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Labour Costs and the Future of North America's Auto Industry

Jim Stanford

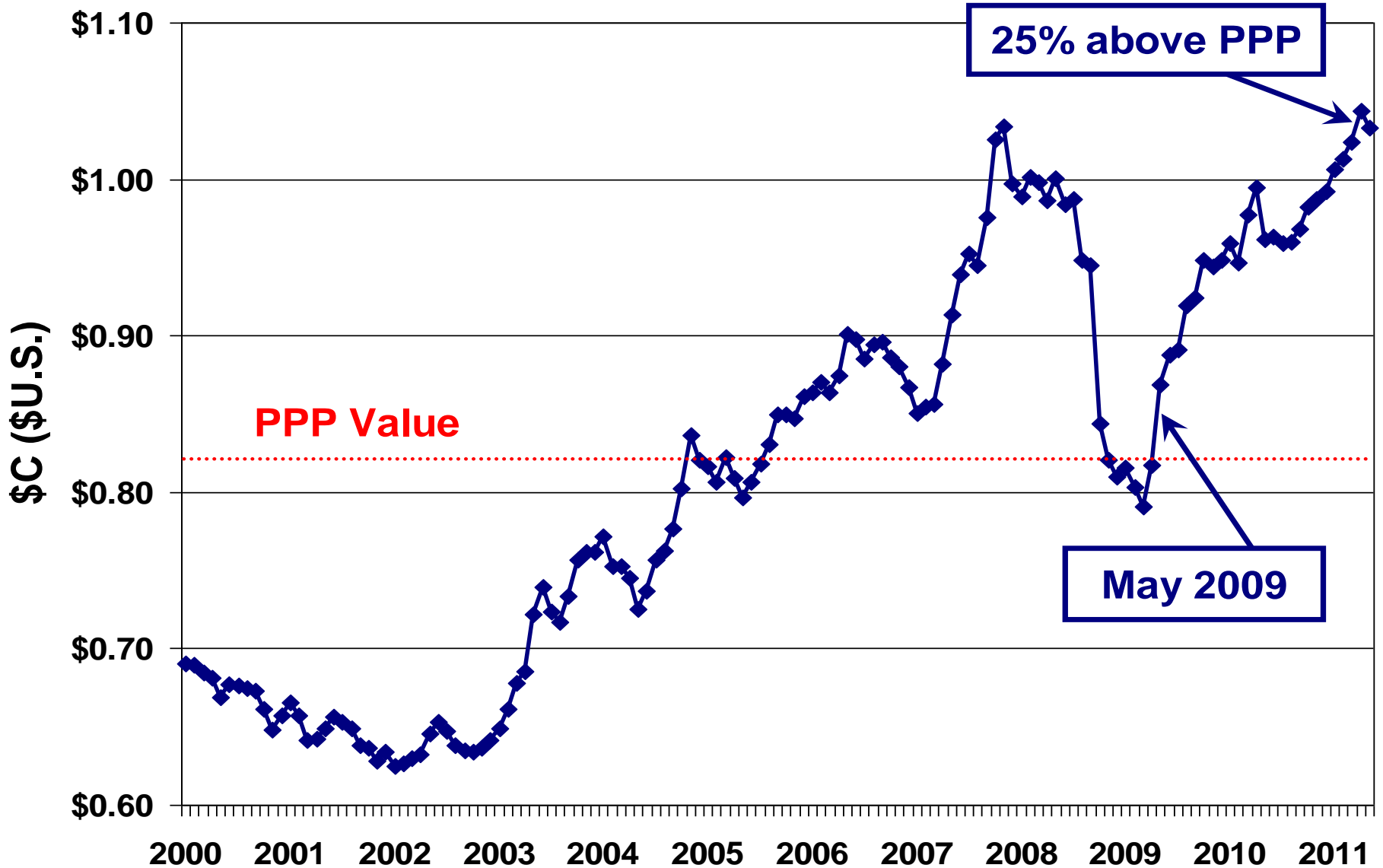
Economist, CAW-Canada

To CAR Management Seminar, August 2011

Automotive Labour Costs: A Canadian Twist

- CAW founded in 1985.
- Membership up 50% since then.
- Egalitarian philosophical approach, but with commitment to a viable, productive industry.
- Record of innovation in labour relations:
 - CAMI, 3-shift, M80, Magna FFA, WCM
- Canadian productivity advantage $\approx 10\%$.
- More activist policy context.
 - Auto Pact, higher PITs, health care (\$5/hr)
- Different currency (volatile).

