Asian Corporate Finance and Business Strategy

Japan, Nissan and the Ghosn Revolution

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Introduction

Workers at a Nissan car dealership in Mie Prefecture were nervous as they prepared for a visit from their new CEO in the fall of 2000. The dealership—in a suburb of the industrial city of Nagoya, sometimes referred to as the Detroit of Japan in the heart of Japan’s manufacturing rust belt—was suffering. The malaise of the Japanese economy had hit blue-collar, working-class communities such as this one especially hard, and the withering fortunes of Nissan, once prized as one of Japan’s premier manufacturers, weren’t helping.

Salesmen at the dealership had a lot of complaints. Nissan management didn’t have a coherent marketing message, so the salesmen didn’t exactly know what kind of image Nissan was trying to sell these days on the rare days when they had any customers. Image wasn’t everything, but it mattered. As one salesman muttered while giving a visitor a quick tour of the showroom floor: “Our cars are boring. Who would want to buy them?” The mechanics weren’t happy, either. They were getting a number of complaints from customers about delays in getting cars fixed, and they themselves were frustrated because parts were hard to order. Nobody listened to their complaints. The manager of the dealership knew things were a mess and was scared that the new CEO was coming to town to shut him down. This new CEO hadn’t earned the nickname “Le Cost Cutter” for nothing. The year before, in a breathtaking press conference, he had announced a corporate restructuring that journalists and analysts compared to Hiroshima because of the scale of destruction on the drawing board.

The 100 or so employees were nervous for all these reasons. But there was something else: This new CEO wasn’t one of them—he wasn’t Japanese. Carlos Ghosn (it rhymes with bone) is a half-Lebanese, half-Brazilian executive imported from Renault when the French carmaker took effective control of Nissan six months before. At 46, he was younger by two decades than the Nissan executives who nominally were his bosses. Ghosn didn’t speak the language, didn’t know the customs and in one short year had managed to challenge just about every convention of doing business in Japan. “I do not want to intentionally offend people, but I am more concerned about making Nissan profitable again than being culturally sensitive,” Ghosn had said. He wasn’t going to lose any sleep over the protocol of tea ceremonies or the appropriate way to bow.

His slash-and-burn style had worked at Renault and at Michelin before that, and his brand of hard-to-swallow medicine looked like just what the doctor had ordered for Nissan. But could it work in Japan? This is a society famous for its insularity and its “allergy” to change. A television drama at the time chronicled the impact of a brash American executive taking over a fictitious Japanese company. The popular media was filled with harbingers of the gloom and doom of a coming gaijin invasion. In the personage of Carlos Ghosn, this media creation—a horror story to the Japanese—had come to life.

The employees, dutifully polite and courteous, betrayed none of their distrust when Ghosn arrived. They lined up—in ascending order from the most recently hired worker, a 23-year-old

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1 Details of Ghosn’s visit to the Mie Prefecture dealership are from the author’s reporting in 2000 while a journalist for Time in Japan.
2 Interview by author in 2001.
3 The word for foreigner in Japanese.
grease monkey, to the most senior manager—and bowed in a traditional sign of respect as Ghosn bounded out of his car and walked past them, like General Patton reviewing his troops. After a whirlwind tour of the dealership peppered with rapid-fire questions delivered through a translator (Ghosn was even shown the rest rooms, and at one point, he gently accosted a customer to quiz her about Nissan’s business), Ghosn sat down with department managers to hear their concerns and share his vision for rebuilding the struggling company. Before they got started, however, he issued this warning: “I don’t want excuses. I want to know what you are going to do to make things better.” These employees in suburban Nagoya had never seen anything like this blunt, brash executive. Nor had anyone in Japan. The Ghosn Revolution had begun.

1. Taking on Detroit

If the people at Nissan, and in Japan, were reluctant at first to join this revolution, it’s perhaps not surprising. After all, this generation of Japanese had grown up in a country miraculously rebuilt from the ashes and humiliation of defeat in World War II into the world’s second-largest economic superpower, all in a span of just three decades. The stunning performance of the auto industry was not just of economic significance for Japan, it was a proud symbol of all the country had achieved. (See Exhibit 1 on Japanese car exports from 1983 to 2000.) Detroit and its Big Three auto companies, after all, had been forced to copy Japanese manufacturing methods to remain competitive in a business that the Americans had pioneered and dominated. In the boardrooms of Tokyo and the factories of Nagoya and Yokohama, it was accepted as an article of faith that Japan was simply superior at making cars.

