General motors bailout problem essay sample

Introduction

Founded in 1908, General Motors has been one of the largest corporation and the second largest automaker in the world coming after Toyota. For 77 consecutive years from 1931 to 1908, GM has been a leading automaker and marketer as ranked by the total number of units sold yearly. General motors have also been a leading employer not only in the United States but also in other parts of the world where it operates. However, the company has been seriously affected by the current economic crisis. The Detroit Three, led by General Motors have been a backbone of the United States economy and there eminent collapse in the current economy crisis is likely to have negative impacts on the United State’s economy. However, the problem at GM and in the general United States automotive industry cannot be attributed to the current economic crisis alone. Their problems can be traced to the oil crisis of the 1970s where the government came up with new rules aimed at reducing the rate of fuel consumption. Consequently, General Motors and other American auto makers continued with their fuel guzzling SUVs especially in the 1990s leading to stiff competition from foreign automakers especially Japanese cars which were considered fuel efficient and friendly to the environment. Therefore the problems facing GM do not attribute to economic crisis alone but also due to other issues related to organization culture.

The company has also negotiated payment package with the union which has continued to drain its resources despite its declining revenues. General Motors has consequently lain off million of workers and closed down some of it plants in a bid to reduce the cost of operation. The company has also sought government bailout package which will prevent the company from collapsing. However, the problems faced by GM may not e easily solved by the government bailout package. The company needs to restructure its operation to reflect the current consumer preference in term of fuel efficient cars. In wake of stiff competition from Japanese cars, the company needs to come up with new operational plan that will include re-negotiation of the labor policies to ensure that the company can pay what it can afford. Like what many have argued, it may not take a one sided approach to awaken the giant company. It requires a complete overhaul from the management, coming up with new operation plan, negotiation of labor laws, extensive market research, and in extreme condition, the company may think of merging with other automakers to reduce the cost of operation. Therefore the current government bailout plan may not turn round the company unless there are other extensive changes that will be taken to complement the stimulant package.

General Motors Company

General Motors was founded in the early days of formation of the U. S automotive industry. The company was founded in 1908 in Michigan first as a holding company which was controlled by William Durant. In its early years of the growth, the company made a number of acquisition including Oldsmobile, Reliance Motor Truck Company, and Rapid Motor Vehicles Company all of them in based in Michigan. However, the company soon faced a number of challenges and it collapsed with the collapse of the new auto market. It was after Alfred Sloan took over the leadership of the company that it started its upward growth trend until the 1980s when foreign automakers made their way to the American auto market.

Since the end of the Great Depression, GM had undertaken globalization efforts establishing its operation in most European countries. The company has also expanded its operation to emerging Asian markets like South Korea, and others. General Motors is one of the largest employers in the world although in recent years it has sent home thousands of its employees. Currently, the company has more than 266, 000 employees in the world. It headquarters are located in Renaissance Center in Detroit, Michigan. Although its sales have been reducing drastically, GM produced more than 1. 9 million cars and trucks in 19 countries where its operations are based.

Although it has reduced the number of acquisitions, GM has collaborated with other automakers in the world. It is a major shareholder in GM Daewoo Auto company operation in South Korea. It has collaborated with Suzuki Motor Corp and Isuzu Motors Limited of Japan in production of vehicle parts, power train and others. The company also collaborates with Toyota Corporation and BMW of Germany in areas of advanced auto technology. GM collaborations also include other leading automakers like Shanghai Automotive Industry Corporation, Renault of France, Fiat S. p. A., Ford Motor Company, and others. It has various stakes in different companies in the world which reassert its global influence in the automotive industry.

Apart from directly employment, the company has created a global empire of the supply chain selling its vehicles or its spare pars. The company accessories are sold branded GM Goodwranth and ACDelco which are retailed thorough GM Services which distributes the spare parts to various distributors around the world.

