The Innovators Dilemma: Car Industry

For decades, automakers like GM, Ford, and Volkswagen, dominated by doing what they did best: making cars safer, faster, and more comfortable. Profits flowed, shareholders rejoiced. What could go wrong?

Then came the 1970s, and Toyota arrived with smaller, simpler, and cheaper cars. Dismissed as inferior by Detroit's giants, these vehicles found an audience among budget-conscious buyers.

The leaders at the giants knew that selling cheap cars to people with small budgets wasn't as good as selling expensive vehicles to people with plenty of money. And so, in their self interest, they decided to leave that segment to the Japanese.

The people at Toyota had nothing to lose, they were happy to serve budget-conscious buyers and over time kept improving their cars. And so they gained market share and then introduced more luxurious models, like the Camry or Lexus, competing directly with well-known brands in a more expensive segment.

The CEOs of the traditional automakers responded as they did earlier, by comparing the profit margins and then shifting to even larger vehicles like SUVs and trucks—where they could still make a lot of money. But it didn't stop there.

The pattern repeated in the 1990s, when South Korea's Hyundai and Kia entered the market with inexpensive compact cars. Dismissed again, these upstarts steadily improved their quality, forcing even Toyota to pivot toward premium models.

And then came Tesla. In 2008, its first electric car was pricey, had limited range, and relied on a non-existent charging network—hardly a threat to traditional automakers. Why chase low-margin EVs when gas-guzzling trucks were selling like hot cakes?

But as batteries improved and costs fell, Tesla's appeal grew. Today, legacy automakers are scrambling to catch up—another reminder of the cost of clinging to the past.

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