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A Forced CEO Turnover Costs a Large Company $1.8B More in Shareholder Value than a Planned Turnover, according to Strategy& Research

Companies undergoing forced CEO turnovers rather than planned successions have foregone US$112 billion in shareholder value annually in recent years; good news is that companies are now far more often planning CEO turnovers

New York, NY (April 14, 2015) – CEO turnovers at big public companies are inevitable and rarely easy. But what is the cost?

In terms of shareholder value, it's more than significant. Simply having a CEO turnover reduces median total shareholder return to -3.5% in the year after the turnover takes place, based on the last three years of data (shareholder return is measured relative to the indices that companies trade on).

That's according to analysis in the newly released 15th annual study of CEOs, Governance, and Success by Strategy&, a part of the PwC network, which examines CEO turnover as well as incoming and outgoing CEOs at the world's 2,500 largest public companies.

Companies with forced CEO turnovers rather than planned successions have left $112 billion of value on the table

When a CEO turnover is forced – i.e., not part of a planned succession or the result of M&A – the cost is especially high. Median total shareholder return drops to -13% at these companies in the year leading up to the turnover and only recovers somewhat to -0.6% in the year after. This compares to figures of -0.5% and -3.5% in the year leading up to and the year following companies' planned successions. Moreover, the report estimates that companies that have undergone forced turnovers in recent years have annually foregone $112 billion – $1.8 billion per company – more than would have been lost if those successions had been planned.

"While firing the CEO can be the right call, it's enormously costly. When you quantify the cost of turnovers, particularly forced ones, you get a strong sense of the importance and payoff involved in getting CEO succession right," says report co-author Per-Ola Karlsson, Senior Partner at Strategy&.

If the share of forced turnovers drops to 10% of all turnovers, from the average of 19% seen between 2011 and 2013, the world's largest public companies could add, in aggregate, an additional $60 billion in value, according to the report.

Companies are moving in the right direction: Planned turnovers on the rise

Companies have indeed been getting better at CEO succession. The percentage of CEO successions that are planned climbed to 82% in the 2012-2014 period from 63% in the 2000-2002 period, according to the report.

Further, 78% of companies undergoing planned successions in 2014 promoted someone from within the company to fill the CEO post. "This is a healthy rate for insider successions – and insiders give companies some advantages. Our research shows that outsider CEOs have been forced out of office – a costly event – 44% more often than insiders," says Ken Favaro, Senior Partner at Strategy&.

"If an industry is being disrupted and new capabilities are required to compete, hiring an outsider can make sense," adds Gary L. Neilson, Senior Partner at Strategy&. "However, insiders typically have slightly longer tenures and have delivered higher total shareholder returns – annualized and regionally adjusted – over their entire tenures in 10 of the 15 years we have tracked."

There's still room to improve CEO succession

Although companies have made significant strides in their CEO succession planning over the last 15 years, there's always room for improvement.

"When companies do succession planning right, they make CEO governance an ongoing agenda item at board meetings, and work to get in front of issues before they become disruptive," adds Favaro. "Hundreds of billions of dollars in potential future value will depend on how well the world's largest companies can improve their succession practices in coming years."

Methodology

Strategy& identified the world's 2,500 largest public companies, defined by their market capitalization (from Bloomberg) on January 1, 2014. We then identified the companies among the top 2,500 that had experienced a chief executive succession event and cross-checked data using a wide variety of printed and electronic sources in many languages. For a listing of companies that had been acquired or merged in 2014, the firm also used Bloomberg.

For more information, visit http://www.strategyand.pwc.com/global/home/what-we-think/chief-executive-study.

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