United States Senate Committee on Commerce, Science and Transportation

Committee Hearing

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Chrysler's Dealer Network

James Press

Vice Chairman and President

Chrysler LLC

Introduction

Chairman Rockefeller, Senator Hutchison and Members of the Committee, I appreciate this opportunity to discuss how and why the new Chrysler Group is realigning its dealer network. Chrysler LLC's decision about which of the company's 3,181 dealers would be brought forward to the new company was gut wrenching, but it was an absolutely necessary part of our effort to assure the long-term viability of the new Chrysler Group. The goal of the sale of our assets to a new company is to position Chrysler to move forward as a strong, financially sound automotive company serving our customers with a broader and more competitive lineup of environmentally friendly, fuel-efficient, high-quality vehicles, and an equally high level of customer service through an efficient dealer network.

The last thing Chrysler wanted to do was enter into Chapter 11. I can empathize with the dealers who were not brought forward into the new company, and can understand their disappointment. This has been the most difficult business action I have personally ever had to take. But the optimization of Chrysler's dealer restructuring plan is necessary to save the company. In an opinion filed May 31, 2009, granting approval for Chrysler's motion to sell substantially all its assets to a new company in an alliance with Fiat S.p.A., U.S. Bankruptcy Court Judge Gonzalez stated:

> *"The underlying argument of many opposing the transaction is not against the Government Entities' involvement. Rather, it is the desire to have the Governmental Entities protect every constituency within the auto industry from economic loss, and not to limit the protection to those interests that the government perceives as being essential to the survival of a successful "New Chrysler." For example, any dealership rejection that is approved will cause hardship to the particular dealership involved, but may well be necessary if New Chrysler is to survive. These are the kinds of economic decisions that have to be made in every bankruptcy case."*

There are two main elements that we can control as an automaker: our products and our dealer network. It's a well-documented opinion of the Administration and many members of Congress that over the years Chrysler has not moved fast enough to make the tough changes necessary to become a formidable competitor. The changes currently underway at Chrysler are needed for the company to produce competitive products and field a healthy dealer body. If we invest in better products while maintaining a disadvantaged dealer body, neither Chrysler nor our customers will benefit.

Why Optimizing Our Dealer Network Is Necessary

At Chrysler, we are realigning our dealer network to ensure that the new dealer body will be strong and competitive in the future. We entered Chapter 11 proceedings because the automobile industry is in a depression, brought about by the economic slowdown and the freezing up of credit markets. Chrysler was unable to survive in that environment because our products and our dealer network were not competitive. The new Chrysler that will be formed as a result of the Chapter 11 process needs to be able to survive and compete in the face of increasing global competition better than the Chrysler that went into it.

As a whole, the Chrysler dealer network is not profitable and therefore not viable. In 2008, the average U.S. automotive dealer sold 525 vehicles and made a profit of $279,000 according to the National Automobile Dealers Association, but Chrysler dealers sold only an average of 405 vehicles…and on average <u>lost</u> $3,431.

Dealer Profitability and Annual Unit Sales Comparisons - 2008

All Automotive Dealers U.S. National Average	All Chrysler Dealers U.S. National Average	Discontinued Chrysler Dealers
Retail Sales: 525 Vehicles	Retail Sales: 405 vehicles	Retail Sales: 163
Profit: $279,000	Profit: ($3,431)	Profit: ($73,000)

2008 Average Retail Sales per Dealership

Chrysler LLC Total	Chrysler LLC Assumed only	Honda	Toyota	Nissan
405	640	1,219	1,292	693

NADA and Chrysler data

Today's automotive industry cannot support the number of dealers currently in the marketplace. From 1990 through 2007, the industry averaged 16 million new vehicles sold each year. As a result of the industry depression, U.S. light vehicle sales fell to 13.2 million vehicles in 2008, and are projected to be only 10 million to 10.5 million vehicles in 2009. As part of the viability plan submitted to the administration on Feb. 17, Chrysler revised its Seasonally Adjusted Annual Rate (SAAR) forecast covering the next four years to reflect the reality of a declining automotive industry. The plan projected, commencing in 2009, a SAAR level of 10.1 million units and for years 2009 through 2012, an average SAAR level of only 10.8 million units.

