

**Statement on
Proposed Rulemaking to Establish Light-Duty Vehicle Greenhouse Gas Emission
Standards and Corporate Average Fuel Economy Standards**

**Detroit Michigan,
October 21, 2009**

My name is Rob Kleinbaum. Permit me to give a brief introduction: I am a management consultant. For the last 15 years, GM has been a major client. Through 2008, I have done at least one major project a year for the company; they have covered many subjects, functions, and regions. Other clients have included global brewers, hotels, shipping, healthcare, and manufacturing. Prior to entering consulting I was a GM executive level employee; I worked for GM for 9 years. I have a Ph.D. in Economics from University of Michigan.

Last February, I authored a paper entitled "Retooling GM's Culture" which argued that GM would not be a viable company unless it changed its culture. Last August, I co-authored a paper with Dr. Walter McManus, "Fixing Detroit: How Far, How Fast, How Fuel Efficient", that described how the Detroit 3, and especially GM had ignored its own research for many years on the importance of fuel economy. The critical finding of that paper was that increasing fuel economy standards would increase the share and profitability of the Detroit 3 by eliminating a competitive disadvantage; the increase in sales and pricing power would outweigh the cost increases.

Rather than impeding turnaround efforts, fuel economy needs to be viewed in the context of long -term viability of the Detroit 3. Based on my experience in the auto industry, I not only support the rulemaking under consideration today but view it as critical to that long term viability.

There are those who argue that regulations mandating fuel economy performance standards will result in lower profitability for the car companies. This would be true if you believed that Detroit automakers have been profit maximizing all these years. I think that everyone now agrees on the importance of changing the culture and world view of GM.

I would like to believe the New GM is indeed a New GM, and I completely grant the sincerity of many within the company in achieving that goal. But Mr. Henderson's genuine desire to change the culture could be thwarted by the fact that the company is still being run by the people who put it into the mess in the first place and who drove the culture of Old GM. While there is a new Board, and it is activist, and many have departed, there is has been no influx of new people.

And, of chief concern is that people who actively ignored the research on the importance of fuel economy and believe in their hearts that GHG is a “crock” are still in senior positions and spread throughout the organization. The net result is a deep concern that while they will say the right words, they will still under invest in fuel-efficient vehicles relative to what the market wants and will continue to lose share and have its very viability threatened.

- a. Note that this under investment could take many different forms. It need not be something so glaring as the number of entries, but is more likely to be seen in the investment in the particular entry, so that the vehicles are uncompetitive in terms of quality and features, when home runs are what GM desperately needs.

As Ronald Reagan used to say, we need to trust but verify. And that, it seems, is exactly what the new rule does.

Central to the success of both the rule and the automakers, is transparency.

Much of the debate on the impact of fuel economy has been clouded by the fact that data and assumptions are not disclosed. NHTSA has historically based its analysis of potential new CAFE standards heavily on private information—extensive and detailed product plans for vehicles, engines, and transmissions. This private information is obtained voluntarily, and NHTSA is obligated to prevent its public disclosure.

The new rule’s proposed approach is more transparent, with most sources in the public domain or readily available. This is a critically important change in the methodology since, in the new process, anyone can repeat and review the analyses done by the agencies.

