

## ***Executive Summary***

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During FY08, SBP-BSC started implementing the Restructuring Plan developed in the last quarter of FY07 to transform the BSC into an effective and efficient organization having capacity to provide adequate operational support to State Bank of Pakistan in pursuit of its strategic objectives. The plan had inter alia envisaged aligning the BSC role and mandate with SBP strategic objectives, enhancing employees' skill-set, optimum use of technology, introducing customer service orientation in the organizational culture and improving quality of service delivery to the stakeholders. A number of initiatives were taken during the year to proceed in this direction; impact of some of these initiatives is already visible in day to day operations of BSC, whereas that of others, particularly those relating to skill enhancement and cultural changes would start making visibility during next 1-2 years. The following paragraphs briefly discuss the initiatives taken during the year, their rationale and impact thereof on BSC's institutional capacity.

### **Currency Management**

The currency management is one of the core functions of SBP-BSC that is aimed at ensuring adequate supply of clean banknotes and coins in the country. Considering the key importance of the function, a full fledged Currency Management Department (CMD) was established during the year under the restructuring and reorganization plan to exclusively focus on all aspects of the currency management system; earlier the function was part of the Accounts Department. The CMD streamlined the fresh currency issuance function, invigorated the system for monitoring of issuance of fresh currency notes, and constituted special monitoring teams for examining the distribution of fresh notes to the general public by branches of commercial banks. Further rigorous efforts were made to collect the soiled currency notes from the market and their early disposal/ destruction. The efforts have yielded encouraging results and the overall quality of currency notes in circulation was improved though still there is a considerable room for improvement particularly in smaller denomination currency notes. During FY08, around 1,408.2 million pieces of fresh banknotes and 366.9 million pieces of coins of various denominations were issued to public as compared to 1,633.8 million pieces of fresh banknotes and 698 million pieces of coins issued during the preceding year. The reduction in number of fresh currency notes and coins issued is indicative of stabilization in the demand for fresh currency notes due to wider dissemination of clean note policy initiated in 2003 and issuance of fresh notes in large proportions during last 3-4 years. Further, the soiled banknotes of different denominations in large quantities were also withdrawn from circulation out of which a total number of 1.157 billion pieces were destroyed.

### **Foreign Exchange Operations**

The BSC facilitates SBP in implanting the foreign exchange policies particularly in processing foreign remittances application, monitoring realization of export proceeds and implementation of special schemes like Research & Development (R&D) Support to the exporters. During FY08, 176,887 entries pertaining to EE and EF Statements were checked and verified as against 170,187 entries verified in the preceding year. Similarly 163,954 cases of R&D Support were

processed and payments of Rs.20,486 million were made during the year compared to Rs.14,100 million paid in FY07 against 118,028 cases; the R&D cases thus registered an increase of 39 percent over the preceding year whereas R&D payment increased by 45 percent over the last year. Further 24,835 R&D cases having discrepancies of multiple natures were returned to Authorized Dealers with objections. The efforts were also made to streamline the export overdue cases, issuance of notices to such exporters and timely referral of the overdue cases to Foreign Exchange Adjudication Department to initiate proceedings against such exporters under FERA of 1947.

## **Foreign Exchange Adjudication**

Foreign Exchange Adjudication Department (FEAD) serves as an adjudication forum to facilitate the stakeholders in repatriation of foreign exchange by exporters. During the year under review, stuck up export proceeds equivalent to US\$12.3 million were realized as compared to US\$5.3 million realized in the preceding year indicating an increase of about 132 percent in the realization of export proceeds. The maximum repatriation of US\$1,096,864 in one case in the FEAD history was also realized during the year. The follow-up for recovery of penalties levied on exporters was also strengthened with the assistance of District Revenue Officers-DRO and penalties recoverable since 1995 was recovered during the year. Further to build FEAD capacity to effectively adjudicate the export overdue cases, the Adjudication Officers were sent to Federal Judicial Academy Islamabad for receiving customized training on judicial processes and procedures. This was again a maiden event since creation of FEAD and got significant coverage in the leading news papers.

## **Export Finance Scheme**

The BSC is also implementing the SBP Export Finance Scheme (EFS) through its field offices in key exporting regions/ districts across the country. During FY08 a total of 26,651 cases were processed compared to 31,010 cases processed in the preceding year. This includes 670 cases processed under Islamic Export Refinance Scheme and 290 cases processed under LTF-EOP. The reduction in number of EFS cases processed during the year may be attributed to the change in SBP refinance ratio from 100% to 70% and requiring banks to finance the remaining 30% from their own resources. This probably discouraged the banks to entertain all the financing requests of exporters under EFS. The ratio was reversed to 100% in November 2008 to ease the liquidity crunch and also to encourage banks to continue funding the exporters' financing requirements under EFS. The BSC field offices also make on-site verification of EFS cases under Part-I of the scheme at the designated branches of commercial banks. During FY08, the verification teams visited 255 branches of 26 commercial banks and examined 14,637 export refinance cases as compared to 14,416 cases at 252 branches of 26 commercial banks examined in the preceding year. The office wise verification/ visit reports were sent to SME Finance Department for information and necessary action, and fines/ penalties on account of irregularities detected during the verification process were also levied and recovered under the SBP rules/ instructions.

