“Prospects for the Auto Industry: from Chapter 11 to Chapter 1”

Address from Sergio Marchionne, CEO of Fiat and Chrysler Group

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Ladies and Gentlemen,

Good afternoon and thank you for the invitation to be here and address you today.

I would like to take this opportunity to share some of my thoughts on the automotive industry, the recent difficulties it has been going through and, even more importantly, the prospects for the future.

My intention is to focus on two issues in particular:

- the historic, structural problems that have been amplified by the recent crisis, forcing both automakers and governments to react, somewhat uneaveenly to shore up the sector;
- and, what we are doing at Chrysler to return it to being a vital competitive force in the auto industry, including drawing from the experience gained at Fiat over the past five and a half years.

Crisis force us, above all, to do one thing. They force us to change our point of view and discard our traditional way of thinking.

They force us to broaden our perspective and to take a global view of the situation. And, in so doing, they make our weaknesses more evident, and they provide clarity for what can or should be done to rebuild a future. Nowhere today is this paradigm more applicable than in the auto industry.
One of the problems which the sector has been suffering from for years is structural, fundamental, economic inefficiency.

Some years ago, the “Lex” column in the Financial Times expressed a view of the automobile industry which, in typical dry English style, says it just like it is:

“Choosing between carmakers is often like trying to pick the least flea-ridden dog.”

The history of our sector has, in fact, been anything BUT brilliant.

Not only has it not generated acceptable returns, it has actually destroyed value.
With the exception of our competitors in the Far East, this severe under-performance has been characteristic of the entire industry.

These graphs tell the story.

Over the last 30 years, automakers worldwide, with the exception of the Japanese, have underperformed the market - and the Americans have actually destroyed value. Changing the time frame for measurement does not help much.

The statement holds true for the last 20 years,
the last 10 years,

and the last 5 years,

with the Europeans and the Japanese also joining in on the value destruction game about 10 years ago. A sympathy vote is actually due to our Asian friends, who were doing well until the markets began a general meltdown in 2007 and they got caught up in a general downgrading of values, which persists even today.
I could show you many more graphs depicting the auto industry over different time periods - but they would all point in the same direction. Some to a greater degree and some less, but we are talking about an industry which by its very nature tends to destroy value and, even when on its best behaviour, does not create any.

In a normal world, in any other industry, if you saw charts like these the very first thing you would say is: “Give me the names of the guys who did this! I want them all out.” But we are all still here, preaching the same gospel we did 5, 10 and even 15 years ago.

The tightening and closure of capital and credit markets that we have been faced with has forced us to get smart and fix things before others do it for us.
We need to accept that the auto industry is in need of a structural change and that such a change will require strategic intervention.

The big automakers need to take on board the reality that the current business model needs to be completely rethought and redesigned around the central pillar of efficiency.

It has become imperative to achieve a level of critical mass which will produce significant economies of scale and enable continued investment in the development of new products and markets.

An increase in volumes per platform, in each of the main market segments, is essential to achieving economic returns which justify the enormous level of investments necessary in the automotive industry.
And this can only be done by expanding geographically in order to take advantage of new growth opportunities.

These factors inevitably lead to the search for alliances. Only by joining forces with a suitable partner is it possible to effectively reduce the risk of being in the car business. Only by working more closely with others is it possible to have continued access to new capital, maintain adequate levels of investment and face competition on an equal footing.

This is the motivation that led to the Fiat/Chrysler alliance, which I will talk more about in just a moment.
The other major structural problem that has been amplified by the current crisis, forcing the auto industry to focus its attention as a matter of urgency, is the issue of production overcapacity.

If you look at this map, it is immediately obvious that no region in the world has reached the minimum level of capacity utilisation necessary to realise adequate returns on investment.

In every region, in fact, the industry is operating well below the threshold.

