CBI ANNUAL CONFERENCE 2011

"Export success from a business perspective"

Address from Sergio Marchionne,

Chairman/CEO of Chrysler Group and CEO of Fiat

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[Mr. Prime Minister],

Ladies and Gentlemen,

Good morning to you all.

Let me begin by thanking Sir Roger Carr and John Cridland for the invitation to address you at this CBI Annual Conference.

It is a particular pleasure to be here today, not only because of Fiat's relationship with the CBI, which goes back some 20 years, but also because of the opportunity it gives me to share some thoughts with you on the historic moment we are currently living through and on how businesses can contribute to the development of their domestic and regional economies.

The recent protests across Europe, soaring unemployment and the social crisis that exists in many parts of the world all provide ample reason for commentators to talk about the "age of outrage" and to fuel a pessimistic vision of the future.

However – although I by no means underestimate the seriousness of current circumstances in Europe and around the globe – I am not here to dwell on the current woes or speak of a dark and uncertain future.

In a recent article in the Wall Street Journal dealing with the untimely death of Steve Jobs, I found the following statement that should serve as a proper start to my reflections tonight.

"It is said that human beings can live for 40 days without food, four days without water and four minutes without air. But we cannot live for four seconds without hope….[T]the oxygen of human society is hope".

Today, I am here to speak to you about hope.

I believe that if we in this room – leaders from the worlds of business, finance and politics – have the ability to imagine a future of growth and development for our enterprises and for our nations, then we also have a collective responsibility to make that vision a reality.

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The contribution I can make to today's debate is to bring you the perspective of someone who is involved in the running of two large industrial groups with more than 250,000 employees around the world and who has to deal every day with the challenges of globalization.

Addressing today's theme of accelerating growth through export success requires that we examine two principal areas.

First is the imperative, imposed by this new phase in the evolution of the global economy, to boost cross-border revenue opportunities and to seek them even further afield. New markets are the new end game.

The second area to examine is our approach to international expansion and the choices we make in terms of localization of new activities and potential delocalization of existing ones.

This is a delicate area, not least because it touches on the moral responsibility that enterprises, particularly multinationals, have toward their home nation.

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The search for new markets, especially for players such as European automakers, is no longer simply a strategic choice aimed at driving revenue growth.

It has become an imperative for survival.

The global auto sector has been suffering for years from chronic overcapacity and in Europe the situation has now reached suffocation point.

Worldwide, installed production capacity is at over 95 million vehicles per year. This translates into excess capacity of 20 to 25 million units – much of that in Europe.

The reality is that while global markets were in full expansion mode, and demand in Europe remained high, we got away with ignoring the problem and deferring a solution.

But the crisis that struck in 2008 pushed our industry's structural handicap well beyond the manageable threshold into critical territory.

Even when demand returns to pre-crisis levels, the problem will remain.

Faced with that reality, there are few alternatives.

Either you rationalize the production side or you look for new opportunities.

And as everyone knows, there hasn't been any rationalization here, as has been done with courage and clearness of purpose on the other side of the Atlantic.

In the major economies in Europe, not a single unit of capacity has been taken out.

That would have required systemic intervention at the EU level.

We have urged intervention on multiple occasions, but neither individual Member States nor the EU as a community have responded to the call.

On the contrary, Member States have often acted unilaterally and the actions they have taken, rather than facilitating the necessary consolidation process, have in several cases directly obstructed it.

Many other industry sectors have already been through a major consolidation and rationalization – such as the steel industry in the 1990s when we did see coordination at the EU level.

There has been no such plan for the auto industry.

For whatever reason, together with the airline industry in Europe, the car industry was for a long period of time left to survive even though it was operating in a very sub-optimal manner.

I doubt there is a single European player today that can make money on the strength of the European market alone. The only exception, perhaps, being German automakers who have used their country's asset base to try and capitalize on some of the export demand coming out of Asia.

But if that demand were to shut down tomorrow for whatever reason, the untenable economics of the European activities would be immediately apparent.

Europe can't allow this problem to fester for much longer, because ultimately it will undermine the competitiveness of European automakers.