In terms of market size, the largest market is in the United States which has remained one of the leading automotive markets in the world. However, GM also sells a good number of its vehicles in China, Canada, United Kingdom, and Germany. In the early years of development of the automotive industry, most auto manufacturers came up with Financial Services which offered finances to purchase automotives. Today GM still retains a 49% stake in GMAC Financial Services which offered varied services ranging from automotive, residence and other insurance services. GM has also established OnStar which is a subsidiary dealing with vehicle safety, security, and provision of other information which is relevant to use and care of automotive.

With such large number of employees, GM has been keen on it human resource management. However, its efforts to attract qualified workers has brought a lot of financial constrain to the company. GM has negotiated with United Autoworkers which is a union body housing all autoworkers in the United States. Compared to other foreign auto manufacturers, GM pays its employee higher salaries which has been one of the factor leading to its economic downturn. The company has been providing medical care, education, continuous training, health and safety measures, and many others (Loornis, 2006).

The current situation in the GM

The current economic crisis is having a great ramification on various sectors of the economy in the world. However, the American auto industry seems to have been hard hit by the changing economic crisis. Except for the foreign manufactures, the Detroit Three are faced with the threat of bankruptcy (Ikenson, 008).

The problem facing the General Motors and the whole American auto industry is not new and has persisted since the 1980s. Since the end of the Second World War, American auto industry had experienced a dramatic growth expanding to different countries in the world. General Motors and other had engaged in buy outs and mergers in different countries outside the united states. Since the end of the Great Depression, General Motors had remained the leading auto company in the world. The company has emerged on top each consecutive year in the total number of sales. However, the 1973 oil crisis came with new fate for the American auto makers and they have not been able to come out of that shock (Jones, 2006).

The problems facing GM can be summarized into five major problems including;

1. Financial statements which shows the company is making staggering net losses
2. A criminal probe that is looking into the relationship for the company with its suppliers
3. Higher labor costs such that the company has considered paying its employees $140, 000 to resign coupled with pressure from UAW which

has refused to relent on its labor and pension agreements with the company.

4. Negotiations with the company seeking to sell its stake in GMAC, which one of its profitable engine
5. Declining GM share prices which have decreased to a third of their net value after every 12 months

Increased competition from the foreign car makers has continuously eroded GM market share leading to loss of sales. This has been coupled with other in labor management issues where the company has continued to pay its worker higher salaries than the standard labor market prices. While most businesses have been promising in America, the results posted by GM have been quite disappointing. Last year, revenues fell from $45. 77 billions up from $47. 83 billion a year earlier. This considered an improvement because massive layoff and closing of its unprofitable plants which has helped to cut back the cost of operation and production (Loornis, 2006). The financial performance of the company has been deteriorating each and every day with major credit companies indicated that there is a probability of dropping GM bonds to junk status.

The problems with GM have been gathering steam since 1970s. However, the turn of the new millennium spelt a new recession era for the company. In 2004, GM reported its worst loss in 13 years when it announced a net loss of more than $1. 10 billion which was equivalent to $1. 95 for every share. The company reported that 98% of their costs were tied to fixed cost with expenses on management and workers health care and pension cost also contributing to a large part of its revenue loss (GM, 2008). Since the company negotiated for new pension schemes, it has continued to pay higher pension and health care cost for its employees and today, GM is paying pension for its retirees who are over 100 years old. The downward spiral has continued for the company. In the first quarter of 2005, GMA announced that it had made a loss of $1. 1 billion with the increased healthcare cost and poor sales hampering its yearly performance (Schneider, 2005). A century ago, GM sold half of all cars in American market but today, their market share has been reduced to an embarrassing 26% which is about a quarter of all cars sold in the country.

The solution to the problems of GM has taken different turns. Most important, GM has resulted to layoff its workers and closing down its plants. Apart from year of job cuts and closure of plants, GM announced that it would cut further 47, 000 jobs from its current 244, 000 jobs. The action further includes closing down five more pants which means the company is to be left with just 33 plants in North America and at the same time reducing its line up of brands to just four including Chevrolet, Cadillac, GMC, and Buick. The company ahs also announced that it has engaged with United Automobile Workers Union to negotiate for terms that would reduce its overall expenses on employees (Corrigan, 2008).

