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BUSINESS/FINANCIAL DESK

How Long Can G.M. Tread Water?

By **DANNY HAKIM** (NYT) 1927 words

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Since the Depression, General Motors has reigned as the world's largest automaker and a pillar of American economic might. But now the company is broadly struggling and facing the humbling possibility that it will be displaced by Toyota at the top of the auto industry within a few years.

General Motors, which controlled nearly half the American market as recently as the late 1970's, held about one-quarter in February. Last week, the company said that it would produce 300,000 fewer cars and trucks in North America in the first half of this year, a 10 percent drop from a year ago.

Its European operations have lost money for five consecutive years and rising interest rates are expected to cool its lending division. With its shrinking profits dwarfed by those of Nissan and Toyota, G.M.'s debt is threatened with a downgrade to a junk bond rating, a move that could force it to pay more to borrow money.

The company's financial health is no trivial matter. With 7,600 dealers across the country, its eight brands, from Chevrolet to Cadillac, have long been American icons. The company has operations in 32 states; in Michigan and Ohio, both G.M. and Delphi, its struggling former parts subsidiary, are top 10 employers. G.M. is also the nation's largest private health care payer, giving coverage to 1.1 million Americans. Hundreds of thousands of retirees depend on the company's pension checks.

G.M. might be in better shape than it was when it lost \$23 billion in 1992 and was on the brink of bankruptcy, but many analysts say it will be treading water for years to come and extending economic distress across the industrial heartland around the Great Lakes.

Company executives, while acknowledging that G.M. faces serious problems, say they are confident they can weather any storm. "We've been ahead for 73 years in a row," Rick Wagoner, G.M.'s chief executive, said in response to a question at a January news conference about Toyota's looming presence. "I think the betting is we'll be ahead for the next 73 years."

"Is it a birthright?" he added. "Absolutely not. Could we blow it next year? I doubt it. Could we blow it in 10 years? For sure. We could do anything in 10 years."

Mr. Wagoner declined to be interviewed for this article. With the company's stock down about 50 percent on his watch, his legacy is on the line, as is the company's.

Five years ago, at 47, Mr. Wagoner became G.M.'s youngest chief executive. He was a protégé of John F. Smith Jr., who became chief executive after a boardroom coup in 1992. Mr. Smith pulled the company from record losses to a record profit by 1999.

Mr. Wagoner did not promise to reinvent G.M.

"The state of business at General Motors Corporation is strong," he told shareholders in 2000, adding later that the company's success "gives us a great chance to build off what we're doing."

Today, however, many analysts say G.M. is still unable to solve some of the problems it had in 1992, namely the seemingly unstoppable surge of efficient foreign competitors like Toyota.

The strategy of Mr. Wagoner, now also G.M.'s chairman, has been to continue his predecessor's work of pushing global expansion even as he is now moving to shrink G.M.'s disparate global operations into a single manufacturing, design and engineering organization.

Few industry analysts call him a visionary leader, but many see him as a skilled executive who has held the company

together despite being dealt a difficult hand. Others say G.M. needs a more radical approach to ensure its survival.

"It's not like this tide can't turn," Mr. Wagoner said in January. "It's not going to turn by cheerleading or me convincing you here; it's going to be great products. It's going to be helped if exchange rates get in line with what they should be so companies that don't need to get subsidies aren't getting them."

At 6-foot-4, Mr. Wagoner briefly played college basketball while attending Duke University and remains an avid Blue Devil fan. He has approached his job more like a coach than an authoritarian chief, assembling a management team of prominent industry executives.

Mr. Wagoner is a career G.M. employee who came up through the company's huge finance operations and is not considered one of Detroit's "car guy" executives. Filling that role is Robert A. Lutz, the 73-year-old former Chrysler president Mr. Wagoner hired in 2001 to shake up G.M.'s product development. Mr. Lutz, a former Marine who commutes to work in a copter, commands most of the company's spotlight.

Far from undermining his authority, Mr. Wagoner's willingness to delegate has earned him praise.

"What's remarkable about Rick's leadership is the strength of the team that he has been able to attract," said Mike Jackson, chief executive of AutoNation, the largest G.M. dealer.

Gerald Meyers, a University of Michigan professor and the former head of American Motors, now part of DaimlerChrysler, called Mr. Wagoner "superb," adding that his drive to globalize could not be accomplished quickly.

"That's a long tough road and it takes almost a generation of executive teams to make that happen," he said. The problem, he added, is "no matter how much they are improved, there are a couple guys out there running faster."

Others are less charitable in their assessment. Sean Egan, managing director of the independent debt rating firm Egan Jones, said Mr. Wagoner was performing "miserably," adding that "some drastic action is needed in the very near future to even have a chance of turning around this slow slide to irrelevance."

