

Promoting Financial Stability

The Bank is mandated to promote financial stability conducive to the sustainable growth of the economy. We discharge this mandate by ensuring that the financial system is resilient throughout the economic cycle and is able to withstand shocks. This involves us promoting resilient and well-managed financial institutions, fostering safe and reliable clearing and settlement systems, and ensuring orderly financial markets. This in turn enables financial activities to be conducted in a safe, efficient and effective manner, and allows consumers to have confidence when dealing with financial institutions.

Financial stability priorities in 2019

The economic environment was challenging in 2019. Hence, our priority was to ensure that the financial system continued to effectively support the functioning of the economy. For this reason, our regulatory agenda was focused on ensuring that financial institutions are proactive in managing risks, while also providing an environment that encourages healthy competition and the development of innovative products and services to meet the needs of individuals and businesses. We also continued to enhance our supervisory and surveillance systems and processes to support the early identification and management of risks to financial stability.

In 2019, the Financial Stability Committee met four times to review financial stability developments. While risks have increased in some areas, the financial system remained resilient. This continued to be firmly supported by strong capital buffers of financial institutions and sound risk management practices. Further details on the assessment of current and potential risks to financial stability are provided in the Financial Stability Review.

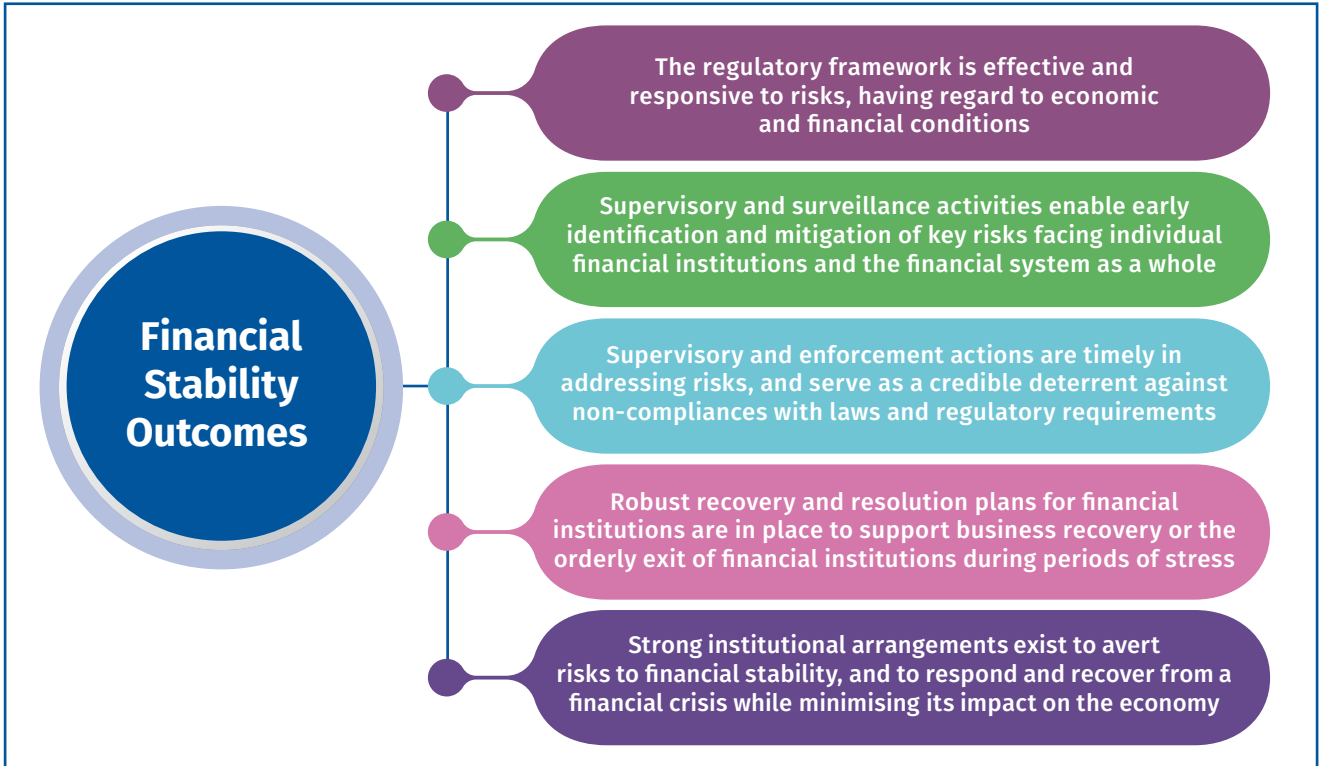
Financial Stability Committee

