COMMUNICATING THROUGH A CRISIS

# The cost of not saying sorry

## In this age of round-the-clock company scrutiny, we see almost as much focus given to how a company handles a crisis as the crisis itself.

With turbulence in our world growing and the always-on nature of the news, the potential for crisis has become an almost daily consideration for business. Globalisation, investor activism, regulatory change, political and cyber risk are all contributing to increasing business vulnerability and the need for Boards to carefully consider their ability to respond effectively.

## Anatomy of a crisis – research study:

With this in mind, FTI Consulting has undertaken a piece of proprietary research of around 100 recent incidents that have made the headlines. Our objective was to shine a light on those crises, and assess how they played out with a view to helping businesses successfully navigate future disruptive events of their own.

The crises we reviewed span the last 20 years, and include oil spills, cyber hacks, plane crashes, cases of fraud, product recalls and many more. We were interested to see what patterns emerge from these events – patterns which might be instructive for Boards and communicators when facing their own crisis scenario.

## Our findings:

### 1. Existential impact:

As we all know, the effects of a crisis can be significant and long-lasting. So we started by analysing just how significant that impact could be. The findings revealed that in 14 of the 100 cases, the crisis event had been so catastrophic that they had resulted in companies ceasing to exist. Additionally, in almost a third of the 100 cases, a senior executive of that company ended up losing their job. This idea of a sacrificial lamb is nothing new, but such a high number suggests that Boards' tolerance for missteps is low.

- $200bn of market value was lost in the 100 cases we looked at
- 14 of those companies went out of business and in 32 cases a member of the senior management team lost their job
- Companies can expect a 35x increase in media coverage following a crisis event – for social media, it's even more
- Companies are hit much harder where the public perceive a degree of culpability on the part of management
- The financial cost of not saying sorry – measured in terms of share price impact – easily outweighs the total cost of litigation

In terms of share price impact, we discovered that around $200bn of value has been lost as a result of the crises we analysed. Also, nearly a quarter of the surviving public companies in the study (23%) have failed to recover their share price to pre-crisis levels in the time since.

**32%**
Senior executives lost their job

**$200bn**
Total value destroyed over 100 crises

**14%**
Of companies went out of business

## 2. Impact on share price

Next we wanted to analyse the typical course of share prices in the aftermath of a crisis to see whether any trends could be seen. The typical pattern is to see a big drop in share price at the end of day 1. This continues through the first week and only starts to plateau after a month or so.

But we saw huge discrepancies in the way that share prices behave following different types of crisis.

For example, as the chart below shows, a month after a crisis event had become known, the average share price decline across cases of systemic financial mismanagement was 70%, whereas individual corruption cases showed a decline of just 5%.

In terms of recovery after a crisis, those same cases of mismanagement were still on average 63% below their origin after three months, whereas individual corruption cases had recovered most of their value, on average sitting at just 1.9% below their origin.

