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MANAGEMENT DISCUSSION SECTION

Operator: Good day. My name is Jason, and I will be your conference operator today. At this time, I would like to welcome everyone to the Ford Motor Company first quarter earnings conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session, and instructions will be given at that time.

Thank you. I would now like to turn the call over to our host, Lynn Antipas Tyson, Executive Director of Investor Relations. Ma'am, you may begin.

Lynn Antipas Tyson
Executive Director-Investor Relations, Ford Motor Co.

Thank you, Jason. Welcome, everyone, to Ford Motor Company's first quarter 2018 earnings call. Presenting today are Jim Hackett, our President and CEO, and Bob Shanks, our Chief Financial Officer. Also joining us are: Marcy Klevorn, Executive Vice President and President of Mobility; Joe Hinrichs, Executive Vice President and President, Global Operations, Jim Farley, Executive Vice President and President, Global Markets: and Brian Schaaf, CFO of Ford Credit.

Jim will begin with a brief review of the quarter, and then cover a review of our strategy and updated financial targets. Bob will then review the quarterly results in more detail. After Bob's section, we'll open the call up for questions. And following Q&A, Jim will have a few closing remarks.

Our results discussed today include some non-GAAP references. These are reconciled to the most comparable U.S. GAAP measures in the appendix of our earnings deck, which can be found along with the rest of our earnings materials at shareholderford.com.

Today's discussions include some forward-looking statements about our expectations for future performance. Actual results may vary, and the most significant factors are included in our presentation.

Also, all comparisons are year over year unless noted otherwise. Company EBIT and EPS are on an adjusted basis, and product mix is on a volume-weighted basis.

Now, let me turn the call over to Jim.

James P. Hackett

President & Chief Executive Officer, Ford Motor Co.

Thank you, Lynn, and thanks, everyone, for joining us.

Our goal today is to provide an update on fitness, share with you our strategic approach to creating value, and detail our updated performance targets. I said last October that the transformation of Ford had to start with getting the business fit. In fact, this preceded the ever-important strategic questions. We are improving our speed, decision-making, and execution. And today, we're ready to dimension this for you.

I'm really proud of the work of our team and even more excited about the value we believe these actions will create for our stakeholders. Simply put, the items I want to detail for you are at the center of our value creation efforts.

One, through our fitness and strategy work, we have gained clarity on where we need to focus. This includes answering questions on what do we do with the businesses not earning their cost of capital and identifying which underlying processes need to be modernized.

Two, we have also gained clarity on our vehicle portfolio and where we want to play. And in parallel, we'll leverage a suite of propulsion systems. Think of these as the internal combustion system, hybrids, and battery electric vehicles, to give customers what they want regardless of fuel prices.

And three, I'm also pleased to share that our work to support our vision for smart vehicles in a smart world is starting to gel and showing the potential to create long-term value. Now we'll share more today on this emergent work.

Okay, next I would like to briefly review our first quarter results, so please turn to page 2. Looking at the quarter, we delivered a solid company EBIT and year-over-year improvement in company operating cash flow. Our balance sheet remains strong with $38 billion in liquidity.

We also made several important acquisitions. We purchased Autonomic, which is already leading development of our transportation mobility cloud. And we acquired TransLoc, a provider of transit system software for cities. Both acquisitions are critical to advancing our mobility strategy. In the quarter, we also strengthened our collaboration with Mahindra Group, and we're working to jointly develop new SUVs and electric vehicles for customers in India and emerging markets.

In this quarter, we've also been building momentum from a product perspective. We made investments in manufacturing to meet the surging demand in North America for our new Lincoln Navigator and Ford Expedition. These trucks are selling extremely well. We also introduced the EcoSport in the fast-growing sub-compact SUV segment. We reinforced our leadership in trucks and SUVs with the launch of the first-ever Ranger Raptor in Asia-Pacific. This is a high-performance pickup unique to just Ford Motor Company.

We established our first proving ground for our autonomous vehicle business. This is through a collaboration with Miami-Dade County in Florida and partners such as Domino's and Postmates. With them, we launched a series of pilot programs to build a business that moves goods efficiently and profitably in those congested urban areas. I'm proud to tell you that we're on track together with Argo AI to deliver a commercial-grade self-driving vehicle at scale in 2021 for the movement of people and the movement of goods.

And finally, in the UK we expanded our footprint in mobility and launched our Chariot commuter shuttle services in London. This marks Chariot's first expansion outside the U.S.

Now please turn to page 3, and let's dive into the highlights of our fitness and its impact on our overall business. Over our plan period, which covers 2019 through 2022, we're telling you today that we've identified $11.5 billion of cumulative cost and efficiency opportunities. This is incremental to the $14 billion in reduced material and engineering costs we outlined last October. We've also identified opportunities to reduce the capital intensity of our business model by a cumulative $5 billion over that same timeframe in 2019 through 2022.

By applying just the results of our fitness review over our plan period, we have some great news. We now expect our EBIT margin and our return on invested capital to bottom out this year in 2018. We also expect to meet our 8% EBIT target in 2020. This is a full two years earlier than our previous target of 2022. And we're going to achieve a return on invested capital in the high teens now by 2020.

This reduction in capital intensity means that we now expect our annual CapEx spend to peak this year at $7.5 billion and then decline. By 2022, we expect to deliver balanced CapEx spend and depreciation and amortization. They'll be aligned with each other. These targets do assume continued healthy economic conditions. Now, if there is a down cycle, we believe a more fit Ford will drive a more resilient business model.

Okay, turn to slide 4. Following the work of the past 11 months, we can now give you a more clear view of how we plan to improve our returns. We believe this reflects a profound refocus of our business. In this chart, we used our actual 2017 EBIT results to plot the parts of our business based on margins and return, so let me take your eyes to the green bubble in the northeast corner. This represents the areas of our business that deliver 8%-plus EBIT and 10%-plus ROIC. This part of our business alone generates $14 billion of profit, an operating margin of 16%, and a return on invested capital of 40%. This is a tremendous business, and we have a lot to work with in this category.