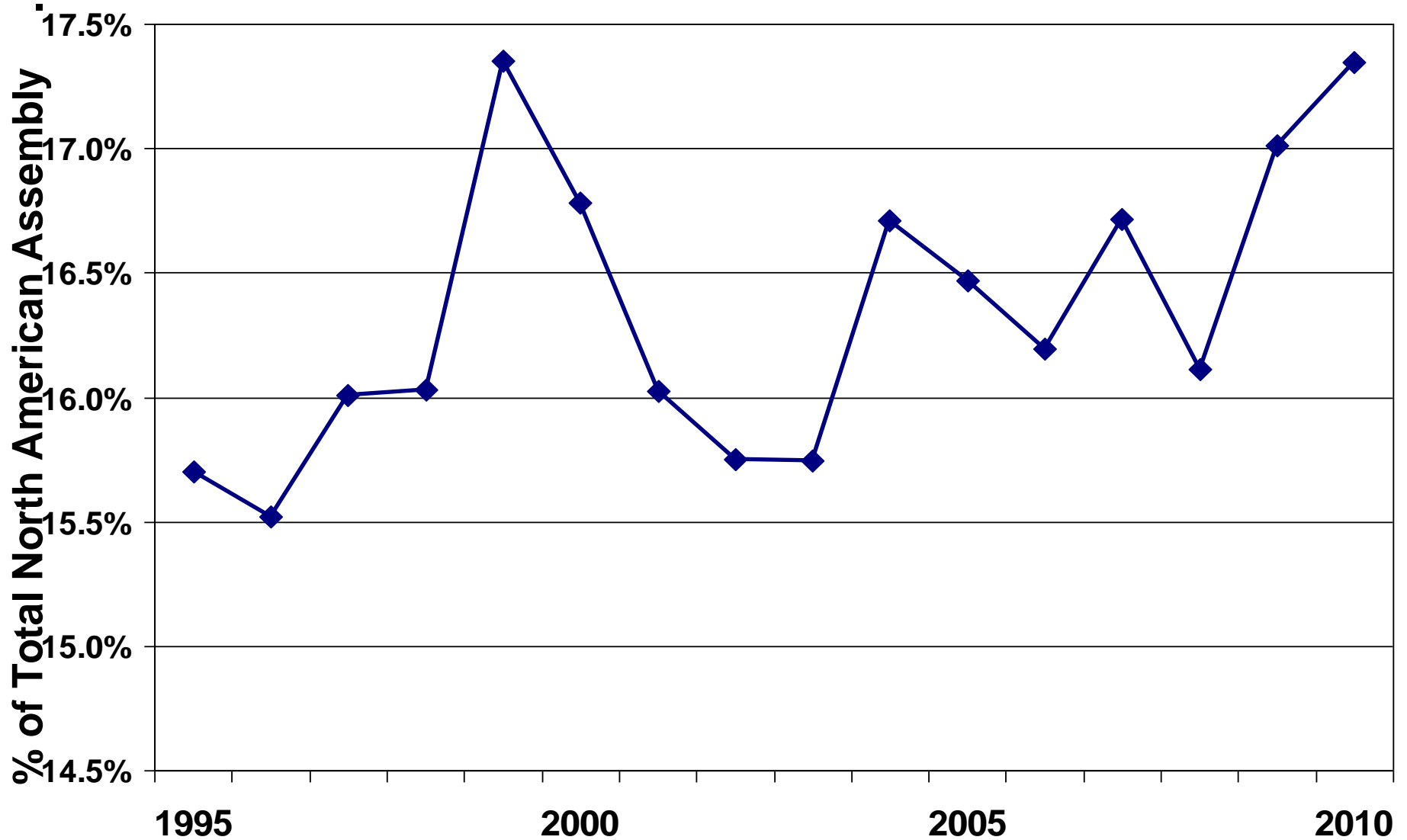
The Loonie Then and Now



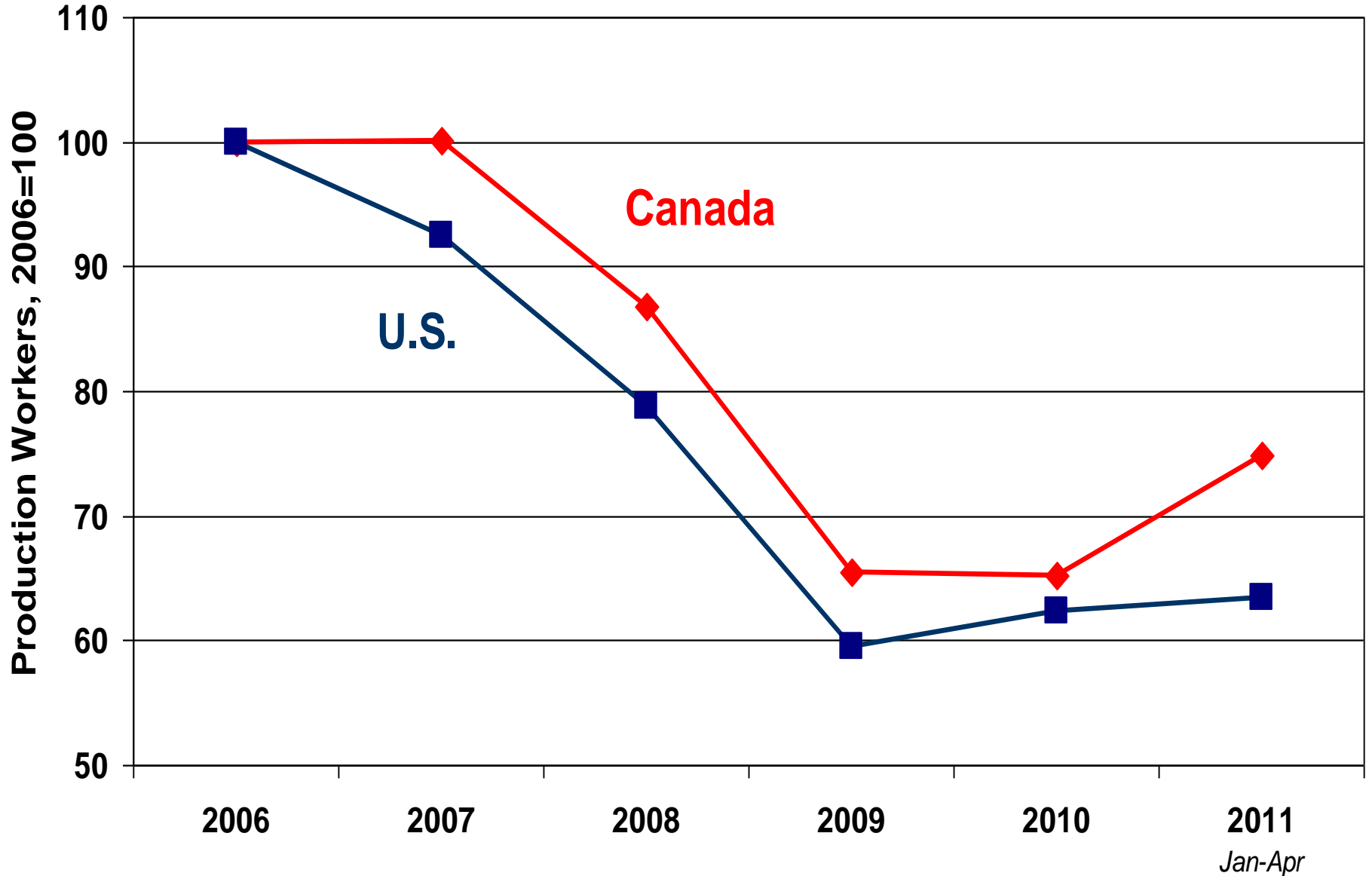
The 2009 Restructuring: North of the Border