The Financial Stability Committee (FSC), chaired by the Governor, is a high-level internal committee of the Bank. It is responsible for monitoring and taking actions to reduce or avert risks to financial stability stemming from both system-wide and institutional developments.

The FSC reviews and decides on:

- macroprudential policies to reduce or avert identified risks to the financial system;
- significant supervisory responses to address risks in individual financial institutions regulated by the Bank;
- actions to resolve a financial institution that has ceased, or is about to cease, to be viable; and
- recommendations to the Financial Stability Executive Committee on the exercise of powers within its remit.

An important part of the FSC's role is to monitor the effectiveness of policies and actions taken, and ensure they remain appropriate, taking into account risk developments.



To communicate our financial stability assessments, we publish the Financial Stability Review twice a year. Regulatory developments are also captured in the Quarterly Bulletins published by the Bank.

Regulatory activities

The Bank issues regulations to promote prudent risk-taking by financial institutions. We also strive to ensure fair treatment of consumers through regulations that foster fair, responsible and professional business conduct practices by financial institutions. In achieving these outcomes, we emphasise the role of the boards and senior management of financial institutions in managing risks effectively.

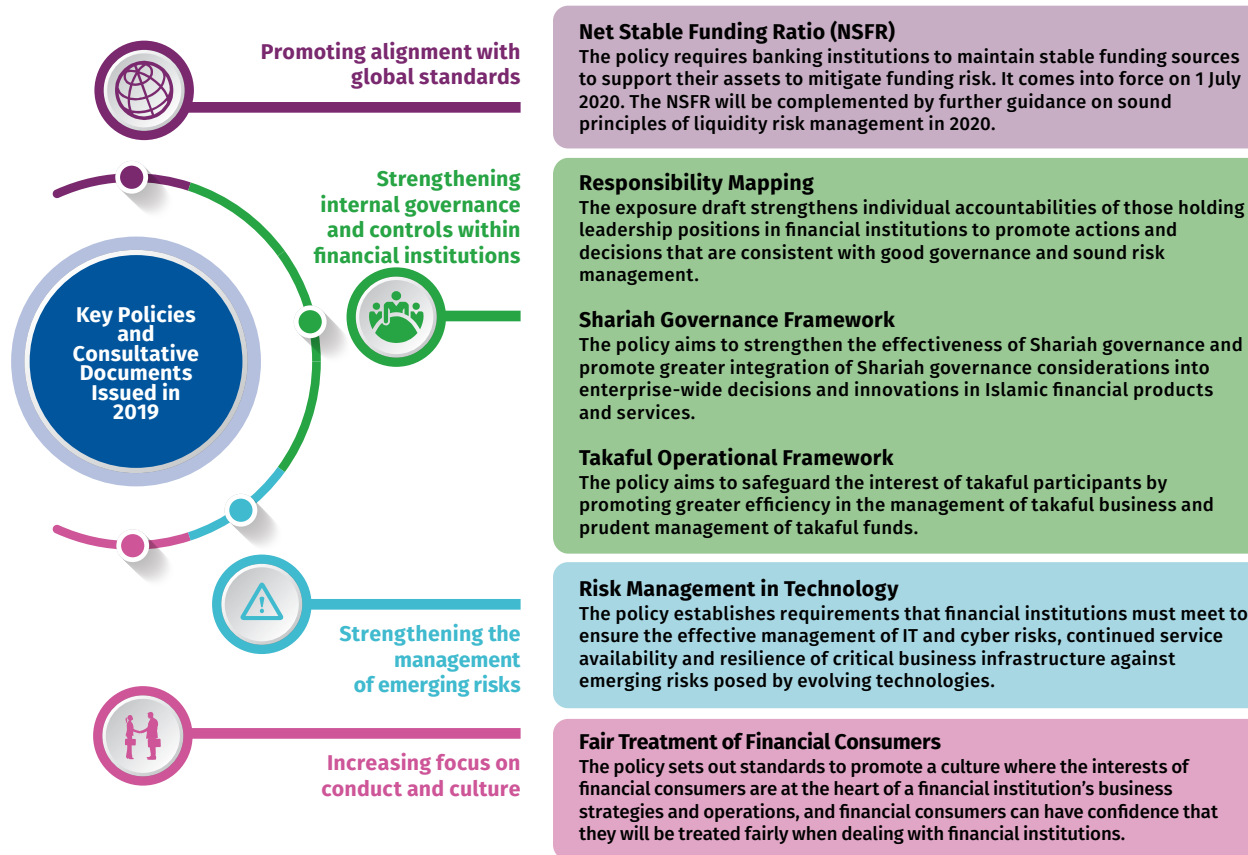
In 2019, we continued to ensure that our regulatory framework remains consistent with international standards and promotes the resilience of our financial system. We also focused on strengthening internal governance and controls within financial institutions, and set standards to ensure the effective management of technology and cyber risks. As part of our continuing efforts to promote ethical conduct and culture within the financial industry, we also published standards on fair

