Detroitosaurus wrecks

The lessons for America and the car industry from the biggest industrial collapse ever.

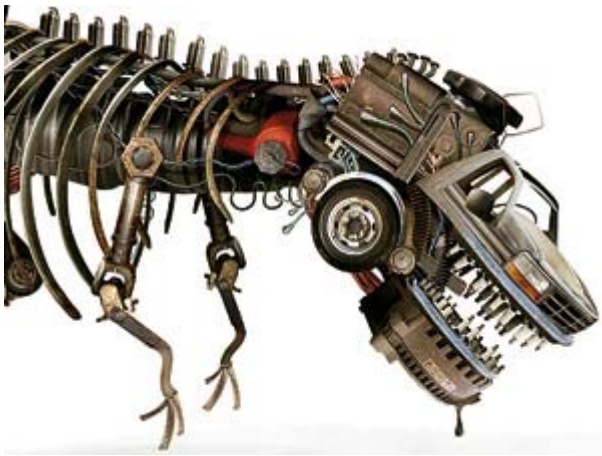

Illustration by Derek Bacon

The demise of GM had been expected for so long that when it finally died there was barely a whimper. Wall Street was unmoved. Congress did not draw breath. America shrugged. Yet the indifference with which the news was received should not obscure its importance. A company which once sold half the cars in America, employed in its various guises as many people as the combined populations of Nevada and Delaware and was regarded as a model for managers all over the world has just gone under; and its collapse holds important lessons about management, about government and about the future of the car industry (see article, article).

Government and GM: a fatal mixture

GM's architect, Alfred Sloan, never had Henry Ford's entrepreneurial or technical genius, but he had organisation. He designed his company around the needs of his customers ("a car for every purse and purpose"). The divisional structure he created in the 1920s, with professional managers reporting to a head office through strict financial monitoring, was adopted by other titans of American business, such as GE, Dupont and IBM before the model spread across the rich world.

Although this model was brilliantly designed for domination, when the environment changed it proved disastrously inflexible. The problem in the 1970s was not really the arrival of better, smaller, lighter Japanese cars; it was GM's failure to respond in kind. Rather than hitting back with superior products, the company hid behind politicians who appeared to help it in the short term. Rules on fuel economy distorted the market because they had a loophole for pickups and other light trucks—a sop to farmers and tool-toting artisans. The American carmakers exploited that by producing squadrons of SUVs, while the government restricted the import of small, efficient Japanese cars. If Detroit had spent less time lobbying for government protection and more on improving its products it might have fared better. Sensible fuel taxes would have hurt for a while, but unlike market-distorting fuel-efficiency rules, they would have forced GM to evolve.

As for the health and pension costs which have helped sink GM, the company and the government bear joint responsibility for those too. After the war GM rejected a mutual scheme that the unions wanted because it smacked of socialism; and around the same time, the company agreed to give retired workers full pensions and health care for life. But if successive administrations had dealt with America's expensive and inadequate health care—a problem with which Barack Obama is now wrestling (see article)—the cost of those union demands would have been far lower. None of GM's competitors has had to shoulder costs per worker

anything like as heavy: until an agreement in 2007 with the union, each car in Detroit carried about $1,400 in extra pension and health-care costs compared with the foreign-owned competitors in America.

GM, Ford and Chrysler tried to improve: by 2006 they had almost caught up with Japanese standards of efficiency and even quality. But by then GM's share of the American market had fallen to below a quarter. Rounds of closures and job cuts were difficult to negotiate with unions, and were always too little too late. Gradually the cars got better, but Americans had moved on. The younger generation of carbuyers stayed faithful to their Toyotas, Hondas or Mercedes assembled in the new cheaper car factories below the Mason-Dixon line. GM and the other American firms were left with the older buyers who were, literally, dying out.

GM's demise should not be read as a harbinger of doom for the car industry. All around the world people want wheels: a car tends to be the first big purchase a family makes once its income rises much above $5,000 a year, in purchasing-power terms. At the same time as people in developing countries are getting richer, more efficient factories and better designs are making cars more affordable. That is why the IMF forecasts that the world will have nearly 3 billion cars in 2050, compared with around 700m cars today. In the next five or six years the Chinese will overtake the Americans in terms of annual car sales: in 40 years' time the Chinese will have almost as many cars as exist in the whole of the world now. Indeed, GM's own experience abroad shows the promise of emerging markets. Brazil has long been a source of profits, and GM has a leading position in China.

Yet although the long-term prospects for sales growth look excellent overall, the car industry has a problem: it needs to shrink dramatically. At present, there's enough capacity globally to make 90m vehicles a year, but demand is little more than 60m in good economic times. Even as the big global manufacturers have been building new factories in emerging markets, governments in slow-growing rich-world markets have been bribing them to keep capacity open there.

Because the industry employs so many people and is a repository of high technology, governments are easily lured into the belief that car firms must be supported when times are tough. Hence Mr Obama's $50 billion rescue of GM; and hence, too, the German government's financial backing for the sale of Opel, GM's European arm, to Magna, a Canadian parts-maker backed by a Russian state-owned bank. German politicians have made it clear that they plan to keep German factories open even if others elsewhere in Europe have to close. At least the American rescue recognises the need to remove capacity from the market: GM will, as a result of the deal, lose 14 factories, 29,000 workers and 2,400 dealers.

It could still be a great business

For all its peculiarities, the car industry is no dinosaur—Toyota, for instance, is a byword for manufacturing excellence. But the unevolved GM deserved extinction. Detroit employed so many people and figured so large in American culture that governments felt they had to protect it; but in doing so, they made it vulnerable to less-coddled competitors from abroad. By trying to keep their car industry big, America's leaders ended up preventing it from becoming good. There is a lesson in that which all governments would do well to learn.

DETROITOSAURUS wrecks. **The Economist**, New York, June 4th, 2009. Disponível em: <www.economist.com>. Acesso em: 8 jun. 2009.