

# The Resurgence of the American Automotive Industry

June 2011

## Introduction

When President Obama took office, the American automobile industry was on the brink of collapse. The President, as part of a larger effort to combat an historic economic crisis, made a difficult decision to provide support to General Motors (GM) and Chrysler on the condition that they, and all of their stakeholders, make the sacrifices necessary to fundamentally restructure their businesses and commit to tough-minded plans to return to viability.

*"Many people thought [the GM] bail-out (and a smaller one involving Chrysler, an even sicker firm) unwise... Yet the doomsayers were wrong."*

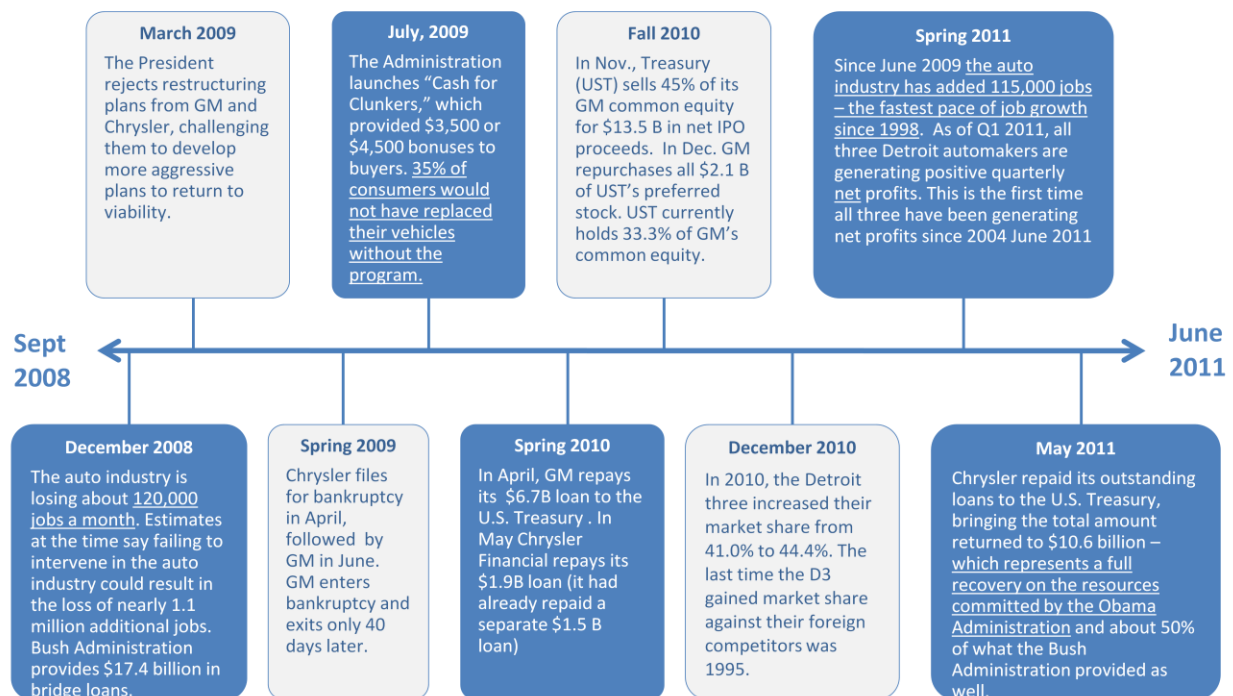
- The Economist, April 19, 2011

The President's decision to save GM and Chrysler was about more than those two companies. It was about standing behind the countless workers, communities, and businesses – large and small – that depend on the automotive industry.

Two years later, the American auto industry is mounting a comeback. General Motors is expanding production and adding jobs, while Chrysler recently repaid its outstanding loans to the U.S. Treasury - six years ahead of schedule. Since GM and Chrysler emerged from bankruptcy, the auto industry has created 115,000 jobs, its strongest period of job growth since the late 1990s. GM, Ford and Chrysler have all returned to profitability, and in 2010, the "Detroit three" gained market share for the first time since 1995.

