GM announces sharply lower profit figures

Decline of auto giant highlights crisis of US manufacturing

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General Motors announced Wednesday that it faces a huge loss for the first quarter of the year and much lower profits than previously projected for all of 2005. The news from GM, the world's largest auto manufacturer by sales, provoked a sell-off of the company's shares on Wall Street.

Chief Executive Officer Rick Wagoner and Chief Financial Officer John Devine announced that the company expects to post a loss of about $846 million ($1.50 per share) for the first three months of 2005. This would be GM's largest quarterly loss since 1992, when it was on the verge of bankruptcy. The company had previously announced that it would break even for the quarter. GM also revised downward its expected profits for 2005, from $4-$5 per share to $1-$2 per share, excluding one-time expenses.

Following the announcement, the price of GM stock plummeted, ending the trading day down by 14 percent. The sell-off eliminated some $12.7 billion in shareholder equity. It was the steepest decline of the company's stock since the stock market crash of 1987. During trading on Thursday, share prices fell below $28, down from over $80 five years ago.

Indicating the lack of confidence of investors in the future of the company, GM's bond rating was downgraded by all major ratings firms. Its bonds are now hovering just above junk bond status. A junk bond rating means investors are skeptical that the company will pay off its debts. If the rating is downgraded any further, GM will face sharply higher interest rates on the bond market, further eroding its bottom line.

A downgrading to junk status could trigger a sell-off with serious consequences for the broader bond market. One *Wall Street Journal* article on Thursday began by noting that the announcement by GM has prompted "investors [to reassess] the risk of lending money to US companies."

The immediate problems that GM faces include a sharp decline in sales, increased competition from non-US companies, and rising material costs. It also faces increased so-called "legacy costs" associated with the pension and health care programs provided to its employees and retirees.

GM's market share in the US dropped to a near all-time low of just over 25 percent in February. It faces high dealer inventory levels for many of its older vehicles, and has resorted to high cash rebates and 0 percent financing to increase consumer purchases.

Sharply rising gasoline prices have reduced demand for highly profitable SUV's and trucks, upon which GM has increasingly relied to bolster sagging earnings from its North American operations. In response to declining sales, the company cut production by 12 percent in the first quarter of this year, and has scheduled a 10 percent cut in production for the second quarter.

At the same time it announced its new profit figures, GM made it clear that it plans to place the burden of the company's problems on the backs of its workers. All 38,000 North American salaried employees will be denied merit pay raises this year, and the company plans to reduce its contribution to retirement accounts for all workers by 60 percent.

To cut production, GM has scheduled for this summer the permanent closure of three assembly plants. They are located in Baltimore, Maryland; Lansing, Michigan; and Linden, New Jersey. The closing of the Lansing plant alone will result in 3,000 layoffs. Other plants are scheduled for temporary shutdowns, including the truck assembly plant in Janesville, Wisconsin.

These, however, are merely preliminary measures. Wagoner said that while the company "made a lot of progress on reducing structural costs, what we have saved on the operating side has been filled in by higher legacy costs...We need to be more creative and more effective in addressing legacy costs. They are kind of swamping a competitive operational performance."

Put more simply, pension and health benefits that GM workers were able to win over previous decades are to be sacrificed to improve the company's bottom line. GM's health care spending alone is expected to rise to $5.6 billion in 2005, up from $5.2 billion last year. Over 1.1 million Americans—including current workers, retirees and their families—are presently covered by GM health care obligations, making the company the largest private health care provider in the country.

In addition to benefits such as health care and pensions, GM workers have won the right to continue to receive compensation—at least 75 percent of their pay—after being laid off. From the perspective of management and Wall Street, all of

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these "legacy costs" are intolerable constraints on the company's ability to radically restructure itself so as to once again become profitable.

Wall Street analysts are placing pressure on the company to take ruthless measures. Stephen Girsky, chief auto analyst at Morgan Stanley, argued, "The company's market share doesn't support its size. They have too many plants, too many workers, too many models, too many dealers and their employee benefits are too high."

It is impossible for the company to cut production significantly without sharply reducing its costs for employee health care and pensions. Most of these costs will not be significantly reduced by laying off current workers. Already, GM uses about $1,800 per vehicle sold to cover the cost of its contractual "legacy" obligations, mainly for retired workers.

To achieve these cuts, the company will turn to the United Auto Workers union (UAW) for massive concessions, and the union has amply demonstrated its willingness to push through cuts in the interests of management. An article on the *BusinessWeek* website ("Running Out of Gas at GM") notes that "GM's worsening woes could give it the leverage to wrest concessions from the United Auto Workers, and talks between management and union leaders have begun." To deal with the contract requirement that GM continue to pay laid-off workers, the company "could negotiate a buyout package similar to the one it got from its German union last fall, when its Opel subsidiary cut 12,000 jobs. That could allow GM to shed jobs without adding to its fixed costs."

GM will also look to the union for an agreement—similar to one the UAW has accepted at Caterpillar—that forces workers to pay for a portion of their health care costs, potentially saving the company hundreds of millions of dollars.

Increasing the pressure on the UAW and GM workers is talk that has already begun of a possible bankruptcy of the auto giant, though the company currently has ample cash reserves. There is a precedent for this. GM is facing similar problems to those faced by the major airlines in the US, all of which have either declared or threatened bankruptcy in order to push through a restructuring of their pension obligations.

The problems faced by GM are common to all of the Big Three auto makers, although Ford and the Chrysler division of DaimlerChrysler AG have recently posted small gains. The overall US market share for the Big Three companies continues to fall, and it reached a low of 57.6 percent in February. The US-based auto companies are facing increased competition, particularly from rivals such as Toyota and Honda.

In response, the Big Three auto manufactures have placed more pressure on parts suppliers to reduce prices, sending some, such as Michigan-based Tower Automotive Inc., into bankruptcy. Delphi Corp., formally a GM unit that was spun off as a separate parts supplier, is in the midst of an accounting scandal, centering on allegations it fraudulently inflated its profit margins. Visteon, the Ford spin-off, recently revised sharply downward its reported profits. Both of these companies have sought to reduce labor costs by cutting benefits and wages.

The deep problems that have again come to the surface at General Motors are an expression of a protracted decline of profitability in American manufacturing. Once the paragon of the US economy, the auto industry has undergone a profound decay over the past several decades.

GM once claimed, "What's good for GM is good for America." It can be said today that what ails General Motors is what ails American industry. GM is now a symbol of the decline of American economic dominance.

The problem of profitability at GM is not new. Over the past two decades, the company has seen its US market share steadily erode, from a high of over 50 percent during the post-war period. As its manufacturing has declined, GM has increasingly relied on its financing arm, General Motors Acceptance Corp (GMAC), to remain profitable. In addition to auto financing, GMAC finances home mortgages and engages in other activities unrelated to the auto industry. In recent years, GM would have been consistently in the red if it were not for GMAC.

GM's reliance on its financial subsidiary is indicative of the increasingly subordinate role played by manufacturing in the American economy. As profits from production have declined, the American ruling elite has turned to various forms of financial speculation that do not actually produce anything of value. At the same time, it has sought ever more systematically to shift production from the US to impoverished regions of the world where labor costs are far lower. This process is a concentrated expression of the increasing parasitism of American capitalism.

The crisis of General Motors reveals the underlying weakness of the American economy, which, in turn, provides an insight into the driving forces behind the explosive growth of American militarism. Internally corroded, American capitalism turns more and more to military violence to maintain its position of dominance and impose American-style "free market" relations in every part of the world.

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