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OBSERVATIONS

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Where's the Beef?

This month I received another couple of dozen requests for interviews about the GM Oshawa decision. I suspect this is because Unifor is still actively fighting this issue. They are out across Canada arguing that this is disastrous for the automotive industry in Canada and thus we need massive Government intervention to prevent this from occurring. They are also calling for a boycott of GM vehicles. This I don't get at all. More on this later in this Observations.

I always like to check the facts, so I looked up the actual monthly employment numbers published by Statistics Canada for the automotive sector for Canada and Oshawa. Year-end numbers are not yet available so I include their third quarter numbers for 2018 and final annual numbers going back to 2006. Now I follow this industry pretty closely, but even I was surprised by the stats.

Since General Motors announced that it would be shutting down production at five plants in North America including its Oshawa plant, the oldest in Canada, many have painted a gloomy picture of the future of what was once Canada's Motor City. However, despite the steady erosion of the city's largest private sector employer over the past seventeen years, total employment in Oshawa is now 36 percent higher than it was in 2002. Indeed over the past year, total employment in Oshawa has risen by 4.9 percent year over year, the fourth highest increase among Canada's 33 Census Metro Areas.

Employment in the automotive manufacturing side of the sector in all of Canada (we define this as assembly of vehicles of all types and production of components) is up by 9 thousand workers in 2018 over 2017 at just under 140 thousand total workers making vehicles and components for this industry. And non-manufacturing jobs (head office jobs of the OEMs, vehicle dealers, aftermarket players etc.) were up by a little over 30 thousand jobs this year at just under 704 thousand workers, this number doesn't surprise me at all. Ownership of vehicles in Canada is at an all-time high of about 88 percent of the driving age population which means there are now 10 million more vehicles on the road today than in the year 2000 (27 million versus 17 million). When a country adds 10 million vehicles to its roads it represents one heck of a lot of additional economic activity with distributing, retailing both new and used vehicles, maintenance and repair etc., and Statistics Canada doesn't break out some other obvious automotive employment numbers from other sectors.

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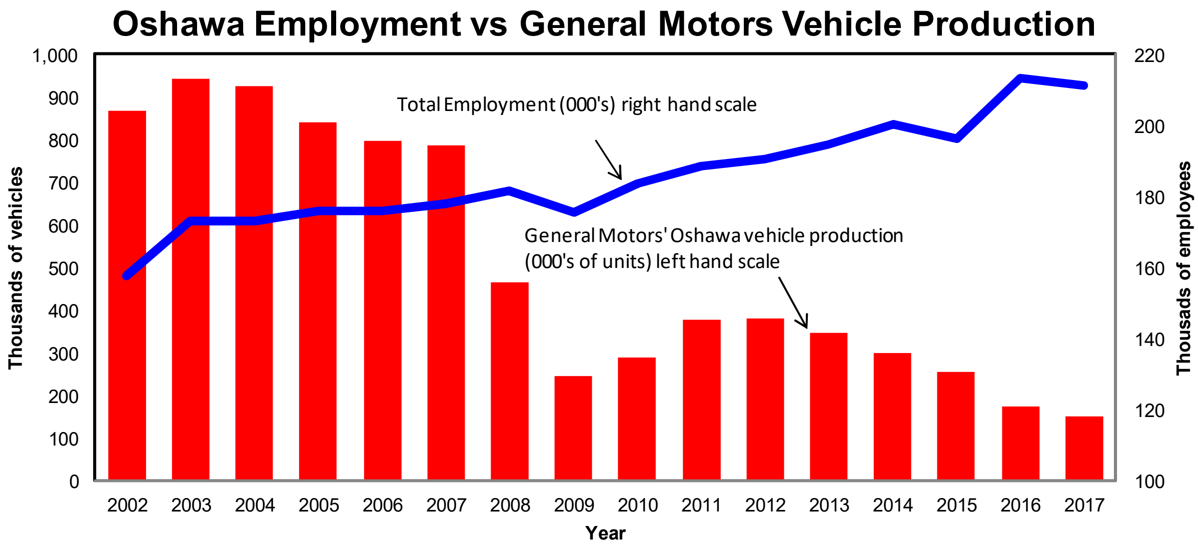

Source: Statistics Canada, DesRosiers Automotive Consultants Inc. (DAC)

Last year, for instance, Canadians financed over 1.9 million vehicles but nowhere can I find how many jobs at banks and credit unions are directly related to this activity. If we were able to track down more accurate numbers for all direct jobs (excluding indirect jobs like workers at restaurants feeding workers in the auto sector; I call these the butcher, the baker and the candle stick maker jobs then up to 1 in 7 jobs in Ontario are also tied indirectly to the sector) it is possible that total "direct" non-manufacturing workers in the automotive sector could approach 800K rather than the published 700K+ in the table.

