

Sustainable Shareholder Value: Why Values Matter

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Good evening. It's a great honour to be invited to give the Hugh Kay memorial lecture in the beautiful setting of this Chapel, and I would like to thank CAGE for inviting me to speak this evening.

As many of you will know, this is the fourth cathedral to occupy this site; indeed, since 604AD a church dedicated to Saint Paul has provided a spiritual counterpoint to the trade and commerce that has prospered in this ancient heart of London.

For Christians, St Paul's clearly has great significance as one of the nation's foremost cathedrals. But I think it is also true to say that St Paul's distinctive profile on the London skyline, and its location in the heart of the City, makes it an icon also for London, and for Britain.

Within these hallowed walls, events of tremendous importance and people of great distinction have been celebrated, mourned and commemorated for 300 years. Wren himself is buried here, and near his tomb, which is not far from this chapel, there are tombs and memorials to some of Britain's distinguished citizens. I would like to highlight a couple of individuals in particular. The connection between these people and my subject this evening may not be immediately evident, but please bear with me.

The first individual is Arthur Sullivan – of Gilbert and Sullivan fame. I expect many of you will be familiar with some of Gilbert and Sullivan's comic operas, if only by name. But I suspect that relatively few people will have heard of their penultimate work, *Utopia, Limited*. It wasn't a storming success in the 19th century, and I doubt that it is often revived.

The second individual I want to mention who is honoured in this cathedral comes from a completely different walk of life. He is the man who discovered penicillin, Alexander Fleming. As you all know, Fleming's accidental discovery revolutionised medicine, providing the first effective treatment for bacterial infections.

Sullivan and Fleming are poles apart as individuals, but there is a connecting thread, albeit a fine one; the modern corporation.

The Gilbert and Sullivan opera *Utopia, Limited* was a reaction to a Victorian innovation, the Joint Stock Company Act of 1862. This was a radical piece of legislation, one that created limited liability companies.

Gilbert and Sullivan, however, were not fans; their opera satirised the new institutions, for acquiring power without responsibility or risk. It is one of the more curious librettos ever written, containing as it does the following lines:

Some seven men form an Association ...
They start off with a public declaration
To what extent they mean to pay their debts.
That's called their capital; if they are wary
They will not quote a sum immense.
The figure's immaterial – it may vary
From eighteen million down to eighteenpence.

Before going on to conclude:

If you succeed, your profits are stupendous
And if you fail, pop goes your eighteenpence
Make the money-spinner spin!
For you only stand to win.

Notwithstanding Arthur Sullivan's dislike of the new institution, the corporation has flourished ever since and, arguably, revolutionised our economic lives.

The conclusion of the Fleming story provides one small example of how. Although Fleming discovered the wonder drug, penicillin, he and other scientists could not find a way to mass-produce it. It was a pharmaceutical company, Pfizer, who completed that task. Pfizer's management decided to put their shareholders' capital at stake to invest substantial sums to test an alternative and unproven method to mass produce the drug. The new method was an outstanding success, and Pfizer was able to produce significant quantities of penicillin in the early 1940s. It was desperately needed: the availability of penicillin reduced significantly the number of deaths and amputations from infected wounds in the Second World War, saving untold lives. Hundreds of millions, indeed billions, of people have benefited from antibiotics since.

What this story illustrates is the power of the corporation as an institution to harness the energies of human beings and make their efforts more productive.

Corporations have been one of the most significant catalysts of economic development, development that has raised living standards at a faster rate over the last 150 years than in all of our prior history. They have driven growth and prosperity all over the world. Indeed, we can

**companies as
catalysts for
economic growth**

see the power of private enterprise in action in, say, China today.

China's economic growth over the past quarter century has been well-documented, and the extent of the contribution of private corporations is formidable. Private companies – predominantly small and medium sized enterprises – provide the dynamism of the Chinese economy, accounting for 70 per cent of the growth in GDP, exports and employment in China. No wonder the respected economist Martin Wolf describes the corporation as “the most extraordinary organisational innovation of the past two centuries”.

Corporations have succeeded also because of their important role in mobilising private capital; one of the core ingredients of successful economies, without which few human inventions would find their way into common use.

I don't intend to use this speech to make the case for market economies, other than to say that I believe it has become very clear that markets and the capital that supports them – shareholder capital – can achieve results that, however well meaning and well-directed, governments cannot. There are relatively few people left who are prepared to ignore the mounting evidence of inflexibility, inefficiency, corruption – and excessive debt – which seems to result from the state playing a major, or central, role in capital investment.

Private sector, publicly-quoted corporations are an essential feature of a market economy and have proved themselves to be powerful agents for the good of society, so why then is there such a pervasive distrust of the institution of the company? A suspicion that is deeply embedded and increasingly felt.

Part of this distrust no doubt derives from the rapid growth of corporations and their higher visibility in our interconnected world, which is creating the perception that they are playing an ever larger, and less accountable, role in society.