- Canadian/Ontario governments contributed proportionately to the binational rescue.
 - Proportional to Canadian share of output.
- GM and Chrysler avoided CCAA ("Chapter 11").
- "Target" for labour costs: \$57 (Cdn.).
- Formation of Canadian Health Care Trusts.
- Canadian "footprint" commitments.
- Canadian production & employment shares grew.
- CAW contracts expire Sept. 2012.

Canadian Assembly Share



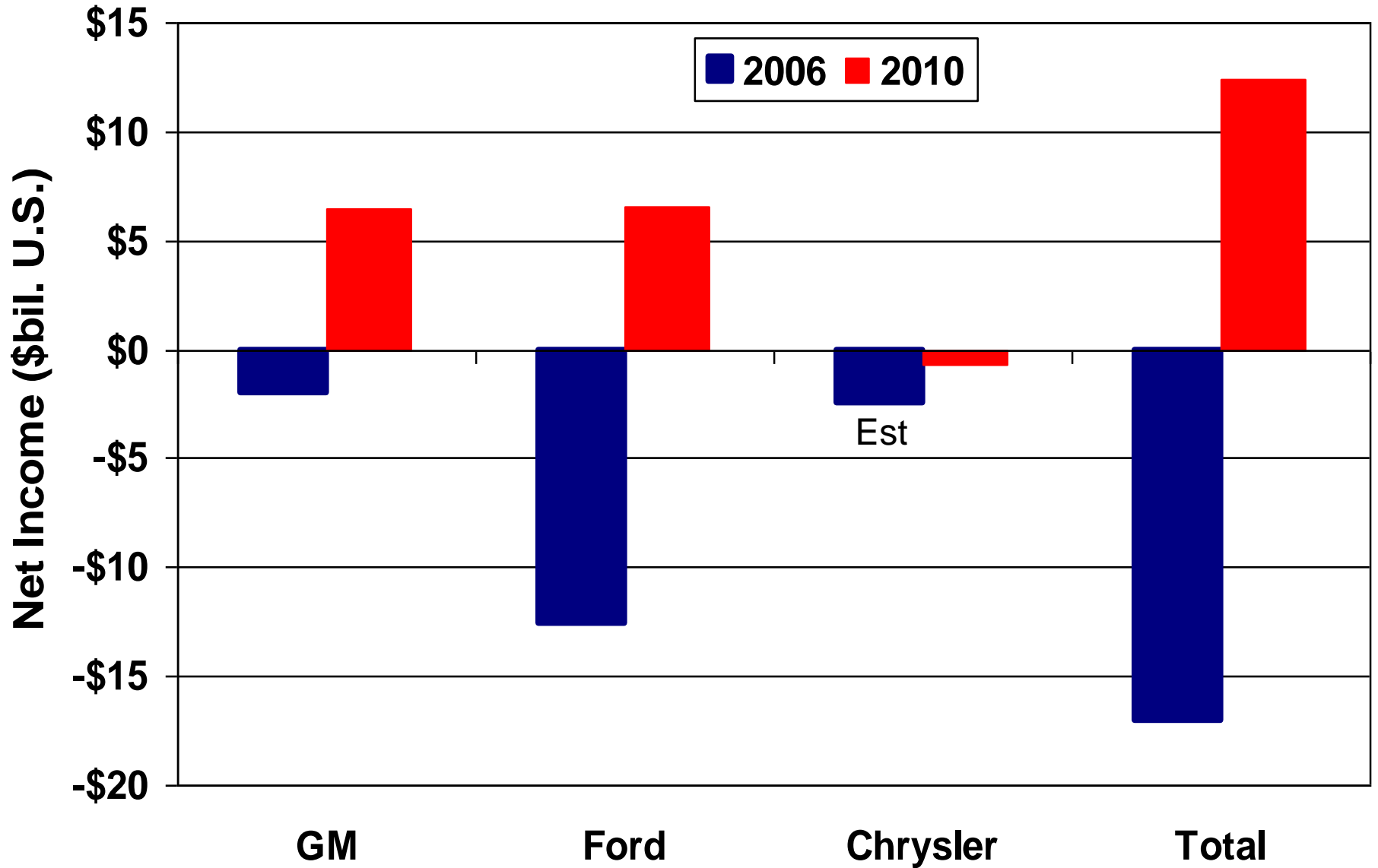
Employment Index: Assembly



Labour Costs in Context

- Widespread assumption: Detroit 3 recovered because they cut labour costs.
- "We can't go back to our bad old ways."
- Misdiagnosed problem → false solutions.
- Other things happened:
 - Shrinking of the overall market.
 - Higher unit revenues.
 - Lower interest charges.
 - Capacity & overhead downsizing.
- Need to understand labour costs and contract talks in context.

