Strong auto sales in U.S. offset weakness in Europe

Despite slumping sales and continuing financial turmoil inEurope, the third quarter still turned out to be a profitable one for U.S. automakers.

Both General Motors Co. and Ford Motor Co. saw earnings slip during the period compared with last year, but strong results from their operations in the U.S., and those in Chinafor GM, allowed the automakers to post profits. Chrysler Group, the smallest of the Detroit Three, reported earnings nearly double last year’s level.

Wall Street took notice.

GM shares rose $2.23, or 10%, to $25.51, near the automaker‘s highest price since April. Shares continued to rise in after-market trading.

Ford climbed 85 cents, or 8%, to $11.16, its highest level since May. Chrysler is majority owned by Fiat and doesn’t have shares that trade, but its 80% profit increase to $381 million in the quarter enabled the Italian automaker also to post a profit for the period.

“The strength in sales on this side of the Pacific helped mitigate the losses in Europe for the Big 3 in the third quarter,” said Jesse Toprak, an analyst with auto price information company TrueCar.com. “Despite losing market share, domestic automakers were able to improve their profitability by cutting production costs and lowering incentive spending while selling more expensive vehicles in the U.S.”

In recent months investors were worried that Ford and GM earnings might be constricted by high-cost union contracts, said Peter Nesvold, an analyst with Jefferies & Co. But “recent restructuring news out of both Ford and GM have helped to ease these investor concerns, and have redirected the market’s focus to North America where profits continue to surprise to the upside,” Nesvold said.

The industry is expecting more good news Thursday. Though the industry may have potentially lost as much as 100,000 vehicle sales because of the havoc wreaked by Sandy this week, automakers are still expected to report sales of about 1.1 million vehicles in October, well above the same month a year earlier.

“The October retail sales pace is solidifying an accelerating recovery in the automotive market,” said Deirdre Borrego, vice president of U.S. automotive operations at research firm J.D. Power and Associates. “Each month, we’re seeing stronger signs of a healthy market, not only in terms of sales volumes but also in dealer inventories, transaction prices and incentive levels.”

This week, Ford reported a third-quarter profit of just over $1.6 billion, down $18 million from the same period a year earlier. Revenue slipped 3% to $33.1 billion mainly because of a drop in sales in Europe.

GM said Wednesday that its net income fell to $1.5 billion from $1.7 billion in the same period a year earlier, a 12% slide. Excluding one-time items, GM earned 93 cents per share, beating the estimate by Wall Street analysts of 60 cents. Revenue rose to $37.6 billion from $36.7 billion.

"This was a solid quarter for GM in almost all respects," said Dan Akerson, GM's chief executive. "Four out of our five business units were profitable."

"GM offers the most upside of any auto stock we cover," said Adam Jonas, Morgan Stanley Research analyst.

But he also noted that GM presents the most risk, in part because of the thorny problems it still faces in Europe, where differing regulations in national governments prevent the type of broad restructuring the auto industry and GM underwent during the recent U.S. recession.

"We believe the stock has significant upside potential that can best be triggered by decisive strategic action in Europe," Jonas said. "GM's urgency and investor patience are key ingredients for the stock to work."

GM lost $478 million in Europe in the third quarter compared with a loss of $292 million in the same period a year earlier. The Detroit automaker expects to lose $1.5 billion to $1.8 billion in Europe this year.

Other automakers are also suffering in Europe, where auto sales are at a 20-year low and are not expected to rebound any time soon. Ford said this week that its losses were widening in Europe and could reach $1.5 billion this year.

On Wednesday, the Eurostat agency said unemployment in the Eurozone hit 11.6%, the highest level on record. Some 18.5 million people are now unemployed in the 17 nations that make up the monetary union.

GM doesn't expect to break even, let alone make a profit, in Europe until mid-decade.

The automaker's other overseas operations performed well. Operating profits in Asia — primarily ventures in China — soared 89% to $689 million. South America swung to a profit of $114 million from a loss of $44 million.

In North America GM posted an operating profit of $1.8 billion, down from $2.2 billion a year ago.

GM is the last of the U.S. automakers to report third-quarter financial results and will probably draw the most attention because of the 2009 bankruptcy restructuring and federal bailout. Taxpayers still own about 26% of the company's shares on a fully diluted basis — after all outstanding stock options and warrants are exercised. GM's shares need to trade at more than $50, double Wednesday's price, for the government to recoup its investment in the automaker.

"GM's quarterly earnings will be scrutinized more closely than usual with the U.S. election just a week away and the auto bailout still an issue on the campaign trail," said Jessica Caldwell, an analyst with auto information company Edmunds.com. "But anyone looking for political artillery in these numbers will likely be disappointed."