FTI CONSULTING

THE ANATOMY OF A CRISIS

What do the crises of recent times tell us about how best to prepare for future incidents?

FTI CONSULTING RESEARCH REPORT
NOVEMBER 2016

INTRODUCTION:
The anatomy of a crisis

SHINING A LIGHT ON 100 HIGH-PROFILE CRISES OVER 20 YEARS

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 on an almost daily basis and the always-on nature of the news, crisis has become an almost daily consideration for business. Globalisation, investor activism, political and cyber risk are all contributing to increasing business vulnerability and any Board's sense of concern.

If handled poorly, crises can cause deep and long-lasting damage to a company's reputation. If handled well, however, a crisis can become an opportunity for a company's management team to demonstrate their mettle to investors, customers and employees.

With this in mind, FTI decided to undertake a piece of proprietary research around the recent crises that have made headlines. Our objective in this report is 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.

We have reviewed 100 crises over the past 20 years. These 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 crises – patterns which might be instructive for Boards and communicators when facing their own crisis scenario.

In order to capture the key reactions and responses, but also provide some room for reactions to settle and normality to resume, we chose the three-month period after a crisis becomes publically known as our window.

A key element of our research is the variety of crises we included in the study. Of course we looked at some of the best known events of recent years in order to show how some of the crises that have caused worldwide sensation have unfolded. But we also wanted to look at some lesser known crises that companies might be more likely to face day-to-day. These might be here today and gone within several weeks as far as most of us are concerned, but the impact on the companies involved can be much longer-lasting. Here we included issues like cyber breaches, cases of corruption and accidents, for example. We also analysed the data by topic and by region.

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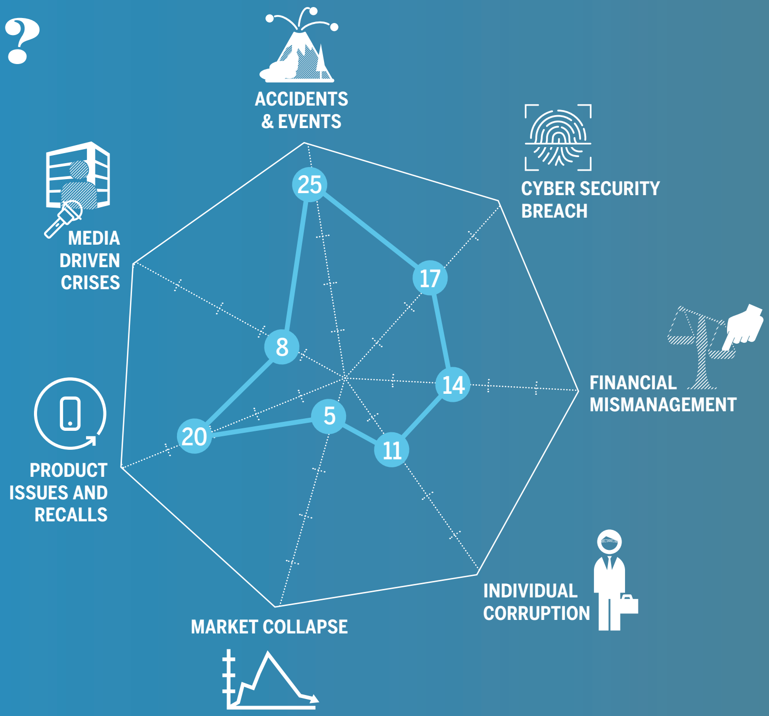

ACCIDENTS & EVENTS
25
CYBER SECURITY BREACH
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FINANCIAL MISMANAGEMENT
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INDIVIDUAL CORRUPTION
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MARKET COLLAPSE
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PRODUCT ISSUES AND RECALLS
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MEDIA DRIVEN CRISES
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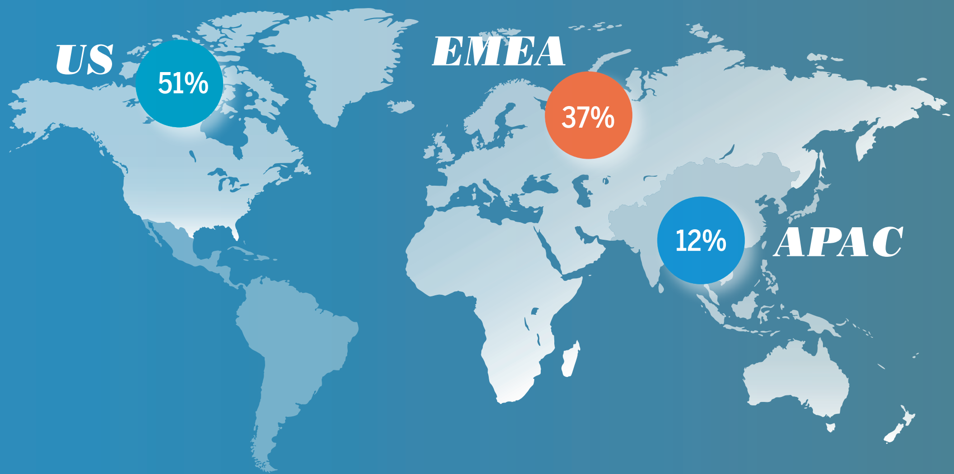


US
51%
EMEA
37%
APAC
12%

IF YOU CAN KEEP YOUR HEAD WHILE ALL ABOUT YOU ARE LOSING THEIRS...

In selecting these seven categories we intended to cover the whole waterfront of different crisis events. The hope was that the results would provide the most useful insight as to the ideal course of action when it comes to similar events in the future. We wanted to be able to guide companies who are thinking about the most likely crisis scenarios facing their businesses and provide a forecast on the direction each crisis is likely to take and how to plan accordingly.

