

WE ARE ALL FLINT, MI NOW



Flint, by afk

I was talking with mr. emptywheel about what one of the bad—but by no means worst—case scenarios in a GM bankruptcy would be. This scenario is just one of several that might happen—but by no means guaranteed, and Congress would fight the scenario at every stage, though with increasingly less leverage. But it is a scenario that follows a great deal of logic about possible outcomes. It is this scenario, though, that explains why both Toyota (I've seen reported—looking for the link) and many in Congress want to bailout GM before it gets to bankruptcy.

Here's the short version: more details below.

1. GM files for Chapter 7 bankruptcy
2. GM's Chinese partner, SAIC, buys much of GM (Buick, Chevy, Cadillac)
3. GM/SAIC starts importing Chinese-made Buicks and Chevys, undercutting Toyota's cost advantages
4. GM/SAIC owns the Volt technology, requiring US firms to lease it if they wanted to use it

GM Files for Chapter 7 Bankruptcy

As Jonathan Cohn points out, an imminent GM bankruptcy is more likely to be a Chapter 7—total liquidation bankruptcy—rather than a Chapter 11 bankruptcy. That's for the same reason why GM is begging for cash right now in

the first place: no one is lending.

In order to seek so-called Chapter 11 status, a distressed company must find some way to operate while the bankruptcy court keeps creditors at bay. But GM can't build cars without parts, and it can't get parts without credit. Chapter 11 companies typically get that sort of credit from something called Debtor-in-Possession (DIP) loans. But the same Wall Street meltdown that has dragged down the economy and GM sales has also dried up the DIP money GM would need to operate.

That's why many analysts and scholars believe GM would likely end up in Chapter 7 bankruptcy, which would entail total liquidation.

So if GM goes bankrupt in January, as may happen, it may well have to sell itself off (unless the government guarantees the same kind of financing that it is refusing now). And I believe one company is one of the most likely—and indeed sensible—buyers: Shanghai Automotive Industry Corporation, or SAIC, the Chinese company with which GM partners to do business in that country.

GM's Chinese partner, SAIC, buys much of GM (Buick, Chevy, Cadillac)

SAIC is, in my opinion, by far the most sophisticated of China's automobile companies. Unlike Chery, the company that makes cheap knock-offs it has threatened to sell in the US (but which even the Chinese don't like to buy), SAIC has high quality and good expertise, gained largely through its partnerships with GM and Volkswagen. SAIC has ambitions to sell cars internationally—and it has been willing to spend money to advance those plans. Consider, for example, its purchase of MG:

In a move that may help pump serious life back into the Chinese MG

experiment, China's SAIC Motor has purchased Nanjing Auto, the company that paid some 53 million pounds (around \$105 million) for the MG brand after MG Rover's collapse in 2005. SAIC, which has partnerships with GM and Volkswagen, is a much bigger player in the Chinese automotive industry than Nanjing, selling 1.25 million vehicles during the first 10 months of 2007 to Nanjing's 79,196.

The move works for SAIC on several fronts. **Buying Nanjing allows the automaker to gain control of the MG brand** and to become an even bigger player in China and other markets. The purchase also allows it to gain control of the MG plant in Longbridge, England, where Nanjing had recently begun producing MG TF roadster prototypes (pictured at left).

During the dissolution of MG Rover, SAIC snagged the Rover expertise and technology, but has been forced to produce Rover cars under the Roewe brand (the Roewe 750 sedan is pictured) due to Ford's ownership of the Rover name. **With the acquisition of Longbridge, SAIC will now theoretically be able to use the plant to produce Roewes as well as MG-branded cars for European markets.** [my emphasis]

As with MG, a GM purchase would give SAIC the ability to sell-Chinese built cars under brands (reasonably) popular in the US. But a purchase of most of GM would be an even better match for SAIC than its MG purchase. After all, SAIC has been building a large volume of GM cars in China for years; it knows the company and the culture.

And SAIC has two more things that make it a likely buyer. First, cash, certainly enough to buy GM at a bargain and more to make a bunch of changes in its US operations. Also, it has got

increasing numbers of factory workers pressuring for higher wages; those wages would be too high for cars built exclusively for the Chinese auto market, but a mere fraction of what American auto workers are making.

An SAIC purchase would be accompanied by a lot of the same angst that accompanied Lenovo's acquisition of IBM's PC and laptop business. After all, SAIC would acquire not only GM's brands, but also a great deal of technological know-how.

But approval for such a deal would face very different pressures than the Lenovo-IBM deal. Unlike IBM, GM would be in bankruptcy, meaning the company itself would have a lot less flexibility to pick and choose between deals. There would be a lot of politicians aiming to save whatever jobs they could in the short term, as well as some pressure from other players in the industry to keep GM cars in production. Moreover, given the economic fragility of the country as a whole right now, China's got a lot more leverage to push through such a deal if it wanted—what are going to do, tell the country's banker that it can't buy what it wants?

GM/SAIC starts importing Chinese-made Buicks and Chevys, undercutting Toyota's cost advantages

Now, in this scenario, we'd be lucky if SAIC just bought what it wanted in January and set right to making changes to the company. The Center for Automotive Research's scenario for lost jobs with GM envisions a lapse of production, which brings a related collapse in the supplier industry that even affects domestically-produced foreign makers (that is, even Honda and Toyota plants may be idled because their suppliers would go out of business and they wouldn't have all the parts they need). And frankly, SAIC might well have an incentive to let GM stew on the market for a while, to get beyond the immediate credit crisis and persuade the government to kick in some money to sweeten the deal (this is similar to what they did with MG). But let's be optimistic and say SAIC jumps

right in to buy and run the parts of GM it would want. I'm imagining it would want Buick, Chevy, Cadillac, and possibly SAAB (though SAAB would be easier to sell off separately); I have no idea what it would do with Opel (presumably, European countries might try to save that as a distinct entity); it almost certainly would not want GMC or Pontiac and those two brands might simply disappear.