Now, if you'll apply even modest valuation assumptions to this portion of our business, there's about a 50% upside to our current stock price. However, three parts of our business dilute our overall returns. The yellow bubble reflects marginally profitable areas that don't return the cost of capital. They're lower margin and they don't return the cost of capital. The low performing areas that have neither the right margin nor the returns are shown on the bottom left in the red. And investments we're making in the new products for future growth are depicted by the gray circle in the middle. They're just getting started.

So here's the key point. We're going to feed the healthy part of our business and deal decisively with the areas that destroy value. Where we can raise the returns of certain underperforming parts of our business via the fitness initiative you hear us talk about or an alternative business model, we will, and then we'll disposition the rest.

Okay, turn to page 5, and I want to take a deeper look now at fitness. As I mentioned, we identified $11.5 billion of cost and efficiency opportunities that will drive improved EBIT margin, and we expect to capture about one-third of this by 2020.

There are some good examples of where this will come from. In marketing and sales, we've identified three key areas. On the fixed marketing side, we can better improve our digital capabilities and improve our return on investment on media. In addition, via regionalization and personalization, we can better optimize our yield management in our incentives program.

Within engineering, we're moving to five flexible architectures that underpin our vehicles, with a modular catalog strategy covering 70% of the value of the vehicle. These changes will reduce the time from sketch to production by 20% and deliver significant new cost savings. Also, it will contribute to complexity reduction in orderable configurations. This will deliver savings throughout the enterprise, from the supply base to manufacturing and to our dealers.

In manufacturing, we're redesigning our freight network using big data, and we developed much more aggressive labor targets for our next-generation vehicles.

If you will, turn to page 6. Our fitness work has also allowed us to reduce the capital intensity of our business by $5 billion over our plan horizon, 2019 to 2022. We had expected to invest $34 billion, and that's now dropped to $29 billion. For example, we've identified opportunities to drive capital reduction through reuse of equipment and tools in our plants as well as additional benefits from the move to the common modules that I mentioned earlier.

To put this all together, I want to share with you the framework on page 7 that we're using to drive a more competitive, higher return, and resilient business. Our industry is undergoing a complete redesign of what we think of as the historic transportation system and the role of automakers and everyone else in that system. This redesign will reshape how our customers live, work, and move, how business is transacted, how cities are managed, how urban congestion and pollution are controlled. At Ford, we want to do more than compete in this new world. We intend to lead its design.

Enabling human progress through freedom of movement has always been central to our mission, and it's the reason we have been successful for 115 years. We'll remain true to our heritage as we transform our business model to capitalize on the trends I just described: by making smart choices; by building smart vehicles that integrate the best technology; and by providing customers with the most trusted mobility platform and services in the industry. We are on an incredibly exciting journey to redefine the automotive industry. And as we said, it starts with making these smart choices.

One of those is our first choice to have a winning portfolio. As I mentioned, we will focus on products and markets where we know we can win. Let me share a specific example. By 2020, almost 90% of our Ford portfolio in North America will be trucks, utilities, and commercial vehicles, including, of course, their electrified versions. Given declining customer demand and product profitability, we will not invest in next generations of traditional Ford sedans for North America. Over the next few years, our Ford car portfolio in North America will transition to two vehicles, our best-selling Mustang and an exciting all-new Focus Active crossover coming out next year.

A second choice is a full commitment to new propulsion, including adding hybrid electrics to high-volume profitable vehicles like the F-150, the Mustang, the Explorer, and the new Bronco. Our battery electric vehicle rollout starts in 2020 with a performance utility, and we will have 16 battery electric vehicles by 2022. In our endeavor to make electric vehicles more desirable, we'll deliver vehicles with the capability, performance, and interior design that customers need and want, without the traditional fuel economy penalty they used to see.

Our third choice is autonomous technology. We're going to develop a profitable autonomous vehicle service that offers the most trusted and human-centered ride-hailing and goods delivery experience. Our partners at Argo AI have assembled an incredible collection of talent and expertise. I can't really exaggerate that. This is a great group of people, and we're working hand in hand with them to build a great AV business model.

Our final choice is the mobility experience. This is about creating and scaling our mobility platform and services that will drive a new what we're calling sticky revenue and profit streams for us. We see ourselves not just as a provider of mobile solutions, but also as an orchestrator of digital connections, from vehicle to street to business to home. That's going to be an exciting proposition.

It's all enabled by fitness, as I said. We're starting here and talking about four components. The first is the improved operating leverage. The second is the adaptive business model, as evidenced by our Mahindra agreements. That's plural. There's more than one, be it build, partner, or buy to generate the highest returns. And the third is improved capital efficiency. The fourth is our bedrock, a strong balance sheet. We work hard to maintain that.

So before I turn it over to Bob, I want to emphasize so there's no question. We're committed to taking the appropriate actions to drive profitable growth and maximize the returns of our business over the long term. We do have a bias towards urgent action. We aren't just exploring partnerships. We've now done them. We aren't just talking about ideas, but we've made decisions.

We're going to host an analyst meeting in New York in September, where we'll walk you through more details on our strategy. September 26 is when we're scheduling that. In the coming months, though, you'll see more announcements about the specific actions we're taking to transform Ford.

So let me turn it over to our Chief Financial Officer, Bob Shanks. Bob?

Robert L. Shanks

Chief Financial Officer & Executive Vice President, Ford Motor Co.

Thanks, Jim, and good afternoon, everyone.

I don't plan today to talk to specific slides. Instead, I'm going to share some details of our first quarter results and our perspective on them, talk to our company guidance for the full year, and provide additional texture on selected elements of the business that are consistent with our full-year outlook.