There's not enough business for the number of dealers Chrysler has today, given that we have less than two-thirds of our former sales volume. The Chrysler dealer network faces the additional disadvantage of a legacy of dealers that sell only one or two of the company's three brands – Chrysler, Jeep® and Dodge – which have led to redundancies and inefficiencies in product development and marketing costs. Poor performing dealers within the dealer network also cost the company in terms of lost sales and low customer satisfaction.

The “overdealering” problem has been well chronicled over the past several years, even before the drastic downturn in sales. In the May 28, 2009, *Detroit Free Press*, journalist Sarah Webster recalled writing about the problem two years ago:

> *“When I was working on the series in 2007, a Chrysler dealer in the Boston area wanted me to visit his Dodge store so he could show me what a dump it was and how badly it was hurting Chrysler's image. This dealer wanted to upgrade his run-down store, but, the way he saw it, Chrysler had crowded so many dealerships into his area to fight over a shrinking pie that he would never be able to sell enough cars and trucks to pay for the renovations. Dealers clustered in an area would move quickly to discount cars and trucks -- sometimes taking a loss -- just so they could close the sale and move a vehicle off their lot.*
> *Cutting the price obviously hurt the dealers and the automakers. But the dealers had no choice. If they didn't, another nearby dealership selling the same models most certainly would.”*

David Cole, chairman of the Center for Automotive Research, was quoted in the May 17 *Crain's Detroit Business* as saying the current dealership network is too large.

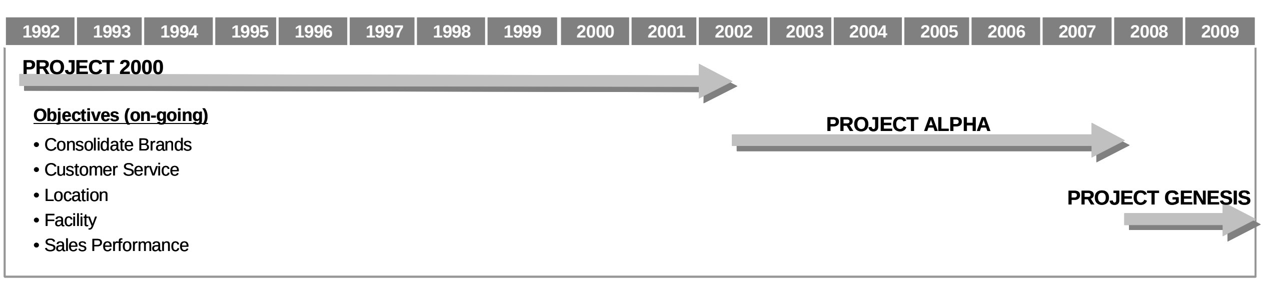
> *“The companies have lost so much volume, so they have dealerships for twice that volume…In the end, it's important to have successful dealers that can present the best possible face to the consumers,” Cole said.*

AutoNation, Inc., one of Chrysler’s largest dealer groups by volume, will be closing seven Chrysler dealerships as a result of our consolidation plan. Nevertheless, Mike Jackson, Chairman and Chief Executive Officer of AutoNation, released this statement:

> *“We believe Chrysler's consolidation plan is a difficult but positive step forward for Chrysler and the automotive retail industry. Dealer consolidation is a necessary measure in today's automotive industry and will strengthen America's dealer network and improve dealer profitability over the long term."*

Even before the current economic crisis, Chrysler realized it needed a smaller dealer network. Chrysler’s efforts to consolidate its dealer network date back to 1992, when we had 4,923 dealers, and have continued since.

History of Chrysler Dealer Network Optimization Initiatives



Chrysler has consistently communicated the need for a consolidation of dealers to our network. Our most recent restructuring effort, Project Genesis, is aimed at bringing all three brands under one roof to go along with our plan to produce fewer products that overlap. Genesis was launched in 2008 with an extensive communication plan including a series of meetings across the United States with our dealers and presentations at the National Auto Dealers Association annual conference. In each market, we identified the optimal number of dealers and locations and we began working collaboratively to build a healthy and profitable network.