Add the manufacturing and non-manufacturing auto jobs together and as of the third quarter of 2018 there were at least 830K direct workers in the automotive sector and possibly as many as a million indirect workers. And this is up by 140 thousand jobs from its trough in 2010. Now I feel very bad about the 2.5 thousand workers that will potentially lose their jobs at the Oshawa manufacturing facility and the several thousand more in the auto parts sector. However, this does not represent the 'end of the automotive sector as we know it'. I also say they potentially lose their jobs because GM has offered to retrain any worker that wants to work in the non-manufacturing side of the sector, which is growing rapidly and some additional workers have been offered a full pension to retire. Vehicle dealers, for instance, are searching high and low for service technicians. And before anyone says "wait a minute, these are low paying jobs", a service technician in a dealer can make as much as a worker on an assembly line. Mind you these are skilled jobs and require a lot of hands-on training but they generally do pay very well. Perhaps not all, but many.

Now, to be fair, the number of workers on the manufacturing side of the industry is down from its peak and there have been some very tough years for workers in our plants. Manufacturing related employment peaked at 158 thousand workers in 2006 and dropped to a low of 109 thousand workers at the depth of the financial crisis in 2009. That's a massive decline of about 50 thousand workers. Fortunately about 30 thousand of those workers have been brought back to work in our factories, but we are still down 20 thousand workers with most of them from the GM/Ford/FCA factories and their related suppliers. There is no doubt that some of these lost jobs were due to closing of plants. Canada at one point (including medium and heavy-duty) produced over three million vehicles in 1999 and produced a little over 2.2 million vehicles in 2017. GM, Ford and Chrysler (now FCA) have all closed plants. Now the question "why?" remains.

To be sure there is politics behind some of the plants that were closed in Canada but we also forget that there was politics behind some of the plants that remained open when all the economics pointed to them being candidates for

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closure. The best example is the GM plant in St. Therese, Quebec which was kept open for a number of years longer than its due date and I believe politics was at least partially behind this decision. In addition, another element that is often forgotten or at least not mentioned is the lost market share of the Ford, FCA, and GM. I have market share stats going back to 1990 and in that year GM, Ford, and Chrysler (now FCA) captured 70.5 percent of the Canadian market. Last year they captured only 40.9 percent of the market. This stat is scary enough but what most haven't caught onto yet is that in the depth of the financial crisis when both GM and Chrysler were bankrupt in the US their market share was 43.8 percent in Canada. In 2009 consumers were afraid to buy one of their vehicles because they didn't know whether these companies would survive yet their market share last year was a full three points lower. A similar situation existed in the US. Is it possible that this is also why the GM's of the world are closing plants?

And some of the lost employment is due to a classic capital-labour substitution impact. The vehicle companies and especially their suppliers have invested billions and billions in their plants to modernize their factories and this is also part of the lower manufacturing employment levels in Canada. Despite all this, our total manufacturing employment grew last year by 9 thousand workers. Shouldn't we be cheering from the rooftops? This is why the decision by GM to close Oshawa is the correct one for their business. By closing these low volume plants (something GM in the past was late to do) it allows GM to remain competitive and to hopefully hold or stop the deterioration in their market share.

I also want to get back to the non-manufacturing side of this equation which is where there is rapid growth in our automotive work force. I mentioned that ownership has grown to record levels. In the year 2000 it was two-thirds of the driving age population and is now about 88 percent. Again, I ask the question "why?" There are many reasons. Much better built product and a significant increase in the selection of vehicles being offered are two core reasons. In the year 2000, the 15 year survival rate for the average GM/Ford/FCA vehicle was only 26.8 percent. Seventeen years later in 2017, it grew to 46.0 percent. That's a massive increase in quality. Japanese vehicle survival rates increased from 21.7 percent to 62.5 percent (no wonder they are picking up market share), Korean vehicles increased from 4.0 percent to 21.9 percent and European vehicles from 41.7 percent to 73.9 percent. All of these stats are for the year 2000 versus the year 2017. With survival rates increasing drastically, the number of well-built older vehicles on the road in Canada also exploded. In 2000, there were about 6 million vehicles on the road in Canada over 10 years old, last year there were about 11 million vehicles. Many of these are well built and because of their age much less expensive to purchase than a new vehicle thus resulting in the growth in used vehicles sales which are

