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Owner as Regulator, Like Oil and Water

Kevin Lamarque/Reuters

President Obama tried out a Sonic subcompact during a tour of a General Motors plant in Lake Orion, Mich., a Detroit suburb.

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Let's say you're the biggest owner of a global auto company. You take the company's flagship new vehicle, twist it, crash it, poke it and leave it outside in the elements for weeks until its battery catches fire. Then you generate a storm of publicity and watch the share price and the value of your ownership stake decline.

This, essentially, is what the United States has done to General Motors and its signature new vehicle, the Chevy Volt.

If it wasn't already obvious, at least one reason the government shouldn't own controlling stakes in major companies is that ownership and regulation are inherently incompatible. This week, the Republican presidential candidate Mitt Romney defended his tenure as head of the private equity firm Bain Capital by comparing Bain's role in troubled companies to the government's rescue of G.M.

Rest assured that if Bain Capital owned G.M., it would not be subjecting the Volt to severe safety tests and trumpeting the negative results.

More than a year after G.M.'s return to public ownership, the government still owns just less than 30 percent of the company, or about 500 million shares. Of course, the government must hold G.M. to the same strict safety standards it applies to all auto manufacturers. The National Highway Traffic Safety Administration, or N.H.T.S.A., said in late November that it would assess the risk of fire in Volts after two incidents of fires following crash tests.

But some Republican congressmen questioned whether the Obama administration had concealed the results. And conspiracy theorists and others have taken to the Internet to argue that the agency has been too soft on G.M. and has a motive to soft-pedal or even distort the results because of the government's ownership stake.

Safety Research and Strategies, a Massachusetts consulting firm, claimed the government's Volt crash report was little more than a "sales pitch" for the plug-in hybrid vehicle.

Others have suggested that the agency was too tough, even if subliminally, in an effort to forestall any perception of a conflict, and that the danger of a Volt catching fire was remote.

Car and Driver magazine noted that the Volt's batteries caught fire three weeks and one week after the crash tests, and said that "if you ask us, even just one day is plenty of time to safely exit a vehicle that's in peril of burning." The magazine noted that no Volts had caught fire in the real world and that only three safety complaints showed up in the government's database for all of 2010 and 2011, none involving fire hazards. "No vehicle is completely and infallibly safe," the magazine said. The risk of fire following a crash in an electric car also appears to be vastly less than in a conventional gas-powered vehicle.

Tim Massad, assistant Treasury secretary for financial stability, told me this week that Treasury, which oversees the government's investment, "is not G.M. or Chrysler's regulator and has no involvement with N.H.T.S.A." I haven't seen any evidence that the agency acted in anything but a professional and independent manner with respect to the Volt, but the controversy illustrates why even appearances of a conflict need to be avoided.

How much has the Volt controversy cost G.M.? One measure of the new G.M. is its aggressive, albeit expensive, response. The old G.M. might have dug in and fought the government. It could have appealed and stalled for years while losing the public relations war. This time, G.M. immediately offered a loaner vehicle to any existing Volt owner concerned about the vehicle's safety. Since then, G.M. has announced that it will make structural enhancements and install a sensor to warn of any battery fluid leak.

Of course, what choice did G.M. have, given that its regulator is also its biggest owner?

Consumers seem to be reacting positively. N.H.T.S.A. has now awarded the Volt five stars, the top ranking, in its crash test results (a ranking that is also suspect to conspiracy theorists). G.M. said December was the best sales month ever for the Volt, but it's still selling in small numbers, and it's impossible to know how many potential customers were discouraged by the bad publicity. And the damage to G.M.'s image is also hard to quantify, but surely considerable. The Volt was expected to deliver a halo effect to all of G.M.'s brands and bolster its overall reputation, much as the Prius did for Toyota until the company ran into its own safety and quality issues. That effort has suffered at least a temporary setback. (A G.M. spokeswoman declined to comment.)

And it's not just safety issues where the government's interests conflict. Along with other bailout recipients who remain under government oversight, G.M. is subject to executive pay restrictions. No private equity owner would agree to such limitations on its ability to attract and keep management talent. The pay constraints apply to the top five executive offices and extend deep into the ranks to include the 20 most highly compensated employees.

At this week's North American International Auto Show in Detroit, Ford was showing off Lincoln's new design director, Max Wolff, who took to the stage to unveil the boldly redesigned Lincoln MKZ. Ford poached Mr. Wolff from G.M.'s Cadillac division in 2010, and design directors are some of the most highly paid people in the industry. The G.M. spokeswoman wouldn't comment on whether G.M. could match or top Ford's offer, but said that the company continued to attract top talent because of its "iconic" status and because people wanted to be part of "an incredible comeback story." Still, G.M.'s chief executive, Dan Akerson, has said he'd like to see pay restrictions eased.

(G.M. got approval to pay Mr. Akerson $9 million for 2011, which was in the lower quarter of chief executive pay at the nation's largest companies, the automaker said.)

"The pay issue is a legitimate concern," Adam Jonas, a Morgan Stanley auto analyst, told me this week just after returning from the auto show in Detroit. "There's a race for talent. Management has to attract and retain people outside Detroit, design talent and engineering talent. I'm concerned about that."

Mr. Massad of Treasury noted that the pay restrictions are embedded in the bailout legislation and could only be removed by Congress. Otherwise, "We're not in any way involved in the day-to-day management of the company," he said, which was confirmed by G.M. officials I spoke to.

The Obama administration also has a political agenda that often conflicts with ownership interests. It wants to keep unions happy, promote the environment and lift employment, among other goals, which may conflict with maximizing returns to taxpayers. Anything having to do with G.M. is likely to be a hot-button issue during an election year.

The Bush and Obama administrations can rightly hail their rescue of the auto industry as a success — a rejuvenated G.M. has spent $5 billion in capital investment and added 15,000 jobs, and the Treasury estimates the rescue saved more than a million jobs in the United States, including those in the supply chain. G.M. has hit many impressive milestones on the road to recovery, including its November 2010 public offering and seven consecutive profitable quarters.

But continued government ownership has not bolstered the stock price. Auto company shares have been battered by many factors beyond the control of the Obama administration, including the debt crisis in Europe and the Japanese tsunami. But G.M. went public at $33 a share, and after trading as high as $39, this week shares were barely above $24. With benefit of hindsight, the government could have gotten out at a much higher price.

A problem should the government decide to sell now is that many analysts believe G.M. is undervalued. Its price-to-earnings ratio, a popular valuation measure, was a mere 5.4 this week, compared with an average for the Standard & Poor's 500-stock index of nearly 15. "In terms of straight valuation, I'd advise the government not to sell," Mr. Jonas said. "I tell clients the same thing. The stock is worth $45 in our view. It's one of our top picks. You have to be patient, and it may be a jagged journey, but it's very undervalued."

But one of the reasons it may be undervalued is that the government owns so much of it, and the longer that continues, the worse G.M.'s competitive position is likely to become.

Mr. Massad said: "The government should not generally be in the business of owning shares in private companies. At the same time, we have to balance that with the goal of maximizing returns to taxpayers. We're prepared to be patient."

The administration has not unveiled any exit strategy, but in my view, it needs one. The Treasury Department is no Bain Capital, nor should it try to be a private equity investor. So far, the Treasury's sense of market timing doesn't seem any more successful than that of most money managers. It's been more than three years since the Bush administration stepped in to save the auto industry. It's time to declare victory and liberate G.M. from the onus of continuing government ownership.

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