TESTIMONY PREPARED FOR WILLIAM B. JOHNSTON, ASSISTANT SECRETARY FOR POLICY, U.S. DEPARTMENT OF TRANSPORTATION BEFORE THE HOUSE COMMITTEE ON WAYS AND MEANS, SUBCOMMITTEE ON TRADE CONCERNING THE U.S. AUTO INDUSTRY, NOVEMBER 18, 1980.

Good morning. I am pleased to have this opportunity to discuss the situation confronting the U.S. automotive industry.

That industry continues to be hardpressed and faces a stern challenge to regain its financial vitality. Recent upbeat reports about the new fuel efficient models that have been introduced by the U.S. manufacturers and the International Trade Commission's finding that imports are not the primary cause of the industry's problems might lead one to believe that the bulk of those problems have already been overcome. We should not, however, be misled by these events. The severity of the industry's problems has not changed. The stiff competition and economic challenge posed by imports have not diminished. The magnitude of the industry's forthcoming investments remain enormous. Now is not the time for government to slacken its efforts to aid this most important industry and the workers and communities that gain their livelihoods from it.

The 1980 model year was a disaster for the major U.S. manufacturers. General Motors' U.S. automobile production was down approximately 22 percent compared to model year 1979. Ford's production was off approximately 45 percent for the year. Chrysler's declined by approximately 34 percent. Accompanying these declines in production were unprecedented financial losses. Through the first nine months of this year these three manufacturers have all run deeply in the red, collectively losing more than $3.5 billion. The industry's challenge is to rebuild its plant and equipment and redesign its product lines to compete more effectively with the imports at a time when it is sustaining record losses and market erosion.

Dealers have also felt the effects of the industry's problems. Since the beginning of the year, more than 1400 dealers of domestic autos have closed their doors. In addition to the problems created by the economic downturn, record high interest rates have significantly cut into dealers' sales and added to their costs.

Not to paint an entirely gloomy picture, the new model year has shown potential to date, but it is still too early to predict a significant short term turnaround in the fortunes of the U.S. manufacturers. With the introduction of Ford's and Chrysler's new fuel efficient front wheel drive models, the imports' share of the market fell to 21.6 percent in October, its lowest level since November 1979. GM's subcompact Chevette and its front wheel drive compacts, the X-bodies, continue to be strong performers. Overall sales, however, continue to be weak. October's daily selling rate was still the worst for the month since 1974, another recession year. Production is being held in check to keep inventories from running up again.

The rapid changes in the world's petroleum markets in the last two years have brought about a dramatic shift in demand to new fuel efficient cars. The auto manufacturers were not ready to meet this demand for numerous reasons: it is an industry which requires long lead times for engineering and design; new designs that are major departures from existing models require that massive capital investments be put in place and amortized over many years; and the U.S. public had been large car oriented for years, in part because of encouragement by the manufacturers themselves, and in part because it had been the policy of the U.S. government to keep gas prices artifically low through regulation.

There is nothing to be gained by attempting to lay the blame for the industry's problems at any particular doorstep. The fact remains that today the auto industry is undergoing a dynamic transition whose reverberations will have major impacts throughout our economy. The nature of the industry is being permanently altered, with gains in market position by some auto manufacturers, and losses by others. These gains and losses are directly translatable into financial strength. In the supplier industries, many will find new opportunities for growth as they shift to supply the products newly in demand; others will experience a marked decline in the need for theirs; still others will find their products and services totally obsolete, and may be forced out of business.

As their employers prosper or decline, so will workers. Some will find added new opportunities, while others will find their jobs permanently gone, and be forced to seek new careers. Some communities will experience substantial growth; others, which have long served the auto industry and benefitted from its prosperity, will lose a major proportion of their primary employment, and with it major components of their tax base.

In bringing about this transition, the U.S. manufacturers are beset with formidable problems. Massive new investments in facilities, in machinery, and in engineering designs are required to maintain competitive positions, not only in the domestic market but in world markets as well. For example, it is estimated that by 1985, the industry will have to build 30 new engine lines, 19 new transmission lines and 89 new assembly lines at a cost of more than $50 billion. In varying degrees, each of the major domestic producers is encountering difficulty in raising the needed cash and financing to fund these investments. These problems have been compounded by the steep decline in sales beginning in the spring of 1980, attributable to the economic downturn, the high cost of credit, lack of interest by consumers in the big cars that have traditionally been the industry's best cash generators, and increased losses of sales to imports.

