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GM gains, faces pains

Despite strong quarter, firm's restructuring has ways to go

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DETROIT -- General Motors Corp. drastically narrowed its losses in 2006 thanks to a host of cost-saving moves, but now the pressure is on the struggling automaker to start turning a profit.

Even as GM reported its best quarter in more than two years Wednesday, swinging to a $950 million profit in the fourth quarter of 2006 from a loss of $6.6 billion a year earlier, the automaker ended the year with $2 billion in losses and its critical North American operations still in the red.

And with tens of thousands of fewer employees on its payroll and popular and profitable new pickups on the market, GM may be running out of plausible explanations should it turn in another money-losing performance in 2007.

"For the first time in a long time, I am questioning their strategy," said analyst Brad Rubin at investment firm BNP Paribas, after reviewing GM's year-end and fourth-quarter results. "The results aren't that great considering everything. It still isn't enough."

GM's recovery leads Big 3

Among Detroit's automakers, all struggling against intense competition from Asian rivals in their home market, GM is furthest along in its recovery and investors are watching its progress closely.

Analysts had been expecting strong results from GM for 2006, a year in which the automaker pared its work force, cut production costs and scaled back less profitable businesses, such as sales to rental-car companies.

Some had even expected GM to post a small profit in North America and were disappointed by Wednesday's results, partly because the automaker had taken a number of actions last year as part of its plan to restore profits following a staggering $10.4 billion loss in 2005.

GM executed a costly buyout program that ushered out more than 34,300 U.S. union workers. Its new full-size pickups, a bastion of profits, arrived on the market. And it was realizing savings from a landmark deal struck in 2005 with the United Auto Workers to cut health care costs.

During a conference call Wednesday to discuss the company's 2006 financial results, investors and reporters grilled GM Chief Financial Officer Fritz Henderson about how GM will make money going forward if it has not been able to despite its moves to reduce costs and increase revenues.

"While improved, we still have some massive strategic issues in front of us," Henderson said. "The results for North America are clearly not an acceptable level."

Henderson said GM expects 2007 earnings to be better than last year, though he would not detail the automaker's predictions.

The company will be bolstered by the debut of new heavy-duty pickups and a full year of sales for the new Chevrolet Silverado and GMC Sierra pickup lineup, Henderson said. The revamped Chevrolet Malibu sedan is also expected to help GM in the increasingly important midsize car market.

GM also will continue its drive to cut costly incentives and less-profitable sales to rental fleets, steps that will help GM make more money on its cars and trucks.

And the cost-cutting will continue on top of the $6.8 billion GM slashed in 2006, Henderson said. The goal is to achieve $9 billion in cost savings in 2007.

GM took a hit from losses incurred by its former finance arm, GMAC, because of problems with defaults on subprime loans through its residential mortgage division. That risk should lessen in 2007, Henderson said.

While its North American operations improved from last year, GM lost $14 million in the fourth quarter here, compared to $1.4 billion in red ink a year ago. The unit finished the year with a loss of $779 million.

The company sold 9.1 million vehicles worldwide in 2006 for record revenue of $207 billion, up from $195 billion in 2005.

Included in the year-end results were 11 months of earnings from GMAC. GM sold a majority stake in the company in a transaction that was completed Nov. 30.

GMAC, which announced its year-end and fourth quarter results Tuesday, made $2.1 billion in 2006. The company said it expects to receive $1 billion in cash this quarter from GM in relation to a change in the lending arm's balance sheet.

Analyst questions some gains

Despite GM's overall loss and the red ink in North America, analysts agreed the 2006 results signal GM's turnaround is gaining ground.

"GM's fourth-quarter profit of $950 million is further evidence that the turnaround plan is working," David Kudla, chief investment strategist for Mainstay Capital Management, said in a research note. "We look for further positive earnings momentum as a result of cost cutting and improved SUV and truck sales."

Still, BNP's Rubin said GM's gains in some areas are questionable. Results for operations in Europe, while profitable, were disappointing, he said, and Wall Street was expecting a profit around $100 million in North America.

In addition, $236 million of GM's fourth-quarter profit came in the category of "automotive other," which is largely one-time gains that can't be counted on year after year, Rubin said.

"When you proclaim that you're going to have good results, after you restate your earnings, and you come out with this -- it questions your credibility," he said.

Such pressure from Wall Street can work against a company trying to stage a major comeback, said corporate restructuring expert Gregory Charleston, managing director of Conway, MacKenzie & Dunleavy in Detroit. GM must be careful to make decisions for the long term and not obsess over quarterly results, he said.

Turnarounds will only be successful if a company can solve the root problem, which, at GM, is its sliding market share, he said. And that will take years to reverse.

"When you're trying to turn around a company and you're focused on pleasing analysts for the particular quarter, you can make the wrong decisions," Charleston said. "Analysts and people who follow the industry have short-term expectations. But the best turnarounds are the ones you look back at over a five-year period."