In the postwar era, Japan engineered an industrial policy to nurture a manufacturing sector that would drive the country’s export-based growth economy. Automobiles were not initially identified as a target sector by the country’s powerful Ministry of International Trade and Industry (MITI). But the car industry would nonetheless benefit from trade policies, including tariffs, as well as domestic fuel taxes and favorable exchange rates, that helped shield automakers from foreign competition and protect the domestic car market. These policies enabled Toyota, Nissan, Honda and the other car manufacturers to experiment, develop and dominate the Japanese auto market during its formative years without the threat of competition.

At the core of Japan’s auto business was a reality that U.S. producers wouldn’t face for many years: Japan was completely dependent on foreign sources for oil. This reality influenced a philosophy toward developing fuel-efficient cars that wouldn’t develop in the United States until after the oil crisis of 1973. The nature of this dependency was taken for granted as part of a national mind-set, the pragmatic self-image of Japan as a resource-poor country that would always be dependent to a certain extent on the outside world. This reality was a significant factor in Japan’s quest to dominate Asia (and its rubber plantations in Southeast Asia, for example) in the 1930s and 1940s. And like any nation lacking an abundance of natural resources, Japan was motivated to create value-added industries and to develop an expertise in manufacturing to boost its export income.

Still, as oil is a fungible commodity, Japan’s dependency on foreign sources alone did not spur the creation of fuel-efficient cars. Instead, it was a tax policy that created high prices at the gas pumps and encouraged consumers to buy fuel-efficient cars—a policy avoided to this day in the
United States. Japanese consumers demanded smaller cars with better gas mileage, so the auto industry was motivated to build them.

In addition, the urbanized area stretching from Osaka to Tokyo was densely populated. The design of the cities, particularly Tokyo, dated back to the 19th century and was characterized by a maze of narrow, winding streets. The gas-guzzling sedans and station wagons that Detroit was churning out wouldn't have suited Japan's roadways or its pocketbooks. These market factors, coupled with a blanket of trade protectionism, gave Japan's automakers breathing space to experiment, develop and build the kind of cars best suited to Japan. All of this happened at a time of dramatic economic growth in Japan, the kind of growth that could boost an emerging car industry.

What no one expected was that those compact, fuel-efficient models would one day be best suited to not only Japan but America, too. The gas price hikes in the United States during the Middle East oil crisis of the 1970s created a demand for precisely those types of cars. The trouble was Detroit wasn't building them. Automakers in the United States hadn't projected such a shift in consumer demand, so they were unprepared to downsize their basic models. U.S. carmakers had no reason to expect a demand for fuel efficiency, and developing new technologies to meet that demand would take time.

In the meantime, however, Japanese automakers had not only developed alternative models that were palatable to Americans, they also had honed the engineering process and streamlined the manufacturing process (they were among the first users of industrial robots) to both equal—if not surpass—the quality of U.S. cars and surpass their rivals in efficiency and cost. (See Exhibit 2 on Japanese automakers' share of the U.S. market from 1978 to 2000.) It was widely reported that by the early 1980s manufacturing costs for a car (of comparable size) were between $1,500 and $2,000 less in Japan than in the United States. By 1985, Japanese imports accounted for 20 percent of car sales in the United States, and some 58 percent of the country's total production was headed for export (Ward's Automotive Yearbook).

It wasn't just technological know-how and manufacturing efficiency that gave Japan its competitive edge, however. Car exports also were boosted by a favorable exchange rate. A weak yen, relative to the dollar, made Japanese imports cheaper than domestic cars in the United States. In the early 1980s, for example, the dollar was trading at between 200 and 250 yen. The situation had helped create a large U.S. trade deficit, and American critics argued that a strong dollar was causing the shuttering of factories and the loss of jobs in some industries, including automobiles.

This sparked a feverish round of Japan bashing in the United States and prompted political leaders to intervene in the currency markets. In 1985, the leading industrial nations (including Japan) signed the Plaza Accord, which served to strengthen the yen. Within a year, the dollar had dropped from its high of 240 yen to just 150. Suddenly, one competitive edge enjoyed by Japan's automakers had evaporated.

Japan responded by finding new ways to cut costs. It also began opening auto assembly plants in the United States, in part to counter proposals in Washington, D.C., to curb quotas of Japanese autos into the country. It looked as if Japan's success would continue despite these changes. But then other factors emerged that undermined the car industry in Japan. In 1990, Japan's economic bubble burst, stocks crashed and the inflated real estate market quieted. The economic growth
engine that had seemed unstoppable was now sputtering, and this had a deep impact on the car industry, as domestic sales lagged.

