Volkswagen CEO announces “painful cuts”

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Martin Winterkorn, CEO of Volkswagen, Europe’s largest auto maker, announced plans to implement €5 billion in annual cost cuts over the next three years. He has not yet said how many employees will lose their jobs. *Deutsche Wirtschaftsnachrichten* (*German Business News*) wrote, “A massive assault is anticipated. The works council is supporting the CEO and his actions.”

The cuts are to begin immediately and are to reach the planned annual level of €5 billion by 2017—i.e., in less than three years. The savings were “urgent, because the profitability of our brand continues to be too low,” Winterkorn wrote in a letter to management. “We have a significant need to catch up to our main competitors,” he added.

With its 12 brands, VW aims to overtake Toyota in sales by 2018 and become the largest auto maker in the world.

While Toyota has achieved a rate of return of 8 percent in the current business year in its auto vehicles division, VW’s core brand managed just 2.9 percent. Currently, it is probably less than 2 percent. Winterkorn set a profitability target of 6 percent.

Since other VW brands are achieving higher profitability rates—for example, Porsche with 18 percent and Audi 10 percent—the rate for the company as a whole stood last year at 6.3 percent. Although Winterkorn is personally responsible for the core brand, and thus from the standpoint of the shareholders for the bad results, he was once again the top earner, with an annual pay of €15 million, among the 30 CEOs on Germany’s DAX stock exchange.

Winterkorn speaks in his letter of increasing efficiency, optimising purchases and reducing production and fixed costs. As an example of ballooning costs, he cited spending on research and development, which is up by 80 percent since 2010. All of this will inevitably lead to attacks on the workforce, both within VW as well as at its supplies.

What lurks behind the management jargon of “reducing complexity” was explained by Winterkorn with an example. He pointed out that the European concern offered 12 different convertible models and called upon management to think about which of the company’s 310 models overall could be discontinued.

In component factories where VW manufacturers its own parts, Winterkorn announced a further increase in flexibility, affecting plants in Kassel, Braunschweig, Salzgitter, Chemnitz and Wolfsburg. In addition, the possibility of outsourcing the production of the parts currently made in-house to cheaper producers is to be reviewed.

In a comparison between the efficiency of VW and Toyota, the *Süddeutsche Zeitung* cited the following figures: Toyota employs 339,000 people and sold 9.98 million vehicles last year; by contrast, with a worldwide workforce of 573,000, VW had only sold 9.73 million vehicles. The newspaper asked provocatively, “Why does the German firm need more than 234,000 more people in order to produce fewer cars?”

According to Winterkorn, VW’s problems are not only caused by internal mistakes. The cuts programme was also a reaction to the economic uncertainties in developing countries, currency fluctuations and the increasingly intense competition in the industry.

According to a study published only a few weeks ago by the auto industry business consultants Alix Partners, the crisis in the European auto industry will continue to persist. But the European market is the most important for VW’s core brand, with its Polo, Golf and Passat models, while Porsche and Audi have achieved high profits through sales in Asia and the US.

According to Alix Partners, the number of cars sold in Europe since the outbreak of the financial crisis in 2008 has collapsed to between 18 and 19 million units.

Car sales would not return quickly to the pre-crisis levels, when 22.3 million vehicles were sold in 2007. More than half of the most important plants in Europe were operating at a loss.

"Some homework has not yet been done here," said Jens Wiese of Alix Partners. To combat the continuing effect of the pressure of high costs, "an adjustment of capacity [is] unavoidable," he said, outlining future plant closures. The consultancy firm estimates the overcapacity at European plants to be 2.5 million vehicles, which equates to up to 10 auto or component plants.

Winterkorn's cuts plan is the "homework" about which Wiese is speaking. Daimler and BMW are also currently working out billions in cost savings with the works council and IG Metall trade union.

VW works council head Bernd Osterloh immediately promised Winterkorn his support. In the face of the problems for VW in Brazil, Russia and India, it was right that Winterkorn was committing the workforce to the profit goals, he said. But he would not agree to cuts in contractual benefits, he added.

This is all a setup. Osterloh, the works council and IG Metall have been cooperating closely with VW's top management for years. Osterloh has been a member of the works council in the Wolfsburg plant for 24 years, and since 2005 he has been its chairman. He took over as the successor to Klaus Volkert, after the latter was forced to resign following a sex and corruption scandal.

In 2001, Osterloh worked out the felxible working model "5,000 times 5,000" with the human resources chief at the time, Peter Hartz. This broke apart the relatively high contractual pay levels in the main plant and introduced sustained wage cutting.

Osterloh is one of those works council members and union functionaries who regard their job as being the defence of "German production" and factories against the constant threat of the outsourcing of jobs to cheap labour countries, in the face of global competition, by working to increase the profits of "their" company.

Osterloh now states that there will be no cuts in contractual payments, then only to make proposals where additional savings can be made, through the slashing of non-contractual payments, increased flexibility of labour, more widespread use of temporary contracts and short-term working, or through job cuts and outsourcing.

Osterloh has worked in the past with supervisory board chair Ferdinand Piëch and Winterkorn to develop such mechanisms. Plants outside Germany, such as in Brazil, Russia or India, serve as bargaining chips in negotiations.

In a statement during the works council elections earlier this year, Osterloh declared, "Piëch and Winterkorn are competitive advantages for Volkswagen." If it was down to him, "then we will only achieve all of the goals of our Strategy 2018 in 2018 with them."

It is hardly surprising that the supervisory board, where Osterloh is a presidium member, signs off on the millions in pay to Winterkorn every year. "Martin Winterkorn is worth his pay," the works council chairman declared last year. Osterloh is himself handsomely rewarded. According to media research, which Osterloh has never challenged, VW pays him at least €250,000 annually for his services. This does not include the fees for his services on the supervisory board.