While American manufacturing continues to face substantial challenges, its future prospects are stronger than they have been in over a decade.

## Auto Industry Timeline



## An Industry in Crisis

*Amidst an historic recession and financial crisis, the liquidation of major American auto companies threatened to eliminate more than one million jobs.*

In late 2008, the combination of an historic recession and financial crisis pushed the American auto industry to the brink of collapse. Access to credit for car loans dried up and auto sales plunged 40 percent. Auto manufacturers and suppliers dramatically curtailed production. In the year before President Obama took office, the industry shed over 400,000 jobs.

As 2008 came to a close, both GM and Chrysler were running out of cash and were only weeks away from complete collapse. Amid the worst financial crisis since the Great Depression, credit markets were frozen and no alternative sources of financing were available to GM and Chrysler. Both companies faced the stark choice of seeking government support or facing almost certain uncontrolled liquidations. In this context, the Bush Administration extended short-term bridge loans to GM and Chrysler, but left it to President Obama to ultimately make the decision about how to resolve the industry's historic crisis and what role, if any, the federal government should play in their revival.

After studying the plans submitted by GM and Chrysler, President Obama decided that he would not commit any additional taxpayer resources to these companies without forcing fundamental change and accountability. He rejected their initial viability plans and demanded that they develop more ambitious strategies to reduce costs and increase efficiencies to become more sustainable.

However, President Obama also recognized that failing to stand behind these companies would have consequences that extended far beyond their factories and workers. GM and Chrysler were supported by a vast network of auto suppliers, which employed three times as many workers and depended on the auto companies business to survive. An uncontrolled liquidation of a major automaker would have had a cascading impact throughout the supply chain, causing failures and job loss on a larger scale. Because Ford and other auto companies depended on those same suppliers, the failure of the suppliers could have caused those auto companies to fail as well.<sup>1</sup> Also at risk were the thousands of auto dealers across the country, as well as small businesses in communities with concentrations of auto workers.

*"The government's intervention was absolutely key to helping create a chance for GM and Chrysler going forward. That's why I testified on behalf of GM and Chrysler, as you know. The reason we did was that we believed—like two presidents [Bush and Obama]—that if GM and Chrysler would have gone into freefall bankruptcy, they would have taken the supply base down and taken the industry down plus maybe turned the U.S. recession into a depression."*

- Alan Mulally, CEO, Ford Motor Company, October 16, 2010

It was the interdependence between the auto companies and suppliers, dealers and communities that led some experts at the time to estimate that were GM and Chrysler allowed to liquidate, at least 1 million jobs could have been lost.<sup>2</sup> Other estimates suggested that the near-term jobs at risk from liquidation could have been even

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<sup>1</sup> See *"The Daily Beast Talks With Ford's CEO," The Daily Beast, October 16, 2010.*

<sup>2</sup> See White House Office of the Press Secretary, *Fact Sheet: Financing Assistance to Facilitate the Restructuring of Auto Manufacturers to Attain Financial Viability, Dec. 19, 2008.*

higher.<sup>3</sup> In addition, the cost to the government to provide social safety net services and health care to these workers and communities would have been substantial.

To avoid this outcome, the President decided to give Chrysler, GM, and their stakeholders a chance to show that they could take tough and painful steps to become viable, profitable companies – and to stand behind them if they could.

## Chrysler's Turnaround

*Chrysler, on the verge of liquidation two years ago, has now repaid its outstanding loans to the U.S. Treasury, nearly six years ahead of schedule, and has returned to profitability.*

With respect to Chrysler, the President faced a particularly difficult decision. After reviewing the business plan submitted by Chrysler in February 2009, it was clear that the company was weaker than GM – lacking a developed product pipeline or the international reach to compete in an increasingly globalized auto market. As a result, the President determined in March 2009 that Chrysler was not viable as a standalone company.