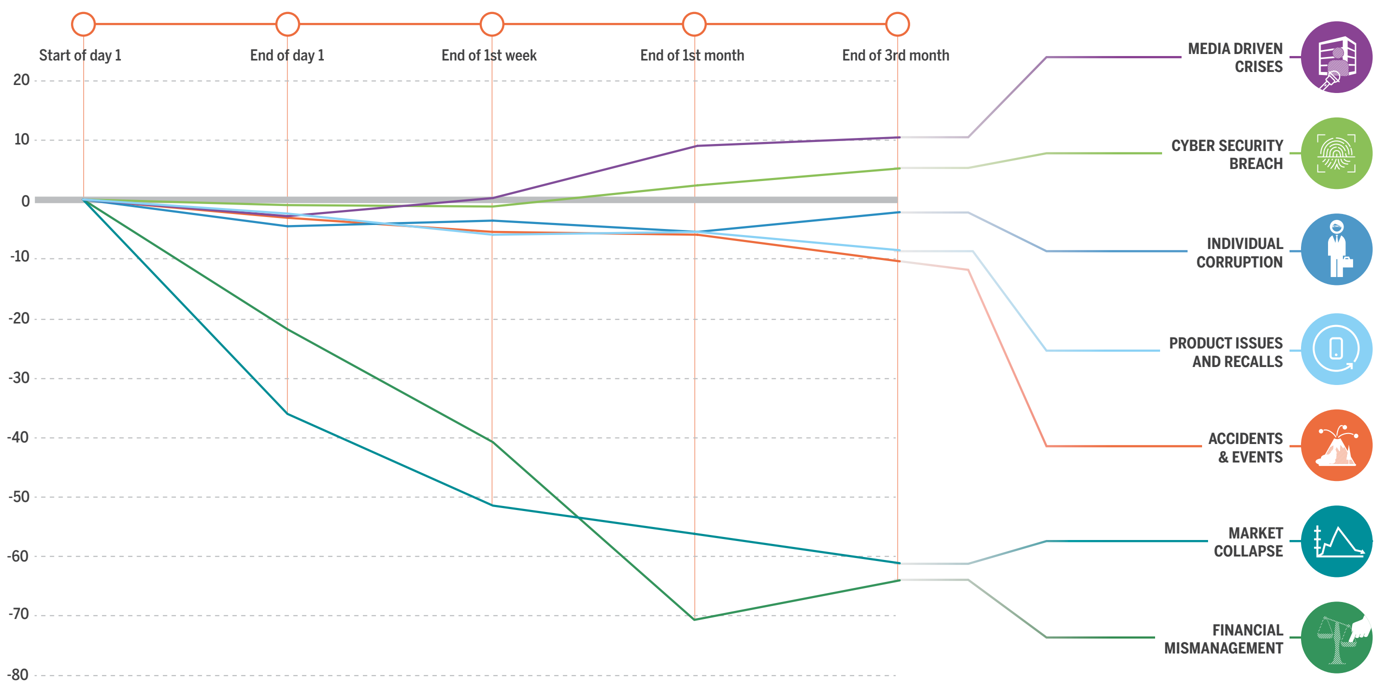
## 3. Media coverage

And what about Media Coverage? Instinctively we know that a crisis will dramatically increase the media's interest in a company, but even we were surprised to discover by how much.

Our study found that in the month after a crisis, a company can expect to receive almost 35 times the amount of coverage than the month beforehand. In terms of social media impact, the post-crisis month saw on average 280 times more mentions than a month before a crisis.

These are significant numbers. Indeed the magnitude of traditional and social media interest around these events begins to shed light on another central learning from our study, namely the intangible impact of a crisis beyond clear and well-understood value proxies such as market capitalisation. This goes to the heart of the unseen element of crisis preparedness and management that all boards need to consider. Are they geared up for this kind of onslaught? Are the relevant processes in place? How can they best respond and continue to protect the day-to-day operations of their business?

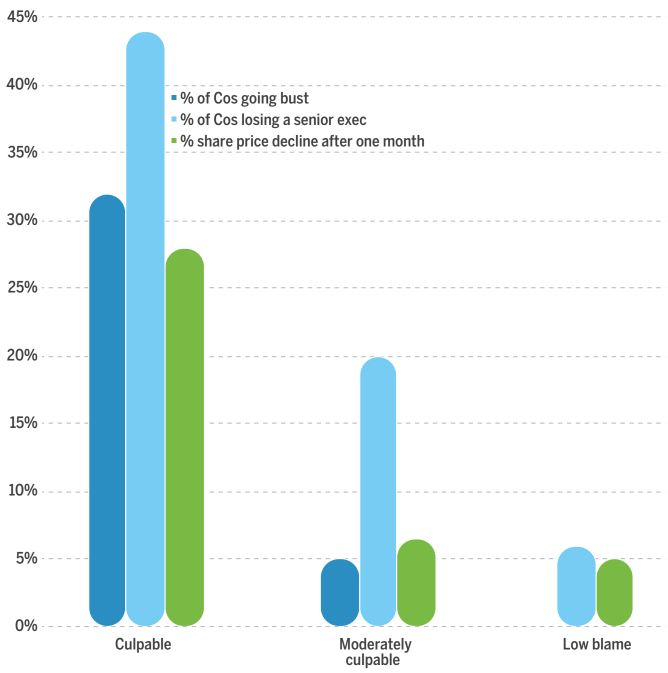
**Average share price performance in the aftermath of crisis (by crisis type)**