treatment of financial consumers. Key policies and consultative documents issued in 2019 are highlighted in Diagram 1.

The Bank is committed to being open and transparent in our policy making process. We also adopt an evidence-based approach to policy making. This involves us consulting widely through a variety of channels prior to finalising these policies. We also commit to periodically review our regulations to ensure that they remain effective in meeting the intended outcomes, and are responsive to changing market conditions and developments in international standards.

We continue to work closely with our international counterparts in support of efforts to promote global financial stability. In particular, the Bank participates in a number of international standard-setting bodies in the area of financial stability. This provides an important avenue for us to engage with the international community on regulatory standards to ensure that they are relevant and appropriate to the financial stability risks that we manage. We are active participants in the work of the Financial Stability Board, the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors

Diagram 1: Summary of key policies and consultative documents issued in 2019



(IAIS), the Committee on Payments and Market Infrastructures, and the Islamic Financial Services Board. Engagements with these bodies enable us to benefit from and contribute to the collective body of knowledge which informs our regulatory responses.

Supervisory activities

Strong and effective supervision plays a critical role in complementing our regulatory activities to promote a resilient and sound financial system. We adopt a risk-based and forward-looking approach to supervision. This means directing our focus and priorities on key risks facing financial institutions and the financial system as a whole. Our supervisory assessments draw on inputs from a wide range of sources. This includes firm-specific data, peer comparison and other relevant factors that determine the risk profile of a financial institution. We also assess the strength and effectiveness of a financial institution's control

functions and its board and senior management. In addition, we engage with external auditors, and cooperate with other relevant regulators, such as the Securities Commission Malaysia, to inform our assessments.

In 2019, our supervisory activities continued to focus on assessments of significant risks to financial institutions and ensure that financial institutions are effectively managing these risks. Our supervisory activities also included assessments of conduct practices of financial institutions. This included targeted reviews of the sales practices of financial institutions and fairness of contract terms for generic retail financial products.

