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General Motors Company (GM) CEO Mary Barra on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-29-19 Earnings Summary

Press Release *10-Q* *Slides*

EPS of $1.72 beats by $0.35 | Revenue of $35.47B (-0.89% Y/Y) beats by $259.03M

Earning Call Audio

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General Motors Company (NYSE:GM) Q3 2019 Earnings Conference Call October 29, 2019 10:00 AM ET

Company Participants

Rocky Gupta - Treasurer & Vice President of Investor Relations

Mary Barra - Chairman & Chief Executive Officer

Dhivya Suryadevara - Executive Vice President and Chief Financial Officer

Conference Call Participants

Joseph Spak - RBC Capital Markets

John Murphy - Bank of America

Itay Michaeli - Citi

Adam Jonas - Morgan Stanley

Ryan Brinkman - JP Morgan

Brian Johnson - Barclays

Dan Levy - Credit Suisse

Emmanuel Rosner - Deutsche Bank

Chris McNally - Evercore

Operator

Ladies and gentlemen, welcome to the General Motors Company Third Quarter 2019 Earnings Conference Call. During the opening remarks, all participants will be in a listen-only mode. After the opening remarks, we will conduct a question-and-answer session. [Operator Instructions] As a reminder, this conference call is being recorded Tuesday October 29, 2019.

I would now like to turn the conference over to Rocky Gupta, Treasurer and Vice President of Investor Relations.

Rocky Gupta

Thanks Dorothy. Good morning everyone and thank you for joining us, as we review GM's financial results for the third quarter of 2019. Our press release was issued this morning and the conference call materials are available on the GM Investor Relations website. We are also broadcasting this call via webcast.

I’m joined today by Mary Barra, GM's Chairman and CEO; Dhivya Suryadevara, GM's Executive Vice President, CFO, and a number of other Executives. Before we begin, I would like to direct your attention to the forward-looking statements on the first page of the chart set. The content of our call will be governed by this language.

I will now turn the call over to Mary Barra.

Mary Barra

Thanks, Rocky, and good morning everybody, and thank you joining the call. As you know, we have a ratified labor agreement and I am very glad that our highly skilled employees are back to work building winning cars, trucks, crossovers and components. From the outside, our goal was to reach an agreement that works for our shareholders, our employees and our company as we confirmed the realities of our rapidly transforming industry.

A contract does the right thing for our employees without compromising competitiveness or flexibility. It includes improve half forward for our in progression and temporary workers that will create more engagements and a motivated team. This is foundational for our improving job satisfaction, health and safety, quality and productivity, all of which will strengthen the future of this company and creates shareholder value.

The contract also affirms our commitment to a strong U.S. manufacturing base with planned investments totaling $7.7 billion. We'll secure the future of our Detroit-Hamtramck assembly plant with an all-new electric pickup truck that builds on established truck leadership. We're also moving forward on an effort to bring battery cell production to the Mahoney Valley in Ohio, which will create 1,000 manufacturing jobs.

Before I continue, I want to thank our dedicated suppliers. They were in constant contact with us throughout the work stoppage and ensuring as they would be ready for a prompt, safe restart once the new contract was ratified. And I'd also like to thank our dealers who helped us sustain our momentum in the marketplace and they worked very hard to minimize the inconvenience to our customers caused by our limited ability to shift service and repair part.

To speed up recovery and get cars flowing to dealership, comprehensive plans are in place to allow the network to recover as quickly as possible. So now, we are moving forward as one team. However, we have a lot of work to do in many areas, as the loss profits from the work stoppage were significant. In a few minutes, Dhivya will talk about the financial impact of this drive and our full year outlook.

Overall in the third quarter, we delivered net revenue of $35.5 billion, EBITDA adjusted of $3 billion, EBIT adjusted margin of 8.4%, EBIT, EPS diluted adjusted of $1.72, automotive adjusted free cash flow of $3.8 billion, and a ROIC adjusted of $21.9 on a trailing four quarters basis.

Looking at North America, we delivered strong business performance in the quarter which was unfavorably impacted by the strike in the United States and increased warranty and retail cost related to our previous generation full size pickup trucks and full size SUV. Overall, retail deliveries rose 6% year-over-year led by double-digit gains and light-duty Chevrolet Silverado and GMC Sierra pickups and strong demand for our all new heavy-duty pickup trucks.

Cadillac continues to capitalize on its expanding crossover portfolio in the United States and China. In the US, Cadillac crossover deliveries increased by 67% in the quarter led by the segment leading XT4 and the all-new XT6 which is gaining momentum in the market.

In China, the XT4 and the new XT5 helped drive deliveries up 11%, amidst lower industry sales. With the XT6 joining the lineup, we expect Cadillac will further strengthen its position in China's growing luxury SUV segment. Our luxury sedan portfolio updates continue with the launch of the all new CT5 midsize luxury sedan in China this quarter by early next year by the U.S. built CT5 and CT4 in North America.

Finally, as we look at meeting customer demand, our U.S. dealerships finished the third quarter with a healthy level of inventory. As the strike continued, our teams work tirelessly to ensure we could ship as many vehicles as possible to our dealers. However with no additional vehicles in the pipeline for many weeks, our dealer inventories will be temporary leaner than we'd like. The team is doing everything that's powered to restore our supply of vehicles back to normal levels.

Regarding our international operations, in China, the business environment remains challenging and volatile. Year-over-year, industry vehicle sales declined nearly 11% in the quarter. We underperformed relative to the industry mostly because of segment shifts and lower demand for outgoing models, partially offset by growth in Cadillac delivery.

In addition to taking appropriate cost actions, we are improving our product mix. We launched seven new models in third quarter with plans to launch five new and refresh models in the fourth quarter. In addition, the team continues to focus on accelerating cost reduction initiatives to improve performance, given the business environment.

