



## Crisis Leadership and Why It Matters

*By Erika Hayes James and Lynn Perry Wooten*

According to the Institute for Crisis Management's annual report on business crises, there were nearly 90,000 news accounts of business crises in the United States alone between 2000 and 2009 (ICM, 2010). In 2010, we witnessed the BP/Deepwater Horizon oil rig explosion and subsequent oil spill in the gulf coast region of the United States. By the time this article makes it to print, there will likely be other noteworthy crises of which to speak. The decade began with financial scandals (remember Enron, Worldcom, and Tyco) and ended with the near collapse of the entire financial system. Wall Street giants Lehman Brothers and Merrill Lynch were casualties, while other prominent banks and government agencies, including Washington Mutual, Freddie Mac and Fannie Mae escaped only with government intervention. In the midst of the financial calamities, communities have been devastated by natural disasters, extreme acts of violence and terrorism, and the life

threatening H1N1 pandemic. Add to this list the run-of-the-mill business crisis such as a product recall (e.g., Toyota), labor strikes, and class action lawsuits (e.g., Wal-Mart), as well as new crises sparked by the proliferation of social media and you may begin to wonder whether crises, generally defined as rare and extreme high-impact events, have become the new normal in organizational life.

The financial implications of a crisis are not insignificant. Crisis events can have associated expenses, such as lawsuits, the loss of business, decreases in stock prices, and declines in productivity. In addition, an organization has to expend not only financial resources, but also human capital to contain the crisis, rebuild the organization's reputation and for business recovery. Thus, some of these expenses are associated with the "crisis after the crisis" and used for managing the aftermath. For example, the expenses associated with BP's oil spill in the Gulf of Mexico are estimated at \$40 billion.<sup>1</sup> These expenses

will be allocated to compensating victims, cleaning the Gulf of Mexico and legal costs.

Given the prevalence and cost of business crises as described above, few can reasonably argue against the need for more effective leadership at all levels of organizations and within all industries across the globe. We wrote *Leading Under Pressure: From Surviving to Thriving Before, During and After a Crisis* as a wake-up call for all current and future leaders, not to mention the business schools and other institutions that train them, in order to highlight the need for a changing leadership paradigm. Circumstances seem to be changing more rapidly than organizations have the capacity to deal with. Moreover, their inability to adequately keep pace with changes in technology, social media, global competition and the public's expectations for increasingly higher profits in a shorter period of time contributes substantially to the pressure business leaders face and the sometimes questionable leadership tactics

and strategies they pursue. In extreme cases, and according to the Institute of Crisis Management (ICM) database, it is in fact leadership decisions and actions that form the basis of most modern day crises--not external threats or acts of God that we most frequently think of as a business crisis. As a result, the ability to lead effectively before, during and after a crisis is a nontrivial matter.

## Crisis leadership

We refer to the capability to lead under extreme pressure as crisis leadership. So, in addressing the question called for by the title of this article, crisis leadership matters precisely because crisis events are inevitable. Crisis leadership matters because leaders of organizations and nations *can* make a difference in the extent to which people are affected by a crisis. Crisis leadership matters, because, in its absence, the stakeholders who are adversely affected by the crisis cannot truly recover from the damaging event. Crisis leadership matters, because despite the damage that is caused by a crisis, effective leadership is the one factor that creates the potential for a company and its stakeholders to be better off following the crisis than it was before the crisis.

Our observations about crises (current crises as well as crises from times past), and the rippling effect they can have, have assured us of a few things. First, crises are inevitable. Some crises may be avoided, and some may be managed well enough to limit long-term damage, but at the end of the day, every organization and every nation will experience a crisis of some magnitude. Second, it is often the handling of a crisis that leads to more damage than the crisis event itself. Third, effective crisis leadership involves much more than good communications and public relations. Although these certainly help, rhetoric and positive spin alone will not resolve a crisis. Fourth, learning from crisis is the best hope we have of preventing repeat occurrences. Finally, crisis events *can* create a potential for significant opportunity to be realized for individuals and for organizations.

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Crises are marked by time constraints, ambiguity, remarkably unusual circumstances, limited or conflicting information, curious onlookers and a need for immediate and decisive action. Given these pressures, the demands of a leader in crisis can be unique and require a different set of abilities than would typically be expected during general leadership (i.e., leadership in non-crisis situations). Moreover, where there are overlapping skill requirements, crisis situations promote a hyper-context that calls for extraordinary capability in some of those shared dimensions of leadership.

