

What's Vital Is Not to Be Content with Present Work

– Toyota to Accelerate Development of Hybrid Cars –

Interviewer: Okamura Yasushi

Toyota Motor Corp. is rapidly expanding automobile production and sales in various parts of the world, threatening to replace General Motors Corp. of the United States as the world's largest automaker. In FY 2005 through March 31, 2006, Toyota's consolidated sales are expected to reach ¥20 trillion for the first time ever, with its group net profit rewriting a record for the fourth straight year. Toyota's brisk earnings are in sharp contrast with those of slump-hit General Motors or Ford Motor Co. also of the United States. Are there any blind spots in Toyota's management? Toyota President Watanabe Katsuaki discusses its business strategy and the challenges faced by the No.1 Japanese automaker.



The Toyota group's motor vehicle production will likely reach the 10 million mark in 2008 under the current pace of increase.

Watanabe: I think the fact is that there can be such a figure according to calculations by people in the media community. We have in-house projections for production through 2010 but they are internal target figures used as data for discussions on the challenges facing us and the measures to be taken. They should not be published. At present, Toyota's annual production capacity and sales are reaching the 9 million level. But this level could turn much bigger should we boost plant productivity, let employees work on holidays or do more overtime work, and increase the workforce. In this sense, our calculations may be used to suggest the possibility of Toyota achieving the 10 million mark in 2008. Of course, we as the management side have plans based on various scenarios.

One of Toyota's advantages is the low-pollution hybrid car strategy. When will Toyota put a next-generation hybrid model on the market?

Watanabe: It is in the offing but still not clear. A hybrid car is made up of many key parts such as batteries, inverters and motors. These parts must be developed simultaneously according to timetables. But development of these key parts has not yet entered the final



stage. We have a goal to sell 1 million hybrid cars annually in the early 2010s but want to achieve the target even earlier, probably before the start of 2010. We will put the next-generation hybrid car on the market before 2010 and will in parallel increase the number of models which will have hybrid varieties. To help achieve those targets, we are pinning high hopes on the new midsize sedan Camry (we will begin production in the United States later this year). We will sell both conventional gasoline-powered and hybrid types of the Camry. Although we have currently no concrete idea about the size of the market for the new Camry in the United States, we would like to step up our marketing and service efforts.

Production Efficiency Can Still Be Improved

As a challenge facing Toyota, some people point out that company employees, priding themselves on being on a winning team, are "bloated."

Watanabe: I myself do not think that we are on the winning side, but frankly speaking, I share the concern that there have emerged some such aspects as you have pointed out. When I inspected in-house educational facilities on Toyota-style production, I felt that there were still insufficient points in the promotion of production efficiency and many issues to be dealt with. We must manufacture products while keeping pace with progress in technology and design. If we are satisfied with the present state and seek to maintain it, it would be the beginning of decline. It is very important for us not to be content with the present state of our work in every field ranging from development and production to personnel affairs, accounting and procurement of parts and materials. If there is a problem at the production level, it may be caused by a defect in design or production facilities. To cope with the problem, one section may transmit such information on defects to another group.

Anyway, the point is to see if we can identify problems. We need to continue efforts to find out problems, expose them, look into their causes and make improvements. If you look for a benchmark, there is always someone doing better. This is true for any business corporation. We are not at such a level as to say, "Toyota is No.1." We have no time to talk big. You can understand this if you visit job sites. We must improve quality, not the number of vehicles, which is a mere result. Since assuming the presidency of Toyota, I have proposed to produce "dream vehicles," free of pollution and accidents.

Regrettably, these vehicles have not yet been completed. Neither exhaust gas nor road accidents have been eliminated. We would lose the competition if we are complacent with such conditions. Toyota's mission is to make our business beneficial to everybody in society. Are we performing duties in compliance with such a mission? Are we doing good for the world around us? A little thought shows that there are still many things to do. I must convey this to all the employees of Toyota throughout the world.

How do you cope with problems associated with the overstretched logistics line, such as a shortage of human resources, resulting from Toyota's rapid global expansion?

Watanabe: Amid the rapid global expansion, it is physically difficult for the Toyota style of production, which has been developed over several decades in Japan, to take root at an early date in such regions as India and Brazil.



Toyota completely redesigned the Camry and released the Camry G "Dignis Edition" in January

Therefore, we have extended various types of support. For example, those of us who are well versed in the Toyota style have visited such regions to work together or local people have been invited to Japan to learn here. There are many places in the world that require such assistance. In fact, Toyota's logistics line has overstretched as a natural consequence. The question is whether we can uncover the problems resulting from the overextended logistics line. A collapse will be the result if problems cannot be identified.