In South America, we continue to take steps to improve the business and protect our strong franchise while navigating FX and other macro challenges. In September, we launched the all new 2020 Chevrolet Onix plus in Brazil. It is the first model in South America from our new global family of vehicles and carries a five star safety rating.

During its initial month on sale, customer demand greatly outpaced available supply and we are doubling our production this month. The Onix hedge back follows next month and together, we believe these new vehicles will further strengthen our Chevy brand leadership and Onix position as the region's bestselling vehicle.

As we execute our turnaround plan for international operations, we continue to take decisive steps to achieve sustainable profitability in every market we participate and cease operations that are not. Earlier this week, we announced our intent to cease selling Chevrolet vehicles in Indonesia over the coming quarters.

Turning to our EV progress, Chevrolet is launching the 2020 Bolt EV with battery improvements that enable an EPA estimated 259 miles of all electric range at a full charge at the same price. The more powerful battery pack is the same size and weight as previous year's models, but its greater energy density delivers 21 additional miles of range and that's more value to our customers.

It's built on our industry leadership and improving battery range and reducing battery cell powers per kilowatt hour, and we expect this progress to continue. The 2020 Bolt also retains what our customers love about this vehicle, instant torque, excellent riding handling, and a zero to 60 times of just 6.5 seconds.

And on the AV front, Cruise increased its testing and validation mile during the quarter and increased its community engagement and relationship building. In addition to Cruise, GM and Honda continued their joint development of a new purpose built shared autonomous vehicle.

So to recap, our strong operating performances in the quarter were supported by a robust sale of trucks and crossovers in the United States. We've also made significant progress at our transformational cost initiatives. GM has achieved 2.4 billion and transformation cost savings in 2018 and is on track to realize our 2019 targets.

Because of additional planned investments in U.S. manufacturing, we will revise our year-end 2020 cost savings started to arrange between $4 billion and $4.5 billion. We will take all of the necessary steps to achieve as much as possible to our original savings target. The strike did have a big impact on our Q3 EBIT adjusted results and will also significantly impact our Q4 results.

Most of our 2019 strike-related production losses will not be recovered in 2019 because of capacity constraints. Therefore, we are revising our 2019 EPS-diluted adjusted in automotive, adjusted automotive free cash flow guidance. Our full year, updating EPS diluted adjusted outlook is now on the range or $4.50 to $4.80, and our new adjusted automotive free cash flow guidance is zero to $1 billion.

I have asked the GM team to find every offset, now that production has resumed and I'm confident they will find many opportunities.

So with that, I will turn it over to Dhivya.

Dhivya Suryadevara

Thanks, Mary, and good morning everybody. Today, I want to discuss our performance for the quarter, the impact of the strike, the labor agreement, and finally our outlook for the year.

In the third quarter, we generated $35.5 billion in net revenues, $3 billion in EBIT adjusted 8.4% margin $1.72 an EPS diluted adjusted and $3.8 billion in adjusted automotive free cash flow. The EBIT adjusted impact of the strike in the third quarter was $1.3 billion on a gross basis.

This reflects lost production of a richer product mix as we launched our high content, high margin heavy-duty crew cab, as well as the impact of last aftermarket sales. This impact was partially offset by approximately $300 million and strike related favorable of timing items.

Net of these turning items, the EPS during the quarter was lowered by approximately $0.52, and the adjusted automotive free cash flow was lower by approximately $400 million due to the strike. Adjusting for the impact of the strike, EPS would have been $2.24

an all-time quarterly record. The $1.72 EPS diluted adjusted also includes a $0.15 loss from Lyft and PSA revaluation.

Now let's take a closer look at North America. North America delivered EBIT adjusted of the $3 billion, up $200 million year-over-year, and 10.8% margin driven by our heavy-duty truck performance, our crossover performance and the benefits from our cost actions. This was partially offset by the impact of this strike, warranty costs and lower pension and health.

Our newly launched heavy-duty trucks contributed favorably to volume, mix and price during the quarter. Market share for our large pickup trucks continues to improve, up 5 percentage points in Q3 year-over-year. We started deliveries of our heavy duties in Q2 and we have gained 6 percentage points in market share since the launch.

Our light duty pickup trucks improved 6.8% at retail in Q3 year-over-year to over 40% as we rolled out diesel and other cab variants. We will have the same launch gate and strategy for the heavy-duty as we did for the light duty with the rollout of double cabs next, followed by regular cab.

Switching to crossovers, U.S. deliveries grew 29% year-over-year with a Chevrolet Blazer and Cadillac XT6 providing strong contributions to our results.

Let’s move to GM International. For the third quarter, EBITDA adjusted in GMI was down $200 million year-over-year driven by lower equity income in China. Continued industry weakness and pricing pressure resulted in Q3 equity income down $200 million year-over-year from record Q3, 2018 level. We did see slight benefits from improved mix partially due to our recently launch vehicle.

A few comments on GM Financial, Cruise in our core segment, GM Financial posted record quarterly revenue of $3.7 billion in the third quarter and record EBT adjusted of $700 million primarily as a result of portfolio growth. Cruise costs were $300 million for the quarter on track with approximately $1 billion communicated previously for the full year as we increased our headcount.

Core segment costs in the third year -- sorry third quarter were $500 million, unfavorable $400 million year-over-year primarily due to net loss of $280 million from Lyft and PSA investments in the third quarter of this year compared to a $170 million gain from our PSA investment in the third quarter of last year.

We have made significant progress on our transformational cost savings initiative with $2.4 billion achieved since 2018. We're on track with our 2019 target of $2 billion to $2.5 billion, achieving $1.9 billion year-to-date and $800 million in the third quarter. Let me update you on our outlook for the calendar year.