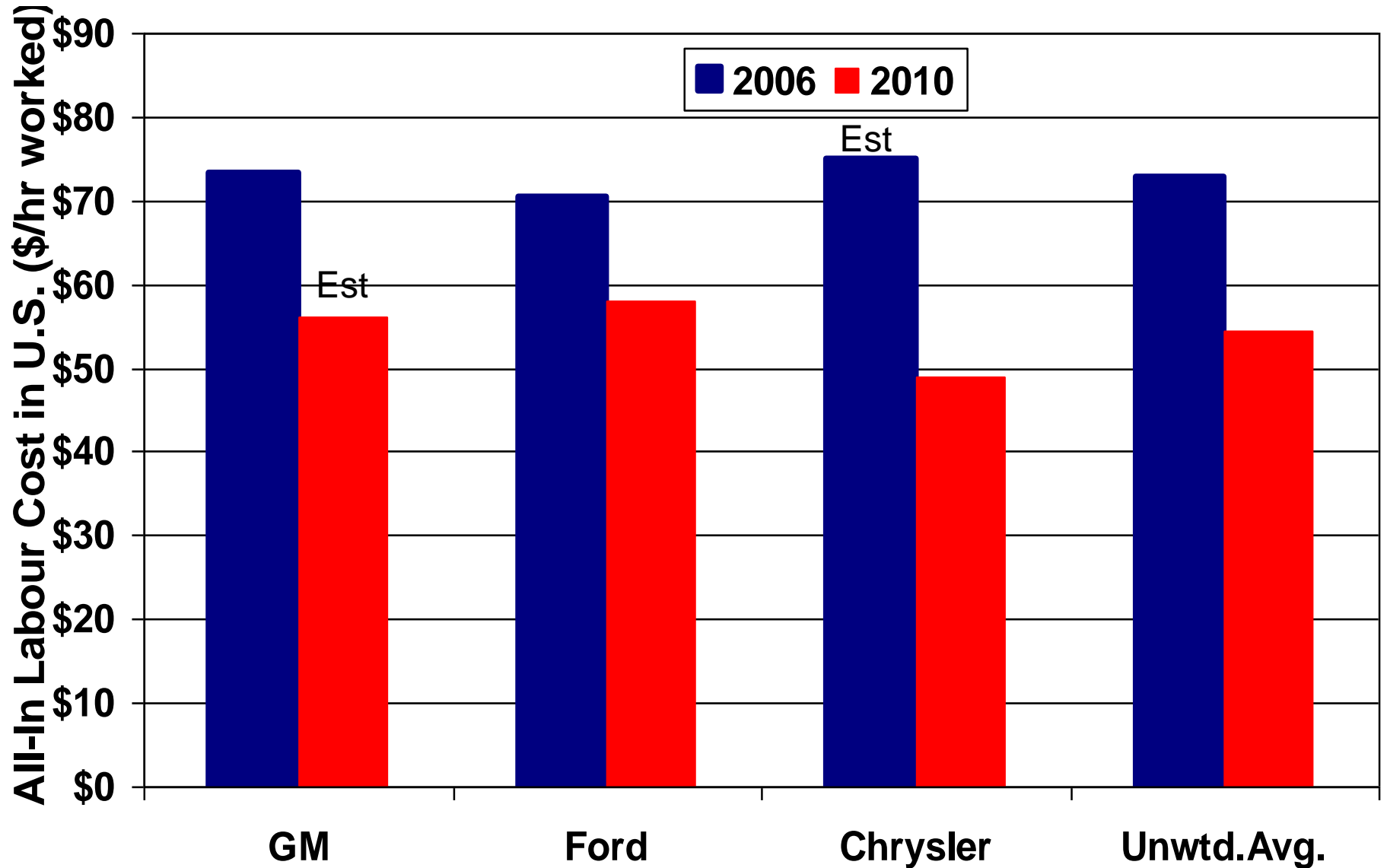
Net Income



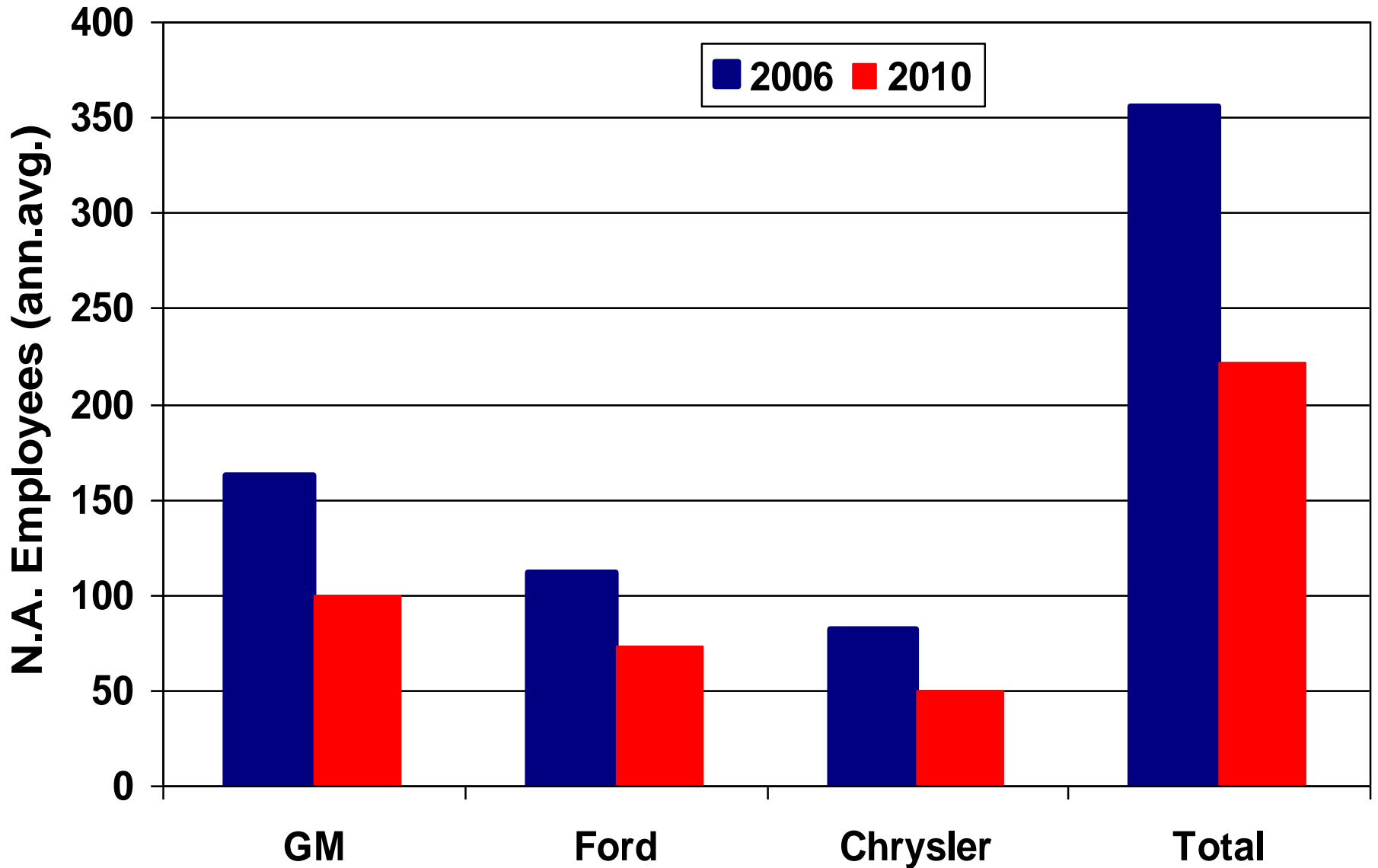
All-In Hourly Labour Costs: Use With Caution