And indeed the findings in this report do help us to address some of the key questions that keep communicators and executives awake at night during a crisis: What can we expect from the media? When should I respond? Will I lose my job? Should we apologise? Is my team large, strong or adept enough deal with what might come?

These results and the guidance that accompanies are intended to form part of the planning process in advance of any crisis, and also inform the ways in which companies respond in the first few hours, days and weeks when one finally occurs. In those early and uncertain moments, it is only natural to seek perspective and an indication of what is to come. Having read what follows, our hope is that companies will be able to see more clearly when a storm is gathering on the horizon, prepare effectively as it makes its way towards shore, and then, when it arrives, weather it.

PART 1
The impact of crisis

IN TERMS OF REPUTATIONAL DAMAGE, OUR STUDY HAS SHOWN THAT THE IMPACT OF CRISES CAN BE SIGNIFICANT AND LONG-LASTING.

1.1
Existential damage

We began our research by trying to get a picture of how significantly the companies in our scope had been affected by crisis. We measured share price, reputational impact (media and social media coverage of the event) and whether or not senior managers at the business had lost their jobs because of the crisis.

To this final measurement, perhaps most starkly, we found that 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 the fact that the number is so high suggests that Boards' tolerance for missteps is low.

In terms of reputational value destruction, we discovered that around $200bn of value has been lost as a result of the 100 crises we analysed. This includes companies that have survived and those that have suffered an event so significant that they have gone out of business.

In 14 of the 100 cases, we witnessed an event so catastrophic that they had resulted in the companies ceasing to exist.

32% — **Senior executive lost their job**

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

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

1.2

How do crises impact share price?

Next, we wanted to better understand how a share price typically performs in the days, weeks and months following a crisis.

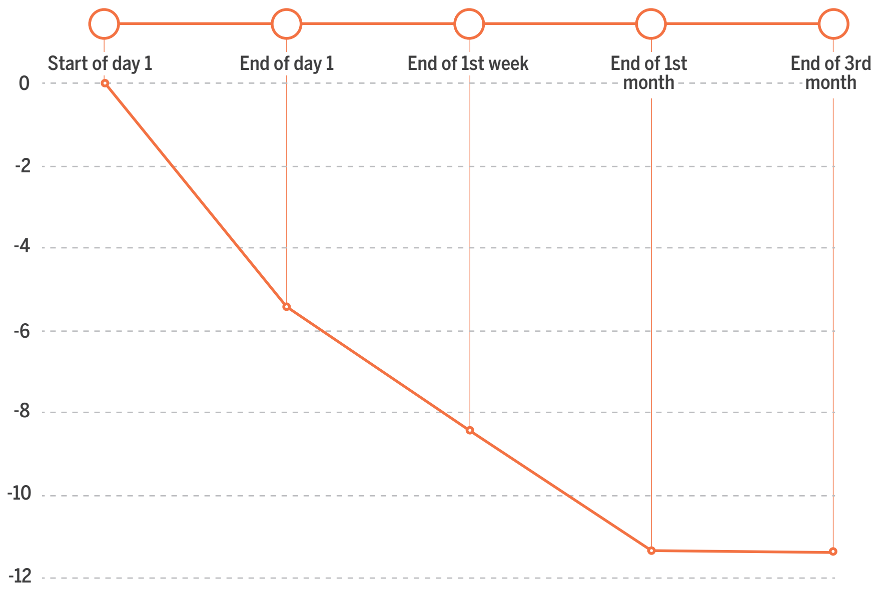
To do that, we tracked stock performance of the publicly listed companies in the aftermath of their crisis events. This analysis provides companies with an idea of the path that a crisis is likely to follow and provides some context for the share price fluctuations one sees when a crisis breaks.

For example, on day one of a crisis, if the shares drop like a stone, it is easy for those inside the company to think that the market has taken a disproportionately strong reaction to the event in question. It's also easy to assume that the stock will continue to slide and respond in a knee-jerk fashion in an attempt to arrest the decline.

But providing a CEO with the ability to look further down the line may delay such a reaction if similar cases in the past have shown a tendency to rebound. Indeed a key learning from our study is that an initial reaction can and should always be placed in the context of an anticipated trajectory. Adding that context could provide comfort to an anxious CEO or act as a useful refocusing device if a company's shares seem unexpectedly resilient in the first instance. Whatever the direction of travel, the real value-add here is a sense of perspective that can help deliver what should be a central aim of any crisis plan: a proportionate response.

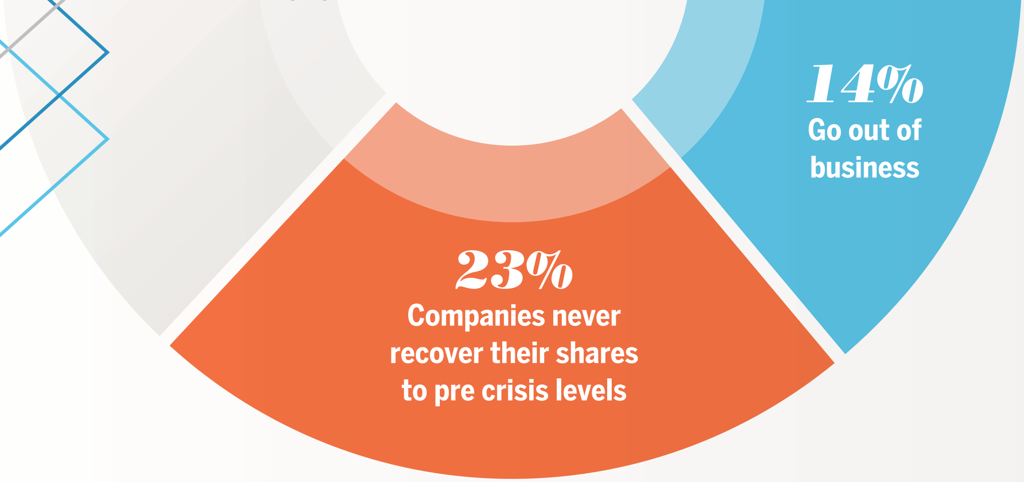
Across all crises and categories, the analysis shows that the average share price drop in response to a crisis is 5% on day 1. By the end of the first week, that number is 8%. After a month, 11%. Interestingly, the average decline after three months is also around 11%.

