Screws Tighten On European Automakers

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MILAN (AP) — As automakers prepare to roll out new models this week at the Geneva Auto Show — one of the major events in the automotive calendar — they are being forced to fight for a slice of an ever-shrinking European market stricken with austerity and recession.

On top of this, carmakers are also having to confront the uncomfortable fact that a large number of their production lines are lying idle and eating up valuable funds. Industry executives, including Fiat and Chrysler chief executive Sergio Marchionne, have estimated that Europe's car industry has the production capacity to build 20 per cent more vehicles than they are currently able to sell, an imbalance that hurts both their ability to compete and bottom line, especially as European sales tumble.

This problem of overcapacity and underused factories is one that automakers have long lamented, but can no longer ignore. Fiat, PSA Peugeot-Citroen, Opel, Renault and Ford Europe all are losing money in Europe — even when sales in emerging economies such as China help keep the companies in the black.

"If I could do only one thing, it would probably be to create a flexible work environment to manage supply and demand," Marchionne, who is also chairman of the European Auto Manufacturers Association, said recently in Brussels.

Cars sales in Europe this year are forecast to decline by nearly 5 percent to 12.9 million units, according to the Center for Automotive Research — down from 15.7 million in 2000.

European auto demand has dried up as consumer confidence buckles under the pressure of government austerity measures, rising and persistent unemployment and the deepening of southern Europe's recession. In addition, most of the pent-up demand was taken out of the market during "cash-for-clunkers" incentives that governments introduced to help automakers in the 2008 financial crisis. The countries with the biggest number of idle production lines are France, Italy and Spain.

Gaining a competitive edge with attractive new models and updated technologies, like those to be showcased by the 260 manufacturers coming to the Geneva event, may be part of the cure. But the tougher medicine will mean taking an ax to European factories — which will lead to job losses.

"There are too many cars, and too many brands making similar cars. There is going to be lots of consolidation in the European market, and closed plants, and consolidation of brands," said IHS Automotive analyst Tim Urquhart.

There has already been a casualty: Saab Automobile filed bankruptcy in January

after a two-year effort to revive the distinctive carmaker with one of the strongest brand followings in the industry.

Meanwhile, Chinese and Indian auto makers are beginning to gain a foothold in Europe. Last month, Great Wall Motors opened a factory in Bulgaria, becoming the first Chinese automaker to assemble cars in the European Union.

More positively, General Motors and France's PSA Peugeot Citroen this week announced a strategic alliance that gives the U.S. auto giant a 7 percent stake in Peugeot in exchange for a euro1 billion ($1.32 billion) capital increase. The two companies said that, together, they'll be better equipped to survive Europe's brutally competitive car market by developing a common small car platform by 2016, and with a combined purchasing power of $125 billion.

"I think (the) announcement from PSA and GM is an indication that people are looking for real solutions now. Just putting two companies together doesn't solve a capacity issue, so things are going to have to happen," Ford chief financial officer Lewis Booth told reporters in Detroit.

Ultimately, industry-watchers are expecting the deal to cut excess production capacity through plant closures.

Joseph Amaturo, an analyst at the Buckingham Research Group, said he expects GM to spend up to $2 billion to reduce European production capacity and headcount this year.

The GM-Peugeot alliance is among the signs that things are starting to shift in Europe, industry insiders and analysts said.

"In terms of the amount of restructuring in Europe, I feel that some things are more likely to happen this time than they have in the past, because all the major countries in Europe, and the minor countries, for that matter, are struggling with their own budget problems," Booth said.

That means governments are no longer prepared to pony up with incentives to scrap old cars or bridge loans to keep the automakers running, as they have in the past.

The GM-Peugeot alliance goes beyond the traditional tie-ups that the industry has seen before — where carmakers combine technology, chassis and production facilities — as the two automakers seek to gain efficiencies.

Family-controlled Peugeot is one of the most exposed to the European market, where it sells more than half of its 3.5 million cars a year. Last year, it lost euro439 million.

The strategic alliance could also help GM, based in Detroit, find a solution for its loss-making Opel and Vauxhall brands in Europe. General Motors Europe, which lost $700 million last year, is studying ways to cut costs, raising union concerns that a

plant or plants could close.

European auto production has dropped from 18.5 million vehicles in 2007 to 16.6 million last year, according to IHS Automotive. It is expected to hit a low of 15.5 million this year, 2.47 million vehicles fewer than it has the capacity to produce.

Despite that, premium carmakers like Audi and BMW, mass producers like Volkswagen and new importers like Hyundai-Kia are ignoring the capacity fears at other European carmakers and beefing up their production to accommodate new models coming to market this year and next.

At Fiat, Marchionne is looking to the U.S. market, through the nearly 3-year-old alliance with Chrysler, to help restore health to Fiat's Italian production sites, running at 60 percent capacity, according to IHS Auto. With the European market waning, his goal is to produce cars in Italy for export to North America — but he will only do that if he can win flexible union contracts that he says are necessary to be competitive globally.

For now, Marchionne has put future investments on hold — once pegged at a total euro20 billion from 2011-2014 — until the impact of the crisis becomes clear.

He has already closed one plant, in Sicily, at the end of last year against fierce labor and political opposition. And he told the daily Corriere della Sera recently that if his plan to export cars to the U.S. doesn't take shape, he'll have to close another two.

Marchionne said the problem of excess capacity is one that needs to have a coordinated response.

"National solutions are not enough," Marchionne said.

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