The other day, I received a report on problems concerning an affiliate in South Africa. Fortunately, people there have sorted out the problems in a proper way, categorizing them into one group which can be solved by themselves, another group which can be solved upon support from the headquarters, and a third which cannot be resolved without full assistance from the headquarters. I can feel secure to know that proper measures have been taken to solve problems. Every affiliated corpo-

ration abroad must assess its own capabilities by itself and check if proper measures are being taken in a steady manner. Whether such action can be taken swiftly is up to each affiliate's maturity and the degree of urgency of the problems. It is important to look closely at these aspects and judge whether Toyota's management resources are effectively allocated. Our logistics line is overstretched, indeed, but what is important is whether measures are taken steadily, even though they are not perfect. I can say more than half of a problem is settled if the problem is identified.

GM's High Potential

General Motors faces a serious management crisis. Do you think GM can come back?

Watanabe: I do not know if "comeback" is the right word. But I think GM possesses very high potential ability.

Do you have any support plans for GM – for example, a takeover of New United Motor Manufacturing, Inc. (NUMMI), the joint venture between Toyota and GM, or purchases of GM's equity stakes in Japanese automakers?

Watanabe: Nothing at all. We have received no such inquiries from GM about NUMMI.

Several US states including Michigan are actively inviting Toyota to locate production footholds.

Watanabe: I met Michigan Governor Jennifer Granholm when she came to Japan last year to attend the events of EXPO 2005 in Aichi Prefecture. She offered us thanks for establishing a technological development center in Michigan and in fact asked us to establish a production base. We have not conducted in-house discussions on where to locate a new plant. As someone at Toyota says that we might set up a new plant in the future, you have seen media reports about its feasible location. It is true that Toyota has been invited from the US side to locate a plant, but we will not launch studies immediately. We are too busy with ongoing expansion plans in the United States – plants in the US State of Texas, Canada and Mexico, and also Fuji Heavy Industries Ltd.'s plant in the State of Indiana.

How do you see the mission of production bases in Japan?

Watanabe: Toyota has production bases not only in Aichi Prefecture (where it is headquartered) but in Hokkaido, Iwate, Miyagi and Fukuoka prefectures. All of them are very important. For example, a Toyota group member's assembly plant in Iwate is boosting production, undertaking exports as a key production base of small vehicles, and transmitting information globally. All the domestic plants in Japan are performing their respective significant roles. Therefore,

we must promote our manufacturing business in cooperation with people in the local communities. Even in Japan it is important for our business to take root in the region as is the case with the rest of the world. If Toyota becomes a company attracting affection and popularity from local people, it will, I think, lead to a boost in the number of Toyota's customers.

How do you see the US pickup truck market showing slower sales?

Watanabe: Among pickup trucks, sales of larger ones are currently affected by a rise in crude oil prices. But I think the US pickup market is big if the country's vast territory and motoring conditions are taken into account. I would like to secure a certain market share for Toyota. If more fuel-efficient models are released, the market can expand. Therefore, product development is necessary. I have instructed our technical section to develop a hybrid-type pickup which can be introduced to the US market. It may take some time to actually equip pickups with a hybrid power system, but basically it is larger models that should be powered by a hybrid system.

Hyundai Is Toyota's Rival

I would like to ask about your rivals and partners. People say Toyota currently cares about Hyundai Motor Co. of South Korea the most. How do you think?

Watanabe: I did say I feel a threat from Hyundai Motor in a speech at an anniversary party held the other day by the Toyota workers' union. I have seen a disassembled Hyundai car and had a test run. It is a good car. I wonder why Hyundai can set such a low price. A low labor cost may be one of the reasons. The ratio of labor costs will rise if we hold down investment and promote our business globally. In other words, a

business company with lower labor costs can gain stronger international competitiveness if it does not mechanize production and puts more weight on manual labor. Makers in China, South Korea and developing countries are advantageous in this regard. Japan's labor costs are high. Toyota's labor costs are also high, but the workers' union understands this.

I have never seen Hyundai's factories. To tell you my guess based on hearsay, Hyundai has a check gate at the end of an assembly line to secure the quality of products and prevent the release of defective products. Toyota thinks that perfect products must be manufactured in the production process and that establishment of many inspection gates is not good in principle. The two companies differ in thoughts. Hyundai holds the idea of eliminating defective products at the final gate to maintain quality. This is possible if you have more manpower. From the viewpoint of labor productivity, however, product quality should be maintained in the manufacturing process after all. I think every worker should have the sense of professionalism and play a leading role to produce perfect goods in his own workplace. This is desirable to raise employees' morale and will to work.