100 CRISES - AVERAGE SHARE PRICE PERFORMANCE (% DROP)



All of this suggests that in a crisis, a public company can expect its share price to start declining after impact, reach a trough after around a month and then plateau. Also noteworthy is that of the 68 crises where companies had the opportunity to revive their share price[1], only 52 have managed to do so. To be clear, that means that nearly a quarter of the public companies in the study (23%) have failed to recover their share price to pre-crisis levels in the time since.

[1]Excludes private companies and companies going out of business within 3 months



The fact that a dent in a company's share price can sustain itself over time suggests crises are a significant threat to long-term growth. Yet the story becomes even clearer when we start to investigate the behaviour of crisis situations by type.

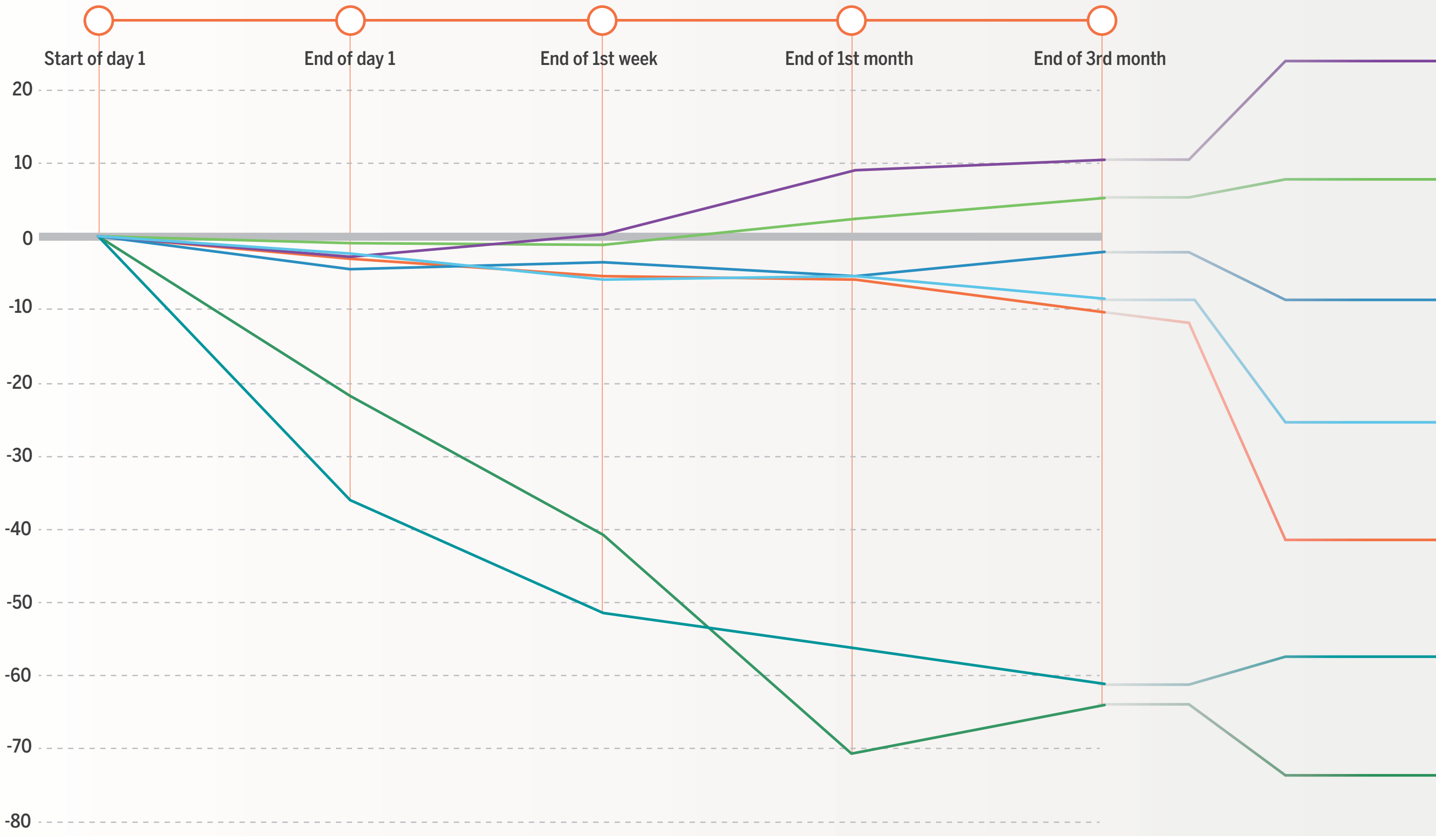
Share price impact by crisis category

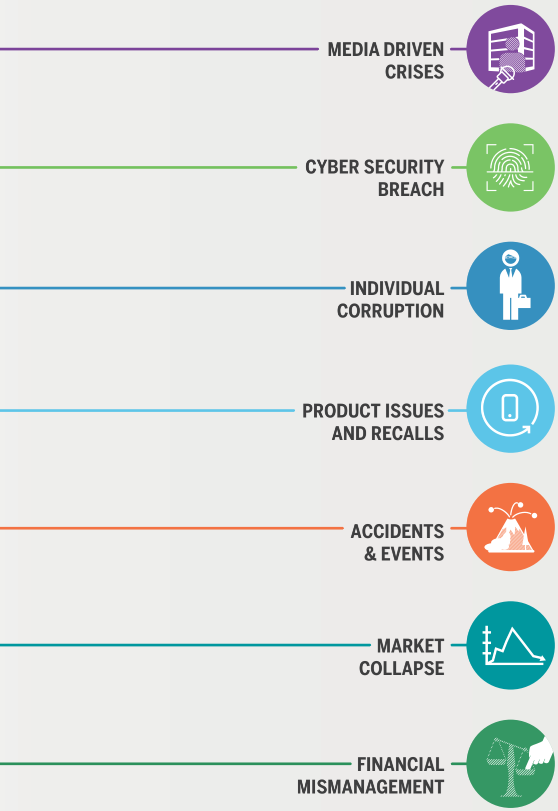
Typically, our evidence shows that cases of systemic financial mismanagement behave differently to cyber-breach events, which behave differently to instances of individual corruption, and so on.

For example, 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 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.

AVERAGE SHARE PRICE PERFORMANCE IN THE AFTERMATH OF CRISIS (BY CRISIS TYPE)





All of this suggests that impact, reaction and recovery are influenced by the manner of crisis you face, and the extent to which an organisation, rather than a single individual or set of circumstances, is deemed culpable by observers.

We decided to examine this angle further and go deeper into the results to see whether assumed management culpability was a major factor in the share price performance post crisis. In the third section, entitled 'The blame game', you can see where this analysis took us.

1.3

Media and social media impact

The third aspect we wanted to examine was traditional media and social media coverage. Do companies see a significant uplift in media commentary in the aftermath of a crisis? Instinctively it feels like that they would, but by how much and over what period? And what conclusions can be drawn from what the numbers tell us?