Thus, this major American industry, which in 1978 contained the nation's 1st, 3rd, and 10th largest companies, as well as thousands of smaller ones, is now in a state of rapid change with far reaching dimensions. It is incumbent on those who are responsible for maintaining our industrial wellbeing to understand the possible long range implications of these changes so that we can anticipate them instead of merely responding reactively to them.

Today's pressures, and the choices being made by the industry in response to them will alter the character of the industry for decades to come. For example:

o Most of the world auto market has reached the stage of maturity, with little growth projected for the 80's. The U.S. market, for example, is expected to grow at less than a 2.5 percent annual rate through 1990.

o The U.S. market will henceforth be much more integrated into the world market. More components will be sourced overseas, benefitting the consumer with lower prices, but reducing the U.S. domestic value added.

o Competitive positions within the U.S. market are changing substantially, fueled by the unprecedented losses being experienced in 1980 by all five domestic producers. Ford is in the process of retrenchment. Chrysler has had to resort to Government aid and AMC to a foreign producer.

o Our auto companies are scrambling to accommodate their lost competitive advantage, even in the domestic market. U.S. wage rates are comparatively high and other countries assemble cars with fewer man hours. The Department of Commerce has estimated, for example, that the Japanese spend $860 less per vehicle on labor than do the U.S. manufacturers because of the difference in wage rates alone.

o In the U.S., GM is aggressvely maintaining its market share while the others are losing share to Japanese producers. On small cars it appears that GM has lost its position as price leader to the Japanese.

o In spite of their severe losses, the U.S. companies must make major investments today, to meet the new market demand and remain competitive, with the result that they will be under a strained capital structure throughout most of the 80s. They need to realize higher margins, but may not be able to because of imports.

o In the drive to reduce production costs, one result will be fewer U.S. plants, with higher productivity and fewer workers. Even if significantly higher production levels are attained, improvements in productivity of 5 percent annually could eliminate as many as 200,000 auto manufacturer jobs by 1985. As a result, many auto industry oriented communities will suffer continued severe economic dislocation.

o In the world-wide competition, our multinationals often compete with Government/industry combinations. Other countries are playing the game by different rules than our own, with their overriding policy considerations being jobs and labor stability.

It was in response to these types of problems and concerns that this Administration undertook this past summer a priority program to aid the automotive industry, its workers and the communities that derive their economic livelihoods from it. I think this Administration can point with pride to the accomplishments of that program.

In the area of regulation, numerous requests for waivers have been expedited, with many granted. High altitude emissions standards have been reviewed to reduce the cost of compliance. OSHA has worked closely with GM, Ford and Chrysler to reach agreement on variances to the standards for worker exposure to lead and arsenic.

In the area of worker assistance the Department of Labor has initiated a $50 million series of positive adjustment assistance demonstration projects. Additional funds were obtained for the Trade Adjustment Assistance Program.

To help auto and truck dealers in financial trouble, the Small Business Administration has made numerous direct loans and loan guarantees. Through October 24 the SBA made more than $17 million in direct loans to 107 dealers and guaranteed loans totalling nearly $237 million for 1,086 dealers.

The Economic Development Administration is working with approximately 20 state, local and county governments, some of which have already received grants, to help them plan for and accommodate the changes that the auto industry is going through.

With an eye toward improving cash flow, Treasury has accelerated its review of depreciation lives of motor vehicle manufacturing equipment and hopes to conclude it by late this month or early December. Not related solely to the auto industry, but vitally important nevertheless, this Administration proposed making the investment tax credit refundable to assist all industries in making needed investment in plant and equipment.

Both we in Government and those in the auto industry have accurately characterized these efforts to aid the auto industry as only a beginning. More can and should be done to build a stronger bond between the two of us. To help bring this about, this Administration formed the Auto Industry Committee to advise the President on major public policy issues affecting this important component of the nation's economy. While the outcome of the election has postponed action by this Committee until the new Administration is in place, I firmly believe that this Committee's efforts must be continued, regardless of which party is in office, to help in bringing the industry, labor and Government closer together in areas of mutual concern. Through the efforts of the Auto Industry Committee and those of the Congress, much can be done to help the domestic auto industry regain its vitality.

Despite the difficult straits in which the industry currently finds itself, I am confident that the next several years will see a significant improvement in its financial condition and competitive position both at home and throughout the world. Our labor has the skills and our manufacturers possess the technology and desire to do both.