During the year, we completed a review of the financial condition, governance, risk management and operating model of *Lembaga Tabung Haji* (LTH). This follows the Government's decision to place LTH under the Bank's administrative supervision. As the Bank does not have formal

Enabling regulatory framework to realise the full potential of development financial institutions

Development financial institutions (DFIs) continue to play an important role in supporting strategic economic sectors and advancing Malaysia’s developmental and socio-economic objectives. In 2019, DFIs approved RM44.9 billion of financing (2018: RM32.3 billion), driven mainly by strong demand from the infrastructure and agriculture sectors, and households. Importantly, more than 14,600 SMEs, including start-ups, benefitted from RM3.8 billion of financing approved.

Building on the Bank’s review of the mandates of DFIs to ensure that their developmental objectives are aligned with the nation’s economic strategies, we have started to apply greater differentiated regulatory and supervisory approach for DFIs, reflecting the nature, size, complexity, and specific roles and mandates of each DFI. This is important to minimise market distortions and ensure that our framework remains appropriate to the specific risk profiles of individual DFIs. In 2019, our policy focus for DFIs was steered towards nurturing a culture of developmental impact, innovation as well as greater accountability and transparency. Key policies and consultative documents issued specifically for DFIs are highlighted below.



Corporate Governance

The policy aims to strengthen DFIs’ corporate governance practices through heightened expectations on the board and senior management to foster a sound risk culture. It also improves disclosures by DFIs on their mandate and performance measurement framework.



Financial Reporting

The exposure draft aims to promote greater transparency on DFIs’ performance, in particular their achievements in meeting developmental mandates and their effectiveness in mobilising government funds/schemes.



Corporate Strategic Plan

The exposure draft focuses on the development of robust and forward-looking corporate strategies that are aligned to DFIs’ developmental mandates, supported by sound risk management practices to ensure their long-term sustainability. This includes expectations to measure their success through an enhanced performance measurement framework.

supervisory powers over LTH, we have submitted our assessment and recommendations to the Government and the Board of LTH.

We continued to enhance and modernise our supervisory tools and approaches. This included automating our supervisory reporting infrastructure, leveraging enhanced analytics tools and implementing more integrated surveillance systems to strengthen our supervisory process. We also expanded our supervisory assessments to better understand how culture drives risk-taking behaviour in financial institutions.

A number of international financial institutions operate in Malaysia. Likewise, a number of our financial groups have enlarged their regional footprint in recent years. For this reason,

we cooperate closely with our international counterparts in the area of supervision. In 2019, we participated in six supervisory colleges¹ and one bilateral meeting as host supervisor, and hosted one supervisory college for a Malaysian financial institution with international operations. These engagements, which review the economic and financial conditions in the home and host countries as well as key supervisory issues, provided important input to our supervisory assessments. To date, the Bank has signed six Memoranda of Understanding (MoUs) with foreign supervisory authorities in line with our commitment to cooperate and coordinate with foreign supervisory

¹ Supervisory college is a forum for supervisory authorities of financial groups with cross-border operations to exchange information and coordinate supervisory activities.

Promoting Financial Stability

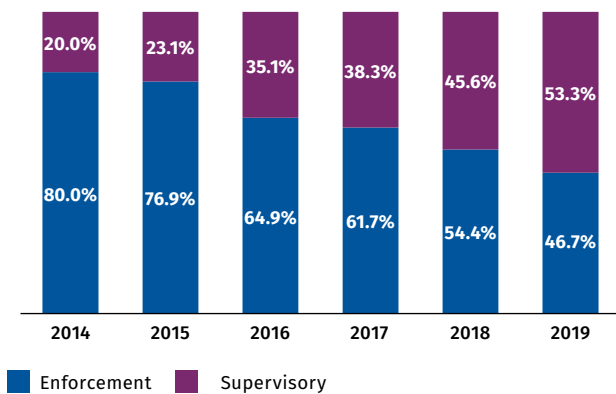
authorities to exchange information, facilitate on-site supervision and combat financial crimes. We are also a signatory to the IAIS Multilateral MoU, which facilitates our cooperation with insurance supervisors globally on information exchange and supervision of insurance companies.

