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Toyota's Governance Crisis:

What It Means for Investor Risk

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Key Findings

- Ahead of the 2025 Toyota Annual General Meeting, Board Chair Akio Toyoda is facing a historic level of investor discontent. He has overseen a growing series of emissions and fraud scandals that threaten Toyota's reputation and have already cost the company billions.
- The board chair's extraordinary consolidation of power has troubled investors, leading them to call for better governance. However, Toyota management's proposal to improve board independence will likely deepen the governance failures that have so concerned investors.
- Chairman Toyoda's unchecked power threatens the company's ability to transition to the growing future of electric vehicles, missing out on a major market opportunity.

Toyota's Reputation at Risk

While Toyota bills itself as a climate leader, it has become the most ardent automotive opponent of climate action. That dissonance—along with a growing series of emissions and fraud scandals—threatens consumer trust and the brand loyalty that Toyota has spent decades building. Instead of building electric vehicles, Toyota has spent the past several years quietly building a global influence operation to weaken climate policy. It has routinely ranked as the worst automaker in the world for its anti-climate lobbying. In the U.S., Toyota has become the largest automotive funder of climate deniers in Congress.

That threatens Toyota's bottom line. In a 2020 poll of one thousand Toyota owners, the company's opposition to climate policy led to a 32% drop in Toyota's favorability rating. 75% of Republicans and 90% of Democrats who own Toyotas said that the company should support stronger emissions standards. The dissonance between Toyota's political spending and lobbying and its customers' values threatens to erode consumer trust.

So do a troubling series of fraud and emissions scandals. In 2021 Toyota agreed to pay a $180 million civil penalty for a decade of non-compliance with Clean Air Act reporting requirements, the largest-ever such penalty. In 2022 Toyota subsidiary Hino Motors admitted to cheating on up to 20 years of emissions tests, later pleading guilty to emissions fraud and settling for $1.6 billion. In 2023 Toyota subsidiary Daihatsu shut all four of its factories in Japan amidst a government probe that forced the automaker to admit that it cheated on thirty years of crash tests. In January 2024 Toyota Chairman Akio Toyoda was forced to apologize for cheating on engine testing that led the Japanese government to raid one of its plants. Less than six months later, he was forced to apologize again, this time for large-scale cheating on certification tests for seven vehicle models that led to Toyota suspending production on three models. The month after that scandal, Toyota's year-over-year global output fell by 12.6% and the following month its global sales fell by 3.7%, with a much steeper 9% sales decline in Japan. Meanwhile, Toyota is currently facing a massive class action lawsuit in Australia for a scandal in which it allegedly produced and sold hundreds of thousands of defeat devices. Famously used by Volkswagen in Dieselgate, defeat devices alter emissions results to fraudulently allow non-compliant vehicles to pass.

Declining Investor Confidence in Chairman Toyoda

Investors have not been impressed, showing their lack of confidence in Chairman Toyoda with steadily declining support. In 2022, in large part due to his dogged opposition to electric vehicles, then-CEO Toyoda was forced to step down in favor of a younger and more forward-looking chief executive in Koji Sato. Ahead of the change, senior director at Fitch Ratings Satoru Aoyama told *the Financial Times* that Toyota could "lose investor confidence" because it "is not correctly responding to calls from the market to take a lead in electric vehicles."

However, many both inside and outside the company are concerned that Toyoda is still holding on too tightly to the reins of power, essentially operating as a shadow CEO. In 2023, he made sweeping changes to Toyota's management, and that year six new directors were appointed to the board.

Michael Garland, the head of corporate governance for the New York City Comptroller's Office, summed it up for *The New York Times*: "You have a case of a particularly empowered executive sitting in a chairman's role. Toyota's need for more independent board oversight is significant." In an exceedingly rare move, even fellow Toyota board members have begun to publicly criticize the chairman, voicing concern over his increased concentration of power.

Investors have also been troubled. Citing governance issues, proxy advisors ISS and Glass Lewis advised shareholders to vote against approving Chairman Toyoda. Board votes at Toyota are usually a formality, but at last year's AGM, investors showed their lack of confidence in Chairman Toyoda with a historically low approval vote. He received just 34% support from foreign institutional investors and 55% from Japanese institutional investors. Propped up by votes from Toyota Industries, Toyota Motor Company's second biggest investor, and reliable retail investors, Toyoda managed to secure 71.9% of the vote, a drop from 85% in 2023 and 96% in 2022.

The poor showing forced Toyoda to admit that "there has never been a director at Toyota with such a low approval rate before" and "if we continue at this pace, I will no longer be able to serve as a director next year...with my behavior over the past year, half of the people are basically telling me to quit." In response to questions about why he was losing support, Toyoda said "I don't know. I think the number of dissenting votes is increasing extremely quickly."