- Subject to major methodological issues.
- Fluctuations in hours worked cause large changes in hourly value of fixed costs.
- Inclusion of statutory costs, income security charges, and other elements creates a wedge between cost and "compensation."
- Legacy cost categories very volatile:
 - Assumptions, experience, amortization.
- See CAW publication for more discussion:
 - *"How Much do Autoworkers Really Make?"* April 2009

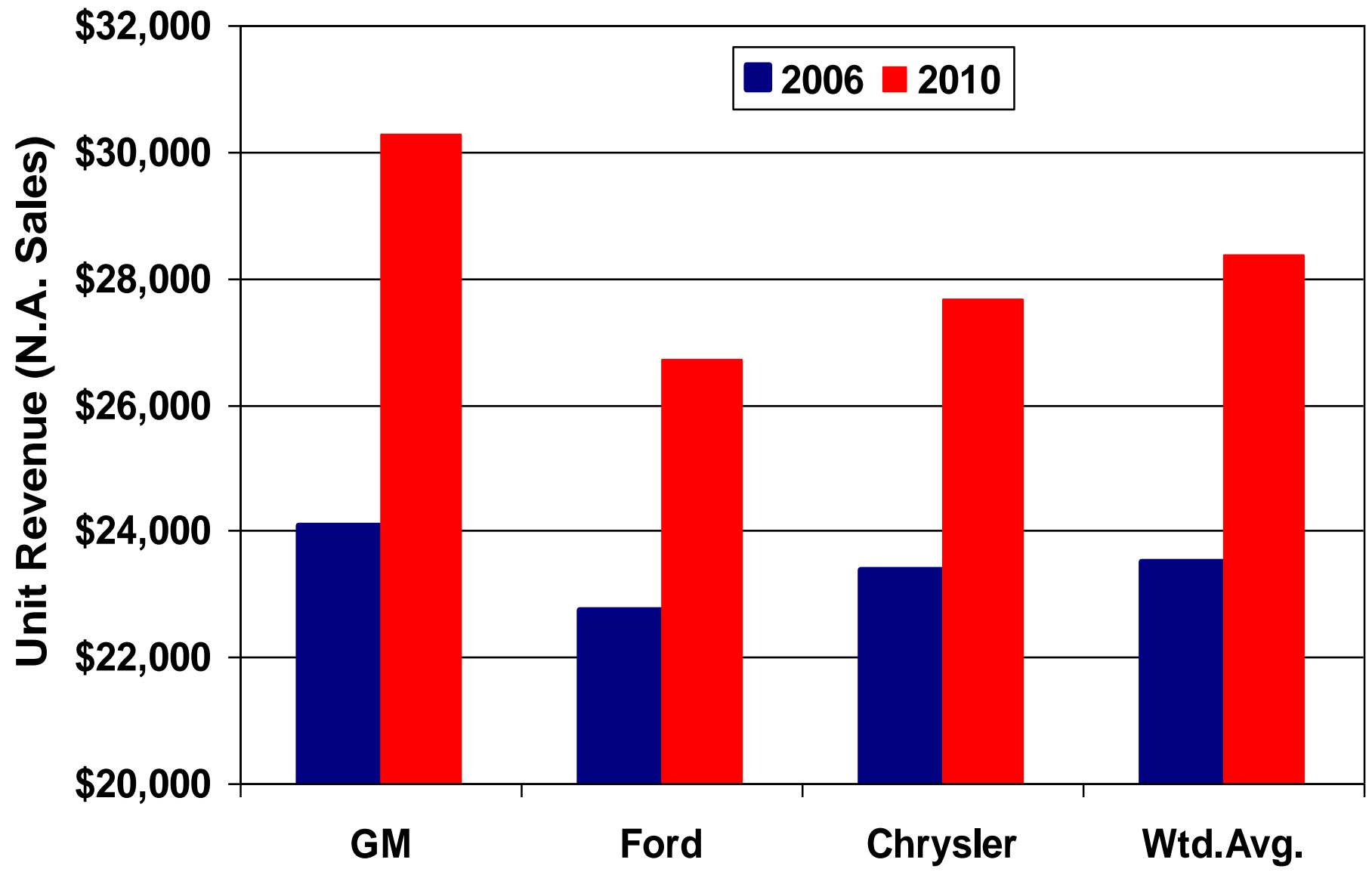
Hourly Labour Cost



Total Employment (N.A.)