Faced with the threat of bankruptcy, GM and other automakers have sought for government intervention in form of a rescue package which would stimulate their growth. The automotive industry has been one of the backbones of the United States economy and the closure of GM would lead of millions of direct and indirect employment. This has prompted the government to prepare a financial bailout plan which will see the company get stimulant package in form of loans from the federal government. GM needs a $25 billion bailout to get through the recession period. This would be expended in financing closure of some plants and also restructuring of some of its operations. However, it is to be reckoned that GM has a $48 billion debt and unless this debt is written off, the stimulus package may not go a long way to reduce the overall cost of operation.

Why GM is in the current financial situation

There are different factors which can be singled out as the main factor contributing to the fall of the Detroit Big three including General Motors. There is no single factor that can be identified as the main cause of woes facing the General Motors but rather different factors have conspired to bring the industry to its current situation (Constantini, 2009).

For GM, it ahs been a recipe of external and internal factors which have lead to its current situation. In the external environment there has been an economic recession which has decreased consumer purchasing powers. This is a factor beyond the control of the company. However, a grate deal of the problems facing GM and other automakers can be attributed to internal structure and organization. For example, while GM and other American automakers have been making huge losses, foreign automakers based in the United States have continued to show impressive growth. This means that there are more than external factors that are contributing to the eventual fall of General motors. In order to understand the genesis of problem facing General Motors, it is important to look at each and every factor (Jones, 2006).

The genesis of the problem facing GM can be traced to 1973 oil crisis. As America suffered from the oil crisis, the government enacted the Clean Air Act 1970 in an effort to increase efficiency in fuel usage and decrease the reliance of the American economy on foreign oil. Although this act had good intentions, it became an instant obstacle for GM and other American automakers since their vehicles did not meet the provision of the act. This act also opened way for the foreign automaker especially japans companies which were producing more fuel efficient cars (Espo, 2008).

The entry of the foreign care maker increased the level of competition in the market. For example in 1970s, the Honda Motor Company which had just been introduced in the market recorded a highest sales volume while GM decreased its total sales. In the whole decade, Japanese automakers sold an average of 2. 5 million car units while the United States automakers decreased their overall unit sales. Japanese automakers sold one in every four cars in the United States market.

GM automakers have continued to lose their market share since 1980s. With increased competition, GM channeled a lot of resource to research and development eventually leading to the development of SUVs. Although SUVs recorded increased sales in 1990s, they have since then been abandoned due to the increasing consumer environmental awareness. For example in 1970s, GM held a sizable share of the U. S auto market. Today, this has declined to less than a quarter of the market share. In 1998, American automakers held 70% of the U. S auto market which as reduced to less than 53% in 2008. As a result of the market loss, GM has been operating before the capacity. In 2005, GM was operating at less than 85% which is considerably lower compared to what its foreign competitors were operating at. This has consequently forced the company to lay off a large number of its employees and close down some of the plants which were operating below their capacity.

Another problem facing General Motors is its agreement with the union representatives. As the labor movement gained momentum in the United States, there was increased negotiation between union representatives and GM which saw the company enter into an agreement to provide workers with higher salaries than industrial standards (Isidore, 2006). This agreement has seen GM struggle to maintain a higher salary to its employees even when its revenues have continued to decrease. This has had an effect on the overall competitiveness of the company since is production cost pushed higher and higher. For example in 2005, industry survey found out that Toyota, which has overtaken GM as leading automaker in the world had a labor productive advantage of more than $250 compared to $500 per every vehicle produced in GM. This means that the company has been using a lot of its revenue on labor instead of investing in research and development. In 1955, the then chairman of GM Charlie Wilson said that what was good for GM was good for American too. This is true as can be reflected today in the situation GM is facing. Analysts have been perplexed by GM obligation to take care of its ex-employee until they die which means it is guaranteeing life to its ex-employees while it cannot guarantee job to its current workers.