During the year, we worked with *Perbadanan Insurans Deposit Malaysia* to further develop the domestic recovery and resolution planning framework for Malaysia. The framework on recovery planning sets out our expectations for financial institutions to be well prepared to execute plans to recover from financial losses under periods of stress. We have issued an exposure draft, initially addressing requirements for banking institutions, for feedback. This will subsequently be extended to insurers and takaful operators. We expect this planning process to be iterative, with close engagements with the financial institutions to draw up robust plans.

Supervisory and enforcement actions

In promoting sound and well-managed financial institutions, we take supervisory actions at an early stage to secure the commitment of financial institutions to rectify weaknesses in governance, compliance and risk management (Chart 1). These may include requiring financial institutions to implement corrective measures, strengthen the board or senior management, or significantly increase resources to undertake improvements in systems and controls. These supervisory actions continue to be an effective way to deliver positive

Chart 1: Proportion of supervisory and enforcement actions taken

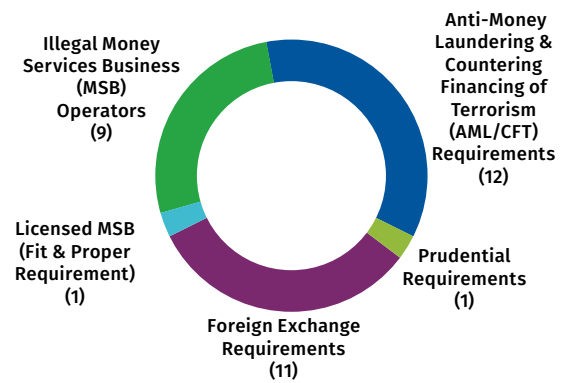


Source: Bank Negara Malaysia

and sustainable improvements in the risk and compliance culture of financial institutions.

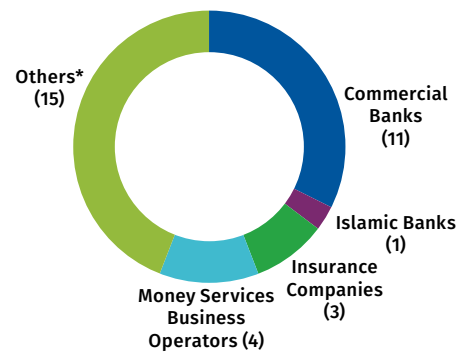
In addition to supervisory actions, we also pursue formal enforcement actions in response to serious failures by financial institutions to meet regulatory standards, or to punish unlawful activities that can create risks to the public or the integrity of the financial system. During the year, we reviewed 34 cases of breaches of our laws and regulations, including those committed by individuals and entities not regulated by the Bank (Charts 2 and 3). Criminal compounds amounting to RM3.45 million and administrative monetary penalties of RM0.9 million were imposed by the Bank. In 2019, we started publishing details of individual enforcement actions on our website.

Chart 2: Number of cases by nature of offences



Source: Bank Negara Malaysia

Chart 3: Number of cases by type of institutions



* Individuals and entities not regulated by the Bank

Source: Bank Negara Malaysia

We also initiated 33 new investigations and brought 33 charges against entities and individuals that we do not regulate. These charges were for offences relating to illegal money services businesses, illegal deposit taking and money laundering. During the year, we secured 43 convictions, including those relating to charges initiated in prior years. These convictions have resulted in criminal penalties amounting to RM1.5 billion.

Consumer empowerment

The Bank strives to ensure that financial institutions are fair, responsible and professional in dealing with consumers. In addition to our regulatory and supervisory activities over the conduct of financial institutions to ensure that consumers are treated fairly, we also seek to empower consumers by raising the standards of financial literacy. This involves equipping individuals with the necessary knowledge and skills on financial management.

In July 2019, we launched the National Strategy for Financial Literacy 2019–2023, a five-year plan jointly developed by the Bank and a few government agencies, to elevate the financial literacy and well-being of Malaysians. The strategy sets out priorities and actionable plans to equip Malaysians with the knowledge to make informed financial decisions, and promote responsible financial management (Diagram 2). The implementation of the strategy is driven and supported by the Financial Education Network².

