

THE CHRYSLER RESCUE

(Note by the Research Department)

Background

1. The demand for motor cars both in Britain and our producers' major export markets - principally Europe - has fallen dramatically, and will take several years (1980?) even to regain the level of its previous peak in 1972/3.
2. Overseas conditions are creating more and more competition for all European car producers. Japan, Spain, Brasil and now Korea and Iran are well down the road to becoming major exporters, both to our traditional overseas markets and to Europe itself. The American manufacturers and the Japanese are taking steps which together make it unlikely that we can expect to sell significantly more cars in North America than we so now.
3. European car manufacturers are operating at not much over two thirds of full capacity today. Even if there is no further expansion of their capacity over the next decade the level of demand and likely sales are such that capacity utilisation will improve only very slowly over the next decade and might well be at levels that are still scarcely profitable at the end of it.
4. It follows that all European motor producers face a long period of most challenging and ruthless competition both at home and overseas. Only those which are strongest today and which are swift and ruthless in rationalising their operations and improving their competitiveness will survive.
5. The British producers - all of them - are amongst the weakest internationally on any measure:
 - number of models produced in economic numbers
 - number of models in the most important market segments
 - quality and after sales reputation
 - price and delivery record
 - number and organisation of plants
 - return on capital and balance sheet strength
 - level and rate of improvement of output and productivity (probably actually negative over recent years)
 - overmanning and output per man
6. Paradoxically shortage of up-to-date plant and machinery is not responsible for most of these weaknesses. For the basic economic reasons already cited a fully competitive British industry would be smaller and concentrated on a much smaller number of plants and models. But although many jobs would be lost, those remaining in employment would be ensuring that the industry's contribution to the economy would be as big as or bigger than it is now, in terms of domestic sales, exports and imports resisted.
7. For the situation to be remedied several things must be done
 - (a) The country must cease to look for alibis in "deindustrialisation" and "underinvestment";

- (b) The Government must give determined and committed leadership to explain the facts; to engineer the consent and commitment of management and unions throughout the industry to the changes that are needed.
- (c) In its dealings with those parts of the industry in which it has a stake it must aim at realistic objectives and ensure that the methods adopted in the pursuit of these objectives are sound.

8. The Government's decision to bail out Chrysler, recent events at British Leyland, the publication of the C.P.R.S. report on the future of the Motor Industry in the U.K. and the imminent debate involve not merely an isolated decision about a single firm. They define the way Ministers are developing a strategy for the motor industry and are a clear pointer to the future of their industrial strategy as a whole.

9. Their actions appear to involve:

- (a) no attempt to dispel the damaging alibis which hinder an attack on the industry's real problems;
- (b) no leadership and no attempt to explain the facts, of which a quite critical example is their refusal to publish the C.P.R.S. study;
- (c) a frighteningly feeble start to the reconstruction of British Leyland;
- (d) even more damaging proposals for rescuing Chrysler.

These general propositions are amplified in the rest of this note.

1. The British producers - all of them - are against the westward internationalisation on any measure:

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2. Paradoxically shortage of up-to-date plant and machinery is not responsible for most of these weaknesses. For the basic economic reasons already cited a fully competitive British industry would be smaller and concentrated on a much smaller number of plants and models. But although many jobs would be lost, those remaining in employment would be ensuring that the industry's contribution to the economy would be as big as or bigger than it is now, in terms of domestic sales, exports and imports retained.

3. For the situation to be remedied several things must be done:

- (a) The country must cease to look for alibis in "structural-lack" and "underinvestment";

BRITISH LEYLAND

9. The reconstruction plan for British Leyland is at best extravagantly optimistic and unlikely to produce a commercially viable firm when it is completed. For it to work, even on its own terms, the Government and NEB should have started immediately to set out the targets and objectives of the Ryder strategy to the whole labour force and to develop the machinery for worker consultation/participation required if their consent and co-operation was to be assured. They should have made it quite clear months ago that the Ryder plan for capital expenditure was not to be implemented unless there was an immediate improvement in production and productivity, a reduction in disputes and stoppages and a constructive response to measures to reduce costs. No such commitments have been extracted and none of the immediately and urgently needed changes has taken place. The isolated, belated and sudden steps taken by Lord Ryder and British Leyland's management a few days ago give the appearance of being naive, incompetent and ill-prepared, however well-intended.
10. Meanwhile time is passing. Before long almost all the major commitments on capital spending will have to be made. Yet on present prospects it appears probable that the expenditure will be committed without any improvement in performance or even undertakings about such improvements from labour and management.
11. So even before the Government's decision to help Chrysler, its strategy for the industry was not merely highly questionable but simply not being pursued properly. There was every likelihood that its actions would preserve a car industry which was, as in the past, too large and inefficient and bound to have to be rationalised sooner or later on a vast and painful scale.