Unlike other car manufacturers, GM has a problem that continues to eat away its profit. This is specifically its legacy cost. The problems of extra costs have been gathering steam in the company in 1950s when it negotiated for pension and health care for its workers. Before the current financial turndown, GM was said to be spending more than $5. 2 billion in health care cost for 1. 1 million people, which was equal to $4, 727 for every person every years. This means that on health care cost, GM granted another $675 per car for pension costs. In 2007, it was estimated that the total wage and fringe benefits for its worker were about $71. This was comparatively higher compared to Toyotas $47 for every employee. Since 2005, it is estimated that GM had suffered a massive $31 billion in cash drain which is attributed to expense on its workers.

GM also suffered from deterioration of consumer confidence on its vehicles. After the oil crisis of the 1970s, Americans embraced the idea of using fuel efficient cars as the cost of fuel shot up. Although General Motors was producing the main brands in the market, Japanese cars started making an inroad into the American market and consumers were having a wide range to choose from (GM, 2008). General motors found it difficult to meet the criteria set by the new Clean Air Act and consumers started losing their trust in the company.

Towards the end of the 1980s, General Motors found out that it could compete with the foreign automakers by counteracting foreign fuel efficient cars with Sport Utility Vehicles. In 1990s, General Motors and other American automakers produced SUVs which were initially doing well in the market (Corrigan, 2008).

However, there was increase consumer environmental awareness through which consumer organizations increased consumer awareness about the effect of the SUVs on the environment. From 1990, GM continued to experience a decreased demand of its SUVs and despite coming up with new brands, the company was still losing a sizable share of its market. Even when the company understood the consumer demand, it failed to respond to the market demands (Constantini, 2009). When the consumers were demanding for fuel efficient cars, GM continued producing SUVs which were not required in the market.

Therefore we the main factors that have led GM to its current financial situation are quite complex and interrelated. There are external factors which were out of control of the company conspired with internal factors to finally plunge the company in the worst financial crisis for decades. For example the Clean Air Act of 1970 affected the technical capacity of the GM vehicles to withstand new rules. In the ensuing technological restructuring, the company started producing SUVs instead of responding to consumer demands for fuel efficient and environmental friendly cars. Consequently, GM continued to lose its market share to foreign car makers like Japanese cars. Apart from the marketing issues, GM has also been entangled in salary tussle with its workers after negotiating union representatives for higher wages and benefits which has been considered above the normal market labor prices. The company has continued to pay higher wages to its workers despite its economic problems while the union has refused to back down and re-negotiate new payment terms.

What could have been done to avert the situation?

As has been identified, the problems facing GM are multifaceted and they could have been averted earlier had the company taken drastic measures to reduce its legacy cost. Most of these problems could have been dealt with easily the company has organized its management (GM, 2008).

In 1970s, GM was faced with problems of meeting the standards that had bee laid down by the Clean Air Act.   The company understood very well that it had to take stringent measures to improve its technical aspects to make its cars more fuel efficient. While Japanese cars achieved a higher mileage per gallon, GM reversed to producing SUVs which had a lower mileage per gallon. GM would have averted the current loss of market by responding to market demand and produce automobiles which met the market demand.

GM insensitivity to changing nature of consumer awareness lost its touch with consumer market. Towards the end of the last century, there have been increased consumer concerns regarding the effect continued use of fossil fuel and the effects it was having on the environment (Constantini, 2009). GM had led the way in production of electric cars GM EV1 which had been considered a new level of development in the automobile market. GM EV1 had received consent from several consumers who had rented the car and more people were placing the request. However, conspiracy between GM, oil companies, and other led to the mysterious destruction of these cars. Today it’s still not known what happened to the electric car although currently GM is preparing to launch its electric car brand. It would have done this more than ten years ago and today it could still be the leading automaker and supplier in the world. The electric car saga, SUVs, and other technical problems with GM cars dwindled consumer confidence in the company while there was little that was done to redeem that image.