Meanwhile, in the United States American automakers had hit on a new strategy that caught the Japanese unprepared: light trucks. U.S. fuel-efficiency standards did not apply to trucks. So Detroit came up with a new “truck” to avoid the regulations. These “sport utility vehicles” (SUVs) drove the U.S. car market in the 1990s. But Japan wasn’t in that game (such “light trucks” had no market in Japan) and found itself falling behind its American rivals.

The Asian financial crisis of 1997 also damaged Japan’s automakers, as the key geographic region targeted for growth—Southeast Asia—was now in a tailspin. Markets for high-ticket items such as cars disappeared. The regional crisis caused a general economic slowdown around the world, further eroding auto sales.

Japan’s automakers, then, were losing sales everywhere: at home, where the economy was stagnant and headed toward deflationary pressure; in the United States, where a new breed of “car”—the SUV—was dominating the market; and in Asia, where car sales were plummeting (Shirouzu and Zaun 2003).

That didn’t stop Japan’s automakers, however. They kept churning out cars, creating a serious problem of overcapacity in a society in which the notion of cutting back and firing workers was alien.

2. The Rise and Fall of Nissan

Nissan, which was established in 1933 and was one of Japan’s automobile pioneers, competed for car-making supremacy in Japan with Toyota through the 1970s. It exported its first cars to the United States in 1958, in what was seen as an impossibly naive attempt to break into the lucrative American marketplace. Nobody was scoffing at Nissan two decades later, after its spiffy sports coupe, the Datsun 240Z, wowed car aficionados as an affordable, fuel-efficient alternative to the road hogs Detroit was still producing. “Anyone born after 1965 won’t get it,” Business Week wrote in 2002, “but for 15 years—from 1970 to 1985—the Z sports car was the ultimate thrill machine, an unbeatable combination of rakish lines, raw horsepower and affordability that young Japanese and American guys found impossible to resist” (Dawson 2002b). For Nissan, the Z was a brand leader that created an upbeat, positive image for its entire line of cars. (See Exhibit 3 on Nissan sales in the United States from 1989 to 2000 and Exhibit 4 on Nissan’s market share in the United States from 1978 to 2000.)

In the 1980s, however, Nissan made some missteps in both the United States and Japan. Inexplicably, the company decided to jettison its “Datsun” brand and market cars under the “Nissan” name, an unknown commodity in the United States. To make matters worse, the company that had established a reputation based on its original styling and design rolled out a series of bland, forgettable sedans. As these Nissan cars failed to light a fire under U.S. consumers, Honda, with its image of reliability at a low cost, and Toyota, with its reputation for quality, grabbed the opening left by Nissan. While consumers rejected Nissan’s style, they also blanched at the sticker price, which was about $1,000 more than similar models sold in the United States by Honda.4

4 Interviews by the author with Nissan managers, November and December, 2000; see also Shirouzu, White and Zaun 2000.
Nissan's annual sales in the United States declined 20 percent from 1994 to 1998. Back home, Nissan was distracted by a focus on overtaking Toyota as Japan's No. 1 carmaker while the domestic auto market was shrinking. (See Exhibit 5 on the registration of new passenger cars in Japan from 1993 to 2000 and Exhibit 6 on the production of new cars in Japan from 1993 to 2000.) Nissan didn't pare its production, however, and it found itself swimming in red ink.

The company announced two major restructuring plans in the 1990s, but they had little impact; powerful trade unions, a societal taboo against layoffs and institutional inertia stalled any real changes. The company's global market share of car sales declined from 6.6 percent in 1991 to 4.9 percent in 1998 (Wehrfritz 1999). With Nissan on the verge of bankruptcy, the government-owned Japan Development Bank issued $731 million in emergency loans to save the company from collapsing (Brenner 1999).

The situation was so bad that Nissan did the unthinkable: It started shopping around for a foreign buyer to save this icon of Japanese industrialism. Foreign firms had invested in other Japanese carmakers: General Motors had taken effective control of Isuzu by the late 1990s, and Ford was running the show at Mazda. But these were smaller car companies that had always been secondary players in the Japanese market. Their surrender to foreign competitors didn't carry the symbolic punch that a takeover of Nissan would. In 1999, after DaimlerChrysler balked at the huge debt load, French carmaker Renault, seeking an entrée into both the Japanese and North American markets, bought a controlling 37 percent interest in the company for $5.4 billion. While the company would be saved, at least temporarily, not many people in Japan were happy about the notion of a foreign takeover of one of the country's proudest companies. “When MacArthur came after World War II, the Japanese just surrendered to his leadership,” said a retired Nissan executive. “A similar thing is happening at Nissan today” (Wehrfritz 1999).