Unit Revenues (N.A.)



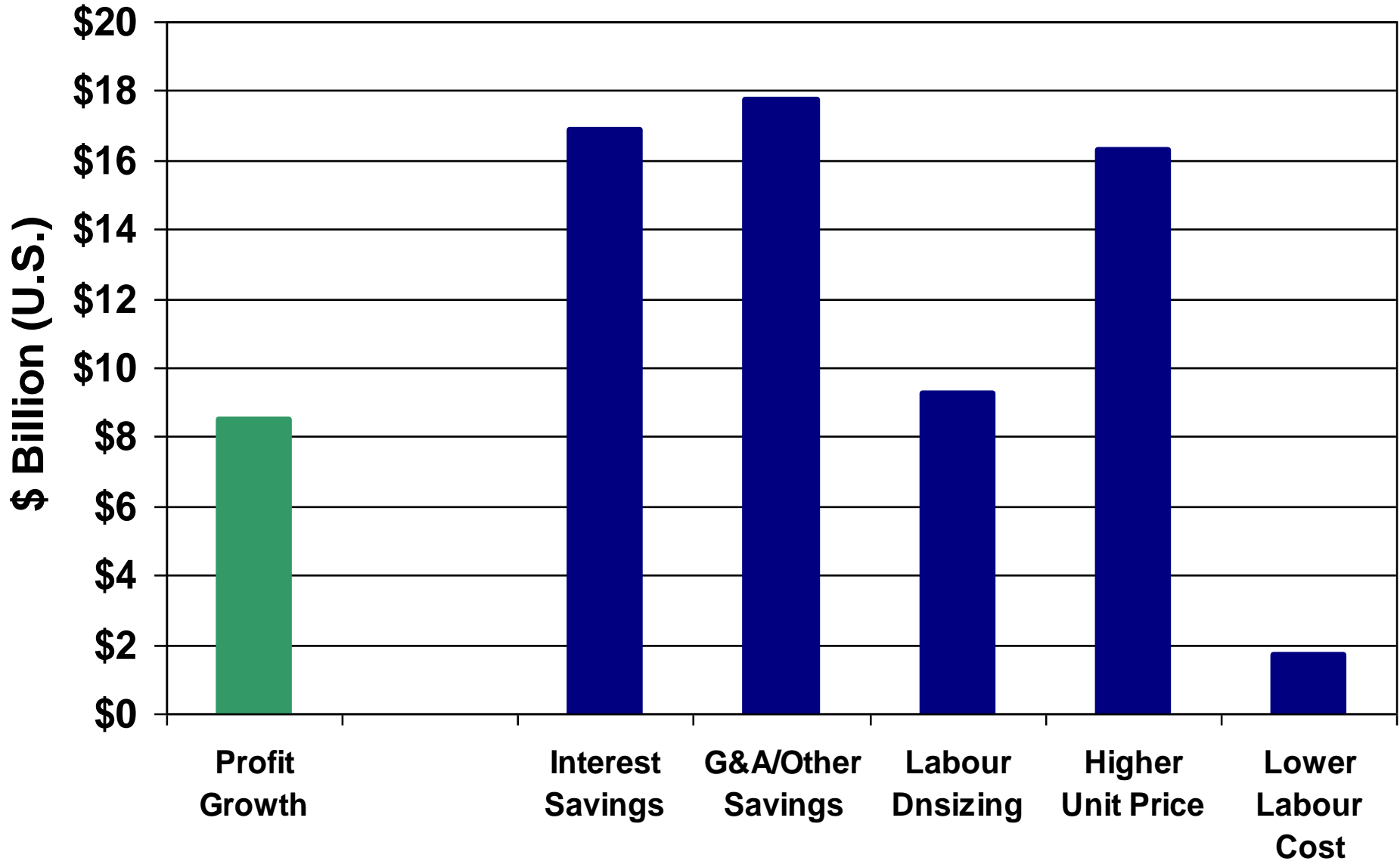
Labour Cost Savings

- Average (unwtd) hourly saving: \$18.50.
- Heroic assumption: apply to entire NA workforce (220,000).
 - Upper bound: \$8 billion.
- Don't forget the VEBAs: Cost shifting.
 - Amortize over 15 years.
- Net saving: \$4-5 billion.
 - 2% of North American revenues (upper bound).
 - Biggest at Chrysler, smallest at Ford.
- Labour cost savings were the least important factor in the companies' survival.

