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## Region braces for car crash; State, business get ready to cope

By [Ryan Beene](#) and [Amy Lane](#)

Economic woes facing the Detroit 3 automakers have Southeast Michigan bracing itself for losses on many fronts — jobs, personal income, revenue for industry, from taxes and, perhaps, a sense of identity.

The region and the state have been trying to compensate for a shrinking automotive industry in one way or another for 30 years. Key future industries have been identified. Incentives have been put in place. Strategies have been mapped to help make sure Michigan remains a major player even within a smaller automotive industry.

Even so, **General Motors Corp.**'s possible descent into Chapter 11 by early next year seems disconcertingly swift — and as *Crain's* went to press last week, the prospect of federal help before the end of the year appeared increasingly unlikely.

And with **Chrysler L.L.C.** being a likely merger or Chapter 11 candidate and **Ford Motor Co.** with its own cash problems, it seems likely the region and Michigan face a long period of regrouping.

"Over the first nine months of this year in Michigan, there's been a 33,000 decline in auto and auto parts manufacturing jobs, and the biggest decline we've ever seen was in 2001 - it was 37,000," said Dana Johnson, chief economist at **Comerica Bank**. He added that the state is on pace to lose 40,000 by year's end - a more than 20 percent decline.

"My starting point to think about next year is: I can't for the world see how we're going to have fewer job losses next year, whether there's a bankruptcy or not."

Johnson said the current pressure on the Detroit 3 to continue restructuring in the hopes of returning to profitability likely will result in a 30,000-job loss, and a bankruptcy at GM or Chrysler could shed an additional 20,000-30,000 jobs at the automakers.

Donald Grimes, senior research associate and economist at the **University of Michigan Institute for Research on Labor, Employment and the Economy**, agrees that a bankruptcy, merger or bailout would each result in massive automotive job losses in the region.

"The basic problem that everybody's got to remember is, car sales have collapsed," he said.

Cars are being sold at an annual rate of about 10.9 million vehicles, according to the *Automotive News Data Center*. That's down from a rate of more than 16 million the same time last year.

"Unless those car sales bounce back up ... which nobody foresees anytime soon, Southeast Michigan is going to get hit because those car companies are going to make drastic cutbacks in their payroll," Grimes said.

Economists and local economic observers agree that a bankruptcy at GM would be the worst scenario for the region.

Van Conway, managing partner at Birmingham-based turnaround firm **Conway MacKenzie & Dunleavy**, said a Chapter 11 filing would do nothing for an ailing automaker unless it came with massive restructuring of its supply

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agreements, dealer network, brand and vehicle portfolios.

"A bankruptcy doesn't create cash flow," he said. "If you've got cash flow problems, a bankruptcy itself doesn't give you anything."

The collateral damage to suppliers that rely on GM for much of their business would be significant. The same goes for banks lending to those suppliers.

If a bank loans to a vendor using its receivables as collateral and does half its business with GM, and GM files for bankruptcy, the half of the collateral backing the bank's loan will have filed bankruptcy too.

In fact, **Delphi Corp.**, still trying to emerge from Chapter 11 bankruptcy, may be forced to liquidate if its former parent company, **General Motors Corp.**, seeks bankruptcy, Bloomberg News reported last week.

"If the banks today were to say, 'We're going to plan for a GM bankruptcy,' they'd have to put the gun in their mouth and pull the trigger, because if they were to call the loans today ... the suppliers can't pay them anyway, what it does is it causes chaos," Conway said. "The ramification (of a GM bankruptcy) on the availability of bank credit for vendors is really negative."

Utilities prep for shrinkage

Michigan's electric utilities are preparing for a combination of continued overall economic downturn and potential sales losses from auto-industry upheaval.

Jackson-based **Consumers Energy Co.** expects a 1 percent sales decline across its service territory in 2009, reflecting economic conditions, but also has planned for a much worse decline.

The utility is taking several cost-cutting steps to prepare for a potential 7 percent, one-year sales drop in total electricity sales. Consumers is delaying about \$180 million in capital expenditures planned for 2009 and reducing working capital, operations and maintenance spending.

The potential 7 percent sales drop is the same amount Consumers' electricity sales dropped during the 1979-1982 recession, said Jeff Holyfield, director of news and information.

At that time, automakers and suppliers represented about 15 percent of Consumers' electricity sales volume and about 14 percent of Consumers' margins, or the amount billed to customers minus the cost of power.

The auto industry currently represents about 5 percent of Consumers' sales and 3 percent of margins, a decline due to a variety of factors including shrinkage in the auto industry and increased power use by other customers.

Consumers' territory includes GM plants and auto suppliers, but no major Ford or Chrysler operations, Holyfield said.

The utility's largest single customer, also its fastest-growing customer, is **Hemlock Semiconductor Corp.**, the world's leading producer of polycrystalline silicone, based in Hemlock, near Saginaw. Hemlock's growth is helping to cushion declines elsewhere. Holyfield said that without Hemlock, Consumers electricity sales would be down about 3 percent in 2009, compared with the 1 percent expected decline.

**Detroit Edison Co.**'s total sales load is down 1 percent year-to-date, compared with 2007. The utility expects 2008 overall will be down about 2 percent.

"Normally we would be seeing one to two percent growth; we're not only not seeing that, we're seeing negative growth. And a good chunk of that is coming out of the impacts of the auto industry," said Gerard Anderson, president and COO of Edison parent **DTE Energy Co.** "They're an important industry to us, and what happens next year to them is going to be a big deal to us."