Some have suggested that because an auto manufacturer like Chrysler sells cars to the dealerships, and these dealerships are independent businesses, they are not a cost to Chrysler. This is simply not true. For Chrysler, excess dealerships are costly in several ways. First is the the problem of maintaining several dealership channels. Maintaining multiple distribution networks is inefficient and costly. Product complexity is increased because of the need to provide products in the same segment to different networks. For example, Chrysler currently supplies dealers with two similar minivans, Chrysler Town & Country and Dodge Grand Caravan; two similar full-size sport-utilities, Chrysler Aspen and Dodge Durango; two similar mid-size SUVs, Dodge Nitro and Jeep® Liberty; and two similar sedans, the Chrysler Sebring and Dodge Avenger. Based on six major vehicle launches between 2005 and 2008, Chrysler incurred approximately $1.4 billion in incremental costs to develop these multiple pairs of "sister vehicles."

Second, as a result of overdealering, the marketing and advertising messages are split between multiple products, diminishing the reach and frequency of each campaign. For example, in 2008 we spent about $100 million on each of two marketing and advertising campaigns to launch our two redesigned minivans instead of spending half as much to support a single launch to attain virtually the same sales volume.

Going forward, the new Chrysler Group LLC will reduce the number of overlapping products. We are moving from 27 nameplates covering 13 product segments in 2007 calendar year to a target of 20 nameplates covering 17 segments by 2013 calendar year. Fewer nameplates with better product and customer market coverage will help improve the overall return on our product capital investment. This means that dealers need to have all three of our brands under one roof in order to offer a full range of products and to optimize their profit potential.

Examples of Lost Revenue and Cost Associated with Discontinued Dealers

• Product engineering and development for "sister vehicles"	$1.4 billion over 4 years
• Lost sales due to dealer underperformance	$1.5 billion revenue annually
• Administrative cost to maintain the 789 discontinued dealers	$33 million annually

- Marketing and advertising $150 million annually
  Chrysler data

Finally, poor performing dealers cost us customers. It's true that dealers are our customers, but it works both ways. If they don't sell cars, we don't either. Poor performing dealerships cannot afford to keep facilities up-to-date or hire and train the best people, resulting in poor customer experience and lower sales. In fact, in 2008 the 789 discontinued dealers achieved sales of only 73 percent of the minimum sales responsibility, representing 55,000 lost unit sales and $1.5 billion in lost revenue in 2008.

A financially strong, competitive dealership should generate profits over $1 million a year. Profitable dealers can afford to invest in facilities, in people, in training, and in amenities that produce a high level of customer satisfaction.

As I said earlier, we tried our best to avoid Chapter 11. Now as Chrysler moves through the process, we need to do our best to form a new company that will evolve from the process as viable as possible. We recognize that the U.S. government and the American taxpayers have a stake in our success, and we are committed to building a new American automotive company that is financially sound and competitive both from a product and dealer perspective. This was our goal when we presented our viability plan in February and it is our goal in the Chapter 11 process.

How Identified Dealers: a Data-Driven, Objective Methodology

To achieve the necessary realignment, we are using a thoughtful, rigorous and objective process designed to have the least negative impact while still creating a new dealer footprint scaled to be viable and profitable for the long term. The methodology was consistently applied to every dealer in the company's U.S. operations. The decisions made to either continue or discontinue dealer contracts were based on a robust process that looked at all market types, Metro, Secondary and Rural. This analysis reviewed many factors that are unique for each market and dealer. The primary focus of this initiative, as it has been under Project Genesis, was to create a more viable network footprint that enhanced sales per dealer while bringing all three brands together within each retail outlet.