The recent strike is obviously had a negative impact on our financial performance in Q3 and more so in Q4. We estimate the calendar year EPS diluted adjusted impact to be approximately 4$2 per share and adjusted automotive free cash flow impact to be approximately $5.5 billion including the impact of working capital unwind. The $2 in EPS reflects lost production of a richer mix, lost after-market sales, start up and ramp cost, and is net of a higher U.S. tax rate on last earnings.

While we continue to work on strike recovery efforts, we anticipate that we have small portion of the losses sustained during this strike can be recovered this year due to capacity constraints. Factoring in all of this, our updated 2019 EPS diluted adjusted outlook is in the range of $4.50 to $4.80.

Catching on CapEx, we expect 2019 CapEx of approximately $7.5 billion this year due to timing and early achievement of commitment. Updating for this and the impact of the strike, we expect adjusted automotive free cash flow guidance in the range of zero to $1 billion. I would like to provide some additional perspective on this guidance. The underlying EPS and free cash flow guidance is consistent with the range given in January.

We have experienced the highly unusual situation with the shutdown of our North American operations for six weeks. We are restarting our operations very close to year end and the speed of production ramp and timing factors are very difficult to predict at this point. We have provided the best estimated outlook given the information that we have today.

Next, I want to briefly talk about the impact of our new labor agreement. The new agreement preserves our competitiveness, manufacturing flexibility, and balance sheet strength without compromising earnings power.

We have maintained the mix of our North American manufacturing footprint, maintained ability to adjust our work force in response to changing industry levels, protected the balance sheet with no increase to define benefit pension obligation and no payments or increase obligations to retirees.

We maintained breakeven levels in the 10 million to 11 million unit range in the U.S. and therefore preserved our ability to navigate through a downturn. It is important to note that while this labor agreement is inflationary, we expect to offset incremental economics over the contract period with productivity initiative.

Finally, I want to briefly touch on 2020. While we will provide full guidance in February, let me help frame the year by outlining a number of puts and takes. Headwinds for 2020 include likely lower industry volume, downtime and ramp up for the launch of our full-size SUVs, higher depreciation and continued volatility in China and in South America.

Opportunities in 2020 include full year of heavy-duty truck production, transformational cost savings, and product launches including the Corvette, Encore GX, Trailblazer and our global family of vehicles. The ability to recover loss production during the strike in 2020 will depend on industry performance and our capacity availability as we already run our full size truck plans at maximum three ships capacity.

Lastly, as a result of our decision to invest in our Detroit-Hamtramck plant, we will incur operating costs that were outside the scope of our original transformation plan. While this slightly revises are year-end cost savings target to $4 billion to $4.5 billion, we will work to find every opportunity to maximize the cost savings potential. We're committed to our capital plan of approximately 7 billion annually, and our long-term financial trajectory, including 10% core EBIT adjusted margin, and improving our free cash flow conversion.

In summary, the underlying business remains strong, and our guidance is consistent with the range given in January, excluding the impact of the strike. We have a labor agreement that preserves our competitiveness and flexibility and we expect to offset economics over the contract period with productivity. The environment is more challenging than just a few months ago, but the entire team is focused on our execution, both over the short and long-term.

This concludes our opening comments, and we'll now move to the Q&A portion of the call.

Question-and-Answer Session

Operator

[Operator Instructions] Your first question comes from the line of Joseph Spak with RBC Capital Markets.

Joseph Spak

Just to start on maybe some of the cash flow dynamics you mentioned, the CapEx lowered this year. That was on part on timing and then early achievement. Can you -- can we get some color on each factor? I guess I probably want to gauge how much of the timing could impact 2020 on free cash flow. I know you said, on average, $7 billion per year, but it seems like maybe 2020 might be a little bit higher than that. And then also related to free cash, with the working capital unwind in the fourth quarter, how much do we expect to recover into 2020?

Dhivya Suryadevara

Yes, Joe, I would say from a CapEx standpoint, the early achievement of the CapEx commitments and 2019 does not impact our commitment to achieve $7 billion in 2020. So that commitment remains intact. From a timing perspective, even though we pull forward in 2019, we still think we can achieve that.

To your question on free cash flow impact, obviously, there's the flow through from the profit impact into free cash flow. In addition to that, we've seen working capital and sales allowance and policy and warranty and so on timing items are driving the remaining amount there. So, the 5.5 comprises of the lost profit and the working capital unwind. CapEx remains intact, and that's the map to get to the 5.5.

Joseph Spak

Okay, and then I know that you said recovery a volume next year is dependent on the market and as you noted, you're running all out on the trucks. But if we assume an environment in 2020, similar to '19, like just back in the envelope, I was sort of just looking at the calendar and counting days and make some assumptions. It seems like you might be able to get back 50% to 60% of it, is that reasonable?

Dhivya Suryadevara

I think it's really hard to call that now, Joe, partially because you also need to figure out what the trucking industry is going to be like i.e. the segment share within the industry. And to your point, we are running those all out. It's difficult to add over time and travel overtime. So, we will recover every unit that we possibly can. It's just difficult to predict now at this point, what that would look like.

Operator

Your next question comes from the line of Rod Lache with Wolfe Research.

Rod Lache

I had a couple questions. First, looks like the adjusted free cash flow with the adjustments you're making would have put this year's free cash flow at $5.5 billion to $6 billion, if it wasn't for the strike. And it appears that you've got another $1 billion to $1.5 billion of savings for next year. The original number was closer to $2 billion and it sounds like the variants there was Hamtramck. So, what's evolved in your thinking on Hamtramck since earlier in the year?