However, after close and serious deliberation with his team, the President also decided that Chrysler had a chance to achieve viability through a partnership with the international automobile manufacturer Fiat. On April 30, 2009, the President announced that Chrysler had worked with its stakeholders and gained the concessions needed to form this partnership. In order to effectuate the restructuring and alliance with Fiat, Chrysler entered bankruptcy and emerged on June 10, 2009.<sup>4</sup> The President committed to provide adequate working capital to help Chrysler through this restructuring period, including loans to support its restructuring.

*"These are challenging times for America's auto industry and for the American people, but I am confident that, if we as a nation can act with the same sense of shared sacrifice and shared purpose that's been shown by so many of Chrysler's stakeholders, if we can embrace the idea that we're all in it together, from the union hall to the boardroom to the halls of Congress, then we will succeed not only with Chrysler, we will not only see our American auto industry rise again, but we will rebuild our entire economy and make the 21st century another American century."*

- President Obama, April 30, 2009

Since emerging from bankruptcy, this plan and partnership have begun to show impressive results. Chrysler dramatically reduced its structural costs by becoming more efficient and adopting Fiat's new technologies. It has begun to rejuvenate its product lineup, releasing sixteen new or substantially refreshed vehicles (75 percent of its product portfolio) in the last six months. And it has begun to rebuild its brand value by managing consumer and dealer incentives and launching a new advertising campaign, aptly titled, "Imported from Detroit."

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<sup>3</sup> See Mark Zandi, *Testimony before the U.S. Senate Banking Committee, "The State of the Domestic Auto Industry: Part II," Dec. 4, 2008*. The Center for Automotive Research, *"CAR Research Memorandum: The Impact on the U.S. Economy of a Major Contraction of the Detroit Three Automakers,"* Robert E. Scott, *"When Giants Fall: Shutdown of one or more U.S. automakers could eliminate up to 3.3 million U.S. jobs."* These studies estimate the direct and indirect jobs at risk, but do not account for the jobs that would have been created at other firms, like Ford or the domestic plants of foreign automakers, had GM and Chrysler no longer been competing with them.

<sup>4</sup> While the Chrysler bankruptcy received significant media attention, neither the speed nor the substance of the court process was exceptional. As Judge Gonzalez explained, "[t]he sale transaction...is similar to that presented in other cases in which exigent circumstances warrant an expeditious sale of assets prior to confirmation of a plan. The fact that the U.S. government is the primary source of funding does not alter the analysis under bankruptcy law." *In re Chrysler LLC*, 405 B.R. 84, 87 (Bankr. S.D.N.Y. 2009). This judgment was affirmed unanimously by a three-judge panel of the Second Circuit Court of Appeals.

Through April 2011, Chrysler had posted thirteen consecutive months of year-over-year sales gains, with its best sales for the month of April since 2008. As of April 2011, the company had achieved five consecutive quarters of operating profit, and on March 31, 2011, Chrysler realized its first quarter of positive net income since exiting bankruptcy, as its market share continues to recover.

Certainly the company continues to face challenges; its product portfolio still relies heavily on large vehicles and light trucks, and it must prove its ability to overcome past skepticism about its brand and attract and retain customers over the long term. However, with a solid and growing partnership with Fiat, the company's prospects are stronger than they have been in years.

In May 2011, Chrysler repaid its outstanding loans to the U.S. Treasury – a full six years before their scheduled maturity. Chrysler was able to achieve this milestone by accessing the debt markets and raising capital on more favorable terms than the U.S. government loans – another sign of its emerging strength as a private company.

With that repayment, Chrysler had returned \$10.6 billion to the U.S. government, which represents not only a full recovery of the \$8.5 billion committed by the Obama Administration, but also about 50 percent of the \$4 billion provided by the Bush Administration. (The government still holds a small equity position in Chrysler, as well as the right to any additional proceeds received by the Voluntary Employee Benefit Association retiree healthcare trust above a certain threshold.)