Implementing a solution will require a good deal of courage by European political leaders.

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The lack of a common intervention strategy in Europe and a failure to act have forced Fiat to find its own solution.

And that solution was to go elsewhere in search of ways to utilize, at least partially, our existing excess capacity. It meant finding new ways to share investment and achieve the necessary economies of scale.

And that is exactly what we did by striking an alliance with Chrysler – a unique opportunity the likes of which we will probably never see again.

To better understand the significance of this alliance, we need to look at two key factors affecting the auto industry today.

First that it is a very capital intensive industry – with development of a new platform requiring an investment of around a €1 billion – and second that it is highly sensitive to operating leverage.

As such, we need to achieve economies of scale that are sufficiently large to enable continued investment in the development of new architectures and new products.

As I have stated several times, a minimum volume of at least 6 million vehicles per annum is needed for an automaker to achieve an adequate return, with at least 1 million vehicles per platform.

Given these fundamental operating requirements, we are bound to see the elimination of marginal players going forward.

In fact, I believe we will end up with just 5-6 major players whose success will be based on sharing architectures and powertrains at the global level.

Our operating and strategic decisions have all been aimed at ensuring Fiat and Chrysler are in that group of global players.

Long-term, neither Fiat nor Chrysler would have made it on their own.

Fiat was too small, too dependent on the small car segments and too handicapped by the inadequate business model in Europe to have had any hope of a future.

And when we came along at the beginning of 2009, Chrysler was reeling from the shock of the financial crisis and years of mismanagement – together with the rest of the U.S. auto industry – and losing at times almost $1 billion a month.

This year, we will sell around 4.2 million cars combined, making Fiat-Chrysler the fifth largest automaker in the world.

By 2014, we expect to reach 5.9 million units.

And we will have just three main architectures that drive over 80% of total volumes.

By joining forces, we can better leverage our combined production capacity through the optimization of new product allocation.

The partnership also offers us the extraordinary opportunity to address the situation at our Italian plants, where production levels have for years been too low to be competitive.

It offers us an opportunity to upgrade the industrial system to standards necessary to compete internationally and, as a consequence, to be able to produce for export to more demanding markets, such as the United States.

If Fiat were to have continued investing alone in Italy, the risks would have been enormous: large expenditures that are not shared, insufficient volumes and high unit costs.

However, as a result of its tie-up with Chrysler, Fiat has the opportunity to be global once more, gaining access to markets outside Europe and sharing investment in the development of architectures that have a parallel application in North America.

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Acting, thinking and being global is something none of us can avoid.

Like it or not, in one form or another globalization is here to stay.

We can either resist the inevitable, and find our economy two steps behind the others, or embrace it and keep up with the rest of the world.

The time is now and the opportunities are enormous.

To continue to rely on domestic consumption to revive an ailing economy is pure folly.

Reliance on a model that assumes consumption will persistently outpace production is simply unsustainable. In many countries, domestic policy is in urgent need of realignment and businesses need to prepare for change by realigning internal resources and developing strategies that enable prioritization of investment for international growth.

I am not suggesting getting to that point is easy.

International business is a contact sport. When you arrive on the playing field, you will find competitors who are already selling to the customers you hope to reach and competitors who are already offering them highly attractive technological solutions.

But all businesses, big or small, have to accept the challenge of internationalization or risk being relegated to the sidelines.

Being in the game may also mean establishing a local manufacturing capability – a strategy which in large developed markets is advisable and in certain high-growth markets even essential.

That was how Fiat developed in Brazil. The outcome of that strategic choice is that Fiat has become the largest carmaker in the Brazilian market and for many years now has been viewed as a local player.

As a result of our agreement with Chrysler, we now have the ability to repeat this in North America.

And we have also established major in-country initiatives for development in other high-potential markets such as China, Russia and India.

All of these strategic initiatives represent fundamental building blocks for the future development of our business.

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Before opening up for questions and debate, I would like to conclude with some thoughts on the sense of responsibility with which the auto industry and others should approach their industrial mission.

