Toyota's Denouement

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A combination of self-inflicted wounds more than a decade in the making plus a global economic crisis shows us that Toyota Motor Corporation has lost its way. While not completely unexpected, it is still surprising that Toyota could lose its grasp on key fundamentals of its management system. The company's problems and efforts to recover offer many high-value lessons for any manager who is willing to learn.

For those who study and practice Lean management, Toyota Motor Corporation has always been our guiding star, our true north. But what happens when Toyota turns east, or even south, as they have slowly done over the last decade or so?

Toyota has always been the principal Lean practitioner to learn from because they have done such a brilliant job of putting together a wonderful management system based on work done by other people [1] and through the addition of many of their own unique contributions [2] and steady maintenance and improvement. Their non-zero-sum, principle-based, human-centered management system is undoubtedly the best that has been created in modern times. Its practice should be the norm in any organization, not the exception.

Toyota's recent problems originated with Toyota Global Vision 2010 (launched in 2002 and running through 2010), which, among other things, stated an objective to grow and obtain 15% global market share by the early 2010s. This required Toyota to grow at a compound annual growth rate (CAGR) of nearly 7% per year for a decade (staring from a large base). The owners of this plan and the prior one, Toyota 2003 Vision (launched in 1996 and running through 2005), are the past president and chairman of Toyota, Hiroshi Okuda; the past president and current chairman, Fujio Cho; and the past president and current vice chairman, Katsuaki Watanabe.

Toyota's unraveling came soon after its climax of becoming the world's largest automaker. This outcome shows they, too, are human and make the same mistakes that executives in other companies make: growing too large, too fast. Annual growth of 7% or more is challenging for any organization, big or small, when it is done organically (growth through acquisitions, or a combination of organic growth and acquisitions, can lead to 5- or 10-year CAGRs of 15-30%, which is extremely challenging as well). It is almost double Toyota's CAGR of about 4% in the prior decade.

That begs the question of why did Toyota pursue growth (and profitability) so aggressively? What were its reasons for doing so? Was it to establish a global leadership position in environmental technologies? Was it to obtain a more influential seat at the table in negotiations with governments on auto emissions reduction? Was it to improve the stock price and dividend performance after Toyota became listed on the New York Stock Exchange in 1999? Was it to increase corporate value to avoid a hostile takeover in the rapidly consolidating global auto industry circa 1998? Was it to see if they had the capability to rise to their self-imposed challenge? Or was it simply for the sake of growth itself – to be #1?

Whatever the reasons, I would have expected better judgment and less hubris from Toyota leadership. However, I also realize they are not infallible and will succumb to the same decision-making traps [3] as anyone else. You or I could have made the same mistakes – unless we knew how dangerous high growth can be.

Having finally recognized the problem fully, Toyota now has a new president, Akio Toyoda, who is leading a back-to-basics approach to designing, selling, and making automobiles. We will all be watching closely in the coming years and decades to see if Toyota can return to its roots of low volume-high variety vehicles (with increasingly diversified power trains) produced using low cost, demand-driven flow production, or if it will eventually become another General Motors (e.g. continuing commitment to a "full product-lineup strategy" [4] with an arrogant sellers' market perspective). This is a major concern for Toyota's new president, Akio Toyoda, who said in June 2009 that "Toyota might well turn into the next GM in a few years" [5]. Let's hope not, but don't bet against it.

So, in what ways did Toyota unravel as a result of its rapid growth? What is the evidence? Here is a summary of Toyota's problems culled from recently published accounts.

- Allowing engineers to put too much expensive content in vehicles [6].
- Making too many large vehicles with low gas mileage and luxury vehicles (i.e. too many models and wrong model line-up for the times) [6, 7].
- Reduction of part commonality within model platforms [8].
- Forgetting how to profitably produce small vehicles [7] and relying on large and luxury vehicles to achieve aggressive sales volume and profit goals [6, 9].
- Stumbling on quality to achieve growth targets [10].
- Not listening to dealers or customers [7]; focusing on the competition instead of customers [6].
- Generally, blocked information flow internally and externally [6], and lacking speed and responsiveness to problems [6, 7].
- Straying from Taiichi Ohno's buyers' market formula of selling price - cost = profit and instead transitioning to the sellers' market formula of selling price = cost + profit [6, 11], resulting in cars incorrectly priced for their market [4, 6]. Basically, adopting the Lexus pricing model to Toyota's mass-market cars.
- Producing to the company's plan rather than producing to dealer and end-use customer demand [9].
- Reduced internal cooperation between sales and manufacturing resulting in over 100 days of unsold inventory (a reduction in global inventory turns from 12 to 3 from mid-2008 through mid-2009) [9].
- Internal blame-game among Toyota executives in the United States and Japan [6, 12].
- Slow to recognize and respond to reality [6, 13]; e.g. change in market and demand from small cars in China [4].
- Installing expensive manufacturing processes [6, 14], building expensive capacity [6], and then suffering from idle capacity (30%) [6, 11]. Generally, succumbing to economies of scale and becoming volume-driven [15, 16, 17].
- Losing focus on manufacturing – the shop floor, the gemba [11, 18].
- Betting on a winning model (the 2010 Prius) to help save the day [7, 10].
- Toyota falls below Honda in Planning Perspective Inc.'s 2009 supplier working relationship index survey [19], caused by increased emphasis on pressuring suppliers to reduce prices instead of working together to reduce costs.

Wow! It took a global economic crisis to reveal the extent to which Toyota strayed from its roots – and stray it did. From many different directions and for many different reasons, each of the items listed above are inconsistent with The Toyota Way principles of "Continuous Improvement" and "Respect for People" [20].

The critics of Toyota and of Lean management have fully-loaded quivers from which to shoot arrows. This is not a favorable development in terms of our efforts to advance Lean management. In fact, it could turn out to be a major setback. Nevertheless, this is our reality, which we must accept and formulate fact-based responses that acknowledge common imperfections in executive decision-making and honest efforts to recover and improve [21]. Nobody is perfect, not even Toyota senior managers.

The Lean community can lament Toyota’s mis-steps or it can learn from them. The latter is much more valuable, of course, and includes the following:

- Years of practice in Lean management does not inoculate individuals or groups of executives from making bad, expensive decisions.
- Groupthink is a common contagion and can even strike Lean thinkers.
- Growth for the sake of growth is foolish; high growth often leads to distress [22].
- Economies of scale thinking will eventually lead to overcapacity and poor responsiveness to changes in demand.
- The value-creating activities within an enterprise should never be taken for granted.
- It is easy to stop listening to intermediate (i.e. distributors) and end-use customers.
- Generally, the grave perils of serving one’s self instead of one’s customers.

Perhaps the biggest lesson to learn has to do with the basics. Whenever we think we know the basics we become arrogant and then fail to remember and execute the basics. Nobody is so good at whatever they do that they can forget about the basics.

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Notes

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