Philly Firm Faces Fight to Survive

By Bob Fernandez

Salsa music blares from a factory boom box as Akouvi Tokoni grabs a used Honda Civic distributor from a milk crate. The 32-year-old immigrant from Togo checks the metal casting to make sure that it can be rebuilt to the correct specifications.

Satisfied that it can, she inserts bushings and seals, sprays the part with compressed air, and screws in wire harnesses before passing the partially built distributor to a coworker.

By the end of Tokoni's shift, Cardone Industries Inc., Philadelphia, Pa., will convert more than 1,500 used distributors into good-as-new parts ready to ship to wholesalers, repair shops and auto dealers across the country.

Cardone is the city's largest factory employer, with 4,200 workers in five Philadelphia plants. It is also the country's largest rebuilder of auto parts, turning out more than 12 million parts a year.

Now, that is all at risk. As giant parts-makers such as Delphi Corp. shed thousands of jobs in their struggle through bankruptcy, Cardone faces its own fight to survive as a Philadelphia manufacturer.

Competition from China has Cardone so rattled that its normally reticent chief executive is reaching out for help, both in Philadelphia and Washington. "I want to do my best to keep as many jobs here as I can for as long as I can," says Michael Cardone Jr., the son of the company's founder. At the same time, he says, "I still have to be competitive."

He's fighting some powerful forces. Abroad, it's China's newfound economic might, bolstered by its soaring ambition and cheap labor. At home, it's America's seemingly insatiable appetite for lower-priced goods.

Cardone is a beacon for people such as Tokoni who are trying to climb the economic ladder without the benefits of a college degree. A job at Cardone pays $7 to $15 an hour, plus benefits. Imran Abdool, 20, who packages steering components, is using part of his Cardone Industries paycheck to attend pharmacy school. "I feel lucky because a lot of my friends are not even working," he says.

But Cardone Industries is fighting a flood of Chinese imports that are so cheap that they undercut the parts the company rebuilds after salvaging used parts from service stations, auto dealerships and junkyards.

To maintain market share against the Chinese influx, Cardone Industries has cut prices across its product lines by 16 percent in the last five years. In 2005, Cardone slashed prices of its water pumps by 22 percent. Another product under siege, drive axles, has declined in price by about 60 percent in the last decade. The cuts come at a time of dramatic increases in energy costs and double-digit hikes in healthcare costs.

Trying to become more efficient, Cardone last year relocated a Philadelphia line that rebuilds drive-axle components to a new, 250-employee plant in Matamoros, Mexico, and says that more marginally profitable product lines could head south. The company has even turned to China to make some parts, creating in 2004 a line of new products called Cardone Select.

It has ramped up productivity and broadened its product line, but this hasn't stopped the financial slide.

"We've squeezed as much out of the Philadelphia operations as we can," says George Zauflik, vice president for government relations. "We're at that point where something has to shift here."

Although it wouldn't happen overnight, shifting some of Cardone's operations out of the area would be a blow to neighborhoods surrounding the company's plants. Philadelphia manufacturers eliminated 200,000 jobs in the last 30 years, shrinking this part of the city's economy to about 31,000 workers. Cardone, which started up in 1970 with five employees, has bucked this outflow, becoming one of the city's and state's largest private employers.

Michael Cardone, an evangelical Christian who gives inspirational speeches to business groups around the country, has worked hard to make his company part of the Philadelphia community. About 500 of his workers and nearby residents attend church services in his factories on Sundays or when the last shift departs on weekdays. "We feel we are doing a lot of good," he says.

Cardone's predicament illustrates how yet another U.S. industry is slipping away, with jobs and investment going to cheaper foreign markets, particularly China. It also shows why the Bush administration is under pressure to take a tougher approach on trade issues with China.

Since 1998, U.S. manufacturers have eliminated 3.4 million jobs as China's trade surplus with the United States swelled to $201.6 billion from $57 billion. Industries such as clothing, office products, furniture and toys have already ceded much of their production to Asia.

Consumers are the big beneficiaries. When the United States opens its market to imports, consumers get lower prices and more choices. Free trade allows nations to do the things they are good at and relinquish the things they are not good at. Many economists say that U.S. companies shouldn't be engaged in labor-intensive industries such as auto-parts manufacturing if the work can be done more efficiently elsewhere. Instead, they say, because of its well-educated workforce the nation should perform research-intensive tasks, such as drug development.

But others say the price of free trade in its current form is too high. On February 14, U.S. Trade Representative Rob Portman announced several actions to crack down, including stepped-up enforcement of intellectual-property rights and an investigation into Chinese subsidies for industry.