As Jim mentioned, first quarter results were solid. They were in line with our expectations and consistent with our outlook for the full year. Company revenue at $42 billion was up 7%, driven by higher volume from consolidated operations, favorable exchange-related effects, and higher net pricing. Revenue was up across all parts of the business except Middle East and Africa, where it was flat, with Europe delivering the greatest increase. And this was due to exchange and higher pricing on new products and to recover Brexit-related effects, with incentives folding flat year over year.

Wholesale volumes at 1.7 million units were up (sic) [down] (17:58) 2%, driven by lower volume at our unconsolidated China joint ventures. Volumes at consolidated operations were up about 3%. Industry SAARs were up globally and in each region, with the largest growth coming from Asia-Pacific, and that was mainly China. Ford's global market share was 6.5%. That was down 60 basis points year over year, with declines in each region. This reflects mainly lower market shares in China, the U.S., and the UK.

Company EBIT was $2.2 billion, down $335 million from last year. This was driven by Automotive, which delivered an EBIT of $1.7 billion, down $443 million. Now Automotive's lower EBIT was caused by commodity cost increases of about $480 million, along with adverse exchange effects of about $240 million. These effects were offset partially by higher net pricing, particularly in Europe, and higher volumes and favorable stock changes in North America. The North America stock changes reflect pipeline fill for the newly launched EcoSport and a stock build for Focus. The Focus build is to support sales after production concludes at Michigan assembly, as we begin the transition of the facility for production of Ranger.

Importantly, total cost excluding commodities was about flat compared to last year. The increase in commodity cost was largely metals-driven, in part by the market's reaction to potential increases in U.S. tariffs. Nearly one-half of our full-year exposure to commodity price changes is locked in as of quarter end due to fixed contracts for hedges that we have in place.

In Automotive, North America was the largest EBIT contributor, earning $1.9 billion, down $195 million. EBIT margin was 7.8%, which was down 1.1 points. The year-over-year declines were more than explained by higher commodity costs. Market factors, the combination of volume, mix, and net pricing, were positive, and total cost was flat excluding commodities. For the full year, we're guiding to lower EBIT in North America due to higher commodity cost and higher spending-related expense to support growth.

We are committed to returning North America EBIT margin to the 10% level it achieved on average from 2012 to 2016 through fitness and making smart choices to play where we can win. In addition to reallocating capital to strengthen our SUV and truck portfolio, as Jim described, 51% of North America's portfolio on a volume-weighted basis will be new or significantly refreshed from the beginning of last year through 2019. The benefits of fitness actions will start to lift margins in North America next year.

Outside North America in the Automotive segment, results were a combined loss of $203 million, with each region incurring a loss except Europe. The combined loss was $248 million worse than a year ago, more than explained by Asia-Pacific. Asia-Pacific's loss of $119 million was driven by a loss in Ford China. While we earned China equity income of $138 million, this was more than offset by engineering costs incurred by Ford for future products, including for newly localized entries, including Lincoln and next-generation Explorer, as well as a loss for Lincoln as we continue to establish and grow the brand and the network.

The China loss was offset partially by a profit in the rest of Asia-Pacific. This includes a substantial improvement in India, although it still incurred a small loss. This improvement, of course, was achieved without the benefit we expect to see in the future from collaborating with Mahindra. We also benefited in the quarter from record first quarter sales in the Asia-Pacific markets outside of China.

We expect to incur a loss in Asia-Pacific again in the second quarter, with profits returning in the second half as we begin to launch 16 new products. For the full year, EBIT will be lower, driven by our first half performance, with the run rate of the business strengthening through the fourth quarter.

Now, as we announced in December, an aggressive product growth plan gets underway in Asia-Pacific later this year with the new Escort and the all-new Focus, resulting in 69% of the region's volume being all new or significantly refreshed from the beginning of 2017 through 2019. This is part of our announced plan to bring 50 new vehicles to China by 2025, including eight all-new SUVs and at least 15 electrified vehicles from Ford and Lincoln. In addition, of course, the new Zotye Ford JV will launch an all-new range of affordable all-electric vehicles.

Now turning to Europe, we earned an EBIT of $119 million, which was $90 million lower than a year ago. We delivered strong net pricing increases in the quarter, but this was more than offset by lower volume and unfavorable mix, adverse exchange due to sterling, and higher commodity cost. The adverse volume and mix were due mainly to a weaker industry and lower Ford market share in the UK as well as lower demand for diesel passenger vehicle derivatives in the region. For the full year, we expect EBIT in Europe to improve from 2017 levels due to a heavy mix of new products, which should drive strongly higher net pricing. From the end of last year through 2019, Europe will benefit from an 88% volume-weighted mix of all new or significantly new products.

Now at our Mobility segment, we incurred a loss of $102 million, which was driven by autonomous vehicle development cost. Results benefited from a one-time gain on investments in smart mobility of about $58 million. The quarterly loss was $38 million worse than last year, more than explained by increased investment in autonomy. If you adjust for the one-time gain, the quarterly loss would have been $160 million. This would be a reasonably good quarterly run rate this year for the Mobility segment, with about half the projected full-year loss due to investments in smart mobility, and the remainder for AV development.

Turning to Ford Credit, we saw a very strong quarter, with Ford Credit earning $641 million, $160 million higher than a year ago. The improvement was broad-based, including growth in receivables globally. In the quarter, Ford Credit's portfolio remained robust, with healthy U.S. consumer credit metrics, including an improved loss-to-receivables ratio. Auction values improved versus a year ago by about 1% at constant mix. We now expect full-year average auction values to decline just 1% to 2%.