Our fundamental assumption is that crisis leadership is more than managing corporate communication and public relations (PR) during a crisis. We consider these activities to be a necessary but insufficient approach to leading an organization through a crisis. Crisis leadership

even goes beyond the parameters of risk management and legal responsibilities. Indeed, we argue that crisis leadership is about building a foundation of trust not only within an organization, but with a firm's key external stakeholders as well. Leaders then use that foundation to prepare their organizations for difficult times; to contain crises when they occur; and most importantly to leverage crisis situations as a means for creating organizational change and innovation. This sentiment is precisely what the U.S. Congress asked of the Big Three auto manufacturers during the 2008 financial crisis. They wanted the industry's leaders to use their financial woes as a starting point to redesign their business model and to create a new and innovative product line. There is a similar call for change in the U.S. healthcare and public education sectors, both of which are in the midst of their own meltdown and in need of a fundamentally new crisis leadership perspective. Likewise, other organizations and industries are confronting the opportunity to leverage crises. For example, after an accounting fraud that misreported 94% of assets, India's Satyam Computers is trying to rebuild its company, and European airliners are considering how to revise industry standards in response to the eruption of an Icelandic volcano whose ashes shut down air traffic for 5 days and resulted in an estimated industry loss of \$200 million<sup>23</sup>.

At its core, crisis leadership, or the ability to lead under pressure, is a frame of mind accompanied by a key set of behaviors. The frame of mind is characterized by openness to new experiences, willingness to learn and take risks, an assumption that all things are possible, and a belief that even in times of crisis, people and organizations can emerge better off after the crisis than before. Clearly, crises are traumatic and we don't want to leave a false impression or indicate that there is not real pain and suffering that results from them. Indeed this can be, and often is, the case. Crisis leaders must address and deal with these circumstances. Our goal, however, is to emphasize that leadership is also about creating possibilities so organizations can blossom in ways that might not have been predicted or possible in the absence of the pressures that crises evoke.

## The hallmarks of a crisis leadership mindset

In our book, *Leading Under Pressure: From Surviving to Thriving Before, During and After a Crisis*, we propose that crisis leadership is a continuous process that involves developing a mindset for reflecting, adapting and learning from the crisis situation and its aftermath. This requires the ability to strategically scan the environment for knowledge. However, to effectively act upon the knowledge acquired demands the leader make quick and ethical decisions and establish trust among his/her stakeholders. The knowledge coupled with the trust of stakeholders and actions enables leaders to see and respond to opportunities in the midst of a crisis and the associated payoffs.

### A Propensity to Reflect, Learn & Adapt

In a crisis situation, the individual leader's learning should happen in tandem with the organization's learning. At the core of this learning is the skill set for acquiring knowledge and implementing a behavioral change as a result. This calls for a learning orientation that encompasses a propensity to seek knowledge and to use this knowledge for adaptive responses. When learning occurs during a crisis, leaders and their organizations can reduce the negative impact of a crisis if

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they are willing to examine the root causes of the crisis and cultivate a culture that values data for decision-making. Learning promotes resilience by preparing the organization with the mindset for managing adversity and the capacity to recover from the crisis.

For example, when Tyco International confronted a financial scandal and its reputation was in shambles, the new leadership team worked tirelessly at learning how to instill high standards of business practices into Tyco's corporate culture. They engaged in a reflective process that began with the top management team conducting a root cause analysis of the organization's past mistakes. In addition, they evaluated and adopted best practices from other companies, and, as a result of their learning, drafted a list of twenty-five governance practices and a Guide to Ethical Conduct that is used for employee and board training. Tyco's actions following the crisis speak to the importance of a leader adopting a learning orientation.

#### Scanning and Seeing Possibilities

A byproduct of learning orientation is the ability to make sense of the crisis through environmental scanning, and this, in turn, equips leaders to see possibilities for resolving the crisis. To sense-make entails scanning information from multiple sources, integrating the information into a broader context and connecting the dots at both the strategic and tactical levels. Furthermore, during the scanning process, leaders should encourage discussion and debate so organization members challenge the status quo and explore the pathways to the various possibilities. Scanning enables leaders to take a big picture approach so the organization can recognize and appreciate their responsibility and accountability to all stakeholders.