The head winds in auto parts are so powerful that even those with relatively low costs are struggling to make it. Some U.S. auto-part rebuilders have bailed out and now distribute Chinese-made auto parts, says Nabil Nasr, director of the National Center for Remanufacturing and Resource Recovery at the Rochester Institute of Technology.

Rebuilt vehicle parts typically sell for 20 percent to 50 percent less than new parts. As Chinese manufacturers lower the cost of new parts, U.S. rebuilders are finding that they have to slash their prices, too, or get out of the business.

Nasr says that China has made growing a domestic remanufacturing industry one of its five-year goals, which will likely increase competition with U.S. companies.

Indeed, Cardone Industries' largest competitor, American Remanufacturers Inc. of Anaheim, Calif., filed for bankruptcy protection in November and was liquidated. More than 1,600 employees lost their jobs.

"Their business model is breaking apart," Thomas H. Klier, senior economist with the Federal Reserve Bank of Chicago, says of Cardone Industries and other auto-part rebuilders. "For them to do what they do, they have to get cheaper labor."

"The reality is that what we had five years ago, we don't have anymore," Fred Vanstone, president and chief operating officer, says in an interview at Cardone's headquarters and distribution center near the Roosevelt Boulevard.

A Rich History

Michael Cardone Sr., the son of an upstate coal miner and late father of the current CEO, migrated to Philadelphia in the 1930s, fleeing limited job prospects in the anthracite region. Educated through high school, he worked odd jobs before joining four brothers in Cardo Automotive Products Inc., an auto rebuilder in northeast Philadelphia.

He opened A-1 Remanufacturing in 1970 on the 3900 block of North Fifth Street, choosing the name so it would be listed first in the phone book. Michael Jr. joined his father, and their first product was rebuilt windshield-wiper motors.

Anthony Teti, 86, the president of Service Employees International Union Local 252, which represents hourly Cardone workers, visited the North Philadelphia factory in the early 1970s. It had a dirt floor, and Michael Sr.'s wife, Frances, was packing wiper motors. "It looked so hopeless," Teti says. But he also saw that the owner was a fierce competitor. He says that when told of defective parts, Michael Sr. "acted like someone had punched him."

A-1 Remanufacturing tapped the city's pool of unemployed low-skill labor and saved money by buying old buildings when it needed to expand. Philadelphia's location was an advantage: a heavily populated area with plenty of old cars that could be stripped of parts. Michael Jr. changed the company name to Cardone Industries in the early 1990s, though its remanufactured products are still called A-1 Cardone.

Today, Cardone Industries has annual revenue of $700 million to $900 million, The Inquirer estimates, based on comparisons with its competitors and discussions with industry officials. The company doesn't disclose financial details, but does say its profits are down. Cardone has about 300 employees outside of Philadelphia, bringing its total workforce to 4,500.

Remanufacturing is hard, physical work. It requires lifting awkward metal car parts, and scrubbing, machining, moving and packaging them in boxes.

But in a city where full-time jobs with benefits are hard to come by, Cardone has no shortage of job seekers. The neighborhoods around the Cardone Industries headquarters have a poverty rate that is double, and a median household income that is one-third lower, than that of the nation, according to the 2000 Census.

In addition to starting wages of $7 to $8 an hour and a 401(k) retirement plan, Cardone employees get health-care coverage, paid vacations and profit-sharing. They can boost their wages to as high as $15 an hour by learning new skills.

Many applicants simply walk up to the heavily guarded, fenced-in factories and ask for work. Some come from overseas and live with relatives, hoping to use family connections to get hired in the plants. The company estimates that it processes 300 to 700 new job applicants a month. It hires several hundred a year.

Norma Sanchez, 38, of Kensington, inspects and packs up to 800 mass airflow sensors in an eight-hour shift, dotting each sensor with a green felt marker before putting it in the box. Sanchez earns enough to send money each month to her parents in Puerto Rico.

No Good News

One day in late December, company employees were in the midst of "WOW" meetings—Workers of Worth. In the 30-minute, bimonthly meetings, videotaped messages from Michael Cardone are played for employees, giving detail of sales, costs and other trends.

Lately, the news hasn't been good.

Ford and General Motors have announced plans to eliminate tens of thousands of jobs and close about two dozen manufacturing plants.

Delphi, the nation's largest auto parts maker, is grinding through a bitter bankruptcy reorganization as it copes with a legacy of high union wages, pensions, and retiree medical costs.

The Federal Reserve Bank of Chicago said in a January report, coauthored by Klier and James M. Rubenstein of the Miami University in Oxford, Ohio, that Chinese auto-part imports have increased 58 percent annually since 1995. In June 2005, Chinese auto-part makers moved past Germany as the fourth-largest exporters into the United States.

