

INTERVIEW

“Zeppelin will be a different company after this war”

Peter Gerstmann in an interview with Baublatt

Garching near Munich, 04 April 2022. For more than two decades, some 2,000 Zeppelin employees have built up business with Caterpillar construction machines and engines in Ukraine and Russia, and the war in Ukraine has wiped that out all at once. Zeppelin Group has suffered a double blow: Not only in the face of the devastating bombing attacks has operational business become impossible in the war situation – sales and service of Caterpillar construction equipment and engines have had to be restricted for Russia, which has been affected by sanctions. In an interview with Baublatt, Zeppelin CEO Peter Gerstmann explains what the war means for Zeppelin’s future.

The interview was first published in German language on April 4, 2022 in “Baublatt”. For more info refer to www.baublatt.de.

Baublatt: Zeppelin employs 1,400 people in Russia – 600 in Ukraine. What is Zeppelin doing to help them in the war zone?

Peter Gerstmann: We are doing everything we can to bring our employees from Ukraine to safety, to help them evacuate their families and to absorb the economic consequences as much as possible. We continue to pay wages and salaries. We have organized escape corridors, and we have set up assembly points in Poland and Slovakia where Zeppeliner who have fled can report. The refugees will initially be accommodated at our locations in Warsaw and Prague. We have already been able to offer temporary accommodation for around 200 family members. We have also set up an aid fund totaling 100,000 euros. This money is intended to bring employees out of the danger zone. This is not to be confused with a donation. We’re doing that under the umbrella of the “Aktion Deutschland Hilft” (Campaign Germany Helps) alliance, where we have set up a donation account.

Baublatt: Are employees also directly involved in the war?

Peter Gerstmann: In fact, as far as I know, male employees have been recruited – all men between the ages of 18 and 60 must remain in Ukraine. Many have joined the people’s militias. Fortunately, we have not yet received any news that anyone has died or been injured. But unfortunately we can’t rule that out.

Baublatt: Bomb attacks leave behind bombed cities and great destruction. Have branches and construction machines been damaged?

Peter Gerstmann: We are currently not aware of any destruction of our branches. However, the Ukrainian army confiscated a customs warehouse in Kiev. The machines now serve as armored barricades on the access road to Kiev.

Baublatt: Doesn't your heart bleed when brand-new technology that hasn't even been operated yet is destroyed?

Peter Gerstmann: The Mayor of Kiev, Vitali Klitschko, called us and asked for it. Since martial law exists anyway, we released the machines. It's not even up for discussion. In this case, protecting human lives is the top priority. We have to anticipate a major loss of wealth. It's unavoidable.

Baublatt: Last year, Zeppelin invested ten million euros in a new headquarters in Kiev for construction equipment and power systems, which is almost ready. It would have been inaugurated this year. The opening of a new branch in St. Petersburg was celebrated in 2019. 17 million euros have been invested in the company premises, the service workshop for machines and engines, central spare parts warehouse and an office building. Can you quantify how much damage Putin has caused with his brutal attack?

Peter Gerstmann: Depending on the duration of the war, we are currently able to maintain business in parts of Ukraine and Russia at least to a limited extent. Nevertheless, the question arises: What will business look like afterward? Can we still preserve our assets with high losses? For us, the more likely scenario is that we will be forced to exit: Either there will be a nationalization or doing business will be impossible. If one of these two scenarios occurs, we would suffer a low three-digit loss of assets in the millions. 20 percent of our sales and up to 30 percent of our earnings have come from this region in recent years, which would then permanently disappear. If there is no loss of wealth, we will go into the red, but moderately.

Baublatt: Either way: It hits Zeppelin very hard.

Peter Gerstmann: We will survive this, the company is strong enough to do so – we have experienced strong growth in recent years due to our new sales and service territories in Sweden, Denmark, and Greenland. In Ukraine and Russia, we achieved sales of up to 600 million euros in 2021 – it accounts for up to 20 percent of our business. The value fluctuates every year: If we can conclude a large fleet business there, it will be a hundred million euros more. The Cat construction equipment business in Ukraine is now almost completely dormant. As of mid-March, there are still two activities: The mines in the west of the country are still working, and we are supplying spare parts and carrying out service work there. Farms in the west are starting to sow crops. Here, too, we can still keep up maintenance work and the supply of spare parts. There are no business activities in the central region of the country, as people have fled, are serving in the army, or have joined the militia.

Baublatt: How is Zeppelin dealing with the sanctions adopted against Russia?