GM legacy costs have weighed heavily on the eventual fall of the company. The negotiations made between the company and UAW has been validated even when the company has been faced with economic crisis. When GM foresaw possible problems with financial performance, it would have taken drastic measures to either lay down some of its workers or renegotiate new terms with the worker. In other words GM did not wake up to the reality that it finances were not in order and therefore restructure its operation. The company did not have to wait until it was plunged with threats of bankruptcy like it is currently so that it would restructure its operation. Since the entry of the Japanese and other foreign automakers in the US market, there has been a drastic change in the market and GM should have read the writings on the wall. For example the company did not respond to its increased higher wages while it first competitor, Toyota, was operating at a lower labor cost (Selley, 2008).

Therefore, timely and prompt response to the changing nature of the industry and consumer demand market could have done a lot to avert the crisis faced by GM. Although it was difficult to influence the external factors like receding economy, GM would have responded by restructuring its internal operations in a way that it mitigated the overall effect of external factors (GM, 2008). The case of GM clearly shows the problem that can be caused by mediocre management and negotiation with labor unions that overprices the labor. For example if the management had taken an immediate step, it would have renegotiated low labor prices which would have helped the company to adjust its operations to its declining revenues. This step would have save thousands of jobs that have been lost through closing down of plants.

What should be done to turn round the company?

It appears like American economists have been obsessed with the idea that a bailout package would work for GM and other automakers. However, their problems are more complex such than a mere financial bailout may not work at all. There are internal and external factors that need to be addressed before the current crisis is fixed.

In the case of GM, there is already an $80 billion debt that has to be settled. Although the package may stabilize the operation of the company, this debt and its legacy labor and management cost may have severe effects on its future. The problems in GM therefore lay with the way its internal management and the organization culture will be changed, in order to adapt to the changing nature of automobile market. For example when the executive of the Detroit big three came to Washington to request for the bailout package, they all came in private jest. It is on record that the chief executives of Detroit big used a $20, 000 flight while there was an alternative of a $500 flight. GM also comes to record as owning a fleet of fuel guzzling luxurious flights which are used by its executives which add to their overall cost. This clearly indicates that even in time of crisis, these automakers have not responded to the situation are still operating in the lavish lifestyle they have been used to. It is also a clear indication that there is need to change the organization culture of GM (GM, 2008).

The most important step towards bringing GM back to its feet would therefore entail restructuring the internal operation and management. The current management which has not been sensitive to the plight of the compo any should be sent packing and instead hire competitive managers who can carry out full restructuring of the company. This would give the company a new start which addresses its main problems (Constantini, 2009).

GM should also reconsider mandatory negotiation with the UAW in order to reduce its financial obligation to its workers. Although it is ethically correct for the company to take care of its employees, it is ethically wrong to continue paying higher wages than other companies operating in the same industry and to make the matter worse when the company itself is not generating enough revenues to cover wages and salaries (Isidore, 2006). New labor agreement would put the company in a position to reduce the cost of operation.

Internal restructuring should also see GM hire new technical staff that can put the company to another level. Although GM has promised that by 2010 it would be producing electric cars, there are still doubts that its electric brand Chevy Volt would hit the market by the time. First this calls for availing of more funds which are not available. Unless the government increases its bailout package, the company may not be able to achieve this dream. However, there is an option of going back to its GM EV1 which many believe was destroyed as a result of conspiracy with oil industries. This would assist GM to produce cars which are responding to the consumer market demand (Corrigan, 2008).

Conclusion

Since it was established in 1908, GM has been a leading player in the automotive industry. For 77 consecutive years, GM has been the leading automobile producer in the world.   However, the company has been faced by various problems since the oil crisis of 1970s. The enactment of the Clean Air Act brought about a lot of competition in the US automobile market which show decreased sales and loss of market share for the company. Apart form declining market share, GM entered into agreement with UAW which has seen the company pay higher labor cost and   pension and wages increasing its cost of operation. GM also failed to respond to the changing consumer demand by producing SUVs when consumers were demanding for more fuel efficient cars. Currently GM is faced by the worst financial crisis to an extent of being declare bankruptcy. The company suffered from declining sales leading to loss of billion of dollars every year. The company has sought $25 billion financial bailout from the government. However, this may not have an effect on the current financial crisis unless the company adapts more measures by restructuring its operation to the current situation in the market.

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