In empowering consumers, we develop and promote effective avenues for consumers to resolve their complaints and disputes with financial institutions. As the first port of call for consumers, we require all financial institutions to have effective and accessible complaints management processes and procedures. We review these arrangements to ensure that financial institutions manage complaints with adequate oversight, independence and professional care. Over the years, we have observed significant improvements in financial institutions' responsiveness to consumer complaints. This has led to a larger share of complaints that are resolved

by financial institutions themselves, and fewer complaints handled by the Bank.

The Ombudsman for Financial Services (OFS), formerly known as the Financial Mediation Bureau, serves as an additional channel for consumers to seek alternative advice and pursue redress. An independent review was conducted on the operations of OFS in 2019 to assess its effectiveness. Overall, the review concluded that the OFS has been effective in rendering independent and impartial resolutions to disputes and claims made against financial institutions. Several recommendations were made to make the OFS's services more accessible to consumers and to further improve the turnaround time for resolving disputes. These recommendations are being considered by the OFS.

The Bank also plays a role in supporting consumers and SMEs through BNMLINK, our customer service centre. Among others, BNMLINK provides information and assistance to the general public on their rights and obligations. BNMLINK also assists the public with complaints against financial institutions.

In 2019, OFS received 1,047 cases (2018: 761) while BNMLINK handled 5,332 complaints (2018: 5,704).

Going forward

In 2020, the Bank will focus on monitoring and detecting potential stresses in the financial system to enable prompt actions to address any risks to financial stability. Regulatory and supervisory priorities will also be re-focused on ensuring the financial system is strong, and able to support the financial needs of the economy during these challenging times. This involves us calibrating our regulatory and supervisory approach to address material risks in the financial system, while reducing compliance burdens to allow financial institutions to focus their efforts and resources on proactively managing risks and supporting their customers. The Bank will also focus on reinforcing the resilience of the financial system by ensuring that financial institutions take timely actions to rebuild their buffers as the economy recovers.

² Members of the Financial Education Network include the Ministry of Education Malaysia, Bank Negara Malaysia, Securities Commission Malaysia, Employees Provident Fund, *Agensi Kaunseling dan Pengurusan Kredit*, *Perbadanan Insurans Deposit Malaysia* and *Permodalan Nasional Berhad*.

Diagram 2: National Strategy for Financial Literacy 2019–2023: Strategic Priorities and Action Plans



Strategic Priority 1: Nurture values from young

- Expand financial education fundamentals into the curriculum for pre-school, primary and secondary schools
- Reinforce financial education through co-curriculum activities
- Introduce capacity development and support for teachers
- Encourage financial education advocates among students, parental groups and the community



Strategic Priority 2: Increase access to financial management information, tools and resources

- Make basic financial education information easily understood, available and accessible to all
- Heighten awareness and intensify financial education initiatives through nationwide outreach campaigns



Strategic Priority 3: Inculcate positive behaviour among targeted groups

- Impart financial knowledge to promote positive financial behaviour among the youth
- Encourage financial education at the workplace to promote financial resilience, which will have positive impact on employees' productivity
- Foster good money management practices through community-based financial education
- Equip the self-employed with financial knowledge to encourage self and business sustainability



Strategic Priority 4: Boost long term financial and retirement planning

- Promote use of innovative guides and tools to improve long-term financial planning
- Create awareness and promote the benefits of seeking professional advice on financial planning
- Promote voluntary savings channels and platforms to encourage income diversification
- Educate Malaysians to make long-term financial plans for retirement



Strategic Priority 5: Building and safeguarding wealth

- Promote better understanding of risks and returns to build wealth
- Improve awareness on the innovation of financial products and services and its implications
- Raise awareness on financial scams and fraud
- Develop and publish materials relating to sophisticated financial products and services

Source: Malaysia National Strategy for Financial Literacy 2019–2023