Labor costs are the big reason. In China, auto part workers earn about $3 an hour. In the United States, they earn $29 an hour in wages and benefits, says Neal Zipser, spokesman for Motor & Equipment Manufacturers Association.

Cardone, which competes with local auto-part rebuilders throughout the nation, began preparing for the Chinese several years ago. It adopted Toyota's efficient manufacturing practices and expanded its product line to 43 categories and 25,000 separate items. The company also moved into more complex products. Along with parts made of steel or plastic castings, Cardone rebuilds electronics that control vehicles.

At Plant 13, off Rising Sun Avenue, dozens of Cardone employees in safety glasses and blue shirts bend over large round magnifying glasses attached to workbenches, prying at printed circuit boards. At one workstation, a computer-controlled hammer gently pounds a circuit board, simulating a car traveling a bumpy road and testing a finished board for weak solder joints before shipment.

In developing the rebuilt printed-circuit boards, the company's reverse engineering department analyzed the 1,500 or so resistors, electronic connectors, diodes and computer chips that could fail on a typical board on a General Motors vehicle. It found that 240 of them are likely candidates to fail. Instead of hunting for a single faulty electronic part when it rebuilds the board, the company saves time and money by replacing only those 240, says remanufacturing vice president Robert P. Spuler.

Are such efficiencies enough? Spuler, who spends most of his time in the plant, feels the pressure every day.

"There is a breaking point for every product, and right now that breaking point is coming from China," he says, looking at a line of workstations where steering components were being packed for shipment.

For years, Cardone dealt with the

government on minor local issues. Towing abandoned cars. Smoothing relations with neighbors over parking. But to stay in Philadelphia, the company is telling government officials that it needs help.

Last April 15, U.S. Commerce Secretary Carlos Gutierrez visited the Cardone distribution center. Standing on the platform, Gutierrez praised Cardone's "factory family," and said that family-owned companies such as Cardone were the backbone of the U.S. economy.

Michael Cardone shared the stage and microphone, to the applause of 300 seated workers, many of them wearing blue T-shirts with the company logo. But afterward in an interview, he had words of caution. He said the undervalued Chinese currency, the yuan, was damaging his business. An undervalued yuan keeps the price of Chinese products low, making U.S. products less competitive.

John Frisbie, president of the U.S.-China Business Council, a trade group that supports trade with China, says that even if the Chinese yuan were revalued dramatically, his group doesn't believe it would help companies such as Cardone Industries. Low-cost competition from China is the same as low-cost competition from Japan, Taiwan and Mexico that have forced small- and mid-size U.S. manufacturers to be more competitive, relocate plants or close, Frisbie says.

Adjusting the yuan exchange rate could take years. So Cardone Industries is pursuing other actions, too. Through the Automotive Parts Remanufacturers Association, a trade group in Chantilly, Va., the company is promoting the idea of federal tax credits for remanufactured products. Cardone and other rebuilders argue that they keep parts out of landfills and conserve raw materials and energy by recycling metal, aluminum and plastics. In rebuilding, the parts don't have to be melted and recast, and they don't have to be transported many times to China to be processed.

In Philadelphia and Harrisburg, Michael Cardone is lobbying for a tax-free Keystone Opportunity Zone for his Philadelphia plants. It irks him that his company's law firm, Dechert Price, obtained the Keystone Opportunity Zone tax break when it relocated to the new Cira Center near 30th Street Station. Cardone, although the city's largest employer of low-skilled and semi-skilled factory workers, has had no such luck.

At 9.9 percent, Pennsylvania has the third-highest corporate income tax in the nation, according to the All States Tax Guide from RIA, a division of Thomson Corp. The Philadelphia corporate income tax is 6.5 percent.

City officials have told Cardone that it could relocate to tax-free city land in the former Navy Yard in South Philadelphia. But Cardone says that constructing a new plant in the Navy Yard would cost $75 a square foot. Buying old industrial buildings and rehabbing costs $3 to $4 a square foot.

Vincent Dougherty, director of Mayor Street's Business Action Team, says that Cardone's situation "is troubling, but not necessarily something that we can control, given the global economy.... We want to be as supportive as we can."

Dougherty says he has told Cardone Industries it should work with other manufacturers in the city to develop a package of incentives to present to Mayor Street and City Council. The city wants a "more holistic approach," he says.

Meanwhile, Jason Hilts, president of the Brownsville Economic Development Council in Texas, wants Cardone to relocate more of its Philadelphia lines to his area on the U.S.-Mexico border. The area has lost factory jobs to China and is courting new companies to fill the gap.

An incentive package is on the table for Cardone to locate a distribution center and engineering support department near the Matamoros plant across the Rio Grande from Brownsville, Texas, Hilts says. "Whatever we can do to help them out, we will do."

Cardone says it is still evaluating the offer.