Anders Schelde, the chief investment officer at AkademikerPension, said "Toyota's shareholders have now sent a strong signal that better governance is needed at the very top of the company."

However, instead of loosening the reins, the chairman is trying to tighten his control. On April 28, Bloomberg reported that the founder's grandson has launched a $42 billion bid to buy out Toyota Industries Corp. (TICO), a car part, textile machinery, and forklift manufacturer. This is significant because while Toyoda holds under 1% of Toyota Motor Corporation's Stock, TICO owns 9.1% of the automaker. Such a move would consolidate his already considerable control, making it easier for the chairman to ignore investor concerns. Some analysts also worry that it would run counter to Japan's goal of boosting mergers and acquisitions by disentangling cozy business relationships.

A rubber stamp board

While the founder's grandson has been frank about his failures, management continues to enable Toyoda's worst impulses. Its proposal to improve board independence will likely deepen the governance failures that have so concerned investors. At the upcoming shareholder meeting, Toyota is proposing shrinking its board to ten members, increasing the number of independent directors to five, and establishing a new oversight committee. There are a number of reasons why this proposal is flawed:

1. Reducing the number of directors would likely only consolidate Chairman Toyoda's already considerable power. By folding its supervisory and audit committee members into its board without creating new board seats, Toyota is effectively shrinking its board.
2. Toyota ranks at the bottom for board independence when compared to other major Asian automakers and other automakers traded on the New York Stock Exchange.
3. Even if Toyota increases its number of independent directors to half, that is still below the majority threshold that the New York Stock Exchange (NYSE) requires. While Toyota is cross-listed on the NYSE, as a foreign private issuer Toyota is allowed to follow the Tokyo Stock Exchange's less stringent guidelines that require just one-third of its directors to be independent. However, a significant amount of Toyota stock is traded on the NYSE, exposing U.S. investors to risks associated with Toyota's lack of independent governance.
4. Proposed director Chris Reynolds is likely to indulge Akio Toyoda's worst anti-EV impulses. Chris Reynolds, a Toyota Motors North America executive for nearly twenty years, until last month oversaw the company's aggressive anti-EV lobbying efforts.

Automaker	Board Independence Ratio	Traded on the NYSE
Toyota	4 out of 10, proposing to increase it to 5 out of 10	Yes
General Motors	12 out of 13	Yes
Stellantis	8 out of 10	Yes
Ford	9 out of 14	Yes
Honda	6 of 12	Yes
Kia	5 out of 8	No
Hyundai	7 out of 13	No
Nissan	8 out of 12	No

Toyota's lack of independent governance is especially concerning within the context of a historically powerful and unaccountable board chair. Combined, these factors threaten Toyota's future, including its ability to take advantage of the growing market for electric vehicles.

Toyota's Market Risk

Toyota has been scrutinized for neglecting electric vehicles. Instead, it has continued to capitalize on hybrid technology. Toyota still sells more vehicles than any other automaker, but the threats are starting to gather. Despite allying itself with the Trump administration, the Trump tariffs have hurt Toyota more than any other automaker. It is losing roughly $1 million per hour and is expected to lose as much in two months as Ford is in the entire year.