If I were SAIC, I would generally leave Cadillac alone, at least for now—its brand is improving, it's got better margins, and it's not a good fit, yet, for Chinese production.

I would immediately shift production of Buick models to China, starting with the LaCrosse that is already made in China for its domestic market. As part of this, I'd introduce the LaCrosse Eco-Hybrid in the US. Because Buick is a minor brand in the US, it won't attract a lot of bad PR. And by introducing a Chinese-built hybrid into the US market, SAIC could begin to compete more aggressively in the hybrid market while still achieving profits on those vehicles. (This is one of the biggest reasons why SAIC would buy Buick, which is worth much less as a brand here: because it has the most infrastructure and experience working with Buick in its own country, and could use it as a trial run for what it will eventually do with Chevy.)

With Chevy, I'd move toward quick introduction of Chinese-produced Chevy Aveos, GM's sub-compact car that is being freshened anyway and for which American production is not profitable. This would allow SAIC to more competitively vie for this growing segment (think Toyota Yaris, Honda Fit, and Nissan Versa)—and again, by building these cars in China, it could get closer to profitability. But the biggest thing I'd do with Chevy is to dramatically cut the number of dealers in the US (by a third to a half) and renegotiate contracts with those left. Then, for a number of the smaller Chevy models (things like the Cobalt), I'd introduce a 10 year warranty. By cutting the

number of dealers (thereby eliminating a lot of the cannibalization of sales that drives prices down right now and moving away from rebate-based sales) and offering a guarantee of quality, SAIC would shift the ways dealers make money—but more importantly, it would improve brand; this is precisely how rising brands—like Hyundai—have built their brand. Also, during this period, SAIC would make sure its dealers have the access to credit for product—and consumer financing—that is hurting all auto makers right now (I'm not sure, but I suspect that the legacy of GM's financing would give SAIC greater flexibility to offer credit to consumers than the Japanese manufacturers, which, if true, would give it a tremendous advantage over those brands for the duration of this credit crunch, helping it build market share because of the recessionary conditions).

All of this, of course, SAIC could do while just picking at the edges of the current UAW contract, the production of three or four little-noticed models in China, and do without a lot of the backlash that will come when it starts building the "heartbeat of America" in China. But it would lay the groundwork for moving most of Chevy's small vehicle manufacture to China starting about two years from now. That is, by the time the next UAW contract was up for negotiation, SAIC would be prepared to respond to a strike by simply moving production of many of its Chevrolet models to China. At that point, UAW's workers would probably be happy to retain whatever jobs they had assembling Chevy trucks in this country—it's a diminishing market, but it's a job.

The idea, of course, is to capture the rising small car market, but do so with the margins not available—to US car-makers **or** to Japanese makers—by building cars in the US. SAIC would have built up the Chevy brand, and done so with margins that the Japanese manufacturers couldn't match. To say nothing of Ford. If SAIC played things right, it would be set up to beat the Japanese at its own game, and undercut all US-

assembled production by importing cars from China. It would no longer be just union jobs in the Midwest that disappeared, it'd be non-union jobs in the South, too.

(Incidentally, Chevy has an increasingly strong brand position worldwide, so by moving toward Chinese built Chevys, SAIC would be well-poised to compete against Japanese companies in Europe and the expanding developing markets as well.)

GM/SAIC owns the Volt technology, requiring US firms to lease it if they wanted to use it

But that's not the only huge downside to SAIC buying chunks of GM. GM has been dumping lots of money into research in recent years and is close to introducing technologies, starting but not ending with the Volt, that would actually lead the industry in emerging areas.

And I can assure you SAIC would not purchase chunks of GM without getting this technology too.

If you're an environmentalist, this is not all bad for you. After all, a Chinese-produced Volt is going to have a lot lower price point than a US-produced Volt—this is the quick and dirty way to get the price down to \$20,000 at not that great a loss to the company. And since SAIC will have renegotiated contracts with its dealers, it could avoid some of the dealer-based problems that hurt the roll-out of the electric car in the past. (Though, this scenario likely results in a larger number of combustion engines on the road worldwide because it uses the GM infrastructure in developing countries to sell marginally cheaper cars, expanding the total number of consumers who will be first time car buyers.)

But if you're an American hoping to make all of your energy use more efficient, the huge downside is that American companies that wanted to use that technology would have to lease it from SAIC (in the same way that a lot of the US-produced hybrids lease technology from Toyota, which is one of the reasons they're not

profitable); if the Chinese government (which owns a chunk of SAIC) wanted to allow you to lease that technology.

At precisely the time the Obama Administration was emphasizing greening our economy and developing the energy technologies that will move us energy independent, we would be all-but giving away some of the technology that is closest to mass production capability. We could still develop those technologies—but much of those sunk costs would be lost.

Those pundits saying that a GM reorganized after bankruptcy would be much more efficient are right—insofar as it would make dealer structure more lean and produce smaller cars with margins that make them profitable. But it might well utterly devastate the US assembly industry in the 5 to 10 year timeframe. And it would be a terrible setback in efforts to develop the technologies to make our economy more energy efficient.