

BusinessWeek

INSIGHT November 5, 2007, 10:37AM EST

A Comeback for the UAW?

An aging workforce at U.S.-based Japanese plants and a resentful new generation in Detroit could bring the union roaring back to life

by [Ed Wallace](#)

As strikes go, Chrysler's wasn't all that impressive. When Chrysler's unionized workers nationwide [left their assembly line positions in early October to protest the holdup in securing a new four-year labor contract](#) (BusinessWeek 10/10/07), the media reported "the second major UAW walkout in a month"—but it seemed more like a long lunch with picketing during dessert. By nightfall the parties had come to an agreement, and the next morning the newspapers chorused such headlines as "It's a New Day in Detroit" and "Detroit's 3 Finally on Track."

Really? It seems to me we've read those headlines a hundred times in the past 25 years. And each time they're wrong.

Many observers seem to believe that the Big Three's woes are all tied to union wages and the benefits its blue-collar workforce receives. But those are not their biggest problems. While the new agreements with the UAW could help, cutting labor costs won't cure what ails Detroit. In fact, just the opposite could happen.

GAMES DETROIT PLAYS

General Motors ([GM](#)) has cried loudest about the "unfair" wage advantage the Japanese automakers enjoy. It has bemoaned what it sees as a \$1,500 to \$1,900 price disadvantage (owing to active and retiree health-care costs) on every product it sells. But the media completely missed reporting that the moment GM had its new agreement with the UAW in hand, incentives on the [Suburban Tahoe](#), Avalanche, and some [Silverado pickup trucks](#) soared. If GM is financially noncompetitive over that \$1,500-per-vehicle health-care bill, how is its financial outlook improved by giving away \$2,000 in a new rebate?

GM would say that by selling more new vehicles, thereby getting more orders for additional products from dealers, it can run assembly plants at faster line speeds—and the faster the line goes, the less each vehicle costs to produce. Yet Detroit spends approximately \$78 an hour in blue-collar wages and benefits, while Toyota Motor ([TM](#)) spends less than \$50. So, all things being equal, including labor costs, GM's logic would only hold water if Detroit's factories were running at the same line speed as Toyota's—up to 110%. Yes, the assembly line's production pace determines whether wage and benefit costs per vehicle are within industry standards. A plant's productivity may be more important than actual wages paid there.

A hypothetical example: If Detroit Company "X" was running its midsize sedan factory at 90% line speed, while the plant making the Camry ran at 110%, and both had the same wage structure, Detroit Company X would have an 18% labor price disadvantage for every midsize car it made (again, all things being equal). However, if Detroit Company X could match Toyota's production speed in this example, its labor costs would immediately be 18% less per sedan produced. Of course, this is why Detroit has announced so many plant closings over the past year: Auto executives know real labor costs aren't framed just by the per-hour pay but are measured by how many vehicles the fewest

workers can build in one shift. (It should also be noted, in many cases, Detroit has already improved in this area.)

On the other hand, consider Ford's (E) last minivan attempt. No matter what Ford spent to develop or build a new minivan, it was DOA at Ford and Lincoln-Mercury dealerships. While both the Ford Freestar and the Mercury Monterey were vastly superior to the models they replaced, they also listed for thousands more than the benchmark Honda Odyssey's sticker price; within months, Ford was quietly offering its dealers up to \$5,000 in cash each to move those vehicles.

Face it, if Habitat for Humanity had built the Freestar and Monterey for free, those vehicles still would have been a financial catastrophe for the Blue Oval Kids. When a new vehicle comes to market and fails, the manufacturer loses hundreds of millions—if not billions—no matter what its labor costs are.

FAR LOWER WAGES

Much has been made of the fact that Detroit already spent much more than Japanese automakers in the U.S. for health insurance. Of course, Detroit supports a huge number of retired workers, and overall the American blue-collar worker at Japanese factories is younger. Yet GM admitted something important after the union contracts were signed: Fully 56,000 of its remaining 74,500 blue-collar workers will be eligible for retirement by 2011. (Not to mention GM also has announced a further downsizing of its workforce.) So the average age of GM's factory workers will be coming down rapidly in the near future. Theoretically this would lower costs associated with health care per employee—not to mention that many of these new workers will be receiving far lower wages and incurring no retirement health-care costs.

At first glance, this looks to be a huge financial win for General Motors, and in the near term it is. However, it could all too easily bring the United Auto Workers roaring back to life.

Here's how it is likely to backfire. First, retired autoworkers don't get to vote on new contracts, so they'll have no say in whatever benefits they may or may not get in the future. Second, up to 56,000 of GM's 74,500 workers might be replaced either by the time of the next union negotiations or by the 2015 negotiations at the latest. Do you think the new and younger workers, paid less and getting fewer benefits, will fight to keep the retirees' benefits? After all, factory work is not much fun; a younger worker might well feel cheated and resentful, doing the same job for maybe half what someone else was paid to do it just five years earlier. It's human nature.

This time around the UAW could sign up the American workforce of foreign car companies for the same reason. The *Detroit News* reported earlier this year that a secret internal Toyota report had been leaked. Written by Seiichi Sudo, president of Toyota Engineering & Manufacturing for America, the 42-page report suggests that Toyota needs to get its labor costs down to whatever the prevailing wages are in the region where their factories are located. Now with companies such as GM allowed to pay as little as \$14 per hour, Toyota studying ways to lower labor costs, and Honda Motor (HMC) deciding to hire new workers for its upcoming factory in southeastern Indiana only from certain surrounding counties, it appears that the era of Americans' building cars for the Japanese but never wanting to unionize might be ending.

If Toyota can move more quickly to cut its labor costs because its \$25 hourly wage is high compared to GM's possible \$14 in some positions, then GM is putting downward pressure on Japanese wages. So the Japanese could use GM's lower wages to put downward pressure on some of their employees—and those earning Japanese wages might start to think that union representation isn't a bad idea.

SUICIDAL INCENTIVES

The long-term outlook isn't great for anyone. Henry Ford proved beyond doubt that paying his workers well not only stabilized his workforce but allowed his moving assembly line finally to reach its maximum potential. Ford lowered his car's price, paid his unskilled workers America's highest wages—\$5 a day—and still became one of America's richest men.

But old Henry firmly believed something else: If his own workers could not afford to buy the products they made, his company would fail. At \$14 an hour, these new workers will be able to afford few of the cars GM makes—or Ford, for that matter—so consumer wages and price deflation will continue their downward spiral.

This is the opposite of the scenario that created great wealth for everyone and defined the American Century. The only thing that will save Detroit is more hit vehicles, faster line speeds, and less suicidal incentives. In fact, Detroit's incentive costs are far greater than their costs for health care. Regardless of the deal they cut with the UAW today, absent those fundamental market moves, somebody in Detroit is bound to go away.

*[Ed Wallace](#) holds a Gerald R. Loeb Award for business journalism, bestowed by the Anderson School of Business at UCLA. His column heads the Sunday Drive section of the Fort Worth Star-Telegram, and he is a member of the American Historical Society. The automotive expert for KDFW Fox 4 in Dallas, Wallace hosts the top-rated talk show *Wheels*, Saturdays from 8 a.m. to 1 p.m. on 570 KLIF AM in Dallas.*

Xerox Color. It makes business sense.

Copyright 2000-2007 by The McGraw-Hill Companies Inc. All rights reserved.

The McGraw-Hill Companies