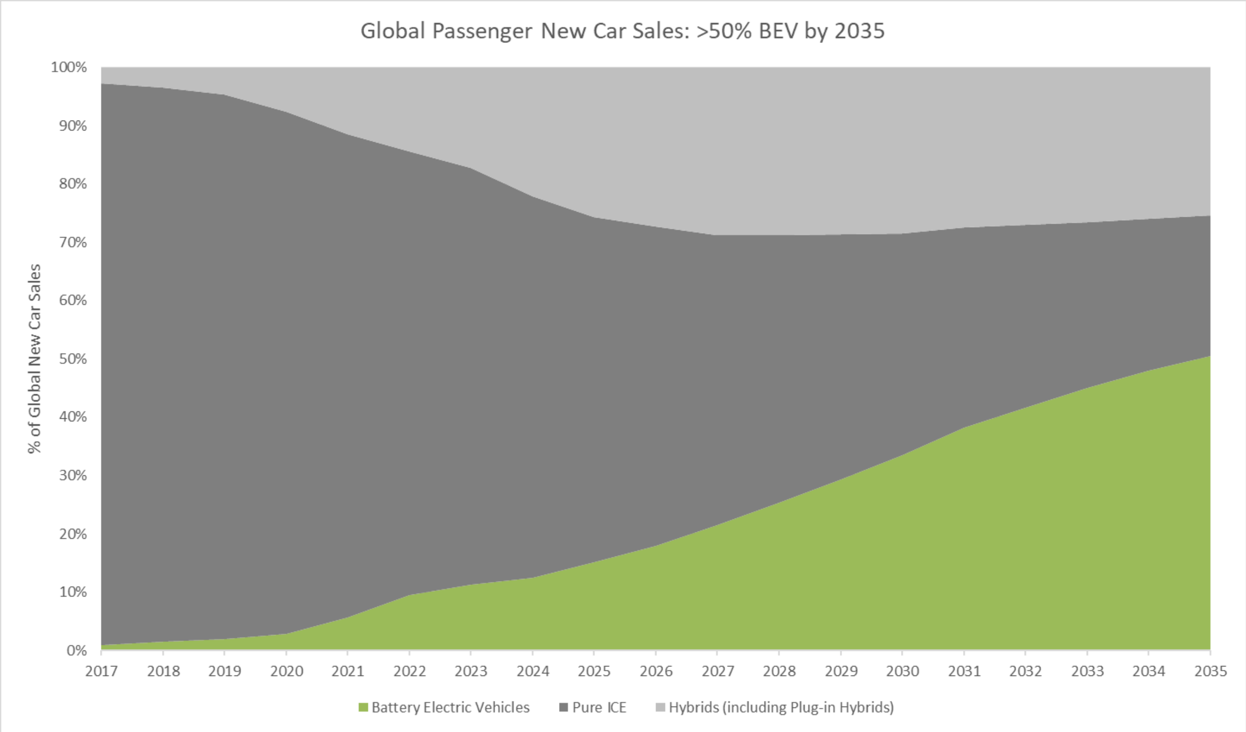
It faces another growing threat: how will the world's largest vehicle manufacturer survive and remain relevant in an increasingly electric world?

2024 Global Electric Vehicle Sales		
Rank	Automaker	Electric Vehicle Unit Sales (millions)
1	Tesla	1.8
2	BYD	1.8
3	Geely Holding Group	0.8
4	GM Group	0.8
5	VW Group	0.7
↓	↓	↓
26	Toyota	0.1

Note: Includes Joint Venture vehicle sales
Source: MarkLines, Company Information

A good litmus test for the financial and market opportunity of a technology is the arrival of new entrants. The last 20 years has seen an influx of EV startup companies including Tesla, Rivian, and many more including companies hailing from China. It is quite likely that only a handful of these startups will survive, but the message is clear—the opportunity is large enough for startups to enter the market. Are hybrids the future? The number of purely hybrid startup automakers is zero. Hybrids are a transition bridge to nowhere, yet Toyota considers this technology a key part of their product strategy.

Demand for vehicles with an internal combustion engine (ICE), including hybrids, peaked in 2017. Global hybrid sales are expected to plateau from this year at around 25 million vehicles per year out to 2035. Meanwhile, new EV sales will grow and could make up more than 50% of the global new car market by 2035. Investors should ask why a leading company is not chasing the growth area of their market.