At the end of the quarter, Ford Credit's managed leverage was 8.4, in line with our target of 8 to 9-to-1. For the foreseeable future, we plan to maintain Ford Credit's managed receivable levels at about the same level as at the end of the quarter. Our focus is to maintain a strong risk profile for Ford and Ford Credit, balancing receivables, funding requirements, liquidity, profitability, and distributions. This will allow us to continue supporting auto sales while preserving capacity for future Mobility initiatives. It also will enable relatively consistent distributions to Ford, approximately equal to Ford Credit's annual net income.

For the full year, we expect Ford Credit's EBT to be flat to lower than last year, as we continue to plan for lower financing margins due to rising interest rates. And while we expect auction values to trend better than our initial expectations, as I just noted, we do expect them to be down slightly year over year.

Now turning to the company's EBIT margin, we delivered 5.2%, which was down 1.2 percentage points from a year ago. And that reflected the performance in Asia-Pacific, North America, and Europe. Adjusted EPS in the quarter was $0.43. That was up $0.03, driven by a lower adjusted effective tax rate. The adjusted effective tax rate was 9%, which includes a $235 million benefit for capital loss carryforwards. Net income was $1.7 billion, $144 million or 9% higher than a year ago, more than explained by a lower effective tax rate. Company operating cash flow came in at $3 billion, which was up $1 billion from a year ago due to higher distributions from Ford Credit.

Ford's balance sheet, as Jim mentioned, remains strong, with cash and marketable securities totaling $27.6 billion and ample liquidity of more than $38 billion.

Now looking at the full year, our company guidance reflects company revenue to be up modestly, company adjusted EPS to be in the range of $1.45 to $1.70, company operating cash flow to be positive and about the same as a year ago, pension contributions of about $0.5 billion, capital spending of about $7.5 billion, and an adjusted effective tax rate of about 15%. As Jim mentioned, we expect 2018 to be the trough for company EBIT, EBIT margin, and ROIC, and the peak for capital spending.

So with that, let's now turn it back to the operator, who will get us started on our Q&A session.

QUESTION AND ANSWER SECTION

Operator: Thank you, sir. [Operator Instructions] And your first question comes from Adam Jonas of Morgan Stanley.

Adam Michael Jonas
Analyst, Morgan Stanley & Co. LLC

Q

Thanks, everybody. Hey, Jim, first question is a Ford question. You made reference to potential disposition of underperforming businesses. Could this potentially entail exiting a geographic region?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

The short answer is we'll restructure as necessary and we'll be decisive. The decisions have lots of implications for stakeholders, so we're not ready to talk specifics at this time.

Adam Michael Jonas
Analyst, Morgan Stanley & Co. LLC

Q

Okay, but it sounds like it's on the table, all options on table.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Yes, I want to affirm that.

Adam Michael Jonas
Analyst, Morgan Stanley & Co. LLC

Q

Jim, my follow-up question is a bit more macro but relates to Ford indirectly. I'll let others ask about restructuring. What is your position, Jim, on raising the U.S. federal gas tax if the proceeds went to funding improvements in U.S. transport infrastructure?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

That's a creative idea. And the way I've been thinking about the transportation system in the future is that if we cut and paste the old system as we do the kinds of things we're talking about to modernize our infrastructure, we're not going to make the progress that we really need to deal with the congestion and capacity issues in big cities. So we definitely have to in the future think about a model where we're using this cloud structure and these smart vehicles to improve that. I haven't really thought about how we fund that totally, but what we can see in the models that we're talking about with this cloud structure is there's revenue for cities in a model like that.

Adam Michael Jonas
Analyst, Morgan Stanley & Co. LLC

Q

Thanks, Jim.

Operator: And your next question comes from Rod Lache of Deutsche Bank.

Rod Lache
Analyst, Deutsche Bank Securities, Inc.

Q

Hi, everybody.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Hi, Rod.

Rod Lache
Analyst, Deutsche Bank Securities, Inc.

Q

I wanted to also probe your comments about raising the profitability that you mentioned on slide 4. There were three buckets, the fitness improvements, alternatives, business models, and the dispositions. Can you elaborate a little bit on what the alternatives might be, when we might see those deals, how long it would take to get savings from those? And maybe – I know you're not really talking about whether these are regions or anything specific. But how big could these actions be? Are we talking about alternatives and dispositions for businesses that are a few billion in revenue, or are you reassessing tens of billions of revenue?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

I'm going to ask Bob to help with the way that we're planning this. But I would just want to I guess emphasize, Rod, that the way you think about these low performing businesses, it's been easy to identify what's wrong and what we need to do about it. And I think the hand-wringing may be that has been around in our business is gone. We're starting to understand what we need to do in making clear decisions there. So the detail in terms of the construction, I'm going to let Bob.

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

Yes, let me start. The first thing I guess I'd want to focus on is actually the upper right. So I just want to reemphasize that the capital allocation process here is to generate incremental capital for the parts of business where we're already strong and we know we can be even stronger and more profitable, generating even higher returns. So that's the ultimate objective.

If you go to the lower left, Rod, the way I would think about – let me just give you some specific examples. The first thing I want to say is this is a snapshot in time, so it's not necessarily a view of the businesses over a longer period of time, and I'll give you a couple examples. So in there is most of the Lincoln brand. As you know, that only launched in China 2.5 years ago or so. It's grown dramatically. It has a great reputation. It's getting price points consistent with the Germans in the segments in which we compete. But we're importing everything, so of course – and we're growing the business from scratch.

So I've already mentioned to you that we're going to localize the first Lincoln product, but imagine the transformation of the business model, able to get out from underneath these 25% duties, the long freight journey that it takes over there and the expense and so forth, and how that can start to change how that business model looks.

The second example I'd give, we've talked about – within that category is also small cars and essentially most of our [ph] MTB (33:04) type products. So we've already talked about what we're going to do in North America, so that's pretty straightforward. That's just we're not going to invest where it doesn't make sense.