It also, no doubt, reflects the public antipathy caused by the corrupt and greedy behaviour of a limited number of now infamous institutions. The malfeasance of the Enrons and the Worldcoms of this world have prompted understandable outpourings of disgust at their behaviour, which tarnishes the reputation of all institutions. Yet for all the bad press that understandably follows a high-profile example of corrupt behaviour, it is nevertheless true that the majority of companies, and the majority of people who work within them, are simply trying to do a good job.

Sadly, this is not the public perception. Some of you may have read the book called *'The Corporation'*, or seen the film that was based on it. It concluded that if the corporation was a person, it would be a psychopath.

Singularly self-interested, irresponsible, and willing to put others at risk in pursuit of profit.

This is a distrust of the corporation that can be traced back much further. Some four centuries ago, an English lawyer and MP called Sir Edward Coke castigated companies as institutions that had “no souls”.

Perhaps his attitude reflected the Church's traditional suspicion of commerce and finance, which was underpinned by the philosophical outlook of classical Greek thinkers, notably Aristotle, who considered barter the only morally acceptable form of commerce.

It is certainly true that the attitude of the Christian Church down the centuries towards making money has often been hostile. For a thousand years of Christian history, usury was held to be contrary to the law of God. And from earliest times Christian teaching, indeed the teaching of St Paul himself, developed a real dislike to money, holding that the love of money ... although, it is worth noting, not money itself... is the root of all sorts of social evil.

As far as Jesus himself was concerned, while there are plenty of references in what He says to wealth and its effects on its owners in the Bible, there is relatively little about commerce per se. He does talk about labour markets, about taxes, about money exchange, but the underlying point He makes is always spiritual, rather than commercial. One interesting example is in the familiar Parable of the Talents. We know that two of the servants trade with their talents, and are praised for returning to their master double the amount he entrusted to them. Meanwhile, the servant who buries his talent is berated for not putting it to work in a bank where it could at least earn interest.

The story is a metaphor for how we put to use the talents we've each been given – our abilities and aptitudes – to contribute to the greater good. We all have gifts and resources which we can use for the advancement of mankind. Gifts that confer responsibilities.

But I think you can apply it to commercial life. If gifts confer responsibilities, how do those responsibilities manifest themselves in the context of a large company in the hi-tech, globalised world of the 21st century?

Clearly, a company's first responsibility is to its shareholders, who have entrusted their capital to the company. This is why managers are tasked with maximising the value of a company on behalf of its shareholders.

But we would all surely agree that this statement oversimplifies a company's responsibilities. Indeed, if there was ever a time when it was enough to simply maximise profits, it is long gone.

suspicion of commerce and finance

If a company is to satisfy its shareholders, it must also satisfy a number of other constituencies, or stakeholders, to use the jargon of the moment. Who are these constituencies?

First, consumers, or customers, without whom there would be no business. Today, consumers have more choice than ever before. Aided by the changes in technology and communications which have led to the revolutionary technology of the internet, they consumers are better informed and they have more alternatives to choose from if they are dissatisfied with the service or products of any company than ever before.

Second, employees. My colleagues entrust at least part, and often the main part, of their career to HSBC. They are responsible for delivering our services to customers, so their desires and aspirations are inevitably and profoundly important to the well-being of the company.

Third, pensioners; an issue that has become very topical in recent years, as concerns have grown about the security of pension provision.

Fourth, NGOs and single-issue groups, and society as a whole. Today, all businesses are called to account for their actions on a whole host of, and ever-growing number of, social and environmental issues.

Each of these constituencies makes demands, some of which are contradictory, and a company has to respond to them in a balanced way, against a background of a market that is marked by consolidation, that is intensively competitive, and that is, thanks to technology and globalisation, changing very rapidly indeed.

So how do you reconcile profits and wealth creation with these complexities? The answer, surely, must be sustainable growth. The real objective of a business on behalf of its shareholders must be to build a sustainable business, and not just one that is there for the next quarter's results. In my view, the only way management can meet the aspirations of shareholders, colleagues, pensioners, governments and the wider community over time is through focussing on sustainable growth.

Sustainable, that is, in three senses:

Firstly, sustainable profits growth. Of course...!

But any business strategist knows that this depends upon sustainable customer relations. Offering a service that not only attracts new customers, but allows us to retain existing ones and to do more business with them.

Which, in turn, is increasingly dependent upon a sustained sense of community commitment and responsibility – which, for an international business, means both a global and local commitment. Why? Because increasingly, that's

what customers, colleagues and the general public want. It is this interlinking of interests that is one of the most distinctive features of the business landscape, nationally and internationally, today.

In virtually every market where we operate throughout the world, public confidence and respect depends more and more on our responding to those interests appropriately and effectively.

This prompts the question: how do you underpin a focus on sustainable business in this broader context? And the answer is, that for companies to achieve sustainable profits growth, they need to underpin their business model with a set of values that are embraced in every aspect of their business and which will gain public respect. Business strategy needs to be based on clear competitive advantage, obviously; it needs to be executed energetically and efficiently, obviously. But a culture of values is essential to long-term success, too; or, to put it simply, values matter to value.

But this begs the further question; how does a company, indeed how does its Board, ensure that the company really aspires to the values it espouses? This is in some ways a very difficult question to answer, and in others an easy one.