These factors included:

- Total sales potential for each individual market
- Each dealer's record of meeting minimum sales responsibility
- A scorecard that each dealer receives monthly, and includes metrics for sales, market share, new vehicle shipments, sales satisfaction index, service satisfaction index, warranty repair expense, and other comparative measures
- Facility that meets corporate standards

- Location in regard to optimum retail growth area
- Exclusive representation within larger markets

A team of people within our local business centers around the country as well as headquarters staff reviewed every market and dealer situation as a group many times. From this analysis the 2,392 dealers who would best carry the new company forward were identified.

Although Chrysler submitted a plan to reduce total dealer count by 25 percent, those dealers represent only 14 percent of our sales volume. Half of these dealerships sell fewer than 100 vehicles a year, or less than nine vehicles per month on average (that compares with 125 vehicles sold per month on average at Toyota dealerships). About 44 percent of the discontinued dealers who reported revenues were profitable, earning $84 million last year, while the remaining 56 percent were unprofitable, losing a total of $136 million.

Chrysler 789 Discontinued Dealers at a Glance

- 25 % of total dealer network
- 14 % of sales volume
- 50 % sell 100 or fewer new vehicles per year
- 84 % sell more used than new vehicles
- 44 % are dealers dualled with a competing franchise

In many instances, we're moving a franchise as part of our overall Project Genesis consolidation that brings all three of our brands under one roof. So, when a Dodge dealer's contract is not assumed, that franchise in some cases will wind up in a nearby Chrysler/Jeep store. In that case the business should grow, become more profitable and have a beneficial impact on the community. Of our remaining 2,392 dealers, 84 percent will carry all three of our brands compared to 62 percent prior to implementation of this plan. The new Chrysler Group LLC dealer network will be in better retail locations with more modern facilities that are convenient and better positioned to serve customers. With the opportunity for increased sales per outlet, dealers should experience an enhanced franchise value resulting in more willingness to invest in facilities, people and their local communities.

Chrysler Customers Will Still Have Convenient Access to Improved Dealer Network

Of the 789 discontinued dealers, 284 are within 10 miles of a same-line dealer that is being retained. Based on registration data, our customers reside an average of 6.67 miles from the nearest Chrysler, Jeep or Dodge dealer now; this distance will increase to 7.09 miles after the consolidation. With regard to rural dealers, the distance increases from 10 to 11 miles. Even with the consolidation, our dealers on average are more conveniently located to customers than Toyota or Honda dealers are to their customers.

Customer Convenience Comparison

Average distance in miles a customer must drive to reach a dealership

	Old Chrysler	New Chrysler	Change	Toyota	Honda	Chevy	Ford
Metro	4.45	4.82	0.37	5.01	5.11	4.10	4.23
Secondary	6.08	6.44	0.36	7.38	7.58	5.69	5.76
Rural	9.72	10.70	0.98	19.27	24.27	8.04	8.69
Total	**6.28**	**6.80**	**0.52**	**9.11**	**10.31**	**5.58**	**5.81**

Urban Science 2008

It's vital to Chrysler's future that we take care of our customers' needs during this process. We have a comprehensive communications plan to be launched by the new company that will include a letter to all owners, explaining our alliance with Fiat and emergence as a vibrant new company. These letters also will assure customers that all warranty claims will continue to be honored and provide a toll-free hot line number to a call center to answer their questions. Those owners who are customers of terminated dealers will receive another letter a few days after the terminations are official, providing information on other dealers in their area as well as a service offer.

Timing of the Dealer Consolidation

The time frame for discontinuing dealers was driven by the Chapter 11 process and the need for speed in order to preserve maximum value for Chrysler. Prior to May 1, Chrysler had planned to avoid bankruptcy. Only after filing did we begin the necessary process of actually identifying which dealers could go forward with the new company. Timing was mandated by the Chapter 11 proceeding, including the requirement to complete our strategic alliance with Fiat by June 15. It was important to Chrysler and Fiat that a new and stronger dealer network would be in place by the closing date. On May 14, we notified the dealers of our decisions, and later filed the list of discontinued dealers with the court.

In his approval of the sale motion, Judge Gonzalez confirmed, “while in Chapter 11, Chrysler is a wasting asset,” – meaning that while we’re not building cars, our assets are deteriorating and customers are losing confidence.

