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BP Subprime

Maximizing Return on Investment and “Shareholder Value” has claimed another 300 million victims. Or more precisely, the same 300 million victims again. I think it’s probably fair to say that the BP disaster and the financial crisis of 2007-2009 both had at their root the same “business values” problem.

Over the past 30 years the prevailing business ethic has increasingly become that the job of the corporation is to deliver performance aimed almost exclusively at maximum returns for shareholders, to the exclusion of the interests of all the other business stakeholders: the customer, the employee and the general public. This evolution of focus from a broader, more socially oriented commitment to the whole range of those who are impacted by the activities of business entities seems to have begun in the mid-1970’s and gained strength continually, right up to the current era.

The emphasis on maximizing ROI and Shareholder Value to the exclusion of other responsibilities may date to an evolution in the principles advocated by business educators and to some extent to the ascendancy of the Efficient Market Hypothesis. Let’s look at the facts: The financial crisis was tremendously influenced by the belief that financial institutions were doing the appropriate thing when they sought to maximize current and near-term profits irrespective of long-term consequences and customer and societal well being. Could the activities of the various subprime lenders, and the creators of the securitized instruments which supported them have reflected anything except a belief that maximizing profits here and now was the only thing that mattered?

Similarly, could relying on quantitative models which reached conclusions as to soundness and safety which were almost transparently illogical and then failing to provide a margin of safety to back-up and support the resulting financial structures have reflected anything other than attempting to maximize current ROI at the expense of all other interests?

In the case of BP, doesn’t the evidence of the horrific Gulf of Mexico disaster and prior safety breaches indicate that the company was systematically operating to maximize return at the expense of employee safety and the interests of the public? Once again a failure of business values appears to be in place. Providing the safety back-up and the fall-back corrective resources would have raised substantially the cost of doing business for BP without any dollar denominated shareholder benefit unless disaster actually occurred. Disaster had, in fact, already occurred in Prudhoe Bay and BP’s Texas refinery but the philosophy of the company seems clearly to have supported short cuts and substantial risk-taking right up until the explosion of the Deepwater Horizon drilling rig.

Certainly part of the solution to these shocking oversights by business lies in severe financial penalties and improved regulation in both financial markets and off-shore drilling activity but the real sweeping and lasting solution must be found elsewhere.

That "elsewhere" falls clearly in the area of business values and ethics. The whole ethos of business which has moved steadily toward absolute focus on maximizing current and near-term profits has to be refocused at every level from business schools, to management philosophy, to incentives on attention to the interests of all those parties who stand to be benefited or damaged by business' activities. This will require nothing less than a revolution in the principals of world commerce as they are taught, as they are practiced and as they are explained to and understood by shareholders. The problem is in one way much bigger and yet much easier to grasp and address than the separate and highly technical issues about which we have been wringing our hands.

Norton H. Reamer