Why do public corporations and institutional investors exhibit such short-term focus? And why do both generally ignore information that has obvious significant impact on value?

The answers are closely related. Currently, decisions and valuations are based on short-term corporate accounting numbers (quarterly revenue, profits, etc.) and risk analyses that are only capable of using limited types of information. Investors and corporate decision makers have no tools to quantitatively and consistently assess the shareholder value impact of long-term opportunities, risks, and effects. This capability gap represents a key obstacle to the maximization of shareholder value.

The myopia of corporate investors, directors, and executives leads to poor decision making and lost shareholder value.

Myopia is defined as short-sightedness, a narrow view, and a lack of foresight. Myopic decision makers ignore information that is both relevant and available for important decisions.

Companies have traditionally based strategic goals and key performance indicators on short-term accounting numbers such as earnings per share or growth in revenue and profits. But the income statement is not a complete picture of the company's shareholder value. Shareholder value is forward-looking, at odds with backward-looking accounting concepts.

Corporate executives are beginning to shift towards a longer-term approach, but a recent survey[1] indicates that 78% favor quarterly earnings targets over investments such as R&D and capital expansion that would create greater long-term shareholder value. When performance evaluations, bonuses, and jobs are tied to quarterly earnings, it should be no surprise that executives take the short view. CEOs must change the incentive structure, give executives a long time horizon, and instill a different mind-set in the executives as they determine strategy. Executives should diligently search for the distant effects of their strategies and creatively consider alternatives that will maximize shareholder value.

Favoring shareholder value over quarterly earnings numbers may disappoint short-term investors, who might then take their investment dollars elsewhere. But most investors tend to take a longer view than commonly believed, and focus on more than just the yearly earnings[2]. In today's markets, with an ever-increasing sophistication of investors, myopic investors will quickly be replaced and ultimately the traded stock price will rise significantly, reflecting long-term value creation. A board of directors and CEO who lead their company to a longer view and to maximizing shareholder value will enjoy a significant competitive advantage in the long run, and long-term stock prices will reflect this.

Vocal short-term-focused shareholders affect shareholder value mostly through the stock price, which influences the cost of using equity to raise additional capital, acquire other companies, and compensate

[1] http://www.s-ox.com/news/detail.cfm?articleID=835
[2] See "How to escape the short-term trap", McKinsey Quarterly, May 2005

employees. To maximize shareholder value, management must weigh the tradeoff between saving their reputation or manipulating short-term earnings and selectively choosing what information goes public.

Traded stock prices today often lie somewhere between the myopic and longer view. Shareholders who take the longer view therefore have an opportunity to create superior value for themselves; however, even sophisticated investors do not yet fully incorporate all publicly-available information into their investment decisions. The difficulty lies in the reports and in the numerical measurements that are readily available to investors combined with the lack of a consistent calculation method for incorporating other types of information. Most sell-side analysts strive to predict which companies will meet quarterly targets. Many fewer provide the difficult but more valuable service of investigating which companies have long term value. Most investors, then, tend to fixate on retrospective accounting numbers and extrapolate them far into the future, perhaps with a constant growth rate. Accounting numbers were a better predictor of a company's shareholder value in the past, when companies were more stable and more of the value lay in tangible assets. Today, intangible assets such as patents, trade secrets, experience, reputation, and culture, which current accounting practices do not adequately track, constitute the majority of a company's shareholder value.

Corporate decision makers need a tool that definitely and quantitatively demonstrates the shareholder value of a decision, given any type of information.

This tool must account for Market risk and make a specific, numeric calculation at the front end of a decision. The resulting model must be transparent and consistent so that the decision maker can be clear about the critical issues and base decisions on knowledge of the potential opportunities, effects, and risks rather than acting on the basis of 'gut feeling'.