Peter Gerstmann: We strongly condemn the Russian Federation's war of aggression on Ukraine and the aggression that is contrary to international law. This means that we are unconditionally aligning our business in Russia with what we are allowed to do there under the applicable laws and sanctions adopted and for which there is still an obligation that we must fulfill. This means that we will meet our service and warranty obligations and ensure the supply

of spare parts that we procure from Caterpillar's central spare parts warehouse in Moscow. However, this only applies to customers who are not on the sanction lists. We are currently no longer able to import new Cat construction machines and engines into Russia. Instead, we are only able to deliver what is already in the customs warehouse, provided that the customers are not associated with the sanctions. Caterpillar has stated that production at the Russian Caterpillar plant in Tosno (near Saint Petersburg) is being suspended until further notice. We are also unable to offer new financing or leasing contracts in Russia via Caterpillar Financial Services until further notice. Some of our 1,400 employees have been with us for 20 years. They have been extremely loyal. We also have a social obligation toward them as an employer. They didn't start a war. That's why, of course, they are continuing to receive their salary and wages. In Russia, we have a central IT hub for our entire IT infrastructure in the Eurasian region. We cannot simply switch it off because then we would no longer be able to reach our colleagues in Armenia, Tajikistan, or Turkmenistan. Furthermore, we have an obligation not only to our customers but also to Caterpillar. We could not fulfill that if we were to leave Russia. If we were to not fulfill our obligations, the business would not only disappear tomorrow, but there is the threat of nationalization or third parties would take over. Then we would no longer be able to ensure compliance with the rules. Incidentally, Zeppelin is only active as a Caterpillar dealer in one part of Russia. Three other international Caterpillar dealers also work in Russia.

Baublatt: There are initial demands from Moscow for nationalization of company assets. Are you already preparing for the fact that you will have to write it all off?

Peter Gerstmann: In 2019, we invested around 17.5 million euros in the 40,000 square meter company premises in St. Petersburg, in the service workshop, in the central spare parts warehouse and in an office building. Of course the Russians could take this over – the organization for the spare parts and the customer relationships are there for this. They could continue to work and deliver to whomever they want. We are therefore currently also a regulator in this market, which still represents European interests there.

Baublatt: Do customers still have any applications for Cat construction machines?

Peter Gerstmann: Customers in Russia are also encountering difficulties. Those whom we could supply despite the sanctions are barely able to pay for spare parts or construction machinery. The payment systems of the Russian banks have been interrupted, and the ruble is severely devalued. As a result, the payment method and the ability to pay are severely restricted.

Baublatt: Cryptocurrencies are consequently not a way out?

Peter Gerstmann: That's never been discussed. The ruble is no longer so easy to convert. And if it could be converted, then the business would be much more expensive. Right now, customers would have to spend almost twice as much on a Cat construction machine. That's often not financially viable. In a nutshell: Our business in Russia has largely come to a standstill.

Baublatt: As a manager of a company with almost 11,000 employees, what is the top priority for you in these extremely difficult times, and how have you responded to the war on the part of corporate management?

Peter Gerstmann: On the morning of February 24, our tried and tested crisis management team was immediately activated. Since then, it has met every morning to discuss the current situation. We have in the meantime become accustomed to this routine. Our first consideration and top priority has been to bring employees out of the danger zone to safety. We immediately decided to help them evacuate the war zone. This mainly concerned those in the branch on the Belarusian border and in the branch in Donbas in the south-east of the country. At that time, our aid offers were barely accepted. Initially, it was not expected that things would get so bad. At first, it was also a question of which jobs could be maintained. We had to ensure wages and salaries for February. The next disbursement for March was also ordered. We owe it to our employees that we will continue to try to pay them. Of course, we had to consider what kind of business we could do and how we could ensure the commitments to our customers, namely in the war zone of Ukraine and in the sanctioned zone of Russia. We had to deal with sanctions in 2015 due to the annexation of Crimea by Russia. This time, the situation has deteriorated tremendously. We have been confronted again and again with crises for more than ten years, whether it was the financial and economic crisis or the coronavirus pandemic, but the war in Ukraine has also brought us to a threshold for the first time. We have a situation where we no longer can consistently reach all of our almost 11,000 employees with our decisions, and there are divided views of the war.

Baublatt: How difficult is communication with customers and employees in the affected war zones and in Russia, where according to the media law imprisonment of up to 15 years is threatened if the word war is used?

Peter Gerstmann: In Ukraine, we are well connected, for example, via messenger services, email and our in-house digital platform. However, communication is very difficult. The emotional burden on employees caused by the war means that every corporate communication is critically scrutinized and every word interpreted. It's very difficult to find the right words.