3. Nissan's Revival: No Sacred Cows

Renault dispatched to Tokyo an executive with a reputation for saving sinking ships, Carlos Ghosn. At first, it looked as if Ghosn would follow the wisdom put forth by an American military officer during the Vietnam War: He had to destroy the company to save it. When he met a large audience of skeptical stock analysts and journalists in the fall of 1999, Ghosn boldly announced the most dramatic restructuring plan ever attempted in Japan.

There is only “one rule,” he said. “No sacred cows, no taboos, no constraints.”

He promised to make Nissan profitable within two years. His plan was to take a meat cleaver to the company's bloated factories and suppliers, reducing costs of parts, shedding workers and cutting back on production. The first phase of his revival plan for Nissan was all about cutting costs to improve profits. Increasing sales would come later, in the second phase.

4. Phase 1 included several key planks:
- Close three factories in Japan
- Cut 21,000 jobs

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5 See Nissan annual reports.
6 Details of this press conference and of the Nissan restructuring plan are from the author's reporting and other press reports.
• Divest many subsidiaries to help shrink $12.6 billion of debt
• Rationalize parts procurement by cutting the number of suppliers from 1,300 to 600
• Force suppliers to discount their parts by 20 to 30 percent over three years
• Reduce the number of platforms used in production

To carry out phase 1, Ghosn created 12 cross-functional teams, composed of Nissan and Renault managers, to address the company’s key shortcomings: parts procurement, marketing and debt, for example. Those teams were given short deadlines—about one month—to identify areas to cut costs and improve profitability. Ghosn also made it clear that Nissan’s seniority system of promotions (typical of Japanese companies) would soon be history and replaced by a merit system. The traditional respect given to age would be abandoned in favor of competency. “If people didn’t get it, they would have to step aside,” explained one senior executive.

Outside the company, Ghosn was challenging other “sacred cows.” Some 60 percent of Nissan’s cost of production came from suppliers, making it an area ripe for cost reduction (Shirouzu, White and Zaun 2000). To do that meant attacking the keretsu system—that linked large manufacturers, like Nissan, to its suppliers through long-standing relationships, transferring of managers from Nissan to the supply companies and, in some cases, cross-shareholding. The keretsu was like a big family. In the 1980s, it was considered one of the key components of the success of Japanese manufacturing, as the cozy relationships ensured that manufacturers were delivered high-quality parts, manufactured to specification, as they were needed. But in recent years, after U.S. and European firms began closing the quality gap in manufacturing, Japan’s vaunted system was losing its edge. Where it once “took two workers in a traditional Big Three auto plant to do the work of one in a . . . plant built by Nissan, Toyota, or Honda,” by the late 1990s, “the once huge productivity and profit gap between Detroit’s best plants and Japan’s best is rapidly closing—and in some cases already has closed” (Priddle and Winter 2000). Parts suppliers in the United States, for example, were gaining greater economies of scale by consolidating operations, selling to several manufacturers and, in the end, undercutting Japanese suppliers.

Ghosn’s restructuring plan was ambitious, and getting it to work would mean revolutionizing the way companies do business in Japan. Ghosn stated: “To be able to make changes, it is necessary to do some hard things. If you do those things, it does not mean you do not value people. In my opinion, the reverse is true. People who do not tell the truth do not respect people. My concept of respect for people starts with telling the truth and establishing the facts of a situation.”

Phase 1 was a success. In the fall of 2000, a full six months before Ghosn had promised Nissan would return to the black, the company reported profits of $1.5 billion for the previous six months—the company’s best financial performance in a decade (Shirouzu, White and Zaun 2000). In 2002, Nissan announced earnings of $3.8 billion on sales of $47.7 billion (Dawson 2002a), but sales increased less than 2 percent. Cost cutting brought the company back from near extinction, or

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1 Details of the cross-functional teams from interviews by the author with Nissan managers, November and December 2000.
2 Interview by the author in Tokyo in 2001.
3 A network of manufacturers and their suppliers and subsidiaries in related fields of work.
as Ghosn put it, “from the emergency room to the recovery room” (Ibison 2001a). But something more would be needed to make it prosper.

That’s where phase 2 comes in. While Ghosn was busy cutting fat, he also put into place a plan to sell more cars. “We are at the same time accelerating and braking,” Ghosn said (Shirouzu, White and Zaun 2000). He hired away Shiro Nakamura, a respected and flashy designer at Isuzu, to make over Nissan’s stodgy image, and the design team began building a multicultural, global team with experience at several carmakers and in several countries (Zaun and Freeman 2003). Nissan also broke ground on a new plant in Mississippi to build SUVs, minivans and pickup trucks for the U.S. market. And it began abandoning the boxy, boring designs that gave the company such a dowdy image in the 1980s and ‘90s in favor of new models intended to create a buzz. Talking about a new minivan, designer Nakamura said it is “not for soccer moms, but for sexy moms” (Zaun and Freeman 2003).