Notional production capacity worldwide is approximately 94 million cars per year, which is about 30 million more than the market would be able to digest normally. Approximately one-third of this capacity is located in Europe.
A reasonably reliable estimate suggests that the approximate 75 percent capacity utilization in 2008 will drop to around 65 percent this year.

The need for rationalisation is undeniable.

In Europe, many sectors have already been through a major consolidation and rationalization, such as the steel industry in the 90s. But a similar consolidation has never taken place in the European auto industry and, with today’s political climate, it appears unlikely to happen.

And yet, given the projected lacklustre growth in volumes for the next five years, this chronic structural imbalance in our industry will become even more marked with many factories essentially becoming redundant, making a serious restructuring of the industry absolutely necessary to bring it to a point where it is economically sustainable.

The direction taken by the United States, which appears to have chosen to confront this problem head on, is unique.
President Obama formed an industry-focused task force whose mission is to transform the shackles of crisis into extraordinary opportunity.

The objective of what has been dubbed America’s "New Green Deal" is to dramatically influence an entire industry and the habits of consumers, at the same time providing safeguards for industry and promoting the shared objective of reducing emissions and fuel consumption.

We have been witnessing a courageous structural shift in the US, with government, companies, trade unions and financial institutions working side-by-side to do more than merely save the auto industry.

Real and significant measures were taken to rationalise production.
It is a true rethinking of the model from an ecological perspective. An attempt to create a solid foundation on which the sector can be rebuilt. Through Chrysler, we have the privilege of being involved in the process of re-establishing the US auto industry. We can bear witness to the extraordinary determination of the US government and the profound sense of responsibility demonstrated by all stakeholders. Everyone is doing their part so that a better, stronger basis for the future can be built.

In Europe, unfortunately, the central problem of overcapacity has not yet been tackled.
Many governments, each in their own way, have given support to the sector through eco-incentives to stimulate demand, directing it toward more eco-friendly alternatives, as well as direct financial support to domestic producers.

More specifically, the various forms of government aid have included: new credit lines, loan guarantees, research subsidies, contributions toward the development of engines which are eco-friendly and/or use alternative fuels, aid for capital investment, refinancing for consumer financing divisions.

The most significant intervention to date has been in France, where PSA Peugeot Citroën and Renault were the recipients of a government aid package totalling nearly €8.5 billion.
Many other national governments have also intervened. These unilateral interventions are, by their very nature, dangerous, because they put a few players in a position of advantage, while the remainder - such as Fiat - are forced to compete with their hands tied behind their backs. All of this in a “common market” which has been the cornerstone of the European Union since the signing of the Treaty of Rome.

It is also my fear that the lack of a common vision in Europe could act as a dangerous brake precisely at a time when we need to move as rapidly as possible.
The objective, for both America and Europe, would appear to be the same: to revitalise those industries which are crucial to the economy. But there is a real possibility that the results will be drastically different.

The American plan focuses on overcoming problems that have afflicted the automotive industry for years and building a new, more sustainable future from both an economic and environmental perspective.

European plans, by contrast, are not addressing the underlying root causes precisely because they lack a common vision.

Individual member states are looking inside their borders and acting unilaterally out of self-interest, rather than the interests of the community as a whole. Looking at the trees but not seeing the forest.
The recent economic crisis has left us with the sense that the world has irrevocably changed and that nothing will be as before.

Even now, with the precarious economic landscape we have before us, I am convinced that it is essential to look beyond the typical responses to crisis.

Great crises have the ability to create new conditions of equilibrium.

I believe this is also true for the auto industry, which will be pushed toward more efficient organisational models, more eco-friendly production processes, and more conviction in its adherence to the values of sustainable development.

This is the approach we are following with the remaking of Chrysler.
On November 4th in Detroit, we presented the financial community with a detailed 5-year plan – under the heading “From Chapter 11 to Chapter 1” - through which Chrysler will transform itself into a truly competitive force in the auto industry.

The plan includes the launch of 21 new models, the sharing of product platforms with Fiat, billions of dollars in cost savings and a significant increase in sales volumes.