It is in the best interest of Chrysler and discontinued dealers to move quickly through this process. The number of days’ notice provided to discontinued dealers was similar to the 30 days provided under the Chrysler voluntary termination process, and it provided for a quick process in everyone’s best interest. Financial commitments from both the U.S. and Canadian governments require our alliance with Fiat be completed by June 15. This deadline determined a number of other deadlines, including the June 9 termination date for rejected dealers. That termination date is needed to ensure that our new dealership structure will be firmly in place at or about the time the new company is formed with Fiat – something understandably important to Fiat.

The success of our new enterprise depends in large part on this new dealer body, and we must focus our limited resources on this. Similarly, we do not want customers to have any confusion about who is and who is not a dealer for the new company. The termination date for discontinued dealers was chosen, therefore, to meet the demands of our creditors and partners, to bring our new dealer network online as quickly as possible, and to strongly signal customers that the new dealer body will meet their needs.

What Chrysler Is Doing to Provide Relief for Discontinued Dealers

We have worked hard to assure as soft a landing as possible for the dealers whose contracts have not been assumed. We quickly put together a program with GMAC to provide wholesale financing so the inventory could be redistributed to the dealers going forward. Under this program, a dealer would receive the invoice price less holdback and other fees the dealer was already paid, less a $350 dollar fee for inspection, cleaning and transportation of each vehicle. Since the inventory is owned by a dealer, their approval is required for Chrysler to assist in the redistribution process. Every dealer was asked to sign an "Inventory Assistance Acknowledgement Form" indicating that he or she understood the process and wanted our assistance. There were 42,000 vehicles in stock at discontinued dealers on May 14, and working together, we’ve already sold or redistributed 89 percent of all vehicles in discontinued dealer inventory.

Inventory Status of Discontinued Dealers

	5/14/09 Dealer Inventory	Sold/Re-distributed		Balance	
		#	%	#	%
Total	**42,006**	**37,488**	**89%**	**4,518**	**11 %**
(memo) Dealers Accepting Assistance	20,226	19,679	97%	547	3 %

As of 6/1/09

Every dealer on the discontinued list was contacted by a representative from his or her business center by close of business May 22. Each dealer was advised of and received a letter that outlined the process that Chrysler developed for assisting in the disposition of vehicles, parts inventory, special tools and signage. While our objective is to have virtually all units sold or redistributed by June 9, we will continue to work with a dealer after that date in the redistribution of inventory and in the processing of incentive and warranty claims due to the dealer.

The potential job losses associated with discontinued dealers are far less than some of the public speculation you have seen. Based on our data, we estimate a total of 29,982 are employed at the dealerships that we proposed to discontinue. However, it is important to note that 44 percent of these dealers are dualled with our competitors, and are expected to continue selling those other makes. In those dualled dealerships Chrysler brands represent only 12 percent of their total sales volume. In addition, it’s important to note that 84 percent of these dealers sell more used vehicles than new, and many of these dealers will continue selling and servicing pre-owned vehicles. Therefore, it is a safe bet that a substantial number of these employees will not lose their jobs. For those that do, we're expanding our current online job posting hiring process to help place dealership employees who lose their positions. The job loss is painful and tragic, but is much better than the alternative of all dealers closing as a result of liquidation.

Shared Sacrifice Required to Save Chrysler

There’s no question that Chapter 11 has been a painful process. While a number of elected officials, commentators, and other observers of the industry have advocated bankruptcy for the company, it was not Chrysler’s first choice. However, at this point, we are committed to do our best to create a new company that will succeed in the long term. We recognize that you and your constituents have a stake in our success, and that’s why we are committed to take the tough but necessary actions to build a new Chrysler that is fully able to compete and win. To do that we must provide the American public fuel-efficient vehicles with strong consumer appeal and a strong, high-quality and viable dealer network: One without the other will fail.