## Returning to Profitability and Competitiveness

*Chrysler's nascent turnaround is indicative of a broader resurgence of the American auto industry. For the first time in more than a decade, all three American automakers are profitable; expanding production and jobs; and gaining market share against their competitors.*

In the first quarter of 2011, the auto industry reached an important milestone when all three Detroit automakers posted positive quarterly net profits – for the first time since 2004. GM's first quarter 2011 profit was nearly triple its profit from the same quarter just a year prior; Ford's first quarter 2011 net income marked its best first-quarter performance since 1998 and the company's eighth straight quarterly profit.

This positive financial performance is the result of expanded production and sales. In 2010, GM, Chrysler, and Ford increased their market share from 41.0 percent to 44.4 percent. The last time the Detroit three gained market

*"The Obama administration realizes how important auto jobs are. A country that doesn't build things is in trouble."*

- David Cole, chairman, Center for Automotive Research  
(Detroit News, March 29, 2011)

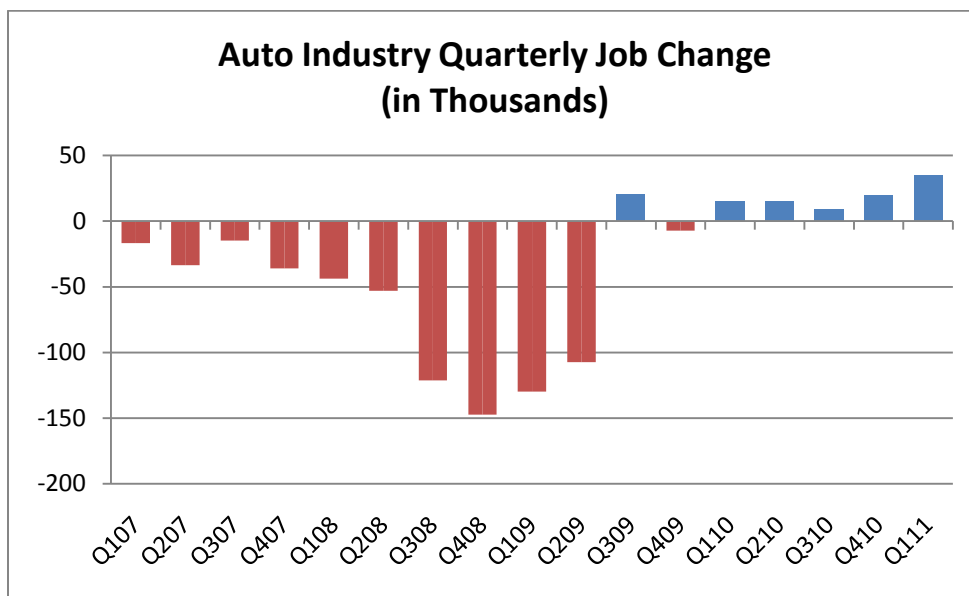
share against their foreign competitors was in 1995. In addition, exports of vehicles and parts from January to May 2010 increased by 57 percent over the same period one year ago. Sales to China are doing particularly well. Within the first five months of 2010, exports of vehicles and parts to China were up 283

percent year-on-year, totaling \$1.85 billion, with overall U.S. exports to China up by 39 percent, totaling \$35.5 billion.

This increase in market share and the expansion of exports, translates into more American jobs. Since GM and Chrysler exited bankruptcy, six GM facilities and two Chrysler plants have added shifts to address growing demand. At GM plants in Kansas, Indiana, Michigan and Ohio these shifts will result in 7,900 new jobs. A second shift at

Chrysler's Jefferson North Assembly plant yielded an additional 1,100 jobs and an additional shift at Sterling Heights added 900 jobs. Last year Ford made a \$400 million investment to convert Chicago's Ford Assembly Plant for production of the 2011 Explorer that was estimated to add 1,200 direct jobs and 600 supplier jobs.