Making cars and managing an industry as complex as ours is more than just a question of proper accounting and operational efficiency.

The auto sector, together with the other activities that are directly and indirectly dependent on it, is one of the most important contributors to GDP and employment for any advanced economy and, therefore, also to the well-being of society as a whole.

That means we have an obligation to act responsibly in the choices we make, including from a moral perspective.

It means ensuring that our every action is guided by values such as fairness, integrity, accountability and service to others in the communities where we live and work.

We also have an obligation to make our business more efficient and equip it with the tools – both industrial and cultural – that will ensure it is capable of competing with the best.

But that can't be done indiscriminately.

The expansion of production internationally clearly has to form part of a coherent strategy for global expansion, which shouldn't be confused with wholesale delocalization.

Excess delocalization does not necessarily translate into success in foreign markets and can even have serious negative consequences for an enterprise's domestic manufacturing activities.

In the auto industry, there has been a trend toward delocalization for some time and the motive is clear.

For an industry that, at the best of times, operates just above break-even, excess production capacity means enormous pressure on margins.

At the first hiccup in the market, this Damocles sword pushes the industry into loss-making territory.

And that fact has prompted many automakers to transfer production activities as a defensive measure against a price war.

I believe that strategy is very dangerous.

The geographic region losing the production activity suffers a contraction in employment and its structural competitiveness is reduced.

But more than that.

Reducing domestic production capacity generally results in a contraction in export volumes, increase in import volumes and a worsening in the balance of trade.

We saw this happen in Britain in the 1980s when a conscious choice was made to shift from a manufacturing to a more service-based economy.

But this didn't just simply lead to a decline in the industrial base – the equilibrium of the entire economic system was undermined.

An economy that forsakes manufacturing to focus on financial and other services depletes itself.

It loses workers, its skill base is eroded, and it sacrifices its economic stability.

All precious resources that, once they have disappeared, are very difficult to rebuild.

I feel I can say these things to a British audience, because these realities have been accepted. The current government is acting with determination to remedy these issues and to revive the industrial sector with the conviction that a strong manufacturing base is central and essential to a solid and sustainable economy.

At Fiat and Chrysler, we intend to play our due part in development of the local economy, wherever we operate.

That is why Fiat acted autonomously – without asking for aid or other forms of support – to eliminate inefficiencies in our manufacturing activities in Italy and ensure them a future.

This was behind our decision – difficult to explain to financial analysts – to shift production of the new Panda to Southern Italy from Poland, where its predecessor has been produced at a very high quality for the past eight years.

This decision was not based on purely rational or financial logic, but with an understanding of the importance of the auto industry to a nation's economy and with the same sense of responsibility that underpins all of our decisions.

Chrysler feels the same moral obligation in the United States.

I am beginning to hear from many corners that China is a big part – if not all – of the automotive industry's future. And there is no doubt our Asian prospects provide a great financial opportunity, an invaluable learning platform, and will call upon all of our resources, especially in terms of culture and innovation.

But none of us can forget, Chrysler for one, the commitment we made when we accepted financial support from the U.S. and Canadian governments to give new life to the automotive industry.

It is important that we keep in mind the key elements of that social contract and the long-term nature of the joint commitment we made, both automakers and organized labor, to establish the foundations for a lasting renaissance of the automotive industry in America.

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As Winston Churchill said, after the British won an important victory in World War II, "Now this is not the end. It is not even the beginning of the end. But it is, perhaps, the end of the beginning".

Fiat and Chrysler are still in their infancy.

Most of the paint is still on the palette and we have to put every effort now into completing this momentous integration, with humility, determination and rigor.

But I am confident because our alliance provides a solid base upon which to create the mosaic of a strong group.

A mosaic where every piece gets its strength from understanding the contribution it can make to the whole and from recognizing the value of the contribution of the other pieces.

Working together, we will chart a destiny that never forgets its roots but boldly welcomes the challenges and opportunities to express our identities in new ways.

This is the true strength – and I believe the most precious part – of our partnership, whose value lies in the incredible human wealth created for our people and companies.

Thank you again.

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