Mary Barra

So when we made the transformation announcement last year, although we had a battery electric truck in our plan. As we continue to evolve that and looked at the full range of what we can do there to really maintain our truck leadership position and grow that into battery electric trucks. We look at Detroit-Hamtramck is a great opportunity and company now getting an appropriate labor agreement there. And so, we think this is a good investment in positions as well to lead in battery electric trucks as well as internal combustion trucks. And so that is that portfolio as we further planted, it became clear that we can be more efficient doing that work there.

Rod Lache

North America and GM Financial look like they were very strong this quarter. Obviously, there's unusual items that affects both of those right now. Could you just talk a little bit about those, aside from just the things like launch, but did you make any adjustments to pre existing warranties in North America? And how should we be thinking about the cadence for GM Financial going forward and what that might, may mean for releasing cash from that business?

Dhivya Suryadevara

From a North American standpoint, yes, it was a very strong quarter. The cadence of our heavy-duty lunch helped a lot from a mix 10 points since we're rolling out, crew cab for the most part. And that will normalize as we roll out the other variants as well. To your question on no warranty, we had a $700 million year-over-year unfavorable and that was primarily driven by the K2 warranty cost that Mary mentioned in her remarks as well as there was a onetime favorable item in 2018 of last year which does not repeat in 2019.

So, from a year-over-year Delta perspective, that impacts as well. And in Q3, I'd say rather that we go through a normal tour process from a warranty perspective and there were some top ups relative to that as well, but that was on the smaller side of things, that you capture that. From a GM Financial perspective, the biggest item I'd point to is the fact that residual values have been coming in stronger than what we had previously accounted for.

So as you go forward there you may want to think about some kind of normalization there. The offset to that would be continued growth in the size of the book as we move closer towards forecast. Those are the normalizing items from GM Financial perspective.

Joseph Spak

And just to clarify in North America, I was asking about the incentive accruals yet over 700,000 units of inventory, and I would have presume that you have make some adjustments just given that prospects for declining inventory. Was there anything unusual there? And can you tell us what's expectation is for Q4 production at this point?

Dhivya Suryadevara

Yes. I'd say nothing specifically on the incentive side, we'll obviously – it will be vehicle-by-vehicle driven by market dynamics and nothing specifically to point out there from a true or whatever perspective. From a Q4 production, we are now back up and running and all of our plans are running all out. Like we said, we're going to take the opportunity to get any excellent that we can and that's all we can comment on at this time. And since we're still in ramp up and we're trying to maximize the number of units, we'll have more to share about that when we report Q4.

Operator

Your next question comes from the line of John Murphy with Bank of America.

John Murphy

First question just around the labor agreement and the special attrition buyout program. It looks like it's only targeting about 2,000 workers, but based on sort of what I've been able to dig up, it seems like half of your workers are senor, meaning they're getting defined benefit, pensions and natural attrition on an annual basis is about 2,000 workers. So just curious why that even the special attrition program that buyout might not target more workers? And then overtime in the next three years before the next contract, would that impact sort of natural attrition, meaning would be still expect to see 2000 per year? So first is why is it a larger program? And second, what kind of impact would it have on natural attrition overtime?

Mary Barra

I think a couple of things here to think about it. First of all, one big component of the special attrition program was to give people choices. Although, we have job for everybody that was impacting by the un-allocation of three plans, we wanted to give them options and so there is a target there from that perspective. And the other thing is, you can -- we think that again people wait and look and see if there is going to special attrition program, but then we also do see the natural attrition over the course of the agreement. So, I would expect that to continue and that's how we size what we thought the SAP should be.

John Murphy

And Mary, when we think about those attritions whether it'd be special or sort of natural over the next few years, what is your plan as far as back feeling for those workers? I mean, would there be replaced one-for-one with in-progression workers or entry level workers? Or could there be folks then get hired out in California to work on cruise? Just trying to understand sort of the thought process of what, how to size the labor for us going forward?

Mary Barra

Well, I think it's a -- there is many different components of the labor force. There is a Cruise labor force. There is our salary workforce and then there is our representative workforce. And I think your question is directed as the represented work force, we're going to continue to work on productivity and we have opportunity there. We also have a lot of opportunity continue to improve our manufacturing processes. We've done a lot of work this year and complexity optimization, and we're driving that in from a design for manufacture ability perspective into how we design vehicles.

We've also been able to find more and more opportunities to reuse without impacting our customers view of vehicle is being all-new especially when you look at some of the architectural components. We also have a program we've been working on for many years call built-in quality level 4. And by the end of the year, virtually all of our plants will have achieved built-in quality 4. Our built-in quality level 4, which leads to first better health and safety and better quality as measured by two months and 12 months warranty performance.

So, we see, I'll say traditional productivity improvements. We see efficiencies on how we designed vehicles and components from the DFMEA perspective. And then, we see the results coming from our built-in quality level 4. All those things are going to help us make sure we optimize the workforce and optimize our manufacturing costs. As we need to hire additional workers, we'll utilize both temps and I'm very proud of the fact that we provided an appropriate path to permanent employment for our temporary workforce and then also maintain the in-progression flow. So, we'll utilize both of those depending on the plan and the situation at that plant.

John Murphy

Got you, that's helpful. Then just on the SUV launch. Is there any change in timing for next year on the SUV launch given what's happened with the strike?

Mary Barra

We haven't specifically said when those launches they will occur and will roll out all three versions next year. And of course, the team is working to do everything possible to make sure we have successful high quality launches with minimizing the impact of the acceleration curve. So those we still we'll get all those done this year and I'm not going to give any more specifics on timing.

John Murphy

Okay. And then just lastly, there's been a lot of negative comments on pricing, and some came from one of your cross-town rivals but also sort of in the press. Yet the quarter, on your majors, you put up a $400 million positive, but more importantly you put up a $200 million positive on your carryovers. What do you see in the pricing sort of competitive landscape for pricing? I mean, is that $200 million positive from carryovers was that benefited by some shortages during the strike or you actually seeing some real net positive price on carryovers?