For some organizations that we studied, their environmental scanning practices included engaging in scenario planning as a strategy for preventing or containing crises. During scenario planning, organizational members create a series of "different futures" based on scanning environmental factors, such as demographics, political, economic, social, technological, legal, natural environment and global trends that are key driving forces. Scenario planning in crisis situations helps leaders create cognitive maps that provide a reference point and increase the organization's ability to navigate unfamiliar terrain. As leaders scan their environment and craft scenarios, they develop a mindset for "thinking about the unthinkable," engage in anticipatory brainstorming and learn how to consider a range of possibilities for the future that take into account uncertainty.

In 2008, the Detroit Free Press newspaper confronted a crisis of declining revenues as sales decreased in its industry because of competitive forces and substitute products for traditional newspaper. To address this "smoldering" crisis, the Detroit Free Press worked with design company Ideo to create scenarios for the future by scanning and



observing a broad spectrum of people in their homes, at their places of work and in everyday settings. These scanning efforts guided development of new offerings, changes in delivery of the newspaper and an expanded web presence.

#### Quick and Ethical Decision Making

The ability to make sound and rapid decisions under pressure becomes a core competency for effectively handling a crisis. Yet, the emotional responses to crisis, characteristics of a crisis itself (time constraints, limited information, required action and pressure for change) contribute to the difficulty of decision making. In situations where leaders have ample time to respond and abundant access to information, they are more likely to engage in sound decision making. For this competency to transfer to crisis situations, leaders must beware of decision-making biases that are dysfunctional and lead to errors in judgment, such as anchoring decisions in one type of information or a tendency to make decisions that justify past choices or investments. In addition, leaders should be attuned to environmental signals, and use these signals to expedite the decision making process.

Leaders in some organizations ignore crisis signals, avoid decision making and try to conduct business as usual. Two years ago, the citizens of mainland China called for a boycott of Carrefour, the French retailer, because of widespread unsubstantiated rumors that one of Carrefour's major shareholders had been making donations to the Dalai Lama. During the early period of the boycott, Carrefour denied the allegations of its support for illegal political organizations, and stated that the rumor was fabricated. As the boycott progressed, Carrefour expressed, as a foreign enterprise in China it did not want to become involved in politics. Also the company suggested it was not concerned with the boycott because there was no significant impact on sales.<sup>4</sup>

Carrefour's defensive actions and lack of response for handling the boycott damaged its reputation. Even though Carrefour had warning of the pending boycott, it took a passive role by making no plans to manage the looming crisis. Carrefour was content to be a bystander as both the French and Chinese governments intervened, and it missed the opportunity to leverage the Chinese government's views on the crisis. When the Chinese government encouraged the boycott

to cease, Carrefour could have aligned the government's stance with its public relations strategy. Moreover, Carrefour could have utilized the boycott to emphasize its positive contribution to the Chinese economy, such as its employment of 40,000 Chinese workers.

Decision making in crisis situations calls for leaders to examine the ethical implications. This entails making a moral judgment aligned with both the leader's and organization's values. In addition when making a moral judgment leaders should consider the various stakeholders and how they are impacted by the crisis. The moral judgment is a springboard for action, and the decision maker must decide what to do in light of it. Aligning actions with ethics can be difficult because executing the plan involves working around impediments, resisting distractions and keeping focus on the organization's goals.

As stated earlier crises are costly, but we believe when leaders incorporate ethics into their decision making process, it enables them to do the right thing from the perspective of the organization's various stakeholders. Take the case of toy manufacturer Mattel, who had to recall over 14 million toys because of excessive levels of lead and small detachable magnets. As suggested in an article in Forbes and Mattel's annual report, because of the crisis, Mattel spent 50,000 labor hours on the product recall, \$40 million on the administration expense associated with the recall, and the crisis impacted the firm's 2007 gross profits by an estimated \$71 million.<sup>56</sup> However beyond the financial implications of the crisis, Mattel's leadership had to make decisions regarding its ethical obligations to stakeholders such as its shareholders, suppliers, the retailers that sell its toys and the children that play with Mattel's toys. For Mattel, these ethical decisions encompassed partnering with suppliers to ensure that both quality and efficiency are incorporated into the manufacturing process and taking more responsibility for testing the safety of the toys it sells.<sup>7</sup> It should be noted that for Mattel, ethical judgment does not end once decisions are made, it also demands that the organization be accountable for its behavior.