The prevailing view among financial analysts is that G.M. is not close to bankruptcy because it is still clinging to profitability and has more than \$23 billion in cash in its automotive operations. While it has roughly \$30 billion in debt, those payments are stretched out over decades.

Mr. Egan thinks bankruptcy is a real possibility because, he says, G.M. can burn through large amounts of cash quickly; he does not recommend buying G.M. bonds with maturities of more than two and a half years.

But Craig Hutson, an analyst at another independent bond rating firm, Gimme Credit, thinks G.M. has "the liquidity to withstand even a worst-case draconian scenario."

Mary Ann Keller, a longtime analyst and author, said, "they're careening from one mess to another," adding, "the only thing that could make things better is a major restructuring."

She says that G.M.'s management lacks urgency and cites the fact that G.M. continues to pay more than \$1 billion in annual dividends, as opposed to reinvesting that money in the business. She and other analysts also say G.M.'s recent agreement to pay \$2 billion to extract itself from a soured alliance with Fiat does not reflect well on management. As part of the deal in 2000, Fiat won the right to sell its troubled auto business to G.M. at any time over a period of five years. In the end, G.M. paid \$4.5 billion to begin and end that bargain and largely abandon its partnership.

John Casesa, an analyst at Merrill Lynch, said the Fiat deal "came at a large cost with little benefit."

While sales globally increased last year, in G.M.'s crucial home market they continue to decline even though G.M. spends more on incentives than any other company and is adding rebates, most about \$1,000, on models that have sat on dealer lots for four months. Nearly half of G.M.'s North American production capacity is either idled or being used to produce cars and trucks sold on the cheap to rental car companies, business fleets or employees and their friends and family, according to a recent Morgan Stanley report.

Labor contracts forbid the company to simply close plants to address this stark inefficiency. The company also has to maintain its size so it can generate enough cash to pay for its health care and pension benefits, which cost more than \$1,800 for each vehicle produced in the United States annually. Automakers based in countries with more socialized systems are not similarly burdened.

In recent speeches, Mr. Wagoner has emphasized this problem, stressed the need for tort reform and criticized the Japanese government for intervening in the currency market.

But critics say that many of G.M.'s biggest problems are self-inflicted and that too many of its vehicles lack the verve that once characterized American cars. To them, the revival of G.M.'s Cadillac brand after years of cultural dormancy only demonstrates that the company can do better.

While G.M. has made huge strides on quality surveys by J.D. Power & Associates, the surveys also show that most of its brands lag in appeal. Only three of eight had sales growth last year -- Chevrolet, Cadillac and GMC.

The company has tried advertising gimmicks and brand revivals. G.M. paid to place its new Buick LaCrosse sedan on "Desperate Housewives" and to feature Aerosmith's "Dream On" in LaCrosse commercials, but sales of Buicks still continue to dive.

Saturn, Saab, Pontiac? Revivals for all three are in various stages.

Both G.M. and Ford Motor have made huge bets on sales of large sport utilities and pickup trucks in the United States, a wager that some analysts say is at risk as gas prices rise. G.M. has upped the ante by creating a new brand around Hummer, the least fuel-efficient brand in the industry. Still, G.M. executives say their fortunes will improve considerably in 2006 and 2007 as a new generation of large sport utility vehicles and large pickup trucks hits the market.

In Detroit, the unfortunate measure of success is not which of the Big Three automakers is doing best, but which is doing the least badly. Three years ago, that was clearly G.M., if for no other reason than that Ford and the Chrysler division of DaimlerChrysler were losing billions of dollars. Three years later, Chrysler is on the upswing and Ford has returned to profitability, though it is hardly a picture of health.

One thing Mr. Wagoner is not betting on is a government bailout, given that steel companies and airlines have been left to fend for themselves.

"That has not gone unnoticed by me and therefore motivated us to think about, well, maybe we shouldn't just wait for somebody else to fix this problem for us," he said.

Photos: "Could we blow it next year?" asks Rick Wagoner of G.M. "I doubt it. Could we blow it in 10 years? For sure." Sales at G.M. are down sharply from a year ago. (Photos by Top, Frank Polich/Reuters; bottom, Tim Boyle/Getty Images)(pg. C1)

Chart: "Coming Up Fast"

General Motors remains the world's largest auto company, but Toyota has gained ground steadily in recent years.

Graph shows WORLDWIDE SALES for G.M. and Toyota. (Sources by G.M.; Toyota; Ward's AutoInfoBank)(pg. C1)

Chart: "Few Bright Spots"

Many of General Motors' brands have struggled in recent years. Figures are for sales of cars and light trucks in the United States.

Graphs show sales figures for Buick, GMC, Pontiac, Chevrolet, and Other*

*Cadillac, Oldsmobile, Saturn, Saab and Hummer
(Source by Ward's AutoInfoBank)(pg. C2)