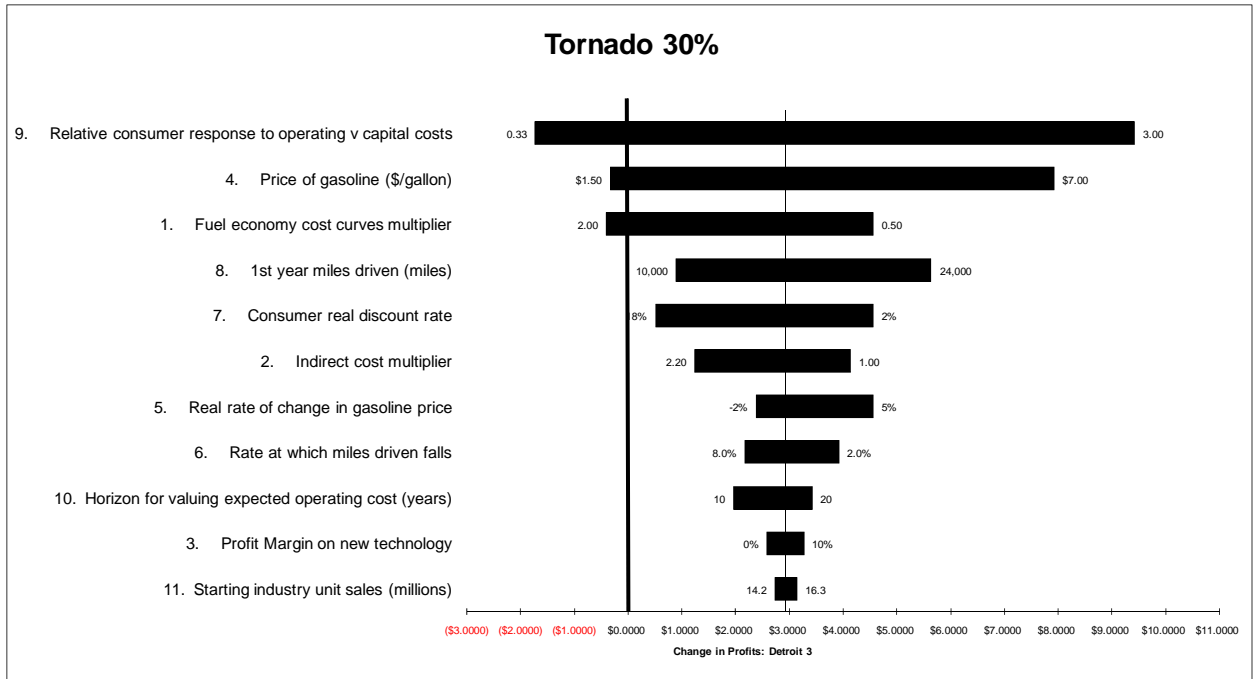
Another safeguard is regulatory support that is independent and vigilant. The regulating institutions need to have the interests of the company and public at heart but cannot be “owned” by either. I believe that previous public policy has enabled many of the Old GM’s worst features. GM’s lobbyists were effective in many subtle ways and the net effect is they and their allies helped drive GM to bankruptcy while those who were considered “hostile” were trying to push the company in a direction that could have saved it. These are hard words from someone who is self described free market libertarian, but they are a product of long and deep observation and of the deepest affection and concern for the company.

Finally, another way to “trust but verify” is to include an important analytic tool that can help focus debate on the right issues – that is, a properly conducted sensitivity analysis. Currently the new rule does not include this kind of analysis. There is a great deal of debate about parameters, but the question is: does it really matter? That is, would it lead to a different decision?

In the paper “Fixing a sensitivity analysis was used to understand the robustness of our results. As far as we can ascertain, no one has taken a thorough look at the impact of uncertainty over the key inputs on sales and profits. People debate what the best single value of a parameter might be, and use the arguments to play “gotcha” and then disparage the overall legitimacy of a particular position. They have such widely different prior beliefs that empirical analysis is always unpersuasive. Rather than add to the noise, we wanted to incorporate the full range of opinion into the results and see how the outcome changes. The table below lists the factors and the ranges used in the sensitivity analysis. They can be grouped into three categories: costs and margins, consumer expectations, and consumer preferences. The range encompasses the debate over each of these issues. As example, to examine the range of debate on the costs of improving fuel economy, the Mesler cost curves, we used a multiplier. The base case is a one, but we also examined the cases where costs might be twice as much and half as much. The table below shows the ranges we used.

Sensitivity Analysis: Factors Subject to Uncertainty				
Factors		Range Used in Sensitivity Analysis		
		Unfavorable	Base	Favorable
Cost & Margins	Fuel economy cost curves multiplier	2	1	0.5
	Indirect cost multiplier	2.2	1.5	1
	Profit Margin on new technology	0%	5%	10%
Consumer Expectations	Price of gasoline (\$/gallon)	\$1.50	\$3.00	\$7.00
	Real rate of change in gasoline price	-2.00%	0.00%	5.00%
	Rate at which miles driven falls (Scrappage)	8.00%	5.20%	2.00%
	1st year miles driven (Future miles)	10,000	15,000	18,000
Consumer Preferences	Consumer real discount rate	18.00%	7.00%	2.00%
	Relative consumer response to operating v capital costs	0.33	1	3
	Horizon for valuing expected operating cost (years)	10	15	20
Industry	Industry size (millions of units)	14.2	15.2	16.3

The chart below shows the impact of the uncertainties on the decision, shown by the thick vertical line at “0”.



If this method became common, debate would be much more fruitful. Let's argue about the stuff that really matters and do so with publicly available data and explicit methods.

Thank you.