Baublatt: Do Russian employees even know what happened?

Peter Gerstmann: They have their own, different information situation. It depends on the environment people live in, how old they are and how digitally savvy they are. You could say: The more urban their lives and the younger they are, the better informed they are because they have better access to information. On social media, many younger people knew of course what was going on, even though it was becoming more and more limited. In rural areas, the odds of accessing information outside the country are low. This is how you have to see the division. A large proportion of our 1,400 employees will be well informed, but some of them will not get any information outside of the Russian media. They have their own view of the 'military operation' and do not believe our statements. However, the media law has also forced us to react. We have decided to block our own platform for our colleagues from Russia. To protect them against potential consequences, they can no longer read and post messages there. Since we do not determine the content that is published there, there is a great risk that information will be disseminated that contravenes the media law.

Baublatt: To what extent will the war affect Zeppelin in other sales territories such as Germany and Austria, and what will happen to the countries in the Eurasian region, such as Armenia, Uzbekistan, Tajikistan and Turkmenistan, which are customers of Cat large equipment?

Peter Gerstmann: That's a difficult question. I don't believe that we and the global economy will emerge unscathed from this war. Energy prices, which in Germany are already the highest in Europe, will continue to rise. Raw material prices, which were already high due to the coronavirus pandemic, will increase. Inflation will rise. We are already experiencing supply chain disruption, and this will continue to impact prices and availability. The global economy will have to suffer a setback. The extent of this depends on the length of the war and how severe the resulting economic and political consequences will be.

Baublatt: Chips and cable harnesses were previously lacking in the automotive sector. What does the war mean for the production and delivery of Cat construction machines – what consequences can your customers expect?

Peter Gerstmann: Due to the high worldwide demand, there are supply problems for Cat construction machines as well. Supply chains are just as disrupted: Not only are chips and electronic components in short supply, which are a prerequisite for telematics applications and assistance systems, but the availability of steel and other important raw materials is also limited. Price increases are a result of that alone. Incidentally, everyone is affected by them. The trend of economic upheaval will intensify.

Baublatt: With Russia and Ukraine, a large market is being eliminated for the time being.

Peter Gerstmann: And precisely that could also be an opportunity. The machines are also available to the remaining markets, and worldwide demand is high due to high infrastructure needs.

Baublatt: Is it actually as easy as that – for example, isn't the engine technology based on different emissions regulations than in the EU?

Peter Gerstmann: That's right. But if these construction machines are no longer built for Russia because sales markets are breaking off, production capacities are available. This could also lead to further positive trends – and I'm not only thinking about reconstruction, but we're also getting new sources of demand. Defense technology will be asking for construction machinery. We need to invest in energy supply. The focus will again be stronger on the promotion of domestic raw materials in order to be more independent. There will be a lot of new opportunities.

Baublatt: Isn't it a platitude: In every crisis there is opportunity?

Peter Gerstmann: That's the case. We will have an opportunity as well as risk, which hopefully will be balanced out.

Baublatt: You warned of an impending global economic crisis early when there was talk about sanctioning Russia by excluding it from the Swift financial system. What possible worst-case scenarios are you currently preparing for?

Peter Gerstmann: For us, that would be if we would no longer be allowed to operate in Russia as a European company and Ukraine would become Russian territory. That would be the worst case. Otherwise, I assume that we will no longer be able to sell our products and services at the usual level in the other markets. The most positive thing would be a diplomatic solution, whatever it may look like. But after that, it will never be the same as before. In Russia, Zeppelin will never again be able to do business with Cat construction machines in the same way as we have done in the last 20 years. Trust has been destroyed, and partnerships have been lost.

Baublatt: In 2015, Zeppelin was once in a difficult situation due to Russia's annexation of Crimea and had to react to sanctions. What lessons have you learned from that?

Peter Gerstmann: With the exception of the exclusion from Swift, we have not experienced anything new this time in terms of sanctions. Russian banks have been suspended from Swift, but we're not doing all that many transactions with them anyway. But as long as European banks can make transfers to Russia, transactions remain possible. The principle of sanctions has not changed in 2022 compared to 2015 – they have only been intensified. We have a stricter dual use from Europe, which means that parts that can be used militarily must not be exported. But dual use already existed in 2015 and before. Even then, it was not permitted to do business with persons and companies related to Putin. There were sanctions of institutions such as banks, but industries such as gas and oil were also not allowed to be completely supplied. At the time, we were prepared for the fact that 30 percent of sales would remain in those regions, but we were able to survive well. We can still do that today. It becomes critical if we can no longer do business, and we are no longer allowed to work as a German company.