Motor Vehicle Manufacturing and Parts Manufacturing

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Annual	**158,279**	**152,557**	**137,602**	**109,117**	**109,376**	**111,816**	**115,187**	**117,415**	**121,499**	**125,404**	**126,876**	**130,889**	**139,900**
Percent Change		-3.6%	-9.8%	-20.7%	0.2%	2.2%	3.0%	1.9%	3.5%	3.2%	1.2%	3.2%	6.9%

Total Automotive Related Employment in Canada - Non-Manufacturing (Retail, Aftermarket, Distribution)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Annual	**612,626**	**621,043**	**625,037**	**600,596**	**594,075**	**603,697**	**617,949**	**628,246**	**645,017**	**657,189**	**663,368**	**672,695**	**701,008**
Percent Change		1.4%	0.6%	-3.9%	-1.1%	1.6%	2.4%	1.7%	2.7%	1.9%	0.9%	1.4%	4.2%

Total Automotive Related Employment in Canada - Manufacturing, Distrubution and Retail

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Annual	**770,905**	**773,600**	**762,638**	**709,714**	**703,451**	**715,513**	**733,136**	**745,660**	**766,516**	**782,592**	**790,243**	**803,584**	**838,903**
Percent Change		0.3%	-1.4%	-6.9%	-0.9%	1.7%	2.5%	1.7%	2.8%	2.1%	1.0%	1.7%	4.4%

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now well over 3 million units per year, up at least a million units from the year 2000. This is a critical element of the additional 140 thousand workers in the non-manufacturing side of the automotive work force.

The new vehicle market has also settled in at new highs. For the longest time (about 20 years) a new vehicle market in the 1.4 to 1.6 million ranges was considered a cyclical high. We have now had three years in the 1.9 to 2.1 million range so we’ve added about 500 thousand more units to our classic cyclical high. Quality and selection are also part of this growth but pricing is the primary reason for this growth. The increased competition (thus the lower market share for GM/Ford/FCA) and the capital-labour substitution equation has meant there has been very little price inflation in the new vehicle sector for quite some time. For most of the last decade and possibly more the Statistics Canada price index for new vehicles has increased by less than 1 percent per year. This index misses a very big part of the cost of buying a new vehicle. About two-thirds to three-quarters of consumers trade in their current vehicle when they buy a new one. Since their current vehicle is so well built (resulting in higher survival rates) the value of their used vehicle has increased and this effectively lowers the price of their new vehicle. According to Canadian Black Book the wholesale price of the average five, six and seven year old vehicle is up by approximately 7.5 points since the year 2000; although, the range by brand is very wide with some seeing no increase in their residual value and others increasing by as much as 20 percent. With the average transaction price in 2012 for a new vehicle being about $30 to $35 thousand an increase in residual value represents at least an additional $2,000 on the typical trade-in whereas 20 percent could represent an additional $6,000 dollars. Combine this with little to no price increase and it is entirely possible that the ‘real’ price of some new vehicles have actually gone down this past decade.

In any market, with any goods, when prices in real terms go down relative to substitute goods, consumers buy more. This is exactly what has been happening in the automotive sector and will continue to happen given the focus on cost reduction in the sector and the massive investments each and every OEM is making focused on technology (such as the focus by most OEMs on autonomous vehicles and electrifying their fleet). Many academics and futurists have written about the demise of the automotive sector and I’ve lost count of the articles in various publications that predict a dire future for light vehicles. I don’t see these trends as the end of the automotive sector; I see them as a new beginning for the automotive sector. Yes it will be radically different than in the past but it will also be more dynamic. The great Yves Landry (President of Chrysler Canada a couple decades ago) had it right when he said, “the future of the automotive industry is the six inches between our ears”. While GM announces 2,500 workers losing jobs in their Oshawa assembly plant they also announce 700 very high paying new engineering jobs going into their Markham R&D centre. Asking consumers to boycott GM vehicles takes away the added profits that GM needs to build on these 700 jobs. Yves Landry had it right two decades before the rest of us. DAR