The Detroit 3 and their large suppliers represent about 10 percent of Detroit Edison's sales volume and about 6 percent of its pretax profits.

General Motors is Detroit Edison's single largest customer, but Anderson said the utility is not speculating or discussing publicly what a GM bankruptcy could specifically mean in terms of plant closings or other impacts.

The auto-industry situation is adding urgency to ongoing efforts to reduce costs and boost efficiencies. Companywide, DTE has cut costs by more than \$300 million over the past three years, and savings the company is now targeting will be "a significant fraction" of that number, Anderson said.

He said Michigan economic conditions are one reason for the moves, as is ongoing investment in the business.

Lost state and local dollars

The auto industry's impact on state revenue spreads wide, through areas that include income taxes, sales taxes, property taxes and business taxes.

"Number of jobs equals income, which equals income tax but also equals income that's spent. It's spread throughout," said Mitchell Bean, director of the **House Fiscal Agency**.

Bean said that "when people suddenly have less money to spend, there are ripple effects through the economy." And he said that with auto industry jobs tending "to be pretty well-compensated," the effect is even greater.

The Detroit 3 employ an estimated 109,180 people in Wayne, Oakland, Macomb, Livingston and Washtenaw counties, or about 5.5 percent of the metro area's total employment across all industries.

The average automaker employee earns an estimated \$90,868 per year, according to calculations made by *Crain's* based on data from the **Michigan Department of Labor and Economic Growth**.

If 30,000 jobs are lost at that wage, more than \$2.7 billion in personal income will be taken out of the regional economy.

As *Crain's* reports in a related story (*See Page 14*), Michigan's current-year and upcoming fiscal 2010 budgets overlay national and state economic uncertainty, not the least of which is in the auto industry. It has bearing both on the state's general fund and the School Aid Fund, with the latter's major revenue sources including sales and property taxes.

Wayne County had about \$64 billion in tax value in 2007, \$2.3 billion of which is owned by the Detroit 3. The city earned more than \$15 million in levied tax revenue last year from the Detroit 3.

In Sterling Heights, where Chrysler metal stamping and assembly factories occupy two miles of Van Dyke Avenue between 15 Mile and 17 Mile roads, the city counts on Chrysler for \$3 million in property taxes, about 5 percent of the city's total tax revenue.

While Livingston County has no factories, GM's vehicle proving ground is in Milford. That location alone accounts for \$47.6 million in taxable value, counting real and property taxes.

Oakland County Commissioner Mike Rogers, who chairs the county's finance committee, said Oakland's budget is balanced for 2009-2010. But more automotive cutbacks would force the committee to make revisions.

"Potentially, one of these automakers may not be in existence in the next few years, and that's what we're taking into account with our budget," he said, adding the county expects late 2010 to be "rock bottom" in the region.

Rogers said the county has scaled back spending on programs to counter the impact of revenue already lost through falling State Equalized Value of properties, home foreclosures and falling income tax revenue.

The county has suspended its juvenile boot camp program, scaled back the Oakland County Sheriff marine budget and replaced its entire reimbursement division with a law firm to collect money owed to the county.

About 10,000 homes in the county are in foreclosure, Rogers said, and he expects that to increase by 10 percent to 15 percent next year as the local auto industry continues to downsize.

Detroit 3 is a crowd

Ilhan Geckil, senior consultant and economist at **Anderson Economic Group L.L.C.** in East Lansing, said that, ultimately, the economy and the competitive landscape can support two major U.S. players, but not three.

"The optimal solution right now is a merger," he said.

The firm projects that a GM-Chrysler merger would result in the loss of about 8,500 factory jobs in Michigan and 12,000 managerial and technical jobs. Factory job losses outside Michigan would be 10,000 to 12,000, Geckil said.

The figures reflect direct job losses at GM and Chrysler and include the closure of three plants, including two in Southeast Michigan.

And the multiplier effect of an automaker job is significant.

Anderson Economic Group says that as of 2007, GM, Ford and Chrysler provided 170,166 jobs in Michigan. But those jobs, the firm estimates, created 816,800 indirect or spin-off jobs in Michigan, including indirect jobs with suppliers, dealers and aftermarket, as well as spin-off jobs in areas such as retail and food sectors.

Metro Detroit 2.0

The region finds itself on the cusp of its defining industry's collapse, or at the very least, an immense metamorphosis.

But American cities have faced similar situations before, and have come out alive - and thriving.

"It's not uncommon at all," UM's Grimes said. "If you go back to the late 1960s early 1970s, the situation was reversed between Boston and Detroit."

Grimes said Boston was heavily dependent on a manufacturing base that began to shrink as it transitioned to other low-cost regions.

"They looked very much like Michigan, and the role was exactly reversed, and of course they made the transformation to the knowledge economy," he said.

Comerica's Johnson says the model for him is Pittsburgh and the collapse of the steel industry that made way for a knowledge-based economy founded on higher education, health care and high-tech industries.

"That's probably where we're heading, (but) it will be far easier to get there if the auto industry returns," he said.

Economists agree that while the next months, and possibly years, will undoubtedly be difficult for the region, Detroit will still be the Motor City.

"It will still be the largest single concentration of motor vehicle activity in the United States, there's no question about that — it will just be a lot smaller," Grimes said.

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