## 4. Culpability

As we began to see variations in the way that different crises behaved (when we cut our media analysis by crisis type we discovered that it showed a similar pattern to share price impact), we began to wonder whether companies are hit harder when external audiences perceive a culture of mismanagement. In other words, were investors hitting the share price more heavily, or do the media apply more scrutiny in events where management is perceived to be to blame? Clearly the degree of culpability in crisis situations contains a heavy degree of subjectivity from the outside looking in but our analysis did show that in crises where the management is deemed to be at fault those instances are punished more heavily.

**Impact of crisis depending on perceived culpability**




## 5. Saying sorry

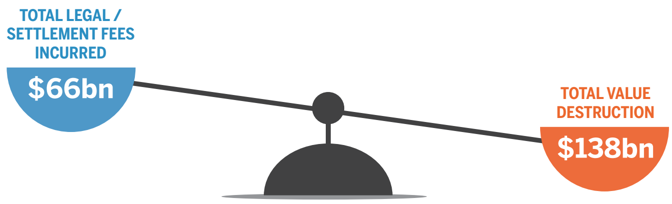
We finally turned to the all-important issue of 'the apology'. Many CEOs instinctively feel that it is right to apologise but some are advised that they should not. The argument against apology is that it is tantamount to an acceptance of guilt and that then opens the door to potential litigation. Reputationally, however, the lack of apology can have significant impact on the credibility of management and the reputation of the wider firm. So, do apologies work?

Interestingly, apologies were found to be relatively few and far between in our study. Indeed, we found evidence of a public apology in only 37 of our 100 crises. We also found that most of those apologies arrived slowly - only 16 of the 37 apologies were issued within two weeks of the crisis incident becoming known to the public.

The main charge against the apology is that it can be bad for business – that it can lead to protracted and expensive legal liabilities. We wanted to see whether there was some way of comparing the financial impact of an apology with the impact of not apologising.

The most effective way to do this was to compare the total cost of litigation and compensation, for as many crises as we could, against the relative value destruction in terms of market capitalisation for those companies. We considered the damage to the value of the owners' shareholdings to be the best proxy for reputational impact under these circumstances (although it is fair to note that the cost of litigation will impact share price itself).

We discovered 37 crisis where the cost of litigation was publically reported. The total cost of the litigation and compensation relating to those crises was $66.73bn. This compares to a total destruction in market capitalisation for the same businesses of $138.36bn.




By this measure, it could be argued that if you don't apologise, you will double your litigation costs in terms of value lost.

## Conclusion

When starting this project, we expected some of our intuitions about crises to be confirmed. We expected share prices to take a hit and the events we surveyed to be a lightning-rod for media coverage. The research supports these views, but the depth and variety of the impacts we saw surpassed our instincts. The three most significant learnings can be summarised as follows:

- Boards need to consider the impact of not apologising in a crisis situation. The effect of reputational damage in terms of share price destruction easily outweighs the cost of litigation.
- The crises which hit hardest are those where management is clearly culpable or endemic cultural decay is evident. For example, the report suggests that culture and effective employee engagement are even more important than planning for cyber risks.
- Companies need to be prepared for the explosion in traditional and social media interest which will come their way in a crisis situation. Does the company have the necessary teams and structures in place to cope?

We anticipate that the findings here will lead companies to think more carefully about how they prepare for their 'nightmare scenario' events. Are they ready? Are they taking these issues seriously enough? Prevention, as we all know, is always preferable to cure.

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