But a second example is the partnership with Mahindra. So is there a way in which we can participate, in this case India, where actually cars, although increasingly SUVs or crossovers, are a big part of the business, but do so in a way that builds on someone who's already very successful. Some of that may involve different segments because they're a really strong player in SUVs, but they're just really successful in general. As you heard us say, we're already improving. Imagine where we might be able to go through a deeper, closer partnership with Mahindra.

And then of course, there's always fitness. Fitness is going to raise all boats. Some areas of that category would benefit from that. So it's a combination of all those things, but everything going back to the earlier response that Jim gave, everything, every tool in our toolkit is on the table in terms of addressing that part of our business.

Rod Lache
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Can you elaborate on the timing on when you would expect to disclose some of these alternative plans or deals or dispositions? And maybe just as a follow-on, restructurings of structurally challenged businesses or plants and things like that could be pretty costly in this industry. At this point, do you see all of this being accomplished with the $28 billion of cash that you have, the cash flow? Any elaboration on, aside from just framing what the savings target is, what is this going to cost?

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

To your first question, and I don't want to be trite. I don't intend to be at all, but Jim did mention, there are lots of ramifications and implications from the types of things that we ultimately will do in this range of options that we have. And so what we will do is we will share with you when we can the decisions that we've made, so you can understand in a progressive manner the progress that we're making in addressing that and moving the business forward.

In terms of restructuring, the first thing I would say is we do expect to continue to generate positive cash flow moving forward. So it may be pulling out as we restructure, if in fact, that's what we have to do at various points in time in various parts of the business, but it's coming in at the same time from the upper right, if you will. That's on this chart, so it's not a zero-sum game.

The other thing that I would expect is that addressing this will take – it's not as if it's all done tomorrow at one time. There will be some element of time. Just go back and look at the North American restructuring, which was the last really significant one. But even the one that we did in Europe in 2011, 2012, 2013, that was over a period of time. That's just the way it works out. So I think that we certainly want to move fast and will do so, but that's what it takes. So I think the element of time probably helps us there as well.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.
A

But again, Rod, the confidence I'd like to get across tonight is decisions aren't in pause or dwell, so the planning is the work.

Rod Lache
Analyst, Deutsche Bank Securities, Inc.
Q

Okay, thank you.

Operator: Your next question comes from Colin Langan of UBS.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.
A

Hello, Colin.

Colin Langan
Analyst, UBS Securities LLC
Q

Thanks for taking my question. Hi, how are you? Just to follow up on the comments about cars and cutting the majority of cars in the U.S., just thinking about there in that red bubble on slide 5 where they're losing money today or any color on how large those losses are? And any color on how should we expect – are you going to close capacity? Do you expect to fill that void with all SUVs, any broad color there?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.
A

So, Colin, let me have Jim Farley talk about the portfolio implications, and then Joe Hinrichs will talk about the industrial system that supports [ph] the same (37:19). Jim?

James D. Farley
Executive Vice President & President-Global Markets, Ford Motor Co.
A

Sure, so thanks for the question. How we think about our lineup in North America especially is that we are developing incremental nameplates we don't have today and shifting the allocation of the capital portfolio to utility body styles, and there will be a variety, a growing variety, of those products.

To give you a flavor, we'll have more authentic off-roaders, building our Built Ford Tough background like Bronco and other new nameplates we don't sell today. We will refresh our entire lineup of traditional crossovers and SUVs that everyone knows, like Explorer and Escape. And then we're going to be introducing and taking capital and redeploying it for also new silhouettes, products that give customers the utility benefits without the penalty of fuel economy. And they will be performance and active executed, so they'll be very emotional.

So what you'll see is a whole portfolio of vehicles that will be much higher performing in terms of returns, much better for our brands, so a stronger business, and we will have a very diverse passenger car business. It just won't be traditional silhouetted sedans that tend to be commoditized.

Joseph R. Hinrichs
Executive Vice President & President-Global Operations, Ford Motor Co.

A

So thanks, Jim. When you look at the manufacturing question, very quickly, we have a plan. We have a very high utilization rate in our North American manufacturing plants today, and we have a plan to utilize those plants and we have a product for Hermosillo to replace when the Fusion balances out. And as we've mentioned previously, the value electric SUV we're launching in 2020 also will be built in Mexico. So we have a really great plan with all the products that Jim talked about to leverage our manufacturing capacity moving forward.

Colin Langan
Analyst, UBS Securities LLC

Q

Got it, and just last question. Your original guidance was $1.6 billion in commodity and FX, I think it was $700 million in Q1. Is it on pace, or did the steel tariffs unravel some of that, any broad color there if that's still the right number?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

I'm going to let Bob clear that up.

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

Based on where we are today, Colin, it looks like $1.5 billion year over year for the full year. So we had about $0.5 billion in the first quarter. So if you think about it on a year-over-year basis, progressively as we move forward, it starts to moderate a bit, which you might expect because we've now had two years – it will be two years of pretty sharp increases. So that's our outlook right now

Colin Langan
Analyst, UBS Securities LLC

Q

So the tariffs and cost of steel price increase were incorporated in your original number?

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

No, the tariffs are not assumed in the $1.5 billion. We'll have to wait and see if that happens. But we do believe that in the case of steel that it has essentially already been priced in by the market.

Colin Langan
Analyst, UBS Securities LLC

Q

Okay, that's not bad. Okay, great. Thank you very much.

Operator: Your next question comes from Ryan Brinkman of JPMorgan.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Hello, Ryan.

Ryan Brinkman
Analyst, JPMorgan Securities LLC

Q

Great, thanks for taking my question. Hi. Maybe just another one on where you selectively compete. Clearly you made a strategic bet on Russia, or rather stuck with Russia when it was going through a very rough patch due to its long-term potential. Obviously, markets like China, nobody's going to question, given the tremendous long-term potential. And India I think falls in that the category. And thinking about South America, how do you assess the current tradeoff there in terms of the losses you're currently making relative to – or maybe even the losses that you could make at this point in the cycle after implementing various different fitness initiatives? How do you weigh that against your assessment of that region's long-term automotive potential?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

I just want to, Ryan, make sure you know. Russia has been good for us. We actually – things have improved there. I don't want it to be left that we're stuck there. I think it's been aware to play, and I'm happy with that. I think I'm going to let Jim talk about the balance of the question around South America.

