Dealing with the Unexpected: BP's Black Swan Experience
Speaker: Dev Sanyal, Executive Vice President and Group Chief of Staff
Speech date: 4 May 2012
Venue: St. Gallen Symposium, Switzerland

Introduction

Good afternoon, ladies and gentlemen and thank you Justin, for your introduction.

This is a great forum for inter-generational debate on the issues of the day – on politics, economics and civil society. I am honoured to be asked to take part.

This magnificent town of St. Gallen is well-known for an unexpected event of its own. Ten centuries ago, Saint Wiborada, the first woman to be canonized by the Vatican, reportedly had a vision of an impending attack on the abbey. She warned the monks to flee and saved the abbey's books. She herself stayed behind and she became a martyr and the patron saint of libraries. But lessons were learned and strong walls were soon built around the monastery. The town has since thrived and grown.

This might well have been what we would today call a 'Black Swan' event. Nassim Nicholas Taleb – the writer, academic and trader – defines a Black Swan as an event that occurs outside the realm of regular expectations – one that has an extreme impact – and one that is only explainable after it happens.

And BP – as you know – experienced such an event with the accident two years ago in the Gulf of Mexico resulting in 11 fatalities. It was a tragic accident and one that we deeply regret.

It caused one of the world's largest oil spills and attracted massive media and political attention. A series of attempts were made to stem the flow of oil for 86 days until the well was finally sealed.

For BP those 86 days represented the greatest challenge in our 100 year history – threatening our very existence.

The clean-up response was massive. At its peak it involved 48,000 people – about two-thirds of the population of St Gallen and 6,500 vessels. We used approximately 2,500 miles of boom – enough to go around Switzerland twice.

The operational crisis soon developed into a financial crisis.

This was best epitomised by our credit default spreads – or CDSs – which is the cost of insuring against bankruptcy. Before the accident they stood at around 40 basis points – which made us a safer investment than most sovereign nations. But at the height of the crisis they soared to over 1100 points – and anything over 400 points is considered sub-investment grade – or in popular parlance, a ‘junk’ bond.

This was a very big, very serious event.

It demanded a massive short term response to stop the leak, to clean up the environment and to pay claims to those affected. And we have travelled to 25 countries to share what we learned about prevention, containment, relief wells, oil spill response and crisis management.

But what of the longer term response within BP and our industry? What can we do to anticipate, prevent or if necessary address, future Black Swans? And - as much as it might sound like an oxymoron – how do we ‘think the unthinkable’?

In my remarks today, I would like share my perspectives on four key dimensions of managing risk:

- Building capability;
- Ensuring clarity of governance;
- Sustaining relationships; and
- Establishing enduring values.

1) Building capability

I start with capability because, in a crisis, success or failure comes down to the actions of individuals - and their effectiveness depends on those people's experience and expertise – their capability.

In the face of an unprecedented event, our engineers used their capability to devise the subsea solutions that ultimately sealed the Macondo well.

Others drew on decades of project management experience to organise the spill response.

Our financial capability was demonstrated in establishing the largest trust fund of its kind – for $20 billion – and mounting the largest ever financial defence to restore stability.

These examples and many others demonstrated the value of having the very best people whose decisions were guided not by past benchmarks but by their ability to judge the situation at hand and to act proportionately.

Key capabilities need to be at the heart of the organisation. You can in-source good ideas but you can never outsource decision making.

This is why we continue to invest heavily in developing our people's capability. For example we have an Operations Academy which we run in conjunction with the Massachusetts

Institute of Technology. We have an in-house Financial University which enables finance professionals to develop their own careers as well as driving continuous improvement.

Where we need fresh capability, we are hiring people to provide us with new perspectives. We recruited 2,000 technical experts last year. We have recruited former astronauts, mining professionals, air accident investigators and many others. We have brought in several former military personnel who have provided new insights into operating in challenging environments with multiple risks.

2) Ensuring clarity of governance

The second area I want to cover is governance, by which I mean all of the structures, standards, processes and policies that are used to manage an organisation.   These are channels for capability. Without the right structures and processes, capability gets blocked; but with the right governance, both individuals and company can work to their full potential.

In the aftermath of the accident, this was best represented by clarity of purpose in each part of the organisation dealing with the response. And it is important to recognise that for the non-US organisation, this meant retaining their focus on their activities, rather than being distracted by the news flow.

Let me identify some principles of governance that I believe are critical.

The first is what we call ‘functional excellence’. This means creating structures and standards that lead to consistent performance globally in a given functional area or discipline.