## **Payment and Settlement System**

The SBP-BSC also lends its operational support to SBP to ensure smooth functioning of payment and settlement system. The currency management, clearing and settlement facilities, the ATMs, POS terminals/ machines, electronic transfers are the key components of the payment and settlement system. The BSC in addition to managing the currency in circulation also supervises the clearing and settlement system. The coverage of automated clearing and settlement facilities available in 15 cities, where BSC offices are located, was extended to 107 satellite cities during the year covering 751 satellite branches; previously the facility was covering 80 satellite cities. This has resulted in an overall coverage of over 4,500 branches of commercial banks country-wide. The extended coverage of the automated clearing and settlement facilities in satellite cities would promote banking habits in the satellite cities/ towns and thus contribute in deepening and broadening of the banking system.

The total number of instruments (cheques, payment orders etc) cleared during FY08 grew by 12 percent to 74,264,349 from 66,347,664 in the preceding year; the volume was 58,747,655 instruments cleared in FY06 and thus the growth in two years was more than 26 percent. This is indicative of increasing use of banking system for making payments as well as improving banking habits of the masses. The efforts are also underway to reduce the clearing and settlement time from existing 3 days to 1 day which would substantially improve efficiency of the payment and settlement system and thus would be instrumental in bringing even larger number of payments transactions in the banking system.

## **Development Finance Support Services**

Lending operational support to SBP for dissemination and implementation of its Development Finance policies and initiatives at grassroots level is a new function and role assigned to BSC during the year under review. A new department viz Development Finance Support Department (DFSD) in BSC Head Office and its Units (DFSUs) in 13 field offices of BSC were established during the year. While DFSD leads and supervises all DF activities/ operations in BSC, its field units are serving as local contact points for continuous interaction with stakeholders at grassroots level. The Development Finance has added a new dimension in the role and functions of BSC and has made its offices as regional focal points for dissemination and implementation of all SBP policies generally and those related to Development Finance particularly.

The separate focus group for SME, Agriculture and Micro finance were also created in the 13 field offices during the year to discuss and evolve strategies for increasing outreach of financial services in each of these three important sectors. This has substantially strengthened the consultative mechanism at grassroots level and has enabled the BSC offices to mobilize local stakeholders for expanding the access of financial system in their respective regions. The units have also started organizing awareness programs, seminars and Melas for Agriculture and SMEs in collaboration with local stakeholders to improve awareness about financial services and to increase interaction between banks and the agricultural/ business communities. Further the Agricultural and SMEs surveys of Gujranwala and Sukkur districts were launched during the year on pilot basis to enhance stakeholder's understanding about the business and risk dynamics of these sectors and thus enable them, particularly the banks, to comfortably enter these markets

and extend market responsive products for these sectors. The initial results and stakeholder's response of these initiatives is encouraging and gives optimism that BSC with its presence in 15 regions/ districts across the country could contribute significantly in broadening and deepening of the banking system.

## **Human Resources Management**

The efforts continued during the year to improve the human resources (HR) quality through skill enhancement, inducing attitudinal changes, inculcation of performance and merit based culture and improved communication across the levels. A new competency based Performance Management System (PMS) was also introduced during the year for OG-4 and above officers of BSC to bring transparency and objectivity in the employees' performance assessment. The PMS envisages identifying key results areas (KRAs), setting goals, demonstrating desired behavioral competencies and identification of training needs for performance improvement in a consultative environment, which would ultimately lead to performance improvement and employees' development. It establishes a linkage between individual performance and achievement of organizational goals as specified in the business plan, which would lead to strategic congruence and performance orientation. The PMS introduced initially for OG-4 and above officers has been extended to OG-3 and OG-2 from FY09. Besides improving transparency in performance appraisal, this will also inculcate the strategic thinking down the line enabling them to appreciate the importance of their respective division's/ unit's role in organizational goals and objectives and thus would accelerate the change management process.

