THE ADVANTAGES AND PITFALLS OF AUTO BAILOUTS

I'm (finally) working on my post on the Chevy Volt.

But before I do that, I want to lay out three data points—and point to some of the policy issues that still need resolved if we're going to have a viable American auto industry.

The first is the excellent news that Obama has will announce really aggressive ~~CAFE~~ efficiency standards tomorrow [they're not CAFE standards]—35.5 miles per gallon.

> The Obama administration is set to announce tough standards for tailpipe emissions of carbon dioxide from new automobiles, establishing the first ever nationwide regulation for greenhouse gases.
>
> It will also establish high fuel efficiency targets for new vehicles that would set a 35.5 mile per gallon average for new passenger vehicles and light trucks by 2016, four years earlier than required under the 2007 energy bill, sources close to the administration said.
>
> The administration is embracing standards stringent enough to satisfy the state of California which has been fighting for a waiver from federal law so that it could set its own guidelines, sources said. Gov. Arnold Schwarzenegger (R-Calif.) will be among a variety of state and industry officials attending an announcement tomorrow, said sources close to the administration.
>
> The compromise deal, which has been under negotiation since the first days

> of the administration, includes the White House, the state of California, and the automobile industry, which has long sought a single national emissions standard and has waged an expensive legal battle against the California waiver. The industry will get its single national standard, but at the price of one that approximates California's targets.

Make no mistake–this is a huge bump in gas efficiency and will have a big impact on our gasoline use.

But I suspect Obama's announcement came with a trade off–and perhaps not the right trade off. As David Sirota and others have reported, GM's current recovery plans have quietly included plans to import their Chevy Spark (that green thing above) from China.

> GM expects to sell about 17,300 China-made vehicles in the United States in 2011 and to triple that to about 51,500 in 2014, according to a planning document that GM circulated among U.S. lawmakers. The document did not name models or say what their brands would be.
>
> The plans are subject to change pending the outcome of negotiations with the UAW and already have drawn fire from lawmakers and others. If GM goes forward with the plan, it likely would become the first major automaker to ship Chinese cars to the United States.

The Chevy Spark is an increasingly popular in China, India, and is being exported from China to Peru (and is, I believe, what GM plans to assemble in the Russian factory it built last year). It's an A car–a mini that will compete with the Toyota Yaris and the Fiat 500 once it comes to the US.

But it’s also assembled in the interior of China, with dirt cheap labor.

Now, these two events are fundamentally tied together. No one–not even Toyota or Honda–can make a car this small profitably in the United States. Want 35.5 MPG in the auto fleet in this country? You’ve got a couple of options: cede the market to companies like Toyota and Honda, which can import small cars from cheap labor countries, and resign yourself to US manufacturers becoming increasingly uncompetitive as gas prices inevitably rise. Find a way to make GM’s importation of such cars palatable. Or, put a steep tax on gasoline, to make it easier for manufacturers to charge more money for these cars (though even in Europe, where you’ve got similar conditions, manufacturers opt to make these cars in cheap labor places like Poland). I don’t know which option is best (I guess alternately, you could forbid any company from importing such small cars, even while increasingly requiring such cars to be made to meet CAFE standards). But those are the options.

It would help, of course, if we had single payer health care and a national pension plan, to make US assembled cars more competitive with foreign assembled cars. I don’t see that happening any time soon (and yes, the auto companies should be leading the push for this to happen, I agree).

Then there’s the other news, the huge numbers of auto dealers being closed by GM and Chrysler–a total of roughly 2000 dealers in all, each employing about 50 people. Observers and members of Congress claim to be surprised by this news, but they shouldn’t be. The Big 2.5 have been talking about shedding dealers since November. I predicted a Chrysler-Fiat deal would bring about the closure of 990 dealers (which I guess means I still expect another 100 or so to close, beyond those that have already been listed for closure). And frankly, I don’t see much option to this, if the Big 2.5 are going to become more competitive (in fact, I expect that the GM and

Chrysler closures will, for the first time in a while, give them big advantages over Ford).

I've worked with dealers around the country, and every one of them complains about the same-brand dealer a short distance away (often just a mile or a few miles). Those dealers are always caught in bidding wars with each other, which has the effect of driving prices down and diminishing the perceived value of the vehicles themselves. Honda and Toyota don't have this problem because the overwhelming majority of their dealers were opened after the time when it made sense to have a car dealer in every town. And they have far fewer dealers anyway, even though Toyota matches GM's volume. And because Honda and Toyota can sell more cars per dealer, they can invest money in things like good service and new service bays.

Now, like I said, I can't imagine any alternative to closing dealers (though I pointed out in November that Congress could have chosen to deal with dealers, which might have led to a politically more palatable solution, yet Congress completely refused to consider doing anything with dealers in its attempted bailout). The only thing that might have prevented this is a restriction on dealer size, making all dealers uncompetitive–and I can't see anyone advocating that.

Still, that doesn't diminish the pain. The people whose dealers are closing–many of them–have been in this business for generations. They're leading businessmen in local communities. And somewhere (I have lost the link), I read that car dealers generate about 16% of all ad dollars, in any given ad market (so this is going to hurt newspapers and so on).

Obama's auto bailout has not entirely ignored dealers. By freeing up credit to auto finance companies (like GMAC), the Administration was basically freeing up the credit that makes the dealers tick. And he made small business loans available to them too. But the price for this, I suspect the auto task force would say, is in requiring that dealers be viable before getting additional loans from the taxpayers.

Tomorrow I’ll have my Volt post (some good news about an American car company!). But for now, here’s the state of play.