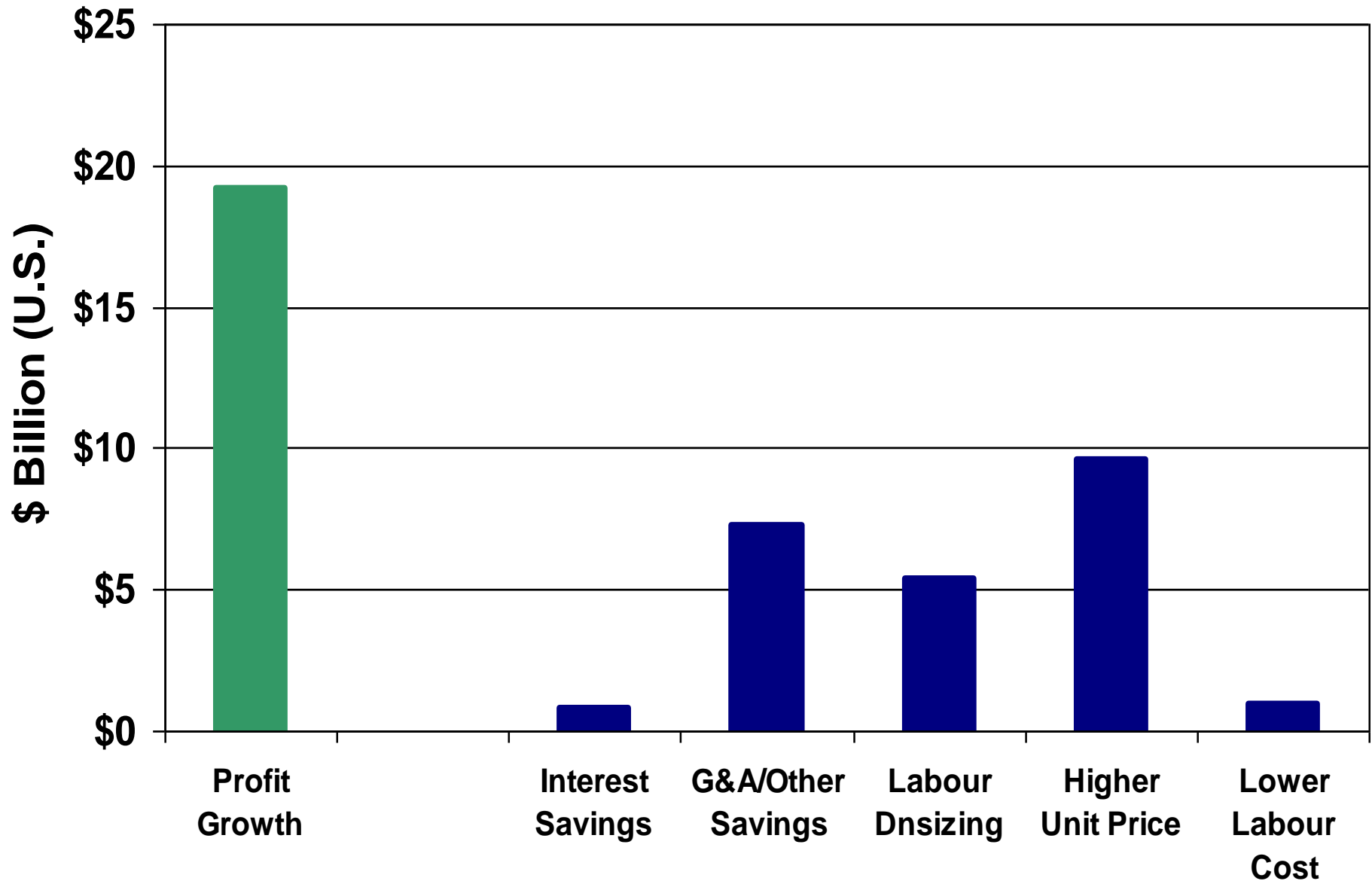
Financial Analysis

- Compare income statements from 2006 and 2010.
- Combined improvement in net income: almost \$30 billion.
- Identify some major sources of saving directly (unit revenues, interest, G&A).
- Hourly labour cost and employment downsizing estimated on basis of hourly cost data.
- Chrysler data incomplete.

