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A Chapter for Detroit to Open

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The Big Three U.S. automakers need more than an injection of $25 billion from the federal government. Because of their ongoing losses, they would burn through that money in less than a year and would soon be back for more.

General Motors, Ford and Chrysler can make excellent cars, but they cannot sell them at prices that are competitive with the prices of cars produced in the United States by Toyota and others or with the prices of cars imported from Europe and Asia. The basic reason is the labor costs imposed by union contracts.

The Big Three pay much higher wages than production workers are paid in the nonunion auto firms and in the general economy. And the health-care costs of current workers and retired union members are an enormous additional burden.

The simplest solution is to allow GM and the others to file for bankruptcy. If the companies file under Chapter 11, they would be able to continue producing cars, and the workforce would remain employed while the firms reorganized. The firms would also be able to get short-term credit under bankruptcy protection.

The bankruptcy court could require the unions to rewrite contracts, bringing wages down to levels that would allow the firms to compete and therefore to maintain employment. Scaling back employee and retiree health benefits would further improve price competitiveness and allow better cash wages. The firms' bondholders and other creditors would have to take losses. Shareholders' fate would depend on how firms responded to this restructuring.

Restructuring in bankruptcy and resetting wages are measures that have saved airlines as well as manufacturers. The claim that bankruptcy would mean the loss of millions of jobs is nonsense intended to scare the public and force legislators and the Bush administration to throw money at the auto industry's problems.

Only by reducing wages and benefits will the firms be able to survive and provide good jobs.

If politicians in Washington cannot live with the thought of the auto industry in bankruptcy and decide that some cash must be delivered, this should be done as part of a fundamental restructuring plan imposed by the government in exchange for those funds.

The goal of that restructuring should not just be to require the companies to make cars that are fuel-efficient and more environmentally sound, as President-elect Barack Obama has said, although that can be included in the government's list of requirements. The goal should be to put the companies on a

course that will allow them to survive for the long term, producing cars and creating jobs.

To do that, the government should insist that the unions accept reductions in wages and benefits to levels that allow the firms to compete with imports and with nonunion U.S. auto firms. The trustees of retiree benefits should be required to accept reductions in those benefits. The government should also insist that management eliminate dividends and restrain salaries until the firms return to profitability. Even creditors should have to accept write-downs in the value of their debts.

The government has substantial leverage to ensure that these changes occur. The auto companies' management, unions, trustees of retiree benefits and creditors would recognize that without government assistance, the firms would be forced into bankruptcy and that the bankruptcy court could require even more severe cuts in incomes, benefits and payments to shareholders and creditors.

Administering bitter medicine is difficult for politicians. President Bush would do his successor a favor by forcing such a restructuring. It would relieve Obama of his promise to help the auto companies and in a way that improves prospects for the American automobile industry.

The writer, an economics professor at Harvard University and an adviser to the McCain campaign, is president emeritus of the National Bureau of Economic Research.