



Weekly Car Dealers Newsletter

June 4, 2007

This information that follows is taken from sources including *The Carconnection*, *Autoweek*, and other industry sources.

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WARRANTY ALERT: TOYOTA SET TO FIX ENGINES IN NEW TUNDRA (Camshaft failures in the V-8 engine option have gotten the attention of Toyota execs.)

Toyota said that it has found a defect that caused the engines to fail in some of its new Tundra pickup trucks, according to a report in *USA Today*. Toyota has received reports of camshafts breaking in the engines of about 20 Tundras so far. The flaw was due to a manufacturing defect by a subcontractor. All of the engines are being replaced.

The factory has not issued a recall. "We're still investigating it. We don't believe it was that many," a Toyota spokesman said. Toyota said earlier this month that its pre-launch forecasts are on track for Tundra. It hopes to sell as many as 200,000 this year, up from about 125,000 of the old model last year.

Although optional, the 381-horsepower 5.7-liter V-8 has quickly stepped out as the most popular engine for the Tundra, which is depicted in ads as having brawny towing capabilities. About 65% of buyers opt for it. If a camshaft breaks, the engine will barely work or not at all. Toyota is giving owners new ones that are shipped overnight to dealers.

CHRYSLER, CHERY TO MEET IN MICH. Representatives of Chery, the Chinese automaker, which is supposed to build Chrysler-branded small cars, will be in Auburn Hills this week to talk over various aspects of the deal. Chrysler offered no details about the agenda for the meetings but they could include the first concrete discussions between Chery and Cerberus Capital Management, which earlier this month submitted the winning bid for the Chrysler Group, which is being sold by DaimlerChrysler AG. Under the provisions of Chrysler's so-called transformation plan, the partnership with Chery is expected to provide the company with new, small vehicles and help it gain access to other markets, particularly in China. Chrysler has said it expects its international sales to grow rapidly following the separation from DaimlerChrysler, which is now expected to be complete this fall. Tom LaSorda, Chrysler Group president and chief executive officer, also suggested Chrysler could even expand its ties with Chery if the joint

venture now in the works proves productive. DaimlerChrysler AG's board of supervisors approved the link-up with Chery this past winter over the vocal objections from both German and American union representatives on the board.

Chery representatives are now denying recent reports in German press that is thinking of re-examining the deal with Chrysler in light of the sale to Cerberus Capital Management. The reports originally appeared last week in the respected German financial daily *Handelsblatt*, Chrysler officials noted. Chrysler officials also minimized the significance of the *Handelsblatt* article, noting Chery officials later repudiated the statements that had appeared in the German paper. However, a Chery official identified by name in the article had said the deal with Cerberus came as a "total surprise" for his company and it had not yet talked with representatives of the New York private equity fund, which is about to become Chrysler's new owner.

"We continue to be in talks with Chrysler, but we don't have any contact with the new owners yet," the Chery officials told *Handelsblatt* reporters.

The deal with Chery still has not been finalized, Chrysler officials acknowledged last week. However, the delays have been the result of an extensive review by the Chinese government, according to Chrysler spokesman David Elshoff. Once the master agreement is approved by the government of the Peoples' Republic of China, Chery and Chrysler will have to negotiate specific project agreements that will cover the development and production of specific vehicles. LaSorda personally spent a substantial amount of time last years, discussing specific projects with Chery executives. The objective is to have Chery build a small "B-class" subcompact vehicle that could be sold under the Chrysler and Dodge brands in North America and Europe. LaSorda has said the new small car could prove invaluable to Chrysler's ongoing efforts to woo younger buyers to the Dodge and Chrysler brands and bolster its position in the subcompact market niche, which has expanded as gasoline prices have increased over the past couple of years.

The small cars from Chery also could serve as a hedge against further increases in the price of gasoline in future, Chrysler officials have suggested.

CERBERUS/CHRYSLER DEAL A SNOW JOB? In "Chrysler at the Gates of Hell," on the Huffington Post blog, *Automobile Magazine's* Jamie Kitman ventures to say that after Cerberus Capital LLC, the owners of the newly named Chrysler Holdings LLC, is through with Chrysler and the UAW, publicly traded companies — often maligned for having short-term returns in sight with long-term strategies left to suffer — will look benevolent in comparison. He also speculates that more predatory loan practices are just around the corner as Cerberus, which bought GMAC last year, now also has access to Chrysler Financial.

But more importantly, one tidbit that Kitman mentions, which has been a sin of omission for many news outlets in recent weeks, is that three ex-politicos, each fallen from grace in the political realm, are involved with Cerberus, with formerly much-ridiculed Vice President Dan Quayle helping steer the well-stocked ship. Quayle is Chairman of Cerberus' Advisory Board, and has been heavily involved with the investment firm since 2000. Additionally, former Treasury Secretary John Snow and former Defense Secretary Donald Rumsfeld are also involved in Cerberus.

In recent years the once much-ridiculed VP has served as the door-opener for Cerberus, helping to get the group into new markets that would be otherwise difficult and buying them

direct access to high-ranking execs. In fact, Quayle helped the private firm establish an office in Germany in 2003 (in of all places Frankfurt), according to information in the former VP's official bio.

Kitman remarks, "The man who forgot how to spell potato is chairman of Cerberus' global investments unit. Can you imagine corporate officers accountable to shareholders choosing him for an important job?"