First, considering 'impact day', it wasn't a huge surprise to discover that a company can expect to garner a significant uptick in traditional media coverage on the first day a crisis becomes known to the public. Roll the clocks forward by a month, and a company can expect to have received more than twice the coverage it had received in the entire year before by that point.

The Crisis Coverage Multiplier

To further understand and explore these dynamics, we began to think about media impact in terms of a 'crisis multiplier': the amount by which a company can expect traditional or social media volumes (coverage hits or mentions respectively) to increase in the immediate aftermath of a crisis, compared with a steady-state comparator – taken as an average month in the year immediately preceding a crisis. This one-month post-impact time period was selected as it captures both the intensity of early media interest and likely company responses to an incident, as well as the most significant share price damage. Looking at the magnitude of pre vs post-crisis volume we were then able to assign multipliers to various crises and crisis types, unearthing some fascinating patterns.

Looking broadly at our 100 crises, our study found that the post-crisis month garnered almost 35 times the amount of coverage than the month before crisis. In terms of social media impact, the same immediately post-crisis month saw on average 28 times more mentions than an average month before a crisis.

35x **Media crisis multiplier (across 100 crises)**

28x **Social media crisis multiplier (across 100 crises)**

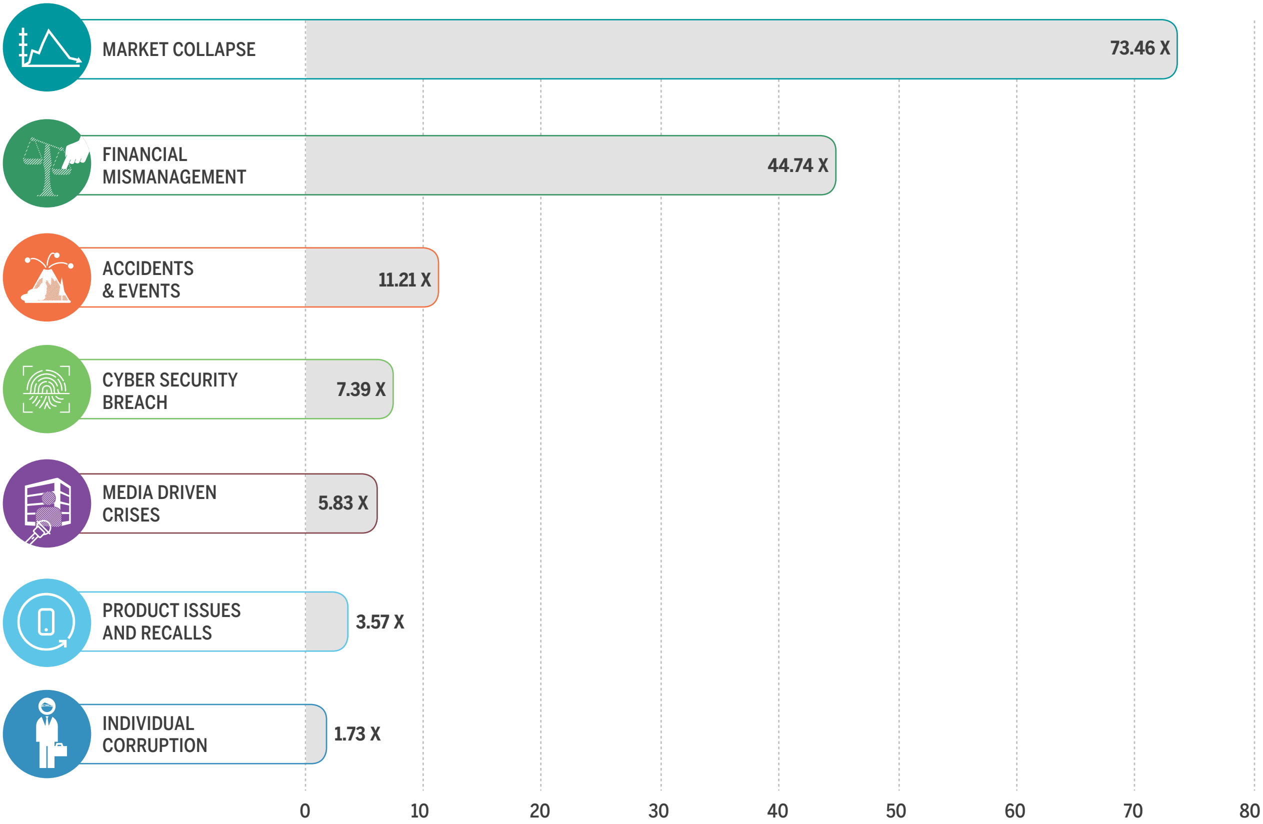
These are significant numbers. Indeed the magnitude of traditional and social media interest around these events begins to shed light on another central learning from our study. This concerns the intangible impact of a crisis beyond clear and well-understood value proxies such as market capitalisation and 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 best to respond and continue to protect the day-to-day operations of their business?