Corporations Need to Build Their Own Characters

Toyota is scheduled to release in May its earnings results for the business year through March 31, 2006. What are the present earnings prospects?

Watanabe: The yen's value against the US dollar is declining. Regardless of our management efforts, the foreign exchange rate is a special wind for corporate management. The yen's decline will no doubt affect Toyota's earnings favorably. There is no change in our

plan to post more than the ¥1 trillion level in group net profit for the third straight business year. In terms of costs, we are constantly considering how to reduce both fixed and variable costs. I feel these cost-cutting efforts are producing results gradually, though not immediately. Anyway, however, it will be the foreign exchange level that most directly affects our earnings.

How do you see the slow sales in Japan of Toyota's luxury Lexus brand cars, which went on sale in the home country for the first time in August 2005?

Watanabe: We are greatly satisfied with the fact that we have achieved our target for establishing an integrated system to develop, produce and sell a premium-brand model and offer after-sales services as well. In fact, we did achieve the original target to build an integrated system of not only producing luxury cars but also giving customers sufficient information and services. We must use the results to develop a new model. It is true that the actual sales results of the Lexus so far cannot be called perfect, but we would like to learn lessons fully from the experience and release the Lexus LS model (which will be put on the market this fall as Toyota's flagship sedan). We plan to review our development system, quality and design at a certain point. We do not care about the sales figures so much. We have had no

intention from the very start to react nervously to the sales volume. Toyota won orders for 13,000 Lexus cars in the four months after its release. I think it is an acceptable result, isn't it? We could not achieve the initial sales target of 20,000 vehicles by the end of 2005 but it was a wishful hope harbored at the start of the sales. We have never got hung up on it. We might have been too optimistic because effectively there are only two models available in the Lexus series. What is important is not the number of vehicles sold but the features and quality of each model.

Corporate ethics are under scrutiny following the Securities and Exchange Law violations by Internet portal operator Livedoor Co. and the falsifications of earthquake-resistance data for condominiums.

Watanabe: Compliance with laws and assumption of corporate social responsibility are most basic matters and preconditions for management and corporate activities. Corporations are given the status of judicial personality, and their character-building efforts are very important as is the case for human being. Compliance is the basic point. Each employee of a corporation must act in accordance with the code of conduct, and this will help cement the company's foundation. Compliance must be thoroughly pursued by every employee. In Toyota's case, compliance must be

further strengthened, I think, because of its position as an automaker which asks each customer to buy its product. It is important for Toyota's business units around the world to take firm root in their countries or regions and acquire "citizenship" there as we are active not only in Japan but in the rest of the world. I would like to see every Toyota unit become a good corporate citizen.

Toyota Wants to Win F1 Race at Any Cost

The 2006 F1 world championship series will soon kick off. What is Toyota's target in the series?

Watanabe: This is the 50th year for Toyota to compete in the Formula One (F1) series and I have told people in charge to win this year at any cost and to stand at the center of the podium.

What is the prospect of hosting the F1 series at the Fuji Speedway in Shizuoka Prefecture which is operated by Toyota ?

Watanabe: It is up to F1's governing body, Federation Internationale de l'Automobile (FIA), to decide. We are hopeful of beginning to host the F1 series in 2007. I have heard reports that FIA is willing to allow us to host the series. But I have never heard that it is a final decision by FIA. It is not clear how a Fuji Speedway series will be related to the Suzuka Circuit in Mie Prefecture which has already hosted such races. **J.S.**

Editor's note: After the interview, it was announced on March 24 that the Japanese Grand Prix race will be staged at the Fuji Speedway as part of the F1 series in October 2007.

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Toyota's growth strategy

The pillars of Toyota's strategy include capturing emerging markets, reducing costs and strengthening environmental technologies. Toyota is establishing production bases in Asian countries and Russia whose car markets are expected to grow in the future. In the low-pollution hybrid car field, Toyota is promoting development of the next generation of the Prius model. Looking several years ahead and making strategic moves, Toyota is set to achieve further growth. Its management target of acquiring a 15% share of the global market in the early 2010s is becoming a possible reality. However, Toyota sees sagging sales and slowing profitability in its home territory, Japan. This is one of the challenges faced by Toyota, which needs to take some measures at an early date to prop up its domestic business.