If you take HSBC, for example, we are a company with more than 9,500 offices around the world, in 76 countries and territories, and we employ 284,000 people.

HSBC feels like a kind of meeting place of the world, a crossroads of different cultures, of people from different ethnic backgrounds, and religious and other persuasions. The diversity of my colleagues – collectively we speak over 130 languages – reflects the diversity of customers we serve around the world, and of people on the planet.

In some respects this might seem to make it difficult for a company to adhere to a single set of principles. Yet for all the obvious cultural diversity, one thing that constantly strikes and impresses me is the extent to which my colleagues share the same desire to work for a responsible and respected company. HSBC is a company made up of people of many different faiths, and people of no faith, but there is an enormous amount of common ground in terms of their value set and their aspirations for the way the company they are a part of behaves.

I believe this is true of most organisations, large and small. Corporations are a human endeavour, and the majority of the people who work for any given institution want to work in an honest environment, and for a company in which they take pride.

As the economist John Kay has observed: “Companies have no immortal soul, but like human beings they live and die. While they live, they prosper by the attributes of their personality.”

satisfying multiple constituencies

A company's personality, its culture, if you like, is a central component of its ability to be successful over a sustained period of time. All companies, and particularly those with a long history, have an inherited corporate culture. One of the most important tasks for any Board or management, as part of its duties of good governance, must be to nurture and strengthen the corporate culture.

It should be the subject of explicit discussion at Board level: how the corporate culture has evolved; how it is contributing to sustainable shareholder value; how it can be nurtured for the good of future generations. And not in self-congratulatory mode – but with an at times uncomfortable spirit of self analysis.

Nurturing a company's personality, its values and ethics, is not an exact science; it can't be represented in figures on the profit and loss account. But it is no less important for that. It is nothing less than an essential leadership task.

Values are not something that can be prescribed smugly by edict from the centre; they run much deeper than that.

In every interaction with fellow human beings, individuals have opportunities to influence behaviour. Every individual has the power to live by – or to abuse – those values and to influence their colleagues to do likewise, however many or few people they have reporting to them on any organisation chart.

So I consider that every one of my colleagues has a leadership role to play in this respect. Companies will only be seen as responsible and a force for good to the extent that each and every employee lives the company's values.

A company's brand is an important standard bearer for those values, internally as well as externally. Companies which seek to position themselves as committed to treating their customers fairly – and which companies do not at least say that they strive to do this? – create brands which resonate with colleagues as well as with the wider world; a company's aspirations are understood internally as well as externally. So it is a real challenge to truly 'live the brand'.

This is easy to say, but so much harder to deliver. Mainly because it cannot be easily pinned down to a single action. It's a multitude of smaller things that add up to a bigger whole.

How people are recruited; how training programmes reinforce the values; how a strategy articulates a company's aspirations to be a responsible, sustainable business. How these values are buttressed by guidelines that spell out the way business should be conducted, and processes such as objective-setting and compensation. Indeed, we consider our values to be of such critical importance to our long-term success that if we are considering an acquisition that makes sense on the

numbers, but that is not compatible culturally, then we will walk away from it. What this all adds up to is the importance of nurturing, underscoring and refreshing those values to ensure they retain currency throughout the organisation.

And it will never be perfect. Corporations are a human endeavour, with all the possibilities and frailties that are intrinsic to human beings. Maintaining values and culture is a task that needs perpetual renewal.

In 2004, the former Chairman of the Fed, Alan Greenspan, forecast that business would see a "re-emergence of the value placed by the market on trust and personal reputation in business practice". How a company makes money, as well as how much money it makes, is becoming an increasingly important part of its investment proposition. In this environment, there is no conflict between sustainable growth, value and values. To repeat: values are essential to value.

That's not to say that there aren't uncomfortable decisions to be made or difficulties to resolve. Of course there are. We live and work in an imperfect world, one in which there are few black and white issues – most are varying shades of grey. So there are clearly challenges for those who want to be associated with a responsible, and sustainable, business.

Let me conclude with a footnote from HSBC's history, which allows me to make one final point. In the 1880s, when HSBC was in its infancy, a man called Charles Addis was 'our man in Peking'. Addis was a scholarly man who was disturbed by the materialism which dominated European society in Asia and worked hard to establish better relations with China.

He was also a lifelong Christian who believed that all great religions shared a common truth. He often quoted the verse from the Book of Micah in the Old Testament: "And what does the Lord require of you but to do justice, love mercy and walk humbly with the Lord." Many of Addis' family and acquaintances told him that his talents were wasted in business. But in a letter to his sister, Addis replied "Business is the beefsteak of life; the *belles lettres* are its *sauce picquante*". Then he quoted Browning: "All service ranks the same with God."

Which brings me back to the parable of the servants and talents.

The point I want to make is that the individuals entrusted with the talents were all servants. And as managers of a company we are also servants – of our shareholders, of our customers and the other stakeholders I spoke about earlier. Managers don't own the company they work for, and the company itself doesn't have an untrammelled right to exist; there is a duty of service that is intrinsic to whatever sphere we are engaged in.

Thank you.

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essential to value**