Media interest by crisis type

As we look deeper at the results, we once again see variance between different types of crisis. Some appear to be one off events and media coverage spikes straight after, but by the following week, it's forgotten. On the other hand, some crises trigger long-lasting legal battles, for example, and the media's interest is sustained for some time.

Unsurprisingly, cases of financial mismanagement and cases of market collapse were found to be the most interesting to traditional media over a sustained period of time. These two crisis types had average one-month coverage multipliers of 44x and 73x respectively. There is a useful point of contrast here with cases of individual corruption, where the coverage multiplier was on average only 1.73x. We'll address the question of why a case of individual corruption might be less interesting to media than a case of financial mismanagement later, but taking this suggestion prima facie for now allows us to briefly introduce two important notions we will describe as a) durability and b) profile.

MEDIA MULTIPLIER (INCREASE IN MEDIA COVERAGE, MEASURING ONE MONTH BEFORE VS ONE MONTH AFTER CRISIS)



Durability

Such discrepancies in traditional media coverage volumes suggest that certain crises live longer in the media memory than others. Indeed, the ebb and flow of the news agenda means that something has to be serious in order to stick, and so it proves with cases of financial mismanagement and market collapse. Such high multipliers lead us to believe that media interest in these categories was sustained at a high level for weeks after an event, whereas low multipliers tell us that in trending towards the pre-crisis norm over a one-month period, the media loses interest in some categories reasonably quickly.

This suggestion really comes to life when we consider that our low one-month multiplier categories like individual corruption (1.73x), Product Recalls (3.75x) and Media Driven Crises (5.83x) all started from far higher bases at the time of impact. Indeed, each of these categories' impact-day multiplier (the coverage volume on impact-day in relation to an average day in the year before the crisis) showed a considerable leap from what had gone before (6.2x, 15.13x and 34.2x), but slid back towards normality before one month had passed.

In our high multiplier cases, such as Market collapse, Financial Mismanagement and Accidents and events, our one-month figures were still at least ten times the pre-crisis norm.

Profile

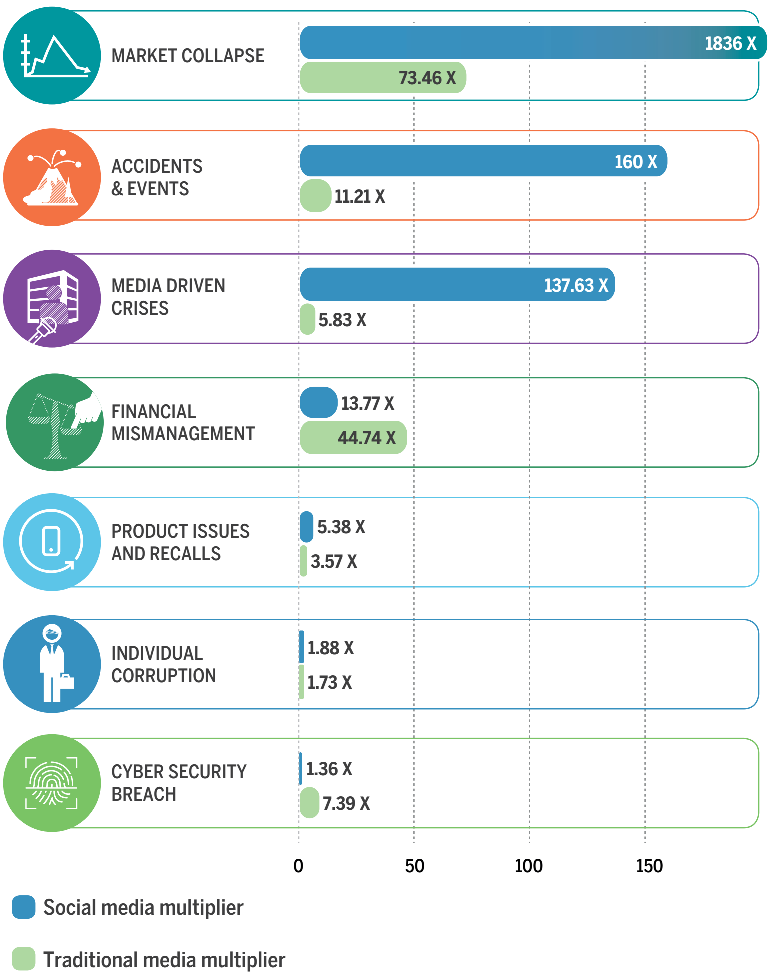
Something worth noting about our cases of financial mismanagement is that this kind of crisis can often make a company you've never heard of famous overnight. This may help account for some of the staggering impact-day and one-month coverage multipliers we're seeing. Here, some of our protagonists were coming from a very low pre-crisis coverage base. However, this also reminds us that nobody is immune from a crisis and prompts a potentially troubling 'what if' question for management teams: Whatever the crisis category, what if something went wrong, and we suddenly became famous for all the wrong reasons? How would we respond? Given a position of relative anonymity, would we even know what to do?