Since GM and Chrysler emerged from bankruptcy in June 2009, they have announced investments totaling over \$8 billion in their U.S. facilities, creating or saving nearly 20,000 jobs. Chrysler recently confirmed its intention to invest an additional \$843 million into its transmission facilities in Kokomo, Indiana, bringing the total investment into the Kokomo community to \$1.1 billion, and retaining nearly 2,250 jobs. GM recently announced that it will invest an additional \$2 billion in U.S. factories in the coming months, creating or preserving more than 4,000 jobs at seventeen facilities in eight states. It is expected that GM will hire back the last of its laid-off workers later this year.



## Strengthening the Supply Chain

*The auto supply chain employs three times as many workers as the automotive companies themselves. A resurgent American automotive sector has strengthened suppliers and stabilized their economic forecasts.*

The auto supply chain, which was also at risk of collapse two years ago as GM and Chrysler faced the prospect of liquidation, is also showing signs of stabilization and resurgence. The automotive supply chain is the backbone of auto manufacturing. Unlike in some industries, there are few auto makers that produce vehicles from start to finish. While it may have made sense in the 1940s for Henry Ford to produce his Model A with a steel mill, glass plant, fabrication, machining and assembly all at his River Rouge plant outside of Detroit, over time as production has become more complex, and the final vehicles became more differentiated, that was no longer the case. Today, there are literally hundreds of suppliers, each with the knowledge, technical expertise, and scale to manage the production of certain components and contribute to the making of a vehicle. This production is associated with many hundreds of thousands of jobs. In fact, auto suppliers employ three times as many workers as the auto makers, and auto dealers employ even more.

Auto suppliers and auto manufacturers are inextricably linked. One cannot do well if the other is doing poorly. During the downturn, when the auto makers were in severe distress, the suppliers were severely distressed, too. Today, it's a different story as the supply base has rebounded to its best shape in over a decade. Since 2009, the supplier base has begun to recover; bankruptcies have dwindled from 59 in 2009, to only a handful in the past year as both automobile manufacturers and the supply chain have stabilized.

In April 2010, the government's Auto Supplier Support Program, which was launched in March 2009 to give suppliers the confidence to continue shipping parts, pay their employees and continue their operations, ended. Both GM and Chrysler repaid their loans from this program in full, including associated interest and fees.

As a sign of its newfound resilience, the supply chain is currently managing through the impact of the Japan earthquake, tsunami, and nuclear crisis; continuing commodity and material pricing pressure; higher oil prices, and sales mix changes, each of which requires significant attention. Further, based on recent industry surveys, 60 percent of suppliers remain optimistic about their prospects in 2011 (up from 45 percent in 2010), and plant utilization rates are expected to increase to 85 percent in 2011-2012 from 75 percent in 2010.<sup>5</sup>