This has led us to accelerate the work we were already doing to systematise, standardise and, to a degree, centralise the way we work. We are doing this in risk management, in drilling, in operations, in project management – in multiple areas of work across the company.

In the upstream – the part of the business which finds and produces oil and gas - , we now have global teams who work at each stage of the project lifecycle - exploration, developments, and operations. This structure means the teams work to consistent standards worldwide and constantly learn from each other.

In the area of finance, we have global policies which provide clear and simple guidance to our business units. They define who is accountable for managing each type of financial risk as well as setting out credit and liquidity requirements.

Financial flows are mainly moved through our Treasury organisation that handles flows of over $1.4 trillion – roughly the size of the Russian economy. It is therefore critical that we have a centralised structure with a clear line of sight to financial exposures and with a single face to financial markets.

The governance of the company needs to be constantly checked and re-checked. This requires a systematic process of ‘checks and balances’ – setting up multiple controls and contingencies and confirming their effectiveness through checking, double checking and triple checking. As one of our board members puts it, “you get what you inspect, not what you expect.”

A key example of this is our new safety and operational risk organisation which has a deployed team of several hundred experts who work alongside line managers in our operations – advising, checking, inspecting, auditing and if necessary, intervening.

A final point on governance is that we have reviewed and updated the way we manage and describe risk across BP – not just safety-related risk, but all risks - financial risk, compliance risk, legal risk, economic risk and so on.

We have introduced a common reporting system and a standardised matrix for documenting risks. This means that risks are assessed against common criteria and can be ranked in a way that enables us to prioritise them effectively. It also allows multiple risks to be examined at the same time.

In other words, it allows for a systematic review of individual and collective risk. It, therefore, seeks to anticipate and address these risks in a dynamic way.

3) Sustaining relationships

The third area of managing risk is to have sustaining relationships. We knew relationships mattered before the accident – we would not have survived 100 years without them. But the 2010 crisis reminded us how much they matter. In the financial area, for example, relationships built up over many years enabled us to mount the biggest corporate financial defence of all time.

Relationships also matter as we look ahead to anticipate and prevent future incidents. As time goes by, the process of embedding learnings from 2010 is becoming more and more of an industry-wide one and we are working in many industry groups to raise standards across the sector.

One such group is the Global Industry Response Group set up by the International Association of Oil & Gas Producers. Another is the International Association of Drilling Contractors – which is working towards a professional certification programme for sub-sea engineers.

4) Establishing enduring values

The fourth, and in some respects, the most critical element is the establishment of enduring values. Values are the bedrock of a company. What you believe in. How you behave. Who you are and what you want to be. These are fundamental in determining how you respond to an emergency and how you decide what you believe to be the right thing.

Companies have their own expectations and ways of behaving. Over time certain ways of thinking and acting become entrenched. But a responsible management will seek to shape that process by setting the compass.

There are five simple, personal qualities that we believe the company stands for at its best – safety, respect, excellence, courage and one team.

We said this at the time – and the words are still true today. We will work hard to prevent accidents. But if the course of events takes a turn that is unexpected, it is the quality of our response that matters. We want to be a company that does the right thing. As we have discovered in the toughest of circumstances, actions in war-time have more resonance than words in peace-time.

BP today

This has been an extraordinary period for us.

We strongly believe that risk management and shareholder value are two sides of the same coin. Apart from the obvious fact that not having accidents prevents value *destruction*, many of the drivers of safety and risk management also drive value *creation*. Standardisation breeds efficiency as well as safety. Respect for capability keeps us safe but also leads us to invest and to excel where we are the strongest.

We are playing to our distinctive strengths – exploration, deepwater production, giant fields, gas supply chains, and a world-class downstream business, all underpinned by technology and relationships.

This means putting value above volume, quality above quantity. Our aspiration today is not to be the biggest but to be the best at what we do.

Conclusion

To conclude, we have come through an unprecedented crisis. A Black Swan event that, by its very nature, created a unique set of circumstances.

We have learned that the best mitigation of risk, but equally, the creation of value, is through building capability, ensuring clarity of governance, sustaining relationships and establishing enduring values.

A global company is best governed through global structures that drive functional excellence. But we cannot mandate every action taken by every individual. We have to rely on people acting responsibly in each situation. What we can do, however, is provide people with tools in the form of global standards and processes which represent the latest and best practice and having alignment on a set of values that represent the heart and soul of the company. This is a continuous process.

We have made progress but we recognise there is more to do.

As Martin Luther King said "the ultimate measure of a man is not where he stands in moments of comfort and convenience, but where he stands at times of challenge and controversy".

Ladies and gentlemen, I hope you see the resonance of these words in our experience.

Thank you.