration among members of communities) and e-Collaboration (which is a system for on-line collaboration), through the Enterprise Portal's platform. The FI@KijangNet portal was launched to the financial industry in February 2007 to provide a one-stop communication and collaboration channel with the Bank. Essentially, the portal supports the entire life-cycle of the policy development process across various industry sectors. Under the current release, financial institutions are able to access cross-sector policy guidelines, manage user rights as well as post and access enquiries and responses online. The FI@KijangNet has significantly improved accessibility of information to the financial industry, while enabling the Bank to reduce the time taken to communicate new policy directives to the industry as a whole. In particular, all branches of all financial institutions can access the information, rather than depending on their respective headquarters to forward the information to them.

Training and Learning Management

In 2007, the Bank continued to put greater emphasis on delivering quality learning solutions to meet the needs for new knowledge and competencies. The orientation towards performance-based and self-directed learning has led to an increase in demand for job specific learning.

In order to ensure greater relevance of content, 80% of the learning solutions offered to the staff throughout 2007 underwent significant customisation, using the data obtained through a comprehensive learning needs analysis conducted by the Bank. A comprehensive learning needs analysis was also conducted for very technical courses, such as

the Banking Supervision Foundation Course, the Insurance Regulation and Supervision Course, the Central Banking Series, the Financial Regulators Forum in Islamic Finance (part of the Global Islamic Finance Forum) and the Islamic Finance Course for Financial Regulators (IFCFR). This was to ascertain that the learning solutions offered provided the latest knowledge and expertise in the specific knowledge areas as required by the participants.

The Bank had also successfully organised an inaugural Advanced Central Banking Course in June 2007. The Advanced Central Banking Course is the final series of a three part series in the Central Banking curriculum which includes the Basic Central Banking Course and the Intermediate Central Banking Course. This three part series provides a comprehensive and integrated curriculum for central bankers.

The progress made by the Bank's leadership development processes implemented since 2004 were acknowledged with the Bank being awarded the Exemplary Practice Award in the 8th Corporate University Xchange Awards For Excellence and Innovation In Corporate Learning under the Leadership Development category in February 2007 in the United States of America. In 2007, the Leadership Development Programme (LDP) for Directors and Deputy Directors was extended to the next level for Managers to ensure a robust talent pipeline.

The year 2007 also saw the Bank putting greater emphasis on assessing the impact and effectiveness of the learning solutions offered. With regard to increased knowledge due to learning, 90% of the functional courses were successfully assessed through participants' feedback and reflection. The average knowledge gained for learning sessions offered in 2007 was recorded at 70%. The result on the learning effectiveness for the LDP showed that a high percentage of knowledge was gained, with 58% of the new knowledge being currently applied at the workplace.

For 2007, the average learning investment per-employee was RM8,700, which amounted to 11% of staff salary. With respect to the training man-days, each employee registered an average of 10 training days.

Technical Assistance and Collaboration Programmes with External Agencies

As part of the Bank's efforts to enhance regional and international cooperation, the Bank collaborated with central banks of emerging economies in the following areas :

- Sponsorship of participants from countries identified under the Malaysian Technical Cooperation Program (MTCP) to attend various training programmes conducted at the Bank. These programmes included the Basic Central Banking Course, Banking Supervision Foundation Course, Insurance Regulation and Supervision Course, and the Global Islamic Finance Forum.
- Study visits from central banks of emerging economies of Asia, Central Asia, the African continent and the Middle-East.
- Advisory services provided by the senior staff of the Bank at the request of other central banks.

The areas cover a wide range of central banking issues as well as organisational development work to build internal capacity in a central bank. The Bank has also benefited from the exchange of knowledge and experience, and has enhanced the network for collaboration amongst other fellow central bankers.

ICT Management

Information and Communications Technology (ICT) has proved a key enabler in enhancing business process efficiency, and supporting the achievement of the Bank's desired outcomes. During 2007, the Bank strengthened the ICT infrastructure by implementing a high performance and cost effective new wide area network infrastructure that connects the Bank with all the financial institutions. The infrastructure provides the performance for high volume and large size of transactions, in line with the current and future business needs. In order to further optimise the use of ICT infrastructure and time to deployment of ICT applications, an exercise was undertaken to consolidate the servers and storage capacity by leveraging on virtualisation technology – a foundation for the implementation of on-demand services.

The Bank also put in place a direct link-up with the Malaysia Deposit Insurance Corporation to support the administering of the deposit insurance system and assessing the risks to ensure sound risk management in the domestic financial system.

In supporting Malaysia's endeavours as an International Islamic Financial Centre, the Bank has implemented a cost-effective system for secure settlement and depository of non-RM bonds, thereby putting in place the necessary infrastructure that minimises settlement risks. In relation to the country's burgeoning bond market, the Bond Info Hub initiative was completed. The new infrastructure provides the capability for content aggregation of bond information from primary and secondary market players for access by the public and foreign investors.

