

GAO: ADVANCED HYBRIDS MAY NOT BE BEST WAY FOR GM TO REBOUND

✖ There's a lot of good information (and bleak news) in this GAO report on GM's and Chrysler's efforts to become viable again—including this picture that shows the key relationships in the industry and the credit that underlies each of those relationships.

But I wanted to point to GAO's explanation of something I've often argued—to much skepticism here and elsewhere. Investing heavily in new technologies like hybrids may hurt GM's efforts (certainly in the short term) to become more viable.

In a section addressing the things that GM and Chrysler aren't doing to achieve viability, GAO warns that advanced technology vehicles don't have the return on investment GM needs to become profitable again.

Several panelists noted that not only is developing advanced technology vehicles expensive, but also the return on the investment in those vehicles can be low because the initial demand for new technologies can be slow to develop. For example, the Toyota Prius was on the market for 10 years before reaching 1 million units sold. According to our panel, given the high development costs and low initial demand, especially if gasoline prices remain relatively low, these new vehicles are not likely to generate a profit for several years. Thus, changing the companies' product mix to include more advanced technology vehicles may not be the best way to improve the financial bottom line in the short term. Furthermore, at least one

panelist questioned whether the necessary energy infrastructure, such as electrical outlets to charge batteries, will be available to support these new technologies. Without adequate infrastructure, consumers will be reluctant to purchase these new advanced technology vehicles. GM officials acknowledged these challenges but indicated that the company decided to continue investing in advanced technologies even during the current financial crisis because they need this technology in their fleet to help meet federal fuel economy standards in the future. In addition, GM officials said they are planning for higher oil prices than current futures market expectations, in order to make GM's plan more robust against oil price volatility. [my emphasis]

Now, frankly GM is right to remain committed to the Volt even given such challenges. The Prius took a long time to become profitable, but the halo effect Prius has had on Toyota's overall brand is one of the main reasons people believe a company that invested heavily, strategically, in the Tundra is all about gas efficiency.

But I wanted to point out that even GAO presents GM's focus on things like the Volt as a challenge to returning to profitability, not the primary means to do so.