UAW president Ron Gettelfinger has been widely criticized in recent weeks for accepting (and endorsing) the purchase of Chrysler by Cerberus before even meeting with the group. Cerberus had provided a written statement saying that there were no plans for additional job cuts directly connected to the sale, but in recent weeks there has been widespread speculation that the group is contemplating how to streamline, or possibly outsource, a significant portion of Chrysler's production.—Bengt Halvorson TCC

HARBOUR: DETROIT CLOSING PRODUCTIVITY GAP Toyota is the most productive automaker operating in North America, according to the latest in a long-running series of studies on factory efficiency, but the Big Three U.S. automakers are quickly closing the gap. Detroit's gains are coming on so quickly that, with recent moves to slash the workforce and gain workplace concessions from once-intransigent unions, the Big Three may soon outpace their Japanese rivals - a trend that Ron Harbour, president of Harbour Consulting, says should be good news for consumers, as well as shareholders. "Toyota is still on top," said Harbour, during a Thursday news conference at the Detroit Automotive Press Association. But he quickly stressed that "The numbers are closer than ever before," with Toyota holding, at best, "a very slim and marginal lead."

Underscoring that transformation, Harbour noted that for the first time ever, a single manufacturer - General Motors - operated three of the four most efficient plants in North America, taking the lead in assembly, engine and transmission production. Honda, meanwhile, took the productivity award for most efficient stamping plant. The annual Harbour Report compares the efficiency at automotive assembly, stamping, engine, and transmission plants - which handle the bulk of the work on a car, truck, or crossover. Each plant is rated in terms of the hours of labor needed to built a particular car or component. In the case of Toyota, a typical, North American-made vehicle required 29.93 man-hours per vehicle, while at the other end of the scale, Ford Motor Co. plants needed 35.10 hours of labor. Ford was an extreme, largely resulting from slumping sales of some of its most important products. The most efficient Detroit maker, GM, required 32.36 hours of labor, or barely two hours more than Toyota.

As recently as 2002, the gap between most efficient and least efficient was more than eleven hours. That translated into a cost advantage for the best Japanese makers of \$800 to \$900 a vehicle, said Harbour, while the gap has now narrowed to just "a couple hundred dollars." "That's money a manufacturer can put back into the product," the manufacturing consultant explained. In years past, Japanese makers used their productivity to their advantage, offering buyers a richer mix of features, such as premium audio systems or more airbags.

Big Three still improving

Don't be surprised to see the traditional productivity hierarchy go through a severe shake-up, cautioned Harbour, pointing to the ongoing buy-outs and other job cuts ordered by Detroit's Big

Three. Meanwhile, their unions have grudgingly begun to accept the need to improve efficiency with so-called Competitive Operating Agreements, which eliminate feather-bedding and other, unproductive work rules. "There's no telling who might be on top, next year," proclaimed Harbour. Like other industry insiders, Harbour said he'll be closely watching contract talks between the Big Three and the United Auto Workers, which begin in July. The troubled U.S. makers are expected to push for concessions aimed at reducing costs and further improving productivity.

The Japanese still hold some critical advantages, he cautioned. Makers like Toyota not only strive for high productivity, but they've also built highly flexible assembly plants. That means they can roll a variety of vehicles down the same line. In turn, that means that if sales of one model dips, production of another, more popular product can be ramped up, keeping the plant running at peak efficiency. Detroit makers also are moving to the flexible plant model, but they remain well behind their Asian rivals. The typical Toyota plant, in North America, operated at 103 percent of its normal, two-shift capacity, according to Harbour, while DaimlerChrysler came in second, at 88 percent. But some of the U.S. maker's facilities were so busy, they ran seven-day schedules, others ran at barely half normal capacity. And that was a money-losing proposition.

On the whole, Toyota made an average \$1266 for every vehicle produced in its North American plants, last year, according to Harbour data, while struggling Ford lost \$5234. "There are still a lot of areas where we need to continue to improve our flexibility, our productivity, and we have to close the gap to every competitor in the world," said GM's director of worldwide manufacturing, Gary Cowger, in response to the Harbour Report findings.

While Japanese makers dominated the overall productivity and capacity utilization charts, one Asian maker suffered a sharp decline. Nissan, long the most efficient manufacturer in North America, slipped a bit, in part because of poor sales. Its own factories ran at just 77 percent of capacity, Harbour estimated. Nissan was the only one of the Big Six who pointedly declined to provide manufacturing data to Harbour analysts for the 2007 study. Even with its sales and productivity issues, however, Nissan made an estimated \$1575 per vehicle, the most of any maker operating in North America. To improve their productivity, U.S. makers have had to undergo sea change shifts in thinking, especially when it comes to quality. In decades past, the conventional wisdom was that preventing problems at the plant meant more manpower and lower production. "Don't let anyone tell you quality costs more because it (actually) costs less, in terms of manufacturing," declared Harbour. Improving quality begins with better design, he said, then taking steps to ensure any defect is quickly caught and corrected on the line, even before it reaches the final inspection stage.

Other data support that contention. Recent studies by the California research firm, J.D. Power and Associates, indicates the quality of vehicles produced in North America is now at record levels and still improving. Power is expected to show further gains when, on June 6, the firm releases its latest Initial Quality Study - which tallies problems with vehicles during their first 90 days on the road.

"The winner in all this is the customer," asserted Harbour.
