What's Volkswagen Up To?

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By Kevin Meyer

Half a year ago Bill made an interesting prediction on the future of Volkswagen that made several of us wonder what he might have been smoking. But once again, he may have been prescient.

I have been known to make a fairly radical prognostication from time to time and I will make one now - within few years Volkswagen will be increasing their lead over the rest, gobbling up Toyota and Ford market share, and they will emerge as the dominant auto maker of the next decade by a wide margin.

His rationale was simple: a commitment to long term excellence and strategic objectives even at the expense of short term returns - a concept rarely found in large especially public companies.

"Starting next year, VW will introduce a so-called "long term bonus" plan, in which managers will be rewarded according to customer and employee satisfaction, as well as their achievements in sales and the company's rate of return. In addition, VW will no longer offer stock options." This according to Deutsche-Welle a few days ago. The article goes on to state that bonuses will be based on results in those areas over four years, rather than yearly or even quarterly stock values. Said VW Director of Human Resources Horst Neumann, "We want there to be a close relationship between bonuses and strategic objectives."

Fancy that - tying executive compensation to long term accomplishment of strategic objectives, including customer and employee satisfaction instead of having it driven solely on the basis of how much money can flow into an investor's pocket in the next couple of months.

In one fell swoop, Volkswagen will be changing the scope of their management thinking, and taking it to a level most cannot fathom.

So today we hear about some of Volkswagen's strategy in an article discussing the challenges still facing GM.

Like awarding one little league team five outs per inning and six strikes per batter, then doing a victory dance because they have a good inning, President Obama applauded the "success" of his GM bailout in a visit to Detroit last week. As much as GM benefited from being able to shed debts and other expensive obligations in a government-financed bankruptcy, the real test will be whether GM can go forward and adapt successfully to a relentlessly competitive market.

GM still has to contend with the United Auto Workers (UAW), a government-orchestrated *labor monopoly that its foreign competitors carefully avoid. It still has to contend with fuel-economy rules purposely tweaked by Congress to prevent GM from sourcing small car production offshore in non-UAW factories. It also still has to contend with the ambitions of powerful competitors seeking to survive and expand in the U.S market—the latest being Volkswagen.*

So what is VW up to?

Chief Martin Winterkorn has trumpeted a goal of becoming the world's largest car maker by volume—an aim suddenly plausible for two reasons. VW gets most of its sales in Germany, China and Brazil, where generous scrappage and stimulus subsidies helped Volkswagen continue to grow even through the subprime abyss.

That's an interesting one - a focus on "being the biggest" was a major factor behind the downfall of GM, and later the stumbles by Toyota. Biggest in terms of sales - which is not necessarily volume - is meaningless. It's value, translated into bottom line, that means something. Is VW pushing to be the "largest" just for the sake of being the largest, or are they predicting they'll be the largest by capitalizing on a solid fundamental strategy?

Secondly, VW is a famous has-been in the U.S, still the world's most important market, with high brand-recognition, meager sales, and nowhere to go but up. Thus, while GM and Toyota have been closing and consolidating U.S. plants, Volkswagen is pressing ahead with a $1 billion new factory to open in Chattanooga next year.

Volkswagen learned at least one thing during its plummet from the heights as the dominant U.S. import brand in the 1960s. It was the first to build a large, wholly-owned U.S. assembly plant. That now-defunct plant, in Pennsylvania, was UAW-staffed and had been open only six months when it faced its first strike in 1979. Taking a leaf from its successors, which includes everybody from Mercedes to [BMW, Honda, Toyota, Hyundai] Kia, VW's new plant in Tennessee will be nonunion.

While competitors strive for a "world car" approach, VW is focusing on more market-specific designs aimed especially at mainstream U.S. tastes. An early down payment is the new Jetta, significantly bigger and boatier than its predecessor, and priced about $1,700 less.

Again, an interesting distinction. Common-design "world cars" can create some efficiencies in terms of design, testing, and manufacturing flexibility - but once again the game is really about delivering value to the customer. Design and functionality value does seem to be converging among different global demographics - smaller vehicles with higher efficiency - but differences remain. Where is the value point?

VW's big bet is on the table. For all of Mr. Obama's happy talk in Detroit, the car wars aren't *over. The relentless pressure of overcapacity is not cured.*

That final statement is critical - is VW working toward a long-term value growth strategy, or are they being sucked into the siren call of being the "largest"... whether it's profitable or not? Time will tell.