Social Media's long tail

A look at how social media responds to a crisis through the same before-and-after lens uncovers some interesting interplay between the new and traditional mediums. Most importantly, social media interest in a crisis appears to have a considerably longer tail than the traditional media under discussion above. Indeed, in 5 of our 7 categories, social media volume multipliers outweighed traditional media volume multipliers one month after a crisis. This was most notable in cases of market collapse where the social media multiplier was 1,836x (vs 73x traditional multiplier). In Media Driven crisis, the multiplier was 137x (vs 5.83x traditional multiplier), and in Accidents and Events the multiplier was 160x (vs 11.21 traditional multiplier). This all tells us that companies need to be ready for conversations around their practices, behaviour and reputations to carry on for longer than ever.

Taking this media coverage information in the context of share price performance can also provide insight into the balancing act of concerns and considerations that confront companies in a crisis. For example, our data indicates that even in certain cases where concerns from investors may be tailing off, conversations online may still be ongoing and therefore sustaining the risk of long-term reputational damage. Indeed, the aforementioned 160x social media coverage multiplier one month after a crisis in the Accidents and Events category is matched by what appears to be a modest 5% average share price decline after the same period. Indeed in purely share price terms, an average Accidents and Events crisis has started to plateau after one week.

SOCIAL MEDIA MULTIPLIER (INCREASE IN COVERAGE AFTER ONE MONTH) COMPARED WITH TRADITIONAL MEDIA



1.4

A new world...

In years gone by, a share price decline of 5% after a month might have been acceptable collateral damage to a management team in the event of a crisis. Now, any financial cost needs to be viewed in the broader context of conversations taking place online that may both amplify bad press and magnify potential shortcomings in a response.

What is more, no crisis is a James Bond fight scene where adversaries always attack one at a time. Here, it's a free-for-all where reactions happen simultaneously, and responses must be coordinated and aligned to ensure the right messages land as often as possible. The lesson here is that an adequate crisis response must consider the whole waterfront of stakeholders and provide tools to defend against a reputational challenge that goes beyond merely supporting the share price. But knowing how to prepare is hard without some insight into what types of crisis make a given audience react in a certain way. In the next section, we turn our attention to that all-important puzzle.

PART 2
The blame game

THE ROLE OF CULPABILITY IN A CRISIS

As similarities in the way that types of crises behave began to emerge, we started to consider why certain crises were being punished more heavily than others. Here we alighted on the idea of perceived culpability: the extent to which stakeholder reactions either betrayed a belief that a Company (or management team) was responsible for a crisis, or was able to distance itself from events in some way. 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. Was BP at fault for the oil rig explosion in the Gulf of Mexico? Could Thomas Cook have done more to prevent the carbon dioxide-related deaths of two children at its site in Corfu? It's hard to tell. Then there are situations, like Madoff and Stanford, where fraud seems to have been widespread and it's reasonable to assume that the culture – from the top down – had much to do with the extent of the problem. The point is that this study is all about perception. Whether a company was truly to blame or not, what was the sense in the public eye?

TO EXPLORE THIS IDEA WE DIVIDED OUR CRISIS CATEGORIES IN THE FOLLOWING BUCKETS:

CULPABLE

FINANCIAL MISMANAGEMENT

PRODUCT ISSUES AND RECALLS

MODERATELY CULPABLE

ACCIDENTS & EVENTS

MARKET COLLAPSE

CYBER SECURITY BREACH

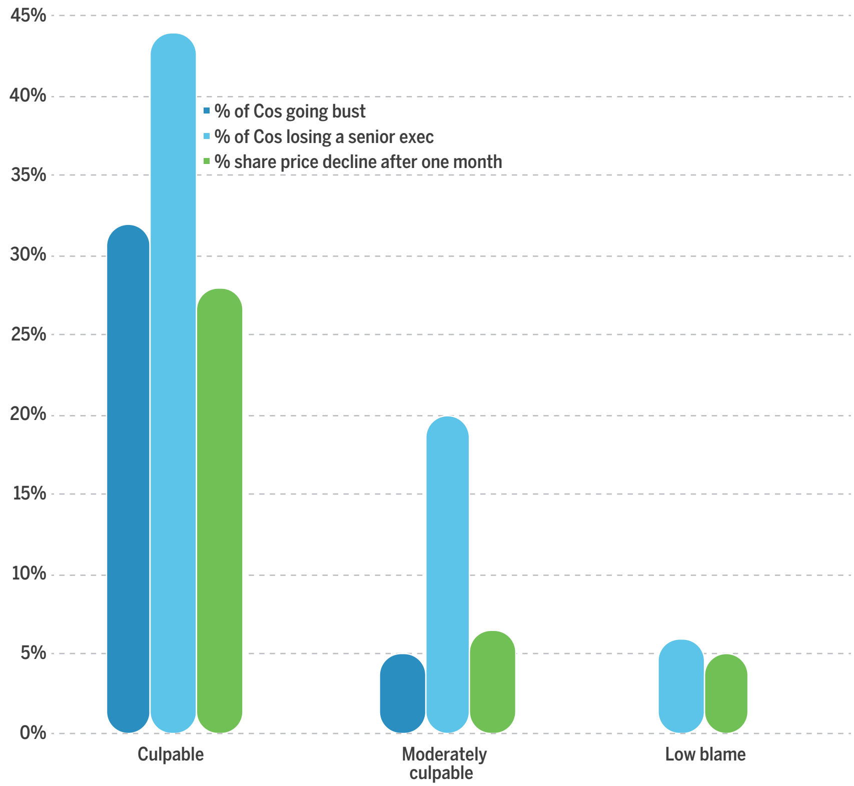
INDIVIDUAL CORRUPTION

LOW BLAME

MEDIA DRIVEN CRISES

To start with the fundamentals, our study found that 11 companies in our 'Culpable' category went out of business as a result of a crisis event. Beyond those 11, 6 further cases resulted in members of the senior management team losing their jobs. That was compared with 3 organisations going out of business in our Moderately Culpable category and 0 in our Low blame category. It's worth noting that all three of those cases in our Moderately Culpable category were the result of Market Collapse, suggesting that without those three cases, perceived moderate culpability for a crisis is highly unlikely to demand a business pays the ultimate price. In the Low Blame category, all companies involved in the study which suffered cases of individual corruption retained their trading status.