THE CHRYSLER PROPOSALS

12. The broad outline of the agreement between the Government and Chrysler is believed to be fairly accurately recorded on page 45 of the Sunday Times Business News of December 15th. Put very briefly, the Government will:
- finance losses of up to £72.5 m. over the next 4 years, some of which will be matched by Chrysler;
 - underwrite £35 m. of working capital from FFI (if FFI agrees) and about £28 m. of money from other sources;
 - share profits 50/50 with Chrysler up to 1979 (if there are any) and on a token basis thereafter;
- For its part Chrysler will:
- split losses 50/50 with the Government over the next four years above the first £40 m., which the Government will meet on its own;
 - jointly guarantee the £35 m. FFI loan with the Government;

- underwrite £27 m. of capital investment in the first two years;
- move Avenger assembly to Linwood from Ryton (Coventry);
- probably begin assembly of a Simca car at Ryton;
- (presumably) sustain the Iran export orders.

13. By agreeing to finance Chrysler's losses the Government have in effect agreed to finance the cost of making redundant 8,000 men (about a third of the labour force). They have permitted Chrysler to escape from the double embarrassment of renegeing on their contract with Iran and shutting down their UK operations in a brutal and abrupt manner which could well have had the most serious implications for their future operations world wide. Indeed now Chrysler may well be in the desirable position of having a two-way option. There is nothing to stop them gently running Chrysler (UK) down, largely at the taxpayers' expense if the new plan does not work. On the other hand, if it does work they have engineered a painful and expensive process of rehabilitation at relatively small political and economic cost to themselves. Having retained the equity, they will enjoy nearly all the profits which might ultimately be made.

14. It is significant that all the many proposals for rescuing Chrysler appear to have been turned down by the Industrial Development Advisory Board of the Department of Industry; and that the NEB neither want nor are being asked to take Chrysler under their wing.

15. It is understood that the deal will be cemented in a planning agreement of some kind. Whether this will turn out to be binding in theory or practice is unclear but doubtful. Mr Varley will be seeing the National Union leaders today (December 16th) to discuss and secure their consent to the redundancies and other matters involved, and this consent may already have been secured in all but name. However, it is scarcely likely that the local union leadership will acquiesce in 8,000 redundancies without stern resistance (sit-ins and work-ins?), particularly in the Stoke, Ryton (and Maidstone?) plants which are to lose the employment and suffer the transference of work to Linwood.

16. Amongst the factors which must have induced the Government to accept these proposals are:

- (1) The compelling electoral case for saving Linwood;
- (2) The feeling that it is worth saving Chrysler in order to secure the benefits of North Sea oil;
- (3) The high cost to the public purse of total closure (Michael Foot is said to have quoted a figure of £100 m.);
- (4) Growing union anxiety about the effect of current and future unemployment levels and, on top of that, a Chrysler closure on the fate of the £3 limit;

- (5) the effect of a closure on imports, combined with the Chancellor's recent late-night pledge to Mr Witteveen not to put import controls on cars and the wider repercussions of resorting to such controls.

Comments on the Proposals

17. Assuming that the scheme finally announced corresponds fairly closely with what is set out above, most or all of the following points can be made about it.
18. Mishandling and Incompetence. The Government were unpardonably slow in waking up to the hopelessness of Chrysler's situation, although most of the important facts must have been clear by the late summer. They then conducted the negotiations with remarkable incompetence, marked by a cascade of growing leaks of all kinds and open disagreement between members of the Cabinet. It is not surprising that Chrysler seem to have made fools of them and driven a most advantageous bargain for themselves.
19. Effect on overseas opinion. It is impossible to see how our Friends and competitors can be anything other than critical of the deal and acutely anxious about the Government's firmness of purpose in any aspect of its economic policy. Sterling holders of all kinds may well show their feelings soon and push the £/\$ exchange rate below $\$2 = \pounds 1$.
20. Public Spending. The deal must involve a significant increase in public spending. If it is not offset in other policy changes, the Borrowing Requirement (and contingent liabilities) of HMG will obviously be raised directly. If it is offset, then the whole rationale of the manoeuvre as job-preservation falls completely to the ground. For either taxes must be commensurately increased, reducing demand production and employment throughout the economy; or spending on other Government projects, not least other assistance to industry, will be cut. In either case unemployment will be created, mounting in time to an increase as large as or larger than the job losses avoided in saving Chrysler itself.
21. An expensive deal
It is immensely difficult to give a fair or accurate assessment of the cost to the exchequer or taxpayer of jobs (or job-years) saved in such a rescue. However, it appears that the Government might have to spend up to £140 m., if the scheme ultimately fails, in order to save 15,000 or so jobs for a few years - a cost of £10,000 per job. This appears a very high figure, particularly when compared either with straightforward investment assistance like the recent schemes for Foundries and Textiles, or even the Temporary Employment subsidy and the other recent "non-Keynesian" job-saving measures of which the Government are so proud.
22. Empty undertakings
It seems very probable that the Government will have failed to extract satisfactory undertakings from either Chrysler or the labour force. It is of central importance both to the Ryder proposals or any other such rescue that