James D. Farley
Executive Vice President & President-Global Markets, Ford Motor Co.

A

So if you think of our business units, North America's story is all about returning to 10%. And China's story, as you said, is all about growth. We have all these great new products. South America and Europe are improving businesses, but we are looking at our strategic plan. And so what I think is important to say at this point for South America is we have made very significant and promising progress on our strategic plan there. And we're approaching the task with the highest sense of urgency. We have a lot of teams deployed, and they're working on a comprehensive review of the business. Obviously, we have a lot of stakeholders. So we'll have more to share, more details to share at a later date. Our business is improving. We're launching new products. In fact, Camaçari is totally maxed out right now. But we think we know that much further, more fundamental actions are required in South America.

Ryan Brinkman
Analyst, JPMorgan Securities LLC

Q

Okay, great. Thanks, that's very helpful, and then just a last question for me. Can you maybe give a couple-year walk in Asia-Pacific? Obviously, we can dissect it from your slide deck. But what has been the primary contributing factor to the softer earnings there? Relative to I think 4Q a few years ago – and there's a one-timer in there – you made over $400 million. You made nearly $300 million in the fourth quarter of 2016. Maybe just how much of it do you see as cyclical or temporal in nature that you see a light at the end of the tunnel? For example, you're launching a lot of new products, versus is there something else, something you feel like you need to target the higher end of the market or more selectively target? Or you tell me, how do you turn that region around?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

I'm going to let Bob give you some of the detail. I think you got near it toward the end of your question when you think of the age of the product. There's a whole refresh that's starting in China. But, Bob, why don't you fill in?

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

And then maybe if Jim has something to add afterwards. So if you go back and look at what happened, I want to start first with outside of China, because we were very challenged outside China. If you go back two or three years ago, we've seen a complete turnaround of that business through a lot of work and effort. So that is a positive story.

What we've seen is weakness inside China, and I think it's around a number of different things. One is the strength of the indigenous brands certainly had an impact I think on most players in the market as they became more mature and more developed and offered a tremendous number of new products that are very attractive. We obviously were not able to keep our portfolio as fresh as it needed to be in that environment. We also saw a downward negative pricing, in part – in fact, in large part driven by the indigenous brands coming up, and that certainly affected the portfolio. We had a lot of cost reductions that we achieved in our China JVs to offset a portion of that. But then incrementally, what we saw when the Chinese government revised its policy, on the renminbi, it has over time depreciated versus an appreciation trend that it had been on. And that had an impact on the business, particularly given imported elements as well as just the fact we have a very high net revenue exposure to the business.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Jim, you might talk about what's coming in China with the new vehicles. I think that's worth highlighting.

James D. Farley
Executive Vice President & President-Global Markets, Ford Motor Co.

A

So where we are right now in the first half of this year, we're at the absolute trough of our product cycle in China. And over the next 24 months, we completely revitalized the lineup. As I said, it's a growth story. And it's not just all products. It's very specific products, especially utilities. In fact, today at the Beijing Auto Show, we showed the new Escort and also our brand-new Focus, which is a really high-volume product. But we're going to fill in the entire lineup of SUVs on the higher end from there. So we're really excited about the opportunity that the new launches gives us. We're also localizing Lincoln, which is a really important part of our – as well Explorer, a really important part of leveraging our profitability improvement.

I also want to highlight though that the fitness exercises are very live for our China team. Today we launched the National Distribution Service division. That's a really important thing. We have a complex business with imported products, different divisions, and different manufacturers there. We've now gone to one company to market, distribute all of that product. It's going to be a lot more efficient, a lot more effective. And we also named our leaders for that business today, which are really experienced local team members. So I think even how we go to market is going to be more efficient and much more sophisticated with this all-new lineup. And of course, we have Zotye right around the corner. That's a big bet for us to compete in the very value-priced BEV business, which no doubt China will be the largest electrified market in the world. So I think we're really well positioned over the next couple of years for growth and profit improvement in China.

Ryan Brinkman
Analyst, JPMorgan Securities LLC

Q

That's very helpful color, thank you.

Operator: And your next question comes from John Murphy from Bank of America.

John Murphy
Analyst, Bank of America Merrill Lynch

Q

Good evening, guys, just a first question for you, Jim. As you're going through this process of reassessing the business, and it seems like you're coming to a formulation on your thought process here. As you think about scale in the business, there seems like there's a shift in the way we all have thought about this traditionally, and some folks are backing away from pure economies of scale in their thought process in the way of thinking about structuring their businesses. Both theoretically and practically, how do you think about it as you're assessing the business? There are a lot of things that are tricky on transfer pricing that it's difficult to allocate cost correctly. So it's both a theoretical and practical exercise that's difficult to figure out. So how are you thinking about that? And is 6.5 million units something plus or minus you need to stick to, or could you go a lot smaller?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Let me start with the theoretical position that you asked about. So the way I think about it, the way we are thinking about it, our whole team, is that to be a global company, you've got to have platform advantages, otherwise you don't get any scale. And so we do see platforms in the future still continuing.

I think probably as we're updating our thinking about One Ford, we realize that the parallel interest and emphasis that I'm bringing about user-centered insights is that we can add to these platforms in regions region-specific characteristics of vehicles. And just that little nuance can make a big difference in the way you achieve scale, but you give share. And if we were just exporting purely vehicles that were made for North America all around the world, I'm not sure that we would be confident in that as the go-forward strategy. The good news about that is we don't disappoint any customers with a move like that. We just have to prove that we're great at building platforms that can have scale.