#### **Establishing Trust**

When Mattel experienced the product recalls

because of lead-tainted and faulty magnet toys, the firm's CEO, Robert Eckert, acted quickly to establish trust by releasing a video that apologized to its stakeholders. In this video, Eckert took full responsibility for the issue and described the action steps the company would implement to improve product quality. Mattel's CEO's actions for building trust were necessary for the company to emerge from the crisis. Trust was established by using multiple channels to communicate a norm of openness and honesty about the crisis situation. Also, Mattel's communication during the crisis expressed that the company was doing something about the problem and the importance of creating rigorous safety standards in toys for the well-being of children.

As observed from the Mattel crisis, truthful communication and value-laden actions convey the four components of trust that leaders should consider in crisis situations: competence, openness, concern and reliability. Leaders need to feel competent and have the confidence that others see them as competent. Open and honest leaders are more believable in a crisis. Showing concern

#### **Believing that Opportunities Can Be Attained**

Often leaders focus on the negative aspects of a crisis and do not perceive the opportunities in the situation. Crises are opportunities for organizational change and revitalization because a crisis brings to leadership's attention issues that have been neglected and present possibilities for innovation and system improvements. This demands that leaders transition from feelings of anger, anxiety, guilt and despair to an outlook of optimism and hope. Perceiving a crisis as an opportunity involves leaders enacting a radical vision that inspires organizational members to audit the strengths of the organization and its environment and to use these strengths as resources. This is supported by an organizational culture that reinforces a collaborative "can-do" attitude because of members' belief that failure is not an option. Moreover, opportunities are better perceived when organization members are empowered to improvise because they learn how to "think outside the box," readjust roles and restructure processes, and, as a consequence, this generates innovation.

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for both the company and for employees during a crisis is especially reassuring. Meeting expectations, or being reliable, is another component of trustworthiness that is valued by stakeholders.

In addition to these components, there is an element of risk in trust. Leaders must believe that subordinates will perform to the best of their abilities, even though the possibility exists that they will not. In other words, this may require the leader's willingness to be vulnerable to those who have been entrusted to handle various aspects of the crisis. This willingness is more likely if the organizational culture is generally perceived as trusting. If that culture does not already have trust as a foundation, then there is work to be done to effectively deal with a future crisis.

McDonald's experience during the 1998 Russian economic meltdown illustrates how leaders can perceive opportunities even in amidst a crisis. During this time, the Russian economy was experiencing hyperinflation. Some Russian citizens could not afford basic necessities. McDonald's leadership found ways to reduce prices of menu items because of supply chain efficiency, while still maintaining the core menu that was the central component of McDonald's brand.<sup>8</sup> Efficiencies in the supply chain were accomplished by employing McDonald's European network of suppliers to train Russian suppliers, and by building its own food production facility to ensure consistent quality of local meat, dairy and baked products. Also, McDonalds used Russia's economic crisis as an opportunity for

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selective hiring of employees and designed a compensation system based on productivity. McDonald's willingness to be price sensitive and maintain its service standards resulted in customer loyalty, which enabled McDonald's to weather Russia's economic crisis.

As we observed from McDonald's story, seizing opportunities in a crisis situation pressures organizations to be resourceful. For McDonalds, some of the resources already existed and could be repurposed to manage the crisis. For other organizations, attaining opportunities in a crisis situations may require forming an alliance with external stakeholders. The McDonald's case highlights the role of innovation for discovering opportunities when leading a crisis. Resolving crises trains leaders to innovate as they explore what can be enhanced or eliminated in the organization. When the seeds of innovation are culti-

vated and institutionalized the organization is transformed.

In sum, the characteristics of crisis leadership may in fact be appropriate for business leaders in all situations, not just during times of crisis. Displaying these leadership competencies during times of crisis, however, poses a unique challenge. First, leaders in crisis are forced to operate in full public view, with the media and others positioned to report and critique their actions. Second, during a crisis, there is the tendency to want to make the crisis simply go away, resulting in decisions and actions that are oftentimes suboptimal (e.g., cover-ups and deception). These shortcuts can ultimately undermine effective leadership. However, by consciously being attuned to the big picture of a crisis and the opportunities that can be created for the organization as a result of crises, leaders and their organizations can thrive. In short, in today's competitive business environment, developing crisis leadership competencies is mandatory.

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### Notes

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