To make that transition from dowdy to sexy, Nissan went back to its roots, with a plan to introduce an updated model of the Z sports coupe. “I could not imagine reviving Nissan without putting the Z back on the road,” said Ghosn (Dawson 2002b). The critics—the car buffs and the trade publications who get early glimpses of new models—uniformly praised Nissan’s new look and reinforced the positive publicity Ghosn had generated during his first phase of cost cutting. Phase 2 projected increasing sales by 1 million, cutting debt to zero and achieving an 8 percent operating profit (Zaun and Freeman 2003). Two of Nissan’s new models have become instant hits in the United States and Japan, beginning to draw wary consumers back into Nissan showrooms (Naughton and Raymond 2001).

Ghosn’s success turned him into a celebrity in Japan, a turn of events that would have been thought unthinkable after the initial doomsday reaction to his restructuring plans. Salarymen copy the cut of his suits, the style of his eyeglasses and the buzzwords of his lexicon. Employees who are downsized out of jobs at Japanese companies no longer say they are “fired” or “laid off.” They say they are “restructured.” Other businesses, from giants like Mitsubishi to small parts suppliers, copy his style of cost cutting, known simply as “Ghosn Style.” He is the darling of TV gossip shows and celebrity magazines. A survey of women found that he was one of four men considered an ideal father figure. He even has groupies and receives marriage proposals in the mail. During a visit to a Nissan dealership in Nagoya, a middle-aged married woman showed up with a gift for Ghosn. She had seen him on TV talking about restructuring, and had fallen in love. 11

5. The Ghosn-ing of Japan?

Does Japan’s love affair with Carlos Ghosn mean the country and its famously stubborn businesses are ready for a jolt of change? Could a Ghosn-style restructuring work elsewhere? Admiral Perry and his black ships are credited with prodding Japan to open up its closed ports, and markets, to the world and ushering in the Meiji era of restoration in the late 19th century. Is Carlos Ghosn the Admiral Perry of modern Japan?

Nissan, to be sure, was a particularly desperate case. It was nearly bankrupt, and its company executives knew it. So Ghosn didn’t have to do much convincing, or educating, that “Nissan is in

11 Author research conducted in December 2000.
bad shape,” as he stated in October 1999. Everybody knew that, and its employees, as much as some of them did resist change, nevertheless recognized that a Ghosn renovation might be the last chance to save the company. “Many of them were receptive to Ghosn-san’s ideas because we knew this had to be done,” said one midlevel manager. “We were getting impatient with the old Nissan management because they kept talking about changes but wouldn’t make them. So we are happy to support Ghosn-san now” (Dawson 2002a). Even the labor unions backed him.

That kind of support might not happen in other companies, where the case for major overhaul might not be so clear-cut. It’s also unclear whether anyone but a foreigner could deliver such direct talk and call for such drastic actions. A Japanese executive might be too beholden to his longtime friends and allies in the companies. Indeed, ending a relationship with a member of a kereitsu would mean cutting off a lifelong colleague, as typically suppliers and subsidiaries are run by executives from the mother company.

Yet there is evidence of a Ghosn Reformation, if not a Revolution. “Ghosn’s results have raised the bar for companies in Japan in terms of what can be accomplished and how quickly,” said Michael Garstka, a Bain & Co. consultant in Tokyo (Dawson 2002a). A recent survey of 800 companies found that less than one-fifth of them plan to hold on to their system of lifetime employment for employees (Dawson 2002a). Other companies are introducing merit-based pay and promotion and even stock options. Blue-chip companies, which for decades had clung to a lifetime employment system, began implementing rounds of layoffs and moving manufacturing operations offshore. Like Nissan, they are selling off noncore businesses. They are starting to face pressure to do this from their banks, which are heavily indebted and under pressure themselves to reduce debt loads. With an aging population, a deflationary economy and competition from such emerging markets as China for manufacturing, it’s clear that Japanese companies do need to engineer a makeover.

Ghosn was asked at a dinner reception, “Have you ever considered running for prime minister of Japan?” (Ibison 2001a).

That’s not going to happen. But the very fact that someone would ask is revealing.

Ghosn gave a simple, curt reply: “We are not missionaries. We are not in the business of changing cultures but of maximizing performance.”

The question is: Can Japanese companies maximize their performance without changing their culture?

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12 The years 2001 and 2002 were characterized by frequent rounds of layoffs at Japanese companies; see Larimer 2002.
13 For a discussion of Japanese corporate reform, see Ibison 2001b.
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