IMPACT OF CRISIS DEPENDING ON PERCEIVED CULPABILITY



	Bust	Job loss	1 month sp damage
Culpable	11	15	-28.7%
Moderately culpable	3	11	-6.5%
Low blame	0	6	-5.3%

A look at average share price impact reaffirms this view. Here, crises in the Culpable category suffered the most, with an average share price decline of 28% after one month, which was sustained until the 3 month mark. In the Moderate and Low Blame categories, the latter had the lowest average share price impact after 3 months at -2%, while the former was only marginally worse at -3%.

Interestingly, at the one-day, one-week and one-month marks, our Low Blame crises actually saw a marginally more severe impact than crises in our Moderate category. It's hard to know the exact reason behind this dynamic, although there is a significant recovery in Low Blame cases from around -5% at one-month to -2% at three months indicating criticism running out of steam. Importantly though, both the Low Blame and Moderate categories have largely recovered to pre-impact levels between one and three months, while crises in the Culpable category are still suffering badly.

Our media coverage multipliers also reflect this pattern. One month after a crisis, the multiplier for cases of limited culpability (i.e. the amount more coverage in the first post-crisis month when compared with an average pre-crisis month) was 1.73x. For Moderate cases the multiplier was 15.16x and for Culpable cases this was 77.66x. Here we clearly see cases of organisational failure living longer and more prominently in the media mind than in cases were blame is affixed to a single individual or smaller group.

These findings give us the clear sense that blame matters in a crisis. Indeed the perception of culpability and the extent to which any misdeeds can be linked to systemic malpractice or deception on the part of an organisation looks like a key driver of reactions to a crisis.

PART 3
Saying sorry

SORRY SEEMS TO BE THE HARDEST WORD

This discussion of culpability prompted us to test whether we could find any useful intelligence to help solve the age old crisis dilemma: should a company apologise?

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?

The first important thing to note here is that by apologies, we don't mean reactive statements. Companies generally issued reactive statements on the day or the day after an incident became known. When investigating apologies, we were looking for specific language apologising for the incident and crucially, accepting responsibility. On this criteria, 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. This may have to do with the fact that many of the crises we analysed were not sufficiently high profile in nature, thus rendering the need for public apology to be inappropriate.

Next, we found that most of those apologies that did come arrived slowly. Indeed only 16 of the 37 apologies were issued within two weeks of the crisis incident becoming known to the public.

How do investors and the public view an apology?

Noteworthy here is of that those companies who did fully apologise, those doing so within our three-month window after a crisis fared on average 9% better in share price terms than their counterparts who took longer to apologise. This indicates that a fast apology is likely to serve a company better than a slow one.

Equally importantly, we wanted to understand better how audiences beyond the investor community feel about companies apologising post-crisis. Are they even aware of companies apologising? And, if companies do apologise, are they left with a more favourable impression of the company?

We asked 1,200 consumers about half-a-dozen of the most high profile, consumer-facing scandals impacting the UK in recent years, focusing firstly on whether they were aware of the apologies made, and secondly on whether the apology had left them with a more favourable impression of the company than before.

The six situations we analysed were:

VW	Emissions
TESCO	Horsemeat
TalkTalk	Data hack
News International	Phone hacking
MERLIN	Accident
Starbucks Coffee	Tax

We saw a high level of awareness from the general public about these crises – 83% said that they were aware of the crises having occurred. Of those who were aware, 56% of people said that they had been aware that an apology had been made by those companies; in our view a comparatively high success rate for in terms of awareness. In four of the six cases, this number was above 60% - VW, Tesco, TalkTalk, Alton Towers – all situations where the apology was particularly strongly made or well represented by senior leaders.

We then wanted to test the effectiveness of the apology among those who were aware that an apology had been made. Interestingly, only 43% of those interviewed said that their opinion of the apology had been favourable, meaning that the remaining 57% were left with an unfavourable view of the apology. For a sceptical public, perhaps they feel that businesses are quick to apologise but that they sometimes don't mean it. For our part, in no way does this detract from our view that in many cases an apology should be made quickly and meaningfully in the aftermath of a crisis. It does however reflect the importance of the substance of an apology beyond the mere fact that one has been made.