By 2014, the Chrysler Group will have annual sales of 2.8 million vehicles, more than double the volume for the current year.
Annual revenues will be at $68 billion and operating income of $5 billion, and the company will have halved its current debt and fully repaid the American taxpayer. The plan was distilled through 5 months of intense dialogue and discovery within the Chrysler organization.

No stone was left unturned, in what, at times, were gut wrenching evaluations of exactly where we are positioned in the food chain of the automotive world. November 4th represented the first day of a new Chrysler.
We laid out our plans and are now publicly accountable for their delivery.

We laid out the aspirations of a group of leaders who are passionate about rebuilding the fabric of a new Chrysler, of a vibrant and competitive American carmaker.

The following morning, I was up early reading the European press and some of the newswires that had come out during the previous day's presentation.

The majority of the coverage was positive but there will always be naysayers out there.

I actually like the idea that we are the underdogs, and that we will have a chance to prove them wrong.

But I also understand the naysayers.

I have been here before.
When I arrived to take the helm of Fiat in June 2004, there was an almost unanimous majority who didn’t believe we had much of a chance: bankers, trade unionists, journalists, financial analysts, economists and, more importantly, our customers were all on Fiat’s case.

The general theory was that in the space of a few months, Fiat would disappear from the automotive landscape altogether.

It was as if there was a competition as to who could write the best chronicle of a death foretold.

Here are some of the reports put out by analysts at the time.
Disappointed by consistently declining revenues and never-ending losses, especially from the car side, they could see nothing other than the inevitable demise of Fiat.

As the *Wall Street Journal* wrote at that time:

“Fiat is like Italy’s soccer team. Everybody in the country seems to have a view about how it can improve its performance”. 

And these are just a few of the front pages that appeared in the international press bidding us farewell.
The Observer, the FT’s most irreverent column, ironically commented on the melody that people calling Fiat heard when put on hold: they suggested that “Wonderful Life” be changed with a song by Tracy Chapman, “Fast Car,” where she says, “starting from zero, got nothing to lose”.

Fortunately, predictions, for the most part, do not end up making history.
In fact, Fiat closed 2008 with the highest trading profit in its 109 years of history and it has weathered incredibly tough trading conditions throughout 2009 in a more than respectable fashion.
No one is bragging though. It is not our style.

But in that process, in the last five and a half years, Fiat has been able to reacquire trust and confidence from its customers and from the markets.

It is now credible.

On November 4th, nearly five months after emerging from bankruptcy, we asked the financial community and the press to extend the same credibility to the Chrysler organization and its leadership team.
That day represented the beginning of a genuine transformation.

We are not planning miracles. We are simply committing to the execution of a few strong and precise choices that will trigger rapid change. What I have learned from my experiences as a Chief Executive over more than a decade, just as Lou Gerstner did some 20 years ago at IBM, is that culture is not just part of the game, it is the game.

Organizations, when all is said and done, are but a collection of the will and aspirations of its people. Every success story is based on the ability of men and women to drive cultural change on a certain order of things.
All of Fiat’s results, the margin improvements and market share gains, and each line item in its financials reflect, in reality, the change in mentality that has been introduced. Chrysler, as Fiat has done, is embracing the challenge of the new and is now beginning to see the future as a huge opportunity.

To do this, it needs to live the culture of change as a necessity, of feeling comfortable in the discomfort associated with uncertainty, of measuring itself each day and of rooting itself in the values of competition and of the market.

Fiat’s achievements can ultimately be traced to the adoption of a concept of leadership that rests on a handful of core principles.
We are a meritocracy, and the right to lead is a privilege granted only to those who have demonstrable capability to lead change and to lead people.

We embrace and relish competition. Because we understand now, finally, that it is at the heart of our survival.

And as we compete, we aim to achieve best-in-class performance with respect to our competitors.

Finally, and most importantly, we deliver what we promise: we acknowledge that we are accountable.

