CREDO WEALTH

Culture of Trust

When companies get beyond the size of a single office where everyone knows each other, culture becomes essential. Like any country or community, a business exists because people believe in it. Money exists, not because it actually represents a physical asset, but because people trust that they can use it. The primary role of banks is to facilitate the functioning of an economy. They are in the business of trust.

Founded in 1852, Wells Fargo traces its history to a six-horse stage coach thundering across the American West. It has long been part of the network building businesses, buying houses, financing education, providing insurance and constructing the bones and veins of American Finance. Now one of the Big Four banks, it maintained its reputation for prudence better than the others through the financial crisis. It operates in more than 8,600 locations and in more than 36 countries and territories, with 268,000 team members.

On 8 September 2016, Wells Fargo reached an $185mn settlement agreement with the Consumer Financial Protection Bureau (CFPB) relating to aggressive sales practices. The hardest part of the growth equation is finding customers. Once you have found them, it makes sense for both parties to try meet all their needs rather than just the one that started the relationship. This can go wrong if the sales team becomes overzealous. The CFPB found that a number of bank and credit card accounts had been opened without being authorized by the clients.

Aware of the problem, Wells Fargo had hired independent consultants to investigate which concluded up to 2% of the accounts may not have been authorised, and up to 0.12% of the accounts had incurred unauthorised fees (115,000 of the 93 million accounts examined). They refunded a total of $2.6 million. At a branch level, disciplinary action included letting 5,300 team members go. They also instituted enhanced training, monitoring and internal controls. New accounts now automatically trigger an email to the account holder.

The heart of Wells Fargo's model depends on trust. An aggressive sales culture created a subculture in the branches that ran counter to those espoused at corporate level. Critics argued executives needed to demonstrate more accountability. Negative media coverage, Congressional hearings and a raft of federal and state inquiries were initiated, including by the Justice department.

CEO John Stumpf did eventually give back $41m of bonuses, and announced his immediate retirement earlier this month. The political fallout is unknowable, but by way of comparison, in the aftermath of the 2007/8 financial crisis, the largest 6 US banks were penalized about $18Bn on average for their role in inflating a mortgage bubble. We view Wells Fargo's share price drop of approximately 12% ($30Bn) as an overreaction. The risk of permanent reputational damage seems to have been avoided. The consumer/retail business is still opening more accounts than they are closing, and there has been immaterial impact on the commercial and government business.

The bank remains a high quality and fundamental part of its diverse client base's future success. Acting as guardians of that culture of trust will need to be management's ongoing focus.

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Important Notice