Dhivya Suryadevara

From a majors perspective, I'd say it's mainly driven by our heavy-duty and the variance of the light duty, that we've recently launched. So those were strong, and that's really the truck franchise that's driving that. On the carryover side, the outgoing model from a car perspective, we reduced our incentives on that quite a bit. From a crossover standpoint, we were disciplined as well.

So overall, I would say positive, carryover a net price. That's going to be quarter-to-quarter John, it's going to vary based on seasonality and so on and so forth. But it's our intention, stay disciplined. And as you can see in the quarter, with the net majors mechanisms that I just talked about, we have grown share for both light duties as well as heavy duties. We plan on continuing on that path of being disciplined.

John Murphy

And Dhivya, in a competitive environment, have you seen any deterioration there? I mean, I understand you guys are pretty disciplined, but I mean, are you seeing sort of any kind of warning signs out there?

Dhivya Suryadevara

I think there's definitely months where you see some competitive activity and then it normalizes and so on, but we're launching, we're going with our cadence. And we're, the strength of the products that we put out are driving our market share gains this time.

Operator

Your next question comes from the line of Itay Michaeli with Citi.

Itay Michaeli

So just first question with inventory now being leaner, can you talk about opportunities you might have in Q4 and beyond to optimize for mix and pricing? Should we expect mix to get richer over the next several months as you try to kind of manage the inventory situation?

Dhivya Suryadevara

We're going to try and build everything that we can get Itay from a mix perspective. We will continue down the path of rolling out the richer mix from an HD standpoint. LD as low, we will, try and maximize it will make sense that our most profitable and as we go forward. So we're going to be opportunistic as we go along.

And the other aspect is, obviously, from a country mix standpoint, there's places where we, there's places that are more profitable and there are places that are less profitable, and we're going to direct the amount of inventory that we have towards the more profitable places as well. So, we will be opportunistic, it's hard to obviously sites that at this time, and we will provide more detail in Q4.

Itay Michaeli

And just second Dhivya, on the 2020 puts and takes I think you mentioned lower industry volume as a headwind. Can you put the more detail what you thinking regionally and globally? Does that include the truck franchise, pickup truck industry and sales there still do not be strong throughout 2019. Any additional color would be helpful there.

Dhivya Suryadevara

Yes, I think we still have another couple of months here to go to see what happens here. But in 2020, we do think that China will remain volatile. South America will remain volatile. And here the United States with the economic growth are moderating here in the recent past and in the next year or so we're anticipating. We're still planning for a lower industry, so healthy industry but a lower industry in 2020. And we're going to have to, as we move forward here in the next few months before we get guidance, we'll put more specifically around that but any more than that it's too early to tell.

Itay Michaeli

But just lastly on Cruise, I think back in July, Cruise mentioned they would accelerate testing and validation in the balance of 2019. Any update that you can share in terms of miles driven and the overall activity that Cruise is undergoing in the second half?

Mary Barra

I would say we're not going to give you a specific mileage, but they are doing exactly what they indicated, they would do in the summer timeframe. Everything's going really well, as they need their milestones and as they continue to develop the economist technology. So very much on track and not only on the technology, but also the work that they're doing in San Francisco in the community to make sure that the consumer is ready understands the technology and trust the technology. So, both of those plans are perfectly on track.

Operator

Your next question comes from the line of Adam Jonas with Morgan Stanley.

Adam Jonas

Mary, over the next five years, will GM spend more R&D and CapEx dollars on EVs or internal combustion vehicles?

Mary Barra

I believe it'll be EV.

Adam Jonas

Thank you. And do you think that do EV is require less labor then internal combustion vehicles, all else equal?

Mary Barra

I mean I think you have to look at the entire vehicle. Clearly from an electrification perspective, it's simpler from a component perspective than it is from an internal combustion engine. But you know what the key things that we've done is light-weighting because light-weighting is so important across every component and from a body structures perspective, that light weighting generally requires a little bit more labor. So, overall, I think it's somewhat last but I think you've got to look at the whole vehicle, not just the propulsion system.

Adam Jonas

Thanks, Mary. And just, I wanted to have a couple questions on Corvette. And I Mark is not on the call here. So, maybe we can follow up with him. But Mary, what do you think of a Corvette SUV?

Mary Barra

I appreciate that you think our core franchise is very strong. I'm not going to talk about future…

Adam Jonas

I do.

Mary Barra

Thank you, I can't wait for the world to be able to drive the CA because its' an outstanding vehicle and the value, the performance is I think just set the new bar and then the affordability I think is something we're really proud of and is very true to the Chevrolet brand. So I will just share with you we look at a variety of things as we move forward, but we recognize the strength of the core brands right now we're focusing and getting the CA out and then the other variants including the convertible. So, very excited about that product and what it will for us.

Adam Jonas

I appreciate it. Then I won't ask about electric core that either right now, we can say that for later. Finally then just you mentioned on China, I think when you were talking about 2020 expect that China that we're headwind. Can you elaborate a little bit more there on what was the market, what was the volume assumption or mix or price assumption within that, any other color on the China headwind, if I got that correctly for 2020 versus 2019? Thanks everybody.

Mary Barra

Yes. Adam, I think it's early to call it, I mean there is so much going on right now as you look at the volatility in China, look at where we're still in the middle of where we're trying to understand where the trades stocks are going to land and how that's going to impact the overall economy. So, we are seeing a vital environment and we're also seeing a lot of pricing pressures. And then as we look forward as we rollout more EVs, initially we're going to see some margin headwind there. So, I think when you look at all those things in 2020, we'll have more color for that as we do that February earnings call for Q4, but those are the things that we're seeing right now that we think we'll carry into 2020.