### **Perspective from Chrysler's Toledo Assembly Complex**

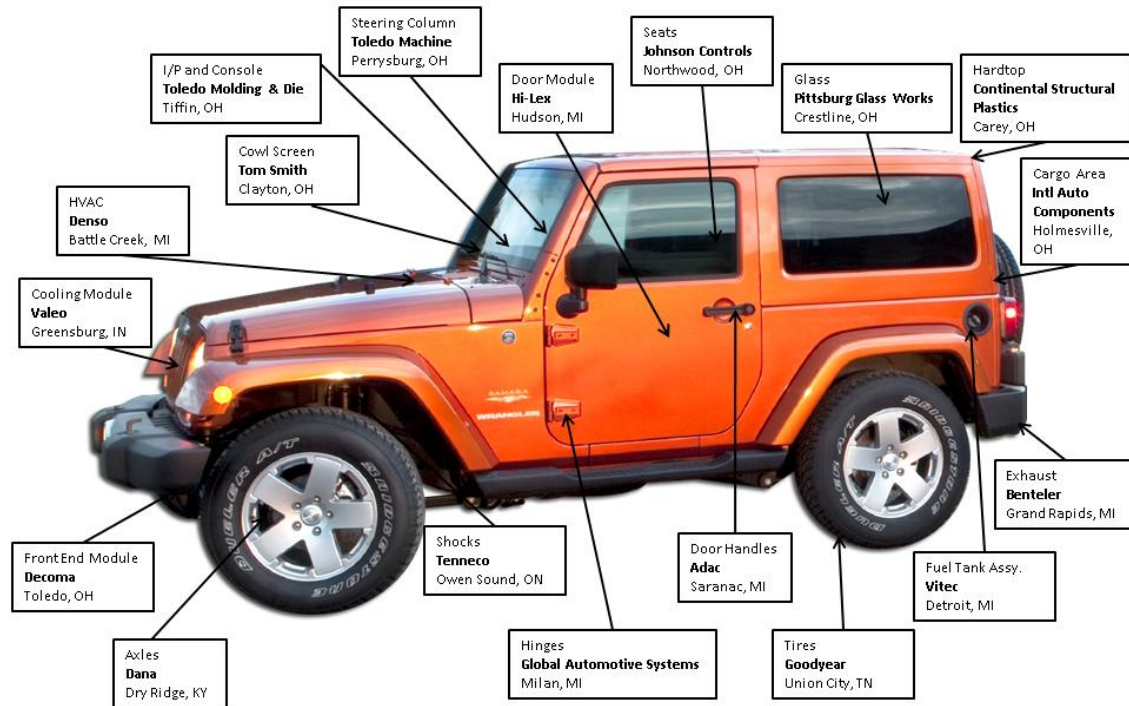
The historic Toledo Assembly plant opened in 1910, with its Stickney and Parkway Annex facilities producing parts for classic American automobiles, such as the Jeep CJ. Two years after Chrysler faced liquidation, the Toledo plant, which produces the 2011 Jeep Wrangler through partnerships with three different suppliers, is an example of how the industry in general, and Chrysler in particular, is emerging leaner, stronger, and with new-found efficiencies. In fact, this facility twice received the Harbour Award as the most efficient assembly plant in North America. The Toledo Assembly plant is able to achieve these efficiencies by locating their major suppliers right next door, providing direct and uninterrupted flows from their assembly lines right into the plant, which reduces downtime so that plant workers do not have to spend time waiting for parts.

The Toledo complex directly employs 2,400 workers and produces 200,000 cars per year with the potential to expand shifts and double output as domestic automotive sales continue to strengthen. Due to the multiplier effect, the plant's success has had positive impacts on its suppliers and resulted in the creation of even more American jobs. For example, over 200 suppliers are responsible for producing the Jeep Wrangler. And Tier 1 suppliers, which provide parts and components for the Toledo complex's Jeep Wrangler, employ 3,000 additional American workers in places like Grand Rapids, Michigan; Dry Ridge, Kentucky; Greensburg, Indiana; and other communities all over the country. Nearby Toledo Molding & Die, which produces instrument panels for the new Jeep Wrangler, employs 115 workers and Johnson Controls Inc., which produces instrument panels for the plant and is located close to the plant, employs 240 workers.

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<sup>5</sup> See "US Auto Supplier Survey Q1 2011," UBS Investment Research, April 11, 2011, and "OESA Automotive Supplier Barometer May 2011," OESA, May 2-4, 2011.

## Tier I Suppliers for the Jeep Wrangler Employ 3,000 American Workers



## Repaying Taxpayers

*The prospect of taxpayer repayment and a faster-than-anticipated exit from government involvement in the industry has improved.*

*"The repayment of loans and interest owed to the United States Treasury and Export Development Canada is a significant milestone in Chrysler's methodical comeback from bankruptcy in 2009."*

- The New York Times, May 25, 2011

The U.S. Government provided a total of \$80 billion to stabilize the U.S. automotive industry through investments in General Motors (GM), Chrysler, Chrysler Financial, Ally Financial, and programs to support automotive suppliers and guarantee warranties. As of today, \$40 billion has been returned to taxpayers. While the government does not

anticipate recovering all of the funds that it invested in the industry, the Treasury's loss estimates have consistently improved – from more than 60 percent in 2009 to less than 20 percent today.