These are now Chrysler’s principles, and they have guided and will guide every leadership choice, starting with the selection of the leadership team.
We are creating an inextricable industrial and commercial linkage between Chrysler and Fiat.
This is absolutely necessary to guarantee the ultimate success of both organizations in an industry which, as we saw earlier, has for at least the last 10 years been unable to generate adequate returns.
The co-development of these two organizations, regardless of the industrial logic supporting it, is going to be executed across a cultural divide.
This is an issue that cannot be ignored.
And especially for Chrysler, which has lived through a sort of international affiliation over the past decade.
It is not my intention to judge the past.
What is important is the future, and the way in which both organizations handle the challenge.
In so doing, we will be guided by a notion expressed by President Clinton at the Labour party conference in Blackpool, England in 2002:

“All of the hopes that I have for my daughter’s generation, for the grandchildren I hope to have, for all those younger than me and, unlike me, who still have most of their lives ahead, rest upon our ability to get the world to embrace a simple set of ideas, that we must move from interdependence to integration because our common humanity matters more than our interesting differences and makes the expression of those differences possible; ...”.

It is this philosophy that has driven Fiat’s internationalization efforts over the last 4 years.
From the very beginning, we committed to executing this daunting task with mutual respect and openness toward our partners. Fiat’s alliance with Chrysler needs to be viewed and understood in these terms. The “common humanity” that binds these two organizations is the irrefutable industrial logic that supports the alliance and the sharing of values that define leadership and the organizational culture within which we function.

But their ultimate expression is through the brands that Chrysler holds. They have, and always will have, their roots in America. Nothing will ever change this.
During the Chrysler presentation, the audience had a chance to hear a variety of music. Most of the pieces were from Bobby McFerrin: a musician you probably know from his very popular tune of a few years ago “Don’t Worry, Be Happy”. Some of the pieces came from a CD titled “Paper Music”: a collection of classical music, in which he uses his voice as an instrument while at the same time leading the St. Paul Chamber Orchestra. Buried inside the cover of the CD is an editor’s note on the title of the CD.
Part of it says:

The most difficult thing for the conductor may not be simply getting through the piece with the orchestra still intact, but actually having something to say about the music.

The composer of classical music puts splotches of ink on paper to suggest to performers what they must do to recreate the sounds heard by the composer in his or her inner hear.

The music always exists – even if it’s not being performed at the moment.

Some African musicians, however, whose tradition is an oral one, call notated music “paper music”.

To capture sound in notation is an odd, abstract idea for people whose music exists because they keep it in their minds and hearts.
Perhaps that’s where the key to Bobby McFerrin’s conducting lies: like many of the greatest composers – Bach, Beethoven and Mozart, for example – he is an accomplished improviser and has the ability to reach that place where the joy of making music overcomes the routine of weekly rehearsals and performances of black shorthand symbols on white paper to attempt to reproduce what they think someone else wanted them to say. Then it’s not just paper music: it is music.

The presentations given that day were light years further on from where Chrysler's leadership team had been a mere five months before. The organisation’s ambitions reflect the views of the people leading it.
Each of them is evolving quickly, feeling more comfortable with dropping sheet music, and accepting the uncertainties and excitement associated with competition, naturally, because it is the only way to derive strength and build great businesses.

The crisis in the automotive sector has put the values fundamental to any organisation to the test: accountability, honesty, and reliability.
It has underscored their importance and the need to protect them.

It is these values that make a company, a system, a nation unique and exceptional.

The real challenge in front of us at Chrysler is to nurture these values and ensure that they guide all of our choices.

Some 500 years ago, Niccolò Machiavelli put it this way:

A return to first principles in a republic is sometimes caused by the simple virtues of one man. His good example has such an influence that the good men strive to imitate him, and the wicked are ashamed to lead a life so contrary to his example.
When all is said and done, the Chrysler plan is exactly that: a commitment to build an enterprise of men and women of virtue.

Thank you all.