## **Capacity Building of Employees**

The training and capacity building of BSC employees is an important component of the restructuring and change management process initiated during the year. A full-fledged Training and Development Department was set up in BSC during the year to exclusively focus on training and capacity building needs of BSC employees. As a precursor for the formulation of a more structured and need based training strategy, an organization wide survey was conducted to get the first hand information on prevailing perception of employees towards the significance of training as a tool for career progression and determining competency gaps in relation to their present assignments. Based on the survey findings as well as assessment of key competencies and skills required for transforming the BSC into an effective operational arm of SBP, a comprehensive training strategy was developed to bridge the skills and competency gaps in the short, medium and long run. The implementation of the strategy was also initiated and a number of training programs on functional as well as management and soft skills were organized during the year in collaboration with NIBAF; about 1000 employees of BSC attended the training programs.

## **Optimum use of Technology**

The efforts also continued during the year for increasing the usage of information technology infrastructure for improving efficiency in day to day operations and discarding unnecessary manual registers/ statements which could be generated automatically by the system (Globus Banking Solution). To improve coordination between IT support team of ISTD and end users

and also to promptly resolve system related issues, the System and Procedure Units (SPUs) were established during the year at BSC Head Office Karachi (HOK) and field offices. The SPUs have also been assigned the business continuity and disaster recovery planning function. The creation of SPUs thus has not only helped in increasing the system usage and improving the coordination with the ISTD IT Support team but also enhanced the field offices' capacity in system maintenance and business continuity and disaster recovery planning. It also enabled field offices to channel their efforts towards their core functional responsibilities, as the IT related issues are being taken care of by the SPUs.

## **Business Process Reengineering**

Business Process Reengineering (BPR) in BSC is closely linked with the introduction of new technologies in the day to day operations. The introduction of Globus banking solution, Oracle ERP applications and other in-house developed software have helped in reducing the processing time of different transactions significantly. All manually prepared (paper based) payment instruments including vouchers have since been replaced by system generated instruments. Government Drafts and Bank Drafts are now printed through Globus banking system at the field offices. A follow-up mechanism for outstanding issues has been introduced and managed effectively through Letter Management System. Banking and Issue Department Manuals have been thoroughly reviewed by the committees especially constituted for the purpose; Medical Attendance Rules have also been reviewed comprehensively and submitted for approval while Manual for Office Procedures is under review by a committee which is expected to complete its work by end 2008.

## **Internal Audit & Control**

During the year under review, on-site inspection and IT audit of 13 field offices and 5 departments of BSC were carried out and detailed audit reports along with briefs thereon containing the significant risk exposure, control issues, recommendations were finalized after discussion with the concerned offices/ departments. Besides, the off-site surveillance team of IAD examined the irregularities/ discrepancies pertaining to the offices/ departments of BSC on the basis of returns received from the 17 Internal Audit Units of IAD housed at field offices and HOK. Necessary improvements in internal controls and risk management systems were introduced based on the findings of the onsite inspection reports and off-site surveillance.

## **Business Planning**

The introduction of business planning process was one of the key initiatives taken during FY08. The initiative is part of the change management process initiated during the year and is aimed at inculcating strategic thinking amongst the BSC employees, explicitly defining and documenting the roles, responsibilities and goals to be undertaken by each office/ department and division, strengthening the accountability mechanism, introducing transparency and objectivity in employees' performance assessment, employees' development. The business planning being a new phenomenon in BSC, arrangements were made for training of middle level managers for disseminating the objectives of the business plans and also to facilitate them in preparation of the plans. The preliminary feedback of the initiative and its impact on the BSC's operations is

encouraging and gives optimism that this would contribute significantly in bringing change and turnaround in BSC. For instance, 66 development projects both relating to functional improvement and institutional development were completed during the FY08 whereas 146 projects have been envisaged for FY09.

### **Role and Performance of Field Offices**

The sixteen (16) field offices of BSC are real operational hubs which carry out all banking functions and transactions on daily basis in an efficient and professional manner. During FY08, BSC field offices continued their efforts to improve the quality of services to their stakeholders and also to improve the physical infrastructure and working environment. The key functions of the field offices include currency management, providing banking services to federal and provincial governments and commercial banks of their area, issuance of Prize Bonds and CDNS products on behalf of CDNS<sup>[1]</sup> and dissemination and implementation of SBP development finance, export refinance and foreign exchange policies. The field offices also monitor the operations of countrywide automated clearing services being provided by NIFT. The Chief Managers of the field offices improved interaction with the chambers of commerce and industry, chambers of agriculture, traders, and farmers' associations, business community and general public through meetings and on-site visits in the areas of their jurisdiction. Periodical meetings of local credit advisory committees and different focus groups (i.e., agriculture, SME and microfinance) were conducted under the development finance support units established at the field offices during the year. Further a number of projects for improvement in physical environments were completed during the year. While there have been significant improvements in the working of the field offices, there is substantial room for further improvement in efficiency, quality of service delivery, customer service orientation and skill enhancement of the field offices workforce to achieve a turnaround in BSC.

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<sup>[1]</sup> Central Directorate of National Savings