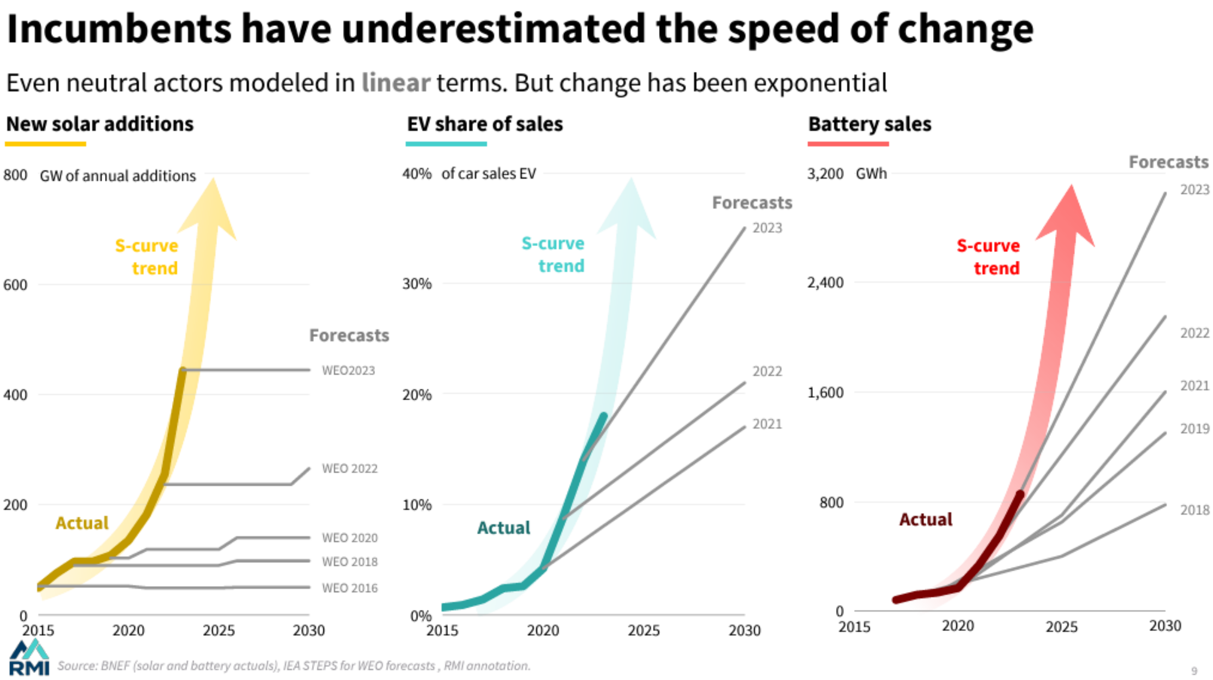


Source: Carbon Tracker, GlobalData Q3 2024 Forecast

By hesitating in bringing compelling and competitive battery electric vehicles to global markets, Toyota risks missing the market and being caught out by the S-curve effect. The S-curve is a well-established phenomenon where a successful new technology reaches a certain catalytic tipping point, and then rapidly reaches a high market share within just a couple more years once past this tipping point. Personal computers and smartphones have seen similar growth curves. Toyota's multi-pathway strategy risks underinvestment in the electric vehicle transition and could put the company behind the curve.

And many incumbents, investors, and research houses have been caught out by this phenomenon and underestimated the uptake of new technologies by modeling in *linear* terms. Following the S-Curve, change has been *exponential* and previous forecasts revised upwards to account for this as shown in the chart below.

Perhaps the most notorious case of neglecting innovation was Kodak, another corporate giant that refused to adapt. In 1975, 24-year-old Kodak engineer Steven Sasson created the first digital camera. However, Kodak saw digital as a threat to its core film and film camera business and buried the invention. [According to Sasson](), "Every digital camera that was sold took away from a film camera and we knew how much money we made on film." Before joining Toyota Motors North America (TMNA) in 2011, TMNA chief lobbyist Stephen Ciccone [spent 23 years leading Kodak's policy work](). During his tenure, Kodak reached [an 80% market share]() in the U.S. and [about 50% market share globally](). However, eschewing innovation eventually caught up with Kodak. That fatal error ultimately helped lead to [the company's bankruptcy]() in 2012, the year after Ciccone moved to Toyota. When Kodak finally embraced the digital future, it was too late. Toyota [sells more vehicles]() than any automaker on the planet and of course will not go bankrupt overnight. However, when Kodak had 80% U.S. market share, no one would have predicted its precipitous decline.



Source: RMI

Emissions Compliance – The Cost of Carbon

Emissions policy [has also been a global driving force]() in the electrification of the vehicle fleet and reducing carbon from tailpipe emissions. While such policy is under attack in the U.S., the effort to use the Congressional Review Act to repeal Clean Cars II faces a number of steep hurdles, including legal questions and the political cost of overruling the Government Accountability Office and the Senate Parliamentarian.

Automakers have a strategy choice on how they will comply with emissions legislation: (1) invest capital in electrification, including batteries; or (2) buy emissions credits from other automakers. Emissions non-compliance comes with penalty fines and reputational risk.

Toyota's mostly hybrid strategy will only get the company so far in complying with longer term emissions legislation. To fill a likely "emissions compliance gap" that is forming, Toyota's North America CEO admitted the company would rather buy carbon credits from other automakers than ramp up BEV production. Buying carbon credits is a waste of capital that could have been used in the development of BEVs, software etc. Toyota is effectively subsidizing the BEV development costs of other manufacturers by buying carbon credits from its competitors.

For an automaker, the cost of failing to decarbonize is falling further behind Chinese BEV competitors. While Toyota recently announced a series of China-focused EVs, they are late to market and domestic Chinese vehicle manufacturers are ready to take market share away from Toyota. Toyota also recently signed an agreement with BMW towards the "advancement of a hydrogen society." These moves will only distract Toyota from serious efforts to decarbonize its vehicle fleet.

Conclusion

Entering the 2025 Toyota shareholder meeting, the company faces a governance crisis. Board Chair Akio Toyoda has overseen a growing series of costly emissions and fraud scandals that threaten the reputation of the company that his grandfather founded. His accumulation of power has worried investors, and Toyota's proposal to improve board independence will, in reality, only deepen its governance crisis. Board Chair Toyoda's unchecked power threatens the company's ability to transition to the growing market for electric vehicles, risking the company's future.