I think the second part of it is that if that doesn't happen, then we've got to make the decisions that you're inferring we have to make. And so that's what I meant by we're not hammering about that. We really tell ourselves what we have to believe is that we're going to get our cost of capital out to continue.

The third thing is that the nature of the technology and the role that it's playing clearly in the western markets, in Europe and North America, is going to be important, as important, more important than China based on what my visits have exposed. Their desire to have electrification is well published, but their commitment to autonomy is going to be huge. And the reason is, as you've heard me talk often about this, is the only way we can get these cities in shape is to have the system be much more choreographed to work together. It's not just the random person in a vehicle driving at any time of day expecting no friction in the way they're getting around or goods being delivered in the center of London where the commercial vehicle only has 10% of the queue being used in the truck. This is all taking up space and reducing the problem. So the technology is going to help us. I believe that there's scale in that kind of thinking as well. It's a difficult thing to design that to work, and I think Ford's going to be able to do that.

Let me point out, by the way, that we're one of the very few companies that actually have the autonomous team and the vehicles teams working in tandem. There are a lot of suppliers for autonomy out there and there are a lot of OEMs, but we're only one of a handful of companies that are actually doing the work together, which we think's going to be an advantage.

John Murphy
Analyst, Bank of America Merrill Lynch

Q

Okay, that's helpful, and maybe a more near-term practical question. Raws sound like they're becoming a bigger issue. There's some inflation. Who knows what's going to exactly happen with tariffs and inflation in the future? But is there any possibility that you share more of this with suppliers? Prior to the downturn, the majority of raws were on the balance sheet or on in the purview of the suppliers, and you guys took them on in the downturn. So is there any way to maybe shift the balance of power back on raws, maybe hold on to steel, but give everything else back to the suppliers?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Let me just – we ought to make the comment about the tariffs and the structure, which is that I've been able to talk to people, let's just say, in the world that are in leadership positions in government and say that what we crave as business people are certainty and equilibrium. So trade can thrive in a world where that's not in question. And so we have, like everyone, we're dealing with the sudden news, and I think we've done a great job internally of dealing with that.

But let me also take you to – we're not going to be victims in this kind of thing. So what we're doing with building this modular architecture that underpins the vehicles helps us in addition to the last question about scale and the implications that you just asked about with suppliers. But let me ask Joe to comment on the history. I wasn't here in terms of what happened in the past and what might happen in the future. Joe?

Joseph R. Hinrichs
Executive Vice President & President-Global Operations, Ford Motor Co.

A

Yes, Jim, thanks. First of all, over time, as Bob has highlighted on a number of calls, our raw material costs follow the curves in the market, so we have some ups and downs based on where we are in the cycle. But as you know, we negotiate our steel contracts on a quarterly basis. We spread them out so we can average things out and don't have so much risk.

As far as the supply base goes, they're Tier 2s et cetera. Most of the time, they're bearing that risk. And there are occasions where we will direct-source and will be a part of the Tier 2 sourcing of raw materials. But there is some, obviously, some of the risk and reward that goes in the supply base. I'd just remind everybody that we've gotten a good balance of the upside when the commodity markets were going the other direction. So I don't see us changing our strategy dramatically with the supply base. When it comes to raw materials, we both manage the risk and reward together.

But as Jim was saying, when you look at the architecture strategy and the lessons that we've learned on One Ford and the way Jim described it, there's value globally in using flexible architectures, and we've talked about our five that we're going to use. Where we've learned is really the modules within the vehicle need flexibility to be able to offer differentiation for the regional markets. And scale of the supply base occurs on the scale of the manufacturing plant locally, not on a global basis. So for example, if you have a corner module, the demand, the costs, and attributes may be different in China than they are in the U.S., but it may be the same vehicle architecture, but the module that we're going to use may be different for Asia than it is for the United States. Whereas in the past, a lot of our global platform vehicles were global across their modules as well as the platform architecture.

So that's a very important nuance. Maybe it's not a nuance, but it's a very important part of our new strategy, which is to offer a catalog of modules for each of the regions to pick from for their vehicles, but still take advantage of the five core architectures that we'll use globally. So we can get the advantage of the engineering skill, the platform level, and take advantage of the local scale from the supply base and the country-specific attributes in the region.

John Murphy
Analyst, Bank of America Merrill Lynch

Q

And just real quick on Ford Motor Credit, the flattening out of the managed receivables, does that mean that you guys are really looking at just generating cash flow out of Ford Motor Credit and keeping their earnings relatively consistent and flat with where they are right now, or is there something else going on?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

We're really happy with the Credit performance. Bob, you might talk about the capital structure.

Robert L. Shanks
Chief Financial Officer & Executive Vice President, Ford Motor Co.

A

It's not an issue with Ford Credit at all. It's extraordinarily healthy and does what it does at the highest level, as J.D. Power has indicated. It's really more around managing the overall risk profile for Ford because as Ford Credit has gotten bigger and bigger and bigger, it does, even though it itself is in fantastic shape, just the nature of the business is that it represents a higher level of risk to Ford. So we want to better manage that. So that's the reason primarily that we're going to cap them at least for the foreseeable future.

The benefit, and certainly that wasn't the driver, the benefit of doing that is they don't have to take the profits, the cash they generate, and then reinvest in its own growth. So as a result of that, they're able to take the profitability and the cash it generates and return it back to Ford. It certainly helps us. We also have a mind towards making sure that we do set some capacity aside at Ford Credit to support the role that it might have in the world in terms of mobility opportunities. So that's another factor that's behind that.

John Murphy
Analyst, Bank of America Merrill Lynch

Q

Great, that's very helpful. Thank you.

Operator: And our last question for the evening comes from David Tamberrino of Goldman Sachs.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Hi, David.