Operator

Your next question comes from the line of Ryan Brinkman of JP Morgan.

Ryan Brinkman

Could you provide an update in terms of the impact of the new labor accord on your downturn resiliency in North America? Can you remind us of your latest estimate of North America breakeven expressed in terms of U.S. light vehicle SAR and whether the contract changes that breakeven while?

Dhivya Suryadevara

Yes. Ryan, what we've previously talked about is the breakeven level of 10 million to 11 million units for the U.S. This contact will not change that and how wide that is, is basically the comment that Mary made about productivity and other efficiencies offsetting the economics of the contract will certainly blame to that.

In addition to that from a flexibility standpoint what we've model in our downturn assumption is the ability to adjust the level of workforce based on what's happening in the industry. And a certain levels of supplement unemployment benefits to go with that and that just not change based on this contract which is primarily the driver the maintaining the downturn assumption of where they are.

Ryan Brinkman

And I was encouraged in the release that you attributed the software banned industry sales in China to demand, to lower demand for your outgoing products. Could you please provide us an update on the income and products in China like earlier in the year you were relatively optimistic about the sales and prospect potential from new launches including the first office, I think so called GEM Architecture. Can you talk about how the sales and cost of the launch vehicles has extended relative to your expectation in China?

And then finally it would be great if you could update us with regards to the extent which you have or have not detected any perceived bias against U.S. based brands and the aftermath trade or other attentions in that market?

Dhivya Suryadevara

Sure, sure. And Ryan first of all, we haven't really seeing and we monitored that we really haven't seen any negative settlement. So we think that's very positive. And we are in the middle of the launches for the year. We had 11 majors including the Buick, which is a battery electric vehicle, the Buick Encore, Buick Encore GX, the Chevrolet Onix, the Chevrolet Trailblazer, and Tracker and then the Cadillac XT6 and then some Baojun products as well. And then, there were several very important MCMs with across Buick [indiscernible] as well as the Chevrolet Monza and the Cadillac XT5.

So I think as you look at all of those vehicles into a market with the uncertainty and the economic issues or the macro issues in China, and say they're all on track, you were correct to note that we did have our first of Chevrolet Onix, which is the global family. It's one of many launches in China and it is on track. However, we did mentioned in my remarks that it is doing exceptionally well in South America because it's at the heart of the market and the biggest segment.

So, I think we need to see these vehicles get into the marketplace. And I think a lot we'll see as we get into next year as well, but the launches are on track. I do think, though, and some of them, as we did see a more significant drop off than we thought we would with the outgoing vehicle.

Operator

Your next question comes from the line of Brian Johnson with Barclays.

Unidentified Analyst

Yes, hi, good morning. This is Steven [indiscernible] on for Brian Johnson. Just wanted to drill that down on the potential recoup, some of the loss production took on the T1 pickup truck side in the 2020. I guess assuming kind of an overall stable large pickup market into 2020. Is it fair to say that GM is already running at max capacity? And that's from a production schedule standpoint tentatively, as you think about 2020 is really no pretension that make up that loss production, especially if we get upside with large pick up market? Or is there any kind of scope so we can work as we think through 4Q and into 2020?

Dhivya Suryadevara

Yes, I would say that your assumption is correct in an industry level and a truck penetration level that similar to what we have today, where we already have scheduled, we can time and a lot of other overtime. On a regular basis, we have these plans working max overtime. So, the ability to add additional days is limited. We will obviously try and find any voluntary opportunities to do overtime beyond that, but it's not something I would call my baseline at this point.

Unidentified Analyst

Understood, thanks for the clarification. And then in terms of the revised UAW contract impact, we outside in kind of got you about $115 million gross labor inflationary impact in 2020 ramping up to about 350 in 2023. Just wondering, if that's kind of ballpark correct, and then also can you quantify the buckets of the dollar savings offsets some attrition buyouts absenteeism and other productivity initiatives?

Mary Barra

Yes, yes, I think we -- given I said more broadly is that we really believe the inclinatory elements of the contracts or the economics that we can offset with productivity and there is plans well established. We don't know yet exactly how the special attrition program is going to play out. People have till the end of the year and find out for that. So I think what you here from us though as a team that is committed to finding the right offsets to go forward and maintain and improve our competiveness.

Unidentified Analyst

Okay, just in terms of the gross inflationary labor cost in fact was that, is that ballpark directionally correct in terms of $100 million in 2020 ramping up 350 in 2023?

Mary Barra

Well, I mean, I think if you look at that, there's some parts of the contract, they're easy to do the math on. And but I think there's others that, we will look to see how it plays out. And some of that depends on the workforce, depend on how many people take the special attrition program, depends on the industry as we go forward, so I'm not going to put projections that far out.

Unidentified Analyst

And then, just a last clarification question. In terms of the revised transformational restructuring savings, the $4 billion to $4.5 billion, does that include the productivity initiatives you've outlined? Or would that potentially provide some upside to get back to the original target of $4.5 billion?

Mary Barra

I think first we're going to work to offset and then we're going to keep going, we won't stop when we get there. So I think over time, there's upside, especially, and the broader elements we've talked about how we continue to improve, how we design vehicles that affect the demand, your manufacturing costs and our ability to continue to build quality institution and improve our quality system.

So all those things are going to contribute and although we revived it based on the decision we made, largely related to Detroit-Hamtramck. We're going to continue to push the organization to continue to find cost opportunities. And I would say that's the goal we set for the end of 2020. It's not like after that we stop. At that point, we'll evaluate the business and look for the next round of cost savings that we can drive into the business and commit to from an improving shareholder value perspective.