ICT was also strategically used to improve the regulatory process through the implementation of the FI@KijangNet communication and collaborative platform, which is deployed using the Bank's Enterprise Portal. This functionality enables financial institutions to access, collaborate and make enquiries on the policies online. In enhancing the performance of the reporting institutions and the Bank's obligations under the Anti-Money Laundering Act 2001 (AMLA), the system has been expanded in year 2007 to enable collaboration, analysis and surveillance on AMLA-related information. The Bank also enhanced its delivery system for managing enquiries and complaints lodged by the public through the new BNM TELELINK contact centre.

Finally, to strengthen security management, the Bank has embarked on an Enterprise Public Key Infrastructure initiative [ePKI] to enhance authenticity, confidentiality and integrity in the implementation of payments system. This would promote public confidence in the safety of the systemically important payments system in Malaysia that includes the Cheque Truncation System and the Real-Time Gross Settlement System.

RISK MANAGEMENT IN BANK NEGARA MALAYSIA

Risk management is regarded as a key element of governance at the Bank with the underlying objectives of safeguarding the Bank's reputation and ensuring the safety and soundness of the Bank's operations. As a principle, the risk management framework is periodically reviewed to ensure that it remains effective in surfacing key risks of the Bank and that appropriate processes and systems are implemented to manage these

risks. In 2007, the Risk Management Committee approved a new framework and approach in managing organisational risk to further strengthen the existing risk management infrastructure.

Risk Management Governance Structure

The risk management governance structure headed by the Risk Management Committee (RMC) chaired by the Governor, is the main driver for risk management in the Bank. Through this dedicated forum for risk management discussion, RMC members carry out focused deliberations on organisation-wide risk issues faced by the Bank. Two sub-committees have been established under the new framework to support the RMC, namely the Financial Risk Management Committee and Operational Risk Management Committee. These two committees are responsible for overseeing the financial and operational risks respectively and to ensure adequacy of its management. It is envisaged that this new structure would allow for greater focus and more in-depth analysis on the two critical risk areas of the Bank, through the involvement of key heads of departments in the two committees to spur better rationalization of issues. It is also aimed at addressing risk interlinkages in the Bank. The new structure would allow the RMC to be focused on high level organizational risk issues, including strategic, policy, reputation and capability risks as well as to formulate appropriate risk mitigation measures at a macro level.

The Risk Management Unit (RMU) is responsible for developing and maintaining the risk management framework of the Bank which encapsulates the development of policy and processes, tools and methodology as well as promoting effective best practices. It oversees the implementation of the framework, and ensures that risk management processes are appropriately carried out.

Key Initiatives for 2007

Over the years, the focus of risk management in the Bank gradually moves away from department centric to a more integrated approach by adopting an Enterprise Risk Management (ERM) framework. A sound ERM framework has allowed the Bank to manage risks in a multi-dimensional perspective by linking risks to the achievement of multiple objectives (which include strategic goals, optimal resource allocation, reliable information and compliance with laws and regulations) and how

they are associated with various functions and levels of accountability in the Bank. In this respect, the main challenge is to aggregate risks across different risk types and also across business units to obtain an overall bank-wide risk situation and subsequently to manage the key risks at the organisational level. In 2007, considerable effort was focused on developing the bank-wide risk profile, which would ultimately evolve to a corporate risk dashboard. To do so, the self-assessment was seen as the main building block to form this profile.

Accordingly, improvements were made to the self-assessment tool to attain better consistency of approach across departments as well as to ensure common language, through improving the Bank's risk taxonomy. This is to facilitate bank-wide consolidation and enable better risk categorisation and treatment in the organisation. Greater engagement with line departments is done to both validate the risk management process in departments and to increase awareness and responsibility, thereby improving the Bank's overall risk culture.

Based on the self-assessment process which is a bottom-up approach, a preliminary corporate dashboard is formulated. This bank-wide risk profile was the foundation for triggering discussion with the management team to link the business area or process perspective to management's perspective and to establish better linkages with the Bank's strategy, key business objectives, and organisation and resource requirements. The ultimate aim is to bring together a top-down and bottom-up approach to complement each other and thus arrive at a holistic picture of risks in the Bank.

Bearing in mind the continuous evolution of risk management practices, benchmarking global best-practices is an ongoing process. Nevertheless, maintaining simplicity whilst ensuring the robustness of the Bank's risk management process remained a pressing challenge. Further work is required in education to enable departments to draw out key risks in their functions for upward reporting, without compromising detailed risk assessments at departmental level.

Overall, risk awareness across the organisation progressed in the year, evident from the growing reference to risk management

in all strategic dialogues and the various levels of decision-making forums across the Bank. Encouraging was the increased commitment to risk management by the line departments. This is reflected by the better usage and more timely submission of self-assessment using RMU's self-assessment tool to respective Assistant Governors and the RMU, the increased quality (in coverage and depth) of the risk issues identified, greater peer-engagement within individual departments to determine the departments' risk profiles, as well as greater requests for the RMU to provide views and technical assistance in managing risk in various projects and initiatives. To raise the level of sound risk management culture and nurture an environment which is conducive for addressing risk issues, more workshops and discussions were conducted in the year.