Independent analysts estimate that the Administration's intervention saved the federal government tens of billions of dollars in direct and indirect costs, including transfer payments like unemployment insurance, foregone tax receipts, and costs to state and local governments.<sup>6</sup>

<sup>6</sup> See, e.g.: Center for Automotive Research: The Impact on the U.S. Economy of the Successful Automaker Bankruptcies, November 15, 2010; Economic Policy Institute: Huge Return on Taxpayer Investment – Benefits of the Auto Restructuring Plan Vastly Exceeded the Costs. Issue Brief #290, November 18, 2010.

## Recovery Beyond One Industry: A Tale of Two Cities

*The resurgence of Kokomo and Sterling Heights are snapshots of communities around the country that are being revitalized by the strengthened American automotive industry.*

As the worst financial crisis since the Great Depression impacted the automotive sector, hundreds of workers in Kokomo, Indiana and Sterling Heights, Michigan braced for the worst. After Chrysler declared bankruptcy, the unemployment rate in Kokomo, where a quarter of the community works in the automotive industry, skyrocketed to 20.1percent.<sup>7</sup> As layoffs mounted not only auto workers were impacted, but the entire community. Two years later, both communities are on the mend.

### Kokomo, Indiana

"It's gloom and doom around here." Those were the words of Rick Ward, a union steward at Chrysler's transmission factory in April of 2009. Cliff Pitcher, an electrician for Chrysler added, "We don't know what to expect." Kokomo is officially known as the "City of Firsts", a proud town in America's heartland where the first internal combustion engine was tested and the push button car radio was invented. However, by early 2009, this town of 45,000 in central Indiana, where a quarter of all workers are employed in the automotive sector, was bracing for the worst. As eyes anxiously turned to President Obama's Auto Recovery Task Force, Ward expressed the hopes of the proud city, "We're just hoping it stays open. There aren't a lot of other opportunities here in central Indiana."<sup>8</sup>

By 2010, Kokomo was leading the state of Indiana in new investments, with Chrysler committing upwards of \$1 billion in three new factories that would retain over 2,250 jobs.<sup>9</sup> The inspiring turnaround of Kokomo is a testament to its resilience and the effectiveness of targeted policies to reinvigorate America's automotive sector. Kokomo's unemployment rate has been steadily falling over the past two years, and is now down by nearly 50 percent from its peak.<sup>10</sup> In the first quarter of 2011, Chrysler recorded its first profit since bankruptcy,<sup>11</sup> generating substantial tax revenue for the community of Kokomo.<sup>12</sup> As Kokomo's UAW Local 685 president Rich Boruff put it, "We hit rock bottom. We got down to 3,200 members [at Local 685]. Now we're at 4,200. We've gained a thousand new members, we've got new product, and business is booming."<sup>13</sup>

As Kokomo's automotive industry rebounded, several businesses decided to invest in new operations in the city,

*"If the bailout hadn't come, then we'd be a ghost town."*

- Jeff Newton, a local Kokomo Pastor

including manufacturers Westwind Wood Specialties, Delphi Electronics and Safety, Electronic Support Services, engineering firm Neupath, as well as Federal Express and others.<sup>14</sup> Jeff Newton, a local Kokomo pastor who runs a network of community food pantries

stated, "If the bailout hadn't come, then we'd be a ghost town." With a healthier automotive sector, the town launched a new riverfront initiative and spurred the development of thirteen new downtown businesses in 2010. One father and son pair, Steve and Blake Kinder, used financing from the Small Business Administration to open a

<sup>7</sup> Bureau of Labor Statistics, Local Area Unemployment Statistics, Kokomo, IN, June 2009

<sup>8</sup> 'Gloom and doom' for auto workers in Kokomo, IN, CNN Money, 4/22/09

<sup>9</sup> "Once 'dying,' Kokomo shows it's the comeback city", The Associated Press State & Local Wire, 5/14/11