Does my heart go out to the dealers who will not be part of the new company? Absolutely. But we've had to make many hard choices to create a viable business and preserve jobs for tens of thousands of people. Many of our stakeholders have made unprecedented sacrifices. In that perspective, the sacrifices of the dealer network are in-line and appropriate considering that 27,000 Chrysler jobs were eliminated, the UAW accepted wage and benefit cuts that place them on a par with workers at transplant operations; many suppliers have experienced pricing reductions in addition to significant job losses resulting from reduced volumes, and many are retirees losing a significant portion of their pensions.

Given the auto industry depression, Chrysler had no choice but to seek Chapter 11 protection. Facing that reality, we used a thoughtful, fair process, and we are doing everything possible to soften the impact to everyone affected.

Realignment of our dealer network will help create a vibrant new company, with a stronger and leaner organization and a key partner in Fiat. Moving forward with 75 percent of our dealer network is far better than the alternative of liquidation, which Chrysler will face if the sale of assets is not finalized and the alliance with Fiat completed. Under liquidation, tens of thousands would be out of work, and all 3,181 of our U.S. dealerships would lose their agreements to sell and service Chrysler vehicles, which would have a far more devastating effect on scores of communities and on our national economy.

We're extremely excited about our prospects going forward. Our alliance with Fiat will provide significant strategic advantages, including access to high quality, fuel-efficient small and compact vehicles, as well as platforms, powertrain technologies and components that will be produced at Chrysler manufacturing sites. Together, the Chrysler Group and Fiat will bring a range of exciting, new fuel-efficient compact vehicles to North American consumers, helping stimulate growth in this segment. The new Chrysler Group's revamped dealer network will help ensure that remaining dealers and the new company will be stronger, and more profitable, providing a solid base of jobs and capable of growth going forward.

Chrysler's Special Bond with the American Public

Throughout its 84-year history, Chrysler has had and will continue to have a special relationship with the American public. The "new" Chrysler Group LLC will continue to provide innovative, high-quality, vehicles and service to the American consumer, and also will be fully capable of competing in the global market. It will be an exciting time for the entire "new" Chrysler family.

We recognize that we have a special bond with America and with American taxpayers, and we're committed to deliver on their investment by building a viable company and building high quality products with strong consumer appeal. We take to heart our responsibility to produce vehicles that serve society and contribute to getting our country and our national economy back on track.

As we have testified before, several actions will help stimulate automotive sales. First, returning to a functioning finance environment for our customers and dealers will help spur sales. Second, programs that will increase demand such as the Drive America Forward Act sponsored by Senators Stabenow and Brownback would be helpful. This fleet modernization program will stimulate sales while improving fuel economy.

A strong new Chrysler can play a key role in rebuilding the American manufacturing base – and manufacturing must thrive if we want the economy to grow in the long term. Simply put our country's health and security depends on our ability as a nation to make things that people want to buy.

Given the fragile state of the economy, a failure of Chrysler would be a severe setback for the efforts to restore confidence and revive growth. A healthy U.S.-based automotive industry is the backbone of the nation's economy – creating wealth. Every direct job at an automaker creates nearly 10 more jobs at suppliers and supporting industries. The auto industry has been a great engine for producing good-paying, middle-class jobs.

We are very grateful to loyal Chrysler customers who have supported us throughout this process and assure them Chrysler Group is well prepared to produce and support quality vehicles under the Jeep®, Dodge and Chrysler brands as well as parts under the Mopar® brand. We also recognize the sacrifices, unstinting loyalty and enduring belief in Chrysler of many stakeholders, including Cerberus and Daimler, the UAW and CAW leadership, employees, dealers and suppliers who made critical contributions to the viability of Chrysler Group, Chrysler Financial and their efforts with GMAC to provide financing, and the energy and commitment of the U.S. Treasury, the President's Auto Task Force, Members of Congress and representatives at the state and community level and Canadian Federal and Ontario Provincial governments in helping to move Chrysler Group forward. Without the extraordinary efforts of all these constituents, the alliance and the creation of a new Chrysler would not have been possible.

All of us at Chrysler take enormous pride in the contributions that the company has made to our industry and country. We also are deeply honored by the trust that customers continue to place in us, and we look forward to continuing to earn their trust for many more years.

Thank you very much.