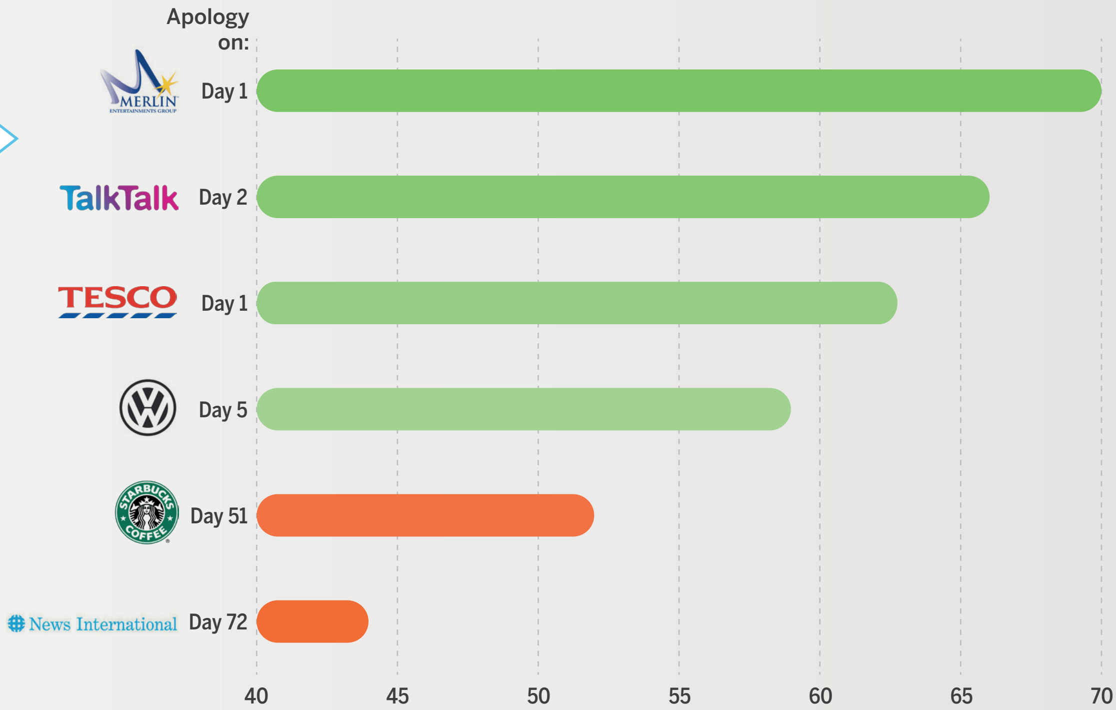
The one company that did leave a favourable impression with its apology was Merlin, after the Alton Towers roller coaster accident. 51% viewed the business' apology favourably. In this case, Merlin's CEO Nick Varney was not just seen to be accepting responsibility for the tragedy, but was also seen to be genuinely contrite. He was available for interview quickly – (59% of consumers said that they felt that the company's apologies had been delivered in a timely fashion) he was clear in how Merlin would seek to ensure nothing of the like happened again; he was quick to minimise any correlation between the day's events and Merlin's desire to provide safe experiences; and he was glowing in his praise of the emergency services. All of this resonated with the public.

In line with the discussion above, another thing that may have helped Nick Varney is that not only did he accept responsibility and apologise for what had happened at Alton Towers, but he also did so quickly. Of course some times in a crisis a full mea culpa might not be appropriate or necessary, but if we assume that companies only apologise when they're guilty of some level of wrong-doing, the evidence definitely suggests that delaying unnecessarily is not a good idea.

If we compare the favourability of the various apologies below with their respective times-to-apologise, we clearly see that those taking the longest to say sorry (News International and Starbucks) were the worst received.

What is more, whereas in the case of a share price movement it could be argued that a negative reaction is more closely related to the nature of the crime than the manner of the apology, here we are simply measuring whether or not a company was deemed to have been honest in their contrition. Simply put, if you're going to say sorry for wrong-doing, say it soon, avoid equivocation and accept responsibility. Otherwise, irrespective of intentions, your apology may fall on deaf ears.

% OF PEOPLE VIEWING THE APOLOGY FAVOURABLY COMPARED TO SPEED OF APOLOGY

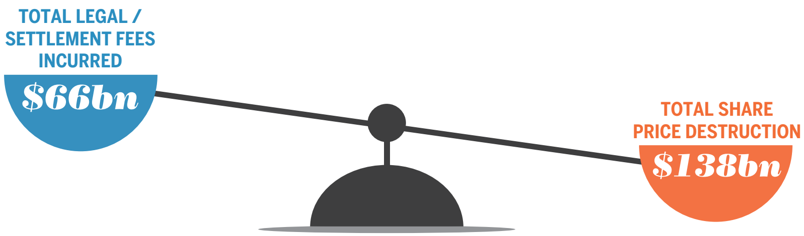


Does the benefit of an apology outweigh the risk?

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

We decided that the best 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.

We discovered 37 crises where the cost of litigation has been evident in media coverage. 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.



In other words, on this measure, it could be argued that the financial case for making an apology outweighs the case for not making an apology by more than 2 to 1.

Again and again in this study we have seen examples of more oblique or less tangible measure of reputation reveal a level of damage that exceeds that shown by more obvious indicators. Litigation and compensation are rightly considered among the potential negative results of a crisis, but neither is the only difficult road a company in crisis might travel. Indeed, our study seems to suggest in the event of any wrong-doing, issuing a swift apology and accepting the fair pay-out that may follow might allow a company to begin rebuilding the trust and belief that is ultimately required to support a positive valuation more quickly than any other tactic.

PART 4
Final thoughts

This research was motivated by a desire to investigate some of the intuitions we all share about corporate crises. Before we began we had a sense that they often cost senior people their jobs; we were convinced that they would prove a lightning rod for media coverage; and we were sure that company valuations would suffer as a result. We were not surprised to find these intuitions confirmed.

But we've also been able to uncover what appear to be some of the fundamental drivers of how people out there in the world respond to crisis situations. Did the company mean it? Was the company itself at fault? Was this a systemic failing, or an individual one? All of these questions have played their part in our discussions and the answers we've suggested should help us all, as communicators, get closer to the right response when the worst happens. We knew before we began this project that we had to be swift, proportionate, and smart. What we didn't necessarily know is how swift is swift enough, and how we would tell if what was being considered was proportionate in a given situation. Nor would we have been able to provide the context we can now give to a management team on how we expect their companies share price to behave during the first week after a crisis, or how long we expect it take to recover its pre-crisis level.

We are closer to that knowledge now and closer to understanding how best to respond when the worst happens.

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