The Bank also continued its participation in the International Operational Risk Working Group (IORWG), which was established to act as a centre of competence on operational risk management for central banks. The Bank was involved in discussions, forums and sharing of ideas which were facilitated by IORWG's dedicated website and annual conference. Annually, expert groups are established to do research on specific topics to further enhance frameworks and methodologies for the central bank community. The Bank is involved in a group which is looking at best ways to integrate risk management with strategic planning.

Strategic and Policy Risk

Strategic risk, or possible impediments to the achievement of the Bank's objectives and strategic aims by its very nature, is inherent in core processes and Bank-wide projects. Thus, in order to allow for active management of strategic risk within the Bank, institutional structures such as Management Committees and Steering Committees chaired by Senior Management are in place to oversee risk in strategic priority areas and key decision making processes.

To complement this, the design of RMU's self-assessment tool (the Annual Declaration) as well as the independent assessments by the RMU, are added measures to ensure the holistic capturing of strategic level risks for timely and proactive management.

In executing its role of promoting sound monetary and financial stability, as well as the role of the Central Bank in shaping the domestic financial landscape, another risk of concern to the Bank is policy risk. To ensure the effectiveness of the Bank's policy making mechanism, structures such as the policy risk and implementation framework are in place within the Bank. Major components of the framework are the internal committees and working groups for cross-functional consultations and deliberations. The high level committees include the Management Committee, Monetary Policy Committee and the Financial Stability Committee; all chaired by the Governor. Policy working groups, chaired by Assistant Governors with membership comprising directors of relevant departments, form the working level forum for policy formulations. These working groups ensure that all information and expertise are tapped in the design and formulation of policies. In certain cases, the consultation process includes external stakeholders. This structure serves to ensure that the Bank's policy-making mechanism is effective in promoting monetary and financial stability.

Financial Risk

An independent Treasury Risk Management Section (TRMS) of the Investment Operations and Financial Market Department is responsible to assess the treasury risk of the Bank and to enforce the Bank's treasury risk management policy with direct reporting to the Deputy Governor. The treasury risk management policy defines the risk parameters and TRMS is responsible to measure and monitor the treasury risk exposure and also reports the performance of the treasury operations. The risk assessment and performance provides value added input in the investment decision making process. In line with market best practices and advancement in IT, the Bank continued to upgrade and update its risk methodology and framework to ensure robust risk coverage on the investment of the foreign reserves. In 2007, a more quantitative market risk framework was adopted by the Bank which provides more detailed risk evaluations across different asset types under increasingly challenging market environment. In addition, the credit risk framework has also been strengthened to meet new challenges in the credit market. A ratings-based framework ensures strong credit risk management and maintains high credit quality of reserves despite the negative development in the credit market globally.

Operational Risk

The management of operational risk, commonly expressed as the risk of loss that arises from inadequate systems, controls or human error or other management failure continues to be a critical role and responsibility of heads of departments. In this respect, the respective directors are accountable for ensuring that risk management is integrated in all daily operations and departmental processes, as well as for attesting the appropriateness of risk treatments in place.

In addition to department specific operational risk mitigation such as detailed procedure manuals, clear roles and responsibilities, dual control/separation of duties and embedded process controls, organisation level controls that encompass an effective budgetary control, a sound procurement framework and the internal audit function are also present as additional check and balance measures.

In an effort to continuously enhance internal controls, a review of the payment policy and procedures was carried out in 2007. The enhanced controls and approving authorities for the procurement and payment processes have been incorporated in the Procurement Management Policy and Procedures.

Business Continuity Management (BCM)

The Bank's detailed BCM programme has two main objectives, which are to provide continuous critical central banking operations in order to pre-empt any systemic risk in the financial sector, as well as to provide for the safety of Bank staff and the protection of the Bank's assets.

A significant development in the year is the refinement of the Bank's BCM planning scope

which covers among others, the expansion of the Bank's planning time-line to prepare the organisation for more prolonged interruptions. This would involve reviewing the Business Impact Analysis, Business Continuity Plan and requirements for the Recovery Centre. For greater recovery preparedness, the introduction of additional scenarios for test and live-runs, and deliberate inclusion of more departments in BCM exercises was also done in 2007.

Structurally, the RMC remains at the apex of the organisation's BCM structure and is responsible for endorsing the Bank's BCM policies and practices. Another important group in the BCM structure is the Crisis Management Team (CMT), chaired by a designated Deputy Governor with an Assistant Governor as the deputy. Tasked with the responsibility of managing events with negative repercussions to the Bank's services and physical infrastructure comprising building, people and systems, the CMT also met in the year to scrutinise results of bank-wide BCM exercises, and approved a new internal incident level-indicator to enhance clarity in roles and responsibilities and streamline incident responses in the Bank.

In 2007, the Bank's numerous designated critical teams also continued to be involved in various types of centralised and decentralised programmes and exercises. Some examples include the regular backup IT systems checks, live-runs and group table-top simulation exercises. These are all designed to provide continual training to the Bank's pre-identified key staff to enable appropriate recovery responses whenever required. Finally, an inaugural bank-wide notification exercise involving the entire Bank was also successfully organised during the year.

BANK NEGARA MALAYSIA Organisation Structure