the labour force should give time and clear commitment and consent to the changes that are needed before cash help and investment decisions are finally agreed. In this case both cash and investment decisions seem to be irrevocable and yet it remains open to the workers to continue to behave as they choose, and as they have done in the past.

23. Aggravation of UK motor industry prospects

The rescue seems to be undesirable since it

- increases rather than reduces the number of models manufactured in the UK;
- shifts production in Chrysler away from the economic south to the less economic north;
- preserves excess capacity and thus helps keep production of other UK producers further below economic volume than would otherwise be the case. This will probably increase import competition in the long run, not reduce it.

24. Dangerous consequences for other UK motor producers

A strengthened and heavily subsidised Chrysler spells trouble for all our remaining producers. It may well undermine at least some parts of the Ryder plan for British Leyland. It could provoke General Motors to consider abandoning car production in the UK completely, to apply to the Government for comparable help or to do both as Chrysler itself has done. The prospect of two and perhaps before long even three heavily subsidised competitors is not calculated to encourage our only reasonably competitive producer, Ford. In particular the Labour force throughout the motor industry will find it less easy to believe that their interests are best served by changing their ways.

25. Dangerous precedent for other sectors

The rescue could be immensely damaging to the position of firms in other sectors where employment is currently too high. One could imagine trouble in other multi-nationals, steel (where the Corporation is rumoured to be looking for £170 m. savings at the cost of 40,000 jobs), shipbuilding (where work prospects are deteriorating very quickly), British Rail and, perhaps, parts of the aircraft industry. There are indications that steel and rail union leaders have already taken steps to put pressure on the Government to help them equally generously.

26. Government economic strategy made absurd

The inconsistencies with the Chequers strategy of November 5th are self-evident, and the task of sustaining a sensible industrial strategy must be much complicated henceforward. But it can be argued that the Government's overall economic strategy has also been damaged badly, since it has been shown to be dangerously vulnerable to crude, short-run, tactical pressures, particularly when Cabinet unity and collective responsibility are not being sustained.

27. Tragic opportunity being missed?

If these forebodings are by and large correct, then the Government may well have missed a major opportunity. For it appears that the problems of the UK motor industry are not irremediable. In particular it is not as under-capitalised as has been widely claimed, and its lack of competitiveness stems far more from other factors such as overmanning, lack of hard work, disruptions, managerial incompetence, poor quality and delivery, and prices. The key to changing these is not the expenditure of large sums of money on job support or new machinery, but a much more fundamental attack on attitudes and performance, rationalisation and reduction of plants, model numbers and employment. If that process is set in train now as a matter of urgency and the extremely painful consequences are explained properly under determined Government leadership and accepted co-operatively by management and workers - which is still just possible if the Government is prepared to shoulder the responsibilities of leadership - then the industry can cut its costs dramatically and quickly and regain sufficient competitiveness to become within a few years viable and profitable at something like today's level of production. Of course one necessary and painful consequence would be the sacrifice of perhaps tens of thousands of marginal jobs today and many plants, for the preservation of several hundred thousand secure jobs tomorrow. However if, as could well now be nearly inevitable, that process is not set in train, the industry is doomed to massive contraction over the next decade. It is no exaggeration to say that hundreds of thousands of jobs in the production and assembly of cars and components could well disappear, and the trade balance in motor cars could quickly shrink from a small surplus today to an astronomical deficit of many hundred million pounds. The example of the motor cycle industry shows on a very much smaller scale what might be the worst consequences of pursuing the easy option in a similar way in the case of the motor industry.