David Tamberrino
Analyst, Goldman Sachs & Co. LLC

Q

Hey, how are you doing this evening?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Good.

David Tamberrino
Analyst, Goldman Sachs & Co. LLC

Q

Wonderful, just a follow-up question on the modular architectures and platforms that you're talking about. Is this very similar to what VW and ultimately GM have gone down the path of? Because if I'm not mistaken, there was some significant CapEx spend in development ahead of those platforms. So I just want to marry that up with maybe net incremental savings that you're looking at over this 2019-2022 period and how much of that CapEx and spend has already been baked in through 2017 and your 2018 spend.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Yes, let me sneak this in before I hand it to Joe, David, is that – and we'll directly get at that, is the thing that I – where I came from, the way I was raised is the nature of interpreting these customer demands and important user insights and the translating of that is what started to differentiate the world-class companies from those that were just trying to get more cost efficiency. The genius in this is using these architectures and giving customers exactly what they want in special ways. So I want to make sure as you're looking for this financial information that it doesn't get stated that we're running to one end of the spectrum here. The balance here is really important. But, Joe, do you want to address?

Joseph R. Hinrichs
Executive Vice President & President-Global Operations, Ford Motor Co.

A

Sure. Thanks, David. First off, as what we started with, we see savings coming from this initiative over the next several years and significant savings, both in the engineering spend, but also in, as was highlighted, the capital expenditures related to that. Importantly, that time reduction is not just about money, but it's also getting to market faster. One of the learnings that we have in looking back over the last several years is Jim Farley and the Markets teams have great ideas for products, and we need to be able to bring those to market faster. So a very important part of this architecture and modular strategy is to be able to execute programs more quickly.

So are there lessons learned from our competitors? Sure, we do benchmarking all the time, and we have learned things from our competitors. But this is a unique solution for Ford, but you will see common elements across the industry because we all learn from each other and we do a lot of analysis of each other. But I want to highlight, this time element is very important. If you think of the discussions we've had around the portfolio age in the United States and China, for example, we can help avoid those situations, those curves of hills, if you will, and valleys, by being able to execute prior programs more quickly and by reducing the cost, so therefore we can afford to do more. And that is a big part of the benefit of this initiative.

David Tamberrino
Analyst, Goldman Sachs & Co. LLC

Q

Understood. As if I could just follow up on one more thing, as you think about the long-term strategy here, and you obviously had some announcements for China today in going into a one-distribution channel, how do you think your relationships with your JV partners could change over time, given the more relaxed stance to JV ownership trends that at least the regulators in China are opening up at this point?

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Thanks for that question. Jim?

James D. Farley
Executive Vice President & President-Global Markets, Ford Motor Co.

A

Sure. We have our two JV partners. We're entering a third now. We're looking for approval for Zotye. We don't see yet. It's early days, but we have don't see those clanging. They're very important. We have a huge job to do to grow the business and improve our profitability in China. And we will absolutely drive change in that business, but we don't see a fundamental change in our JV structure.

David Tamberrino
Analyst, Goldman Sachs & Co. LLC

Q

Got it. And then finally, because you are launching all this new product in China, I'm just curious. What type of new technologies are being adopted and placed into those vehicles that's going to compete with some of the local brands that have very quickly put in incremental ADAS features and have really accelerated their product timelines to almost refreshing a new vehicle every year in order to capture incremental market share?

James D. Farley
Executive Vice President & President-Global Markets, Ford Motor Co.

A

That's a terrific question. So all of our China products will be connected. It's a very important part of our strategy as a company, and there's no place more important than China. We also are working with Alibaba on connectivity and in-car experience. It would be good to get Marcy's input as well. But I think we're really learning from that customer base world leadership in infotainment.

And I think the last thing I want to mention is we've made a commitment companywide, including China, and I think it's very important for our China strategy, for Co-Pilot 360. It's a whole – I think absolutely the most comprehensive ADAS assisted driving suite in the business. And that is going to be a big part of our technology story in China.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

A

Marcy, do you want to add something about the connectivity and the potential? I guess let's think of China broadly.

Marcy Klevorn
Executive Vice President & President-Mobility, Ford Motor Co.

A

Sure. So we're actively talking to partners in China. Actually, [ph] Martin (1:02:19) and myself are going out next week. Stay tuned to hear more about some potential things that will happen there. And we are working closely with Jim and Joe's team on the in-vehicle experience and making sure we understand the local needs so we can deliver the best services possible and also working to launch our transportation mobility cloud in China as well. So we've got a lot going on, and it will all come together soon.

Operator: Thank you, and that concludes today's Q&A portion. I would now like to turn the call back over to Mr. Jim Hackett.

James P. Hackett
President & Chief Executive Officer, Ford Motor Co.

Thank you, everyone. I want to just summarize a couple things just to remind you that in Ford's cadence, we picked this time in the fall to have a meeting with our investors. That's not a target for some restructuring or something like that. It's just the way we plan our calendar to come back to you. And we give you more detail then. It's going to be an exciting meeting.

I also want you to know that, as we've said, we're committed to taking appropriate and decisive action to drive profitable growth. We need to maximize the returns of our business over the long term. We're going to be fit across the entire business. I can't understate how well this has been going as we've launched this. We've identified significant cost and efficiency opportunities, as well as you're hearing the opportunity to reduce capital intensity in our business. The cycle that we're launching we didn't want to disrupt. So it's really all the things that are happening after the launches over the next year that were able to start having an impact. And we're allocating capital to our high-performing business. And we're committed, as we've stated to Rob's question, to either fix or disposition the rest.

And finally, we have a great team. I'm really happy. They're energized. They're acting with this sense of urgency and commitment. We're working really well together. And just to state it simply, we're excited about the future here at Ford Motor Company. So thanks for joining us today.

Operator: Ladies and gentlemen, this does conclude today's conference call. You may now disconnect. Thank you for your participation.