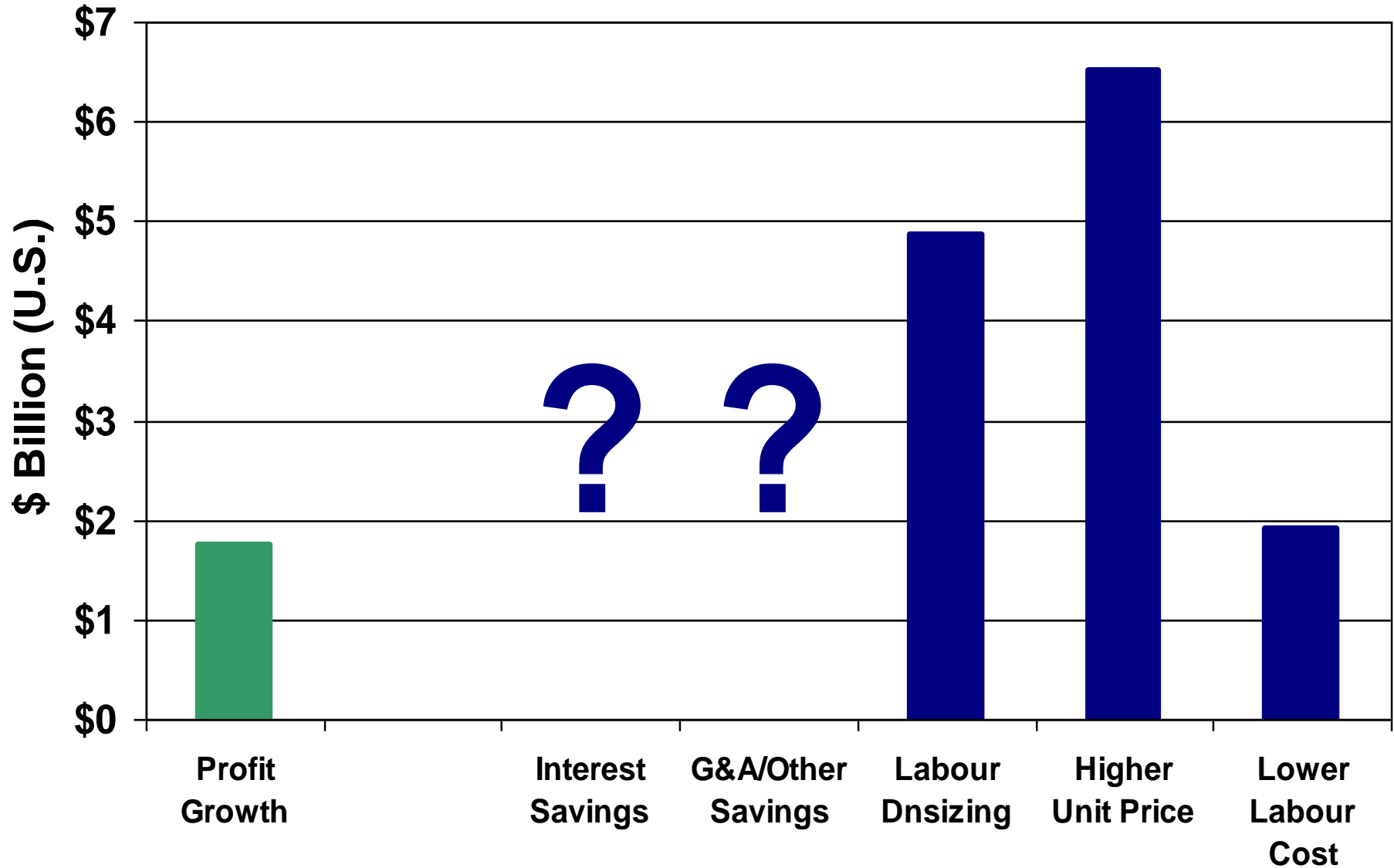
G.M. Improvements



Ford Improvements



Chrysler Improvements



Real Reasons for Recovery

- Product, product, product.
- "A revenue problem, not a cost problem."
- Discipline on incentives, leases, fleets.
- Relaxation of international pressure.
- Restructuring of debt (esp. GM).
- Downsizing to meet capacity (both hourly and G&A).
- All swimming against the tide of smaller scale.

Consumer Reports

Chrysler gets 3 "very goods" (Durango, Charger, Town & Country).

Honda Civic no longer recommended.

Dollar-Yen Exchange Rate

JPY/USD

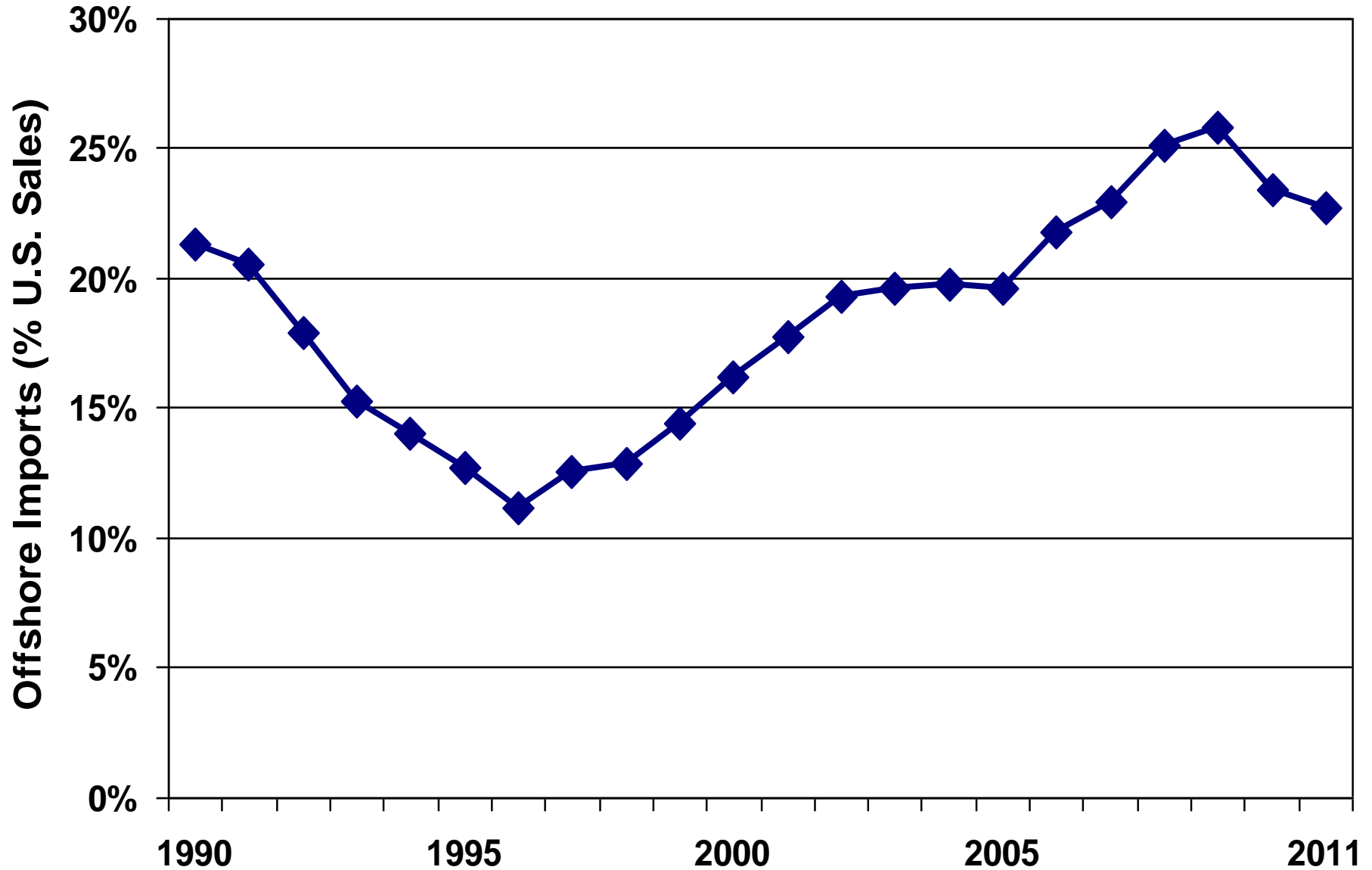
■ JPYUSD=X

Aug 01, 2011



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U.S. Offshore Imports



Conclusion

- "7% of the cost, 99% of the attention."
- Conclusion that labour cost cuts explain Detroit 3 recovery is wrong, misguides strategy by both companies & government.
- Equalizing labour costs to (certain) U.S. transplants does not make Detroit 3 competitive.
 - Certain U.S. transplants are not the benchmark
 - Labour costs are not the key indicator.
- Other actions (by both business and policy) are needed to keep the recovery going.
- Undue focus on labour costs will end in disappointment.



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