Operator

Your next question comes from a line of Dan Levy with Credit Suisse.

Dan Levy

Just wanted to follow up on the question on this productivity gains. Could you give us some color on what initiatives you might be able to pursue or timing? And more specifically, you've obviously been pretty successful with cost saves in the past. I think probably one of the reasons why your earnings level has been rather elevated. Just wondering how much the low hanging fruit may already be exhausted. And you're going to have to dig in a little harder and it's not going to be as easy to some of these gains?

Mary Barra

Well, I think, when we look at our comparison that Harbour or I guess, if Oliver Wyman does from productivity. We still have opportunities to improve. And it's not just, minutes per hour of and the way we design a job, it's much broader than that. And I think we have a lot of opportunities to tap into as we really optimize our complexity and we leverage reuse. And so, those are things that I'm very pleased that the organization has taken to a new level this year, and that will play out over multiple years because a lot of it is if you design the vehicle for design for manufacturer ability, doing that now will play out in years, when we actually launched the vehicle be it two, three, four years from now.

And don't underestimate the work that we've been doing on built-in quality level four, because for the plants that are already there, we definitely see just the fact that more vehicles are built in station means they spend, no time and repair. And that's that savings as well. So I believe, although I'm very proud of the manufacturing team of what they've already accomplished, and working across with the engineering organization, I think there's still much more to tap into and that's what we do.

Dan Levy

And then just as a second question, one that's more existential and sort of touching on one of the prior questions. Obviously, one of your publically stated goals, zero emissions future and that's probably requires a smaller footprint and what you have in place today. So first of all, does this current agreement have any limitations on specifying limitations on what you can build for EVs? And then just more broadly with your zero mission future roll, how aligned is your labor partner with you on this goal? Will they ever service partners with you along this transition. Sort of similar to what we see in Europe and Germany to addressing or future or is there interest simply look this is a four year agreement and once it expires than we'll deal with the future as it comes?

Mary Barra

Well, I think in this Europe agreement we are dealing with the future, if we look at from an EB perspective we already build the Chevrolet Bolt EV in our Orion plant in Michigan, very significant discussions that we had as it relates to the battery electric truck with our UAW as it relates to what we're going to do to tracking and trading. So, I think what we're trying to do is, and first of all, there is no limitation. So I want to make that very, very clear, but we are committed to the United States and committed to manufacturing in the United States.

We see a huge opportunity adding electrification and that's why we're investing and I think in among the leaders in the EV space. I think we are technology roadmaps that we have for sale development, we're going to well position that and with the equipments we've made for the better are next generation or architecture which we call the BEV3. So, this was all part of the discussions and I think as signifies but what we're doing in Orion and what we'll be doing into Detroit-Hamtramck.

Dan Levy

I guess more specifically you have other engine and transmission plans out there that presumably in an EV world are deemed unnecessary. Has there been any sort of discussions with the union in the future on how to deal with these plans that could potentially beyond necessary?

Mary Barra

Yes. I think that's over a very long horizon. We still see, you know, even when you look at the multitude of projections by 2030, is it 15%, is it 30% all in, that means the bells of the vehicles being sold in the country into rail combustion engine vehicles. We're well position because we've renewed all those architectures and we've invested in very efficient instead of combustion engine technology that will continue to improve.

So, I think this is going to play out over a number of years and there are components in the drive unit from an EV perspective that needs to be build somewhere. So, I think we're looking to do the right thing from a company perspective to drive shareholder value to leading EVs and do the right things for our manufacturing footprint and for our employees.

Operator

Your next question comes from the line of Emmanuel Rosner with Deutsche Bank.

Emmanuel Rosner

I was hoping you can provide a little bit more color on your underlying performance this year excluding the strike to the extent that's possible? Your, the revised guidance just and then you add backs sort of this strike impact seems to be fix it 60 to 80 maybe the lower end of to reflect original guidance. Is there anything? Are there any like specific factors that you see that are playing that maybe on the softer end of what you have expected before? I mean again, excluding strike, is it at the international? Or is it China? Is there anything you're seeing in the U.S. that would account for that? And as part of that question also just trying to understand better the tax rate impact, the new guidance is at the lower tax rate, is that correct?

Dhivya Suryadevara

Yes. So, number of questions there, so let me address them one-by-one. The new guidance $4.50 to $4.80, you're correct, we've subtracted the $2 and arrived at, so it's the original guidance we gave in January less $2 on the upper end we clipped it by $0.20 as you've seen we've -- its' been quite a volatile environment in China as well as the microeconomic of volatility we're seeing in South America as well the FX environment that we saw earlier in the year, when we gave our guidance was very different from the FX picture that we have today, which is offsetting some of that as well.

So I would say that the weakness is predominantly more on the international front, the volatility that we're seeing. And from a North America perspective as it seeing the performance quarter after quarter, it continues to be strong. From a just from the tax rate perspective, the revised rate is primarily because the strike impact is you got to apply the

U.S. tax rate to that strike impact, which is about 25% effective tax rate, that we're applying there. So if you take our original tax guidance, subtract out the higher tax rate that's applicable on our strike impact, you get to your UN revised tax guidance. So it's consistent. It's just that you're applying a different tax rate than the weighted average tax rate on the strike impact.

Emmanuel Rosner

Okay, that's great color. And then just I was hoping can you give a little bit more color on the puts and takes for 2020. And in particular, a few discrete items, you're talking about downtime and ramp up for the full size SUV, anything you're able to quantify in terms of specifically in the downtime there? And then you did not mention raw materials as a potential tailwind, I was curious if you can give an update on what is represent this year and then how to think about it for next year? And then the sort of discrete items would be warranty, obviously a fairly big charge which you explained, for the quarter. Does that have a carryover impact as we move into next year?

