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A lighter touch in the auto industry

Governments must not stand in the way of innovation

The auto industry is back on the road after a tumultuous year, but obstacles still lie ahead.

Carmakers face the end of taxpayer-funded incentive schemes to stimulate consumer demand, such as the US "cash for clunkers" plan. In Germany, this is expected to lead to a sharp drop in demand this year from the artificially inflated level of 2009.

As the cautiously optimistic mood at the Detroit auto show this week indicated, however, the companies that remain from last year's shake-out are looking forward to recovery. Both Ford and General Motors unveiled ambitious plans for global passenger cars.

One result of bail-outs is that global over-capacity remains a big problem, making many companies marginally profitable at best. Yet the crisis has instilled a sense of urgency among carmakers to become more international, often with cross-border alliances.

Fiat has linked up with Chrysler and Volkswagen has formed an alliance with Suzuki. The prediction of Sergio Marchionne, chief executive of Fiat/Chrysler, that six global carmakers will emerge from this consolidation looks as if it may soon be proved true.

Governments have a role to play in promoting innovation and efficiency in an industry that badly needs both. Having propped up entire companies that perhaps ought to have been allowed to fail, they need to permit piecemeal consolidation to proceed.

The first priority is to allow car companies to reduce capacity by shutting down plants. It will be impossible to reduce European over-capacity if each national government blocks factory closures in its own country. Fiat faces a test case over its plan to close a manufacturing plant in Sicily.

A second priority is to provide incentives for the industry's switch towards smaller, more fuel-efficient vehicles. One reason for the global weakness of US companies is their over-dependence on domestic demand for trucks and sports utility vehicles.

The axis of the industry is already shifting towards emerging markets, particularly in Asia and Latin America. If US and European companies are to maintain their competitive position – as their governments hope – they need to keep up with these changes.

Governments have intervened heavily in the industry in the past year and will continue to pull strings through regulations and taxes. The best thing they can do now is to adopt a lighter touch, and not to stand in the way of necessary rationalisation.