<sup>10</sup> Bureau of Labor Statistics, Local Area Unemployment Statistics, Kokomo, IN, March 2011

<sup>11</sup> "Chrysler turns first profit since bankruptcy", The Associated Press, 5/2/11

<sup>12</sup> "Chrysler makes \$10.4M property tax payment", Kokomo Tribune, 5/14/11

<sup>13</sup> "Chrysler investment grows another \$85M", Kokomo Tribune, 12/14/10

<sup>14</sup> "Once 'dying,' Kokomo shows it's the comeback city", The Associated Press State & Local Wire, 5/14/11



new local pub. Blake remarked, “The mood has definitely risen. People are starting to feel more comfortable about Kokomo’s future.”<sup>15</sup>

## Sterling Heights, Michigan

Just outside of Detroit, workers at the Sterling Heights Assembly plant anxiously awaited news regarding the future of Chrysler, the city’s largest taxpayer and third-largest employer. As the financial crisis unfolded across the country in early 2009, residents of cities like Sterling Heights worried that the ripple effects of faltering American automakers would be felt broadly by shopkeepers, merchants, and businesses across town.

Today, in Sterling Heights a strong recovery is underway. Chrysler has invested \$1 billion in new equipment and tooling to make new midsize cars at the Sterling Heights Assembly Plant, and added a second shift of 900 workers.<sup>16</sup> A longtime plant employee expressed optimism, saying, “We’ve got some wonderful things going on there. I can see a light at the end of the tunnel.”<sup>17</sup> Beyond autoworkers, the resurgence is impacting businesses across the community with automotive parts manufacturers expected to add nearly 500 new jobs.<sup>18</sup> The steps to retool the American automotive industry are still felt in communities across the country.

For the first time in over two years, Punch Tech, a sheet metal machine company in Marysville, Michigan, is running overtime shifts. Reflecting on the automotive recovery efforts, Phil Leonard, Punch Tech’s plant manager put it simply, “[Without it] we wouldn’t be here.”<sup>19</sup> As new businesses grow and the economy rebounds, the recovery of Sterling Heights is a testament to the resiliency of American workers and their ability to compete in the globalized economy.

## Conclusion

*The actions taken by this Administration have laid the foundation for manufacturing’s quiet resurgence, but we cannot be complacent.*

Over the past 12 months, what has happened in the auto industry is part of a larger story about the positive momentum in the manufacturing sector for the first time in a decade. Manufacturing has quietly led the recovery, adding over 250,000 jobs since December 2009, the first time the manufacturing sector has added jobs since 1998. Companies are actively talking about ‘in-sourcing’ their manufacturing production for the first time in recent memory. Whether those companies are headquartered in the U.S. or abroad, by investing in manufacturing capacity and new equipment, they are demonstrating the attractiveness of operating and producing goods here in the United States. While this is undoubtedly good news, much more needs to be done.

The actions taken by this Administration have laid the foundation for manufacturing’s quiet resurgence, but we cannot be complacent.

That is why Congress must take action to build on our early momentum. The Administration has outlined an agenda to support growth, job creation, and competitiveness in U.S. manufacturing. This agenda includes investing in a 21st century infrastructure, making the R&E tax credit permanent, reauthorizing the Clean Energy

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<sup>15</sup> “Auto Industry Bailout Pulls Kokomo Back From Brink”, The Associated Press, 11/22/10

<sup>16</sup> “Big 3 to invest \$2B in Michigan”, The Detroit News, 10/26/10

<sup>17</sup> “Chrysler to Add 900 Jobs to Midsize-Car Plant”, The Associated Press, 07/30/10

<sup>18</sup> “Chrysler: Sterling Heights plant stays open”, Times Herald (Port Huron, MI), 7/31/10

<sup>19</sup> “Chrysler: Sterling Heights plant stays open”, Times Herald (Port Huron, MI), 7/31/10

Manufacturing Tax Credit, passing patent reform, increasing our efforts in STEM education, and supporting continued investments in clean energy and advanced manufacturing. There is no time to waste.