Dhivya Suryadevara

So, on the 2020 side, the puts and takes that I gave predominantly, a lot of industry uncertainty around the globe, that's what I would characterize as a primary headwind. From a downtime standpoint, this is a complicated SUV full size SUV launch. There's a significant amount of change that's happening from the current generation to the next generation.

So from a downtime perspective as well as more importantly, the line rate ramp up post the downtime, we're anticipating an additional headwind year-over-year, for full size SUVs. I don't want to quantify that now since we're still working on how we can optimize the number of units that we're going to be able to put out in 2020. So I will quantify that further in February. But it is safe to assume that there will be a year-over-year headwind from a full size SUV perspective.

There will also be higher depreciation. That's something has been consistent with in the past several quarters as our depreciation caches up to our CapEx level and we've been seeing a secular increase every single year. And that's going to continue into 2020 as well.

And obviously this is non-cash, if you will know.

From a raw material and tariff perspective to your point, I said this before in prior quarters, there's puts and takes, it's hard to look at just one number and paint it all with the same brush. But steel and aluminum we have seen tailwinds offset by precious metals, tariff as well as fuel costs, which impacts our logistic spend.

And so net-net, we are still at 500 million year-over-year headwind from a 2019 standpoint, we don't see that moderating, necessarily into 2020, since the headwinds that I mentioned are likely to continue into 2020. And it's obviously hard to predict the tariff environment that we're going to be in.

So that's generally the headwind, tailwinds the remaining cost saving so far, we've achieved close to $2.4 billion of cost savings and the remaining cost savings are going to be realized over a period of time, according to our revised guidance. You're going to have a full year of heavy-duty trucks and the product launches that I talked about. Hopefully this gives you some color.

And finally on the warranty question that you had, we do see that a specific to Q3 of this year, I don't see a tail event into 2020 on that.

Operator

Our last question comes from the line of Chris McNally with Evercore.

Chris McNally

Just wanted to jump in on maybe the impact from a working capital standpoint on the change and the free cash flow guide? So just really quick of the 5.5, it looks like 2.8 was worse than just the operations. You back out the CapEx, it looks like something like a $3.5 billion or $4 billion drain on working capital. Can you just confirm that it was all working capital and there's not any other sort of one time drivers for the cash flow because we're trying to think about the reversal next year?

Dhivya Suryadevara

Yes, I would say that your EBIT impact seems to be on the low end maybe you're talking about the net income impact so from an EBIT prospective set up for, you going to talk about growth number there. That, plus the working capital unwind, constitutes most of the 5.5. There's no other like one time item or whatever else that's out there but the profit impact that you talked about us that sounds a little understated but it's potentially because of tax rate.

Chris McNally

And then if we could talk about the without giving numbers like when we think about the reversal at some time in the first half. I know you want to give guidance, but could you just sort of walk through the timing of how that would play out from an inventory standpoint?

Dhivya Suryadevara

Are you talking about the reversal of working capital or the recovery of profits or both?

Chris McNally

The reversal of working capital?

Dhivya Suryadevara

So, reversal of working capital, we think that the low point is probably going to be sometime in November, as we cycle to the rest of the unwind, and payables and receivables will start back up 15 days after we start shipping, that cadence will continue. So we do anticipate that you think part of the recovery in the second half of November and into the December. And Q1, as you know, it tends to be a negative cash quarter because of our shutdown and the reversal after that. But what you would see from a cash balance standpoint is that recovery starting in the second quarter of next year, into the rest of 2020.

Chris McNally

That's perfect on the timing. And then maybe this is more of like a from a communication standpoint. I mean 2020 was already supposed to be sort of a better free cash flow year. I think we asked that question a couple of different times on the call. But you're already getting improvement of CapEx the reduction attention from a cash flow and income statement and then the FinCo dividend. If we get this working capital benefit in 2020, is it the type of thing that you will actually be able to call out, so that we can start to understand what is the true because working capital wasn't one of the working, one of the benefits that we were expecting in 2020 and 2021, which likely will now be sort of core operation? So is that something that you could fact out for the street as we go into 2020 and 2021?

Dhivya Suryadevara

Yes, we will be very clear about how much of our 2020 free cash flow guidance comes from the working capital rewind and we will also be clear about how much of the cash based earnings i.e., the operating cash flow if you will and what that is year-over-year. So from a communication standpoint we're certainly be clear about that and beyond that you're right we don't want to take much more about magnitude of that until February.

Operator

Thank you. I'd now like to turn the call over to Mary Barra for her closing comments.

Mary Barra

Thank you very much and thanks everybody for participating this morning. If you look for several years, the team at General Motors has been making tough decision to make our business more resilient and more agile. This discipline will help us overcome the impact of this strike we continue launching our heavy-duty trucks, the new Cadillac sedan.

And as we move forward, the upcoming launches such as mid engine Corvette and the next generation of full-size SUVs. This leadership team has a proven track record of successfully navigating complex business issues, confronting headwinds and capitalizing on opportunity. And I believe we have the best employees in the industry across the board. They want to work and they come to work every day to do their best. And they want General Motors to succeed and they want to be a part of that successful future.

So as we move forward together, we're going to continue to build on the strong foundation we've laid and share and allow them to share on the future success of the Company. But let me be clear, we're also working hard to lead in both the core and EV and AV world and creates significant shareholder value. And before I close, I want to let you know that we will host our Capital Markets Day in New York on February 5th, 2020. This year in addition to providing our 2020 outlook, it will include our Q4 and our full year 2019 earnings results. And we'll share additional details about the Capital Markets Day in the near future.

So thanks everybody very much. I appreciate your time.

Operator

Ladies and gentlemen, that concludes the conference call for today. Thank you for joining.