Baublatt: What consequences do you expect for Ukraine?

Peter Gerstmann: If the diplomatic solution is that Ukraine remains a self-determined country that is oriented to Europe rather than Russia, we could continue our business. Then that would certainly provide substantial amounts of money for the reconstruction of the country. Perhaps we could benefit from this, but the country could never cooperate with Russia again in the same form as before. We had a joint IT team there with Ukrainians, with Russians, with Armenians. That will no longer be the case.

Baublatt: The war is not only being fought with weapons, but the risk of cyber attacks is increasing. Has Zeppelin already been a victim in that regard?

Peter Gerstmann: On the first day of the war, there was an attack on the systems in Ukraine, which we got under control relatively quickly. We are very aware of the problem and are working hard to secure our data – even outside the country – and to enable direct access and break up the dependency of the companies.

Baublatt: You said: Zeppelin will be a different company after the war. What does this mean in concrete terms?

Peter Gerstmann: It's simple: 20 percent of our previous performance capacity that we accounted for will be missing in the future. We built up the business with a great deal of passion in Ukraine and the Russian territories for well over two decades. We recruited employees and familiarized them with our values and our corporate culture. We set up Zeppelin in Russia and Ukraine according to Western standards so that we could sell Cat construction machines and engines there and support them with the usual standard of service. We'll lose that. It's as if suddenly an important part of the body is missing. We're now losing a great deal. That applies both to employees as well as to customers. Many years of trust relationships have been built up. You were always happy when you met.

Baublatt: This would have been a good opportunity at the upcoming bauma.

Peter Gerstmann: Russian customers always liked coming to Munich. We knew each other really well and also knew about their private worries and needs. That's all gone. We're losing a piece of Zeppelin. We were determined to be the experts for Cat construction machines and engines in Eastern Europe. This entailed special skills and a special understanding, including regarding know-how of large equipment in the mining sector. We will still offer mining in Sweden, but not to the same extent as before. In the future, we will probably be a purely western-oriented Caterpillar dealer.

Baublatt: Following the financial and economic crisis in 2008/2009 and the coronavirus crisis, the war has created the worst scenario to date that you have been confronted with as Group CEO. How do you personally cope with the stressful situation – can you still sleep at night?

Peter Gerstmann: I fall asleep with the war and wake up with it. It doesn't leave you alone. At the moment, it's also not possible to concentrate on what Zeppelin is moving ahead with. Unfortunately, that has to be postponed at the moment. Now crisis management requires our full attention. I became Chairman of the Management Board at Zeppelin in 2010, one year after the financial crisis. Since then, we have succeeded in continuously evolving through all the crises. The last four years have always been record years, and there has been an increase in sales and earnings with a very stable business model. And that was my goal: After the financial crisis, I wanted a sustainable, strong, and growing company. This also meant that we introduced systems such as SAP or initiated innovations related to digitalization that cost money, but which will protect us in the future. Now a war comes along, and you realize that part of the work has been blown away and that the difference this time is that something is threatening to disappear for good that we can't easily make up for. It's a little bit like starting from scratch again. That's something I'm very concerned about. The only thing that consoles me in this situation: Zeppelin is now in an absolutely stable position, so that we will overcome this crisis.

Caption: Peter Gerstmann, CEO of Zeppelin GmbH
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About the Zeppelin Group

The Zeppelin Group offers solutions in the construction industry, drive and energy systems, engineering and plant engineering. The Group provides customers with expertise in a number of areas, from the distribution and service of construction, mining, forestry and agricultural machinery, through rental and project solutions for the construction sector and industry as a whole, to drive and energy systems as well as engineering and plant engineering and enhances its offering with digital capabilities in all areas. Zeppelin is represented at more than 340 sites in 43 countries and regions worldwide. In the 2021 financial year, the Group workforce comprised almost 11,000 employees, which generated sales of EUR 3.7 billion. The Group organizes its activities into six strategic business units (Construction Equipment Central Europe, Construction Equipment Nordics, Construction Equipment Eurasia, Rental, Power Systems, and Plant Engineering) and the Zeppelin Digit Strategic Management Center. Zeppelin GmbH is the Group holding company. It is legally domiciled in Friedrichshafen and has its head office in Garching near Munich. The Zeppelin Group is a foundation-owned company. Its roots can be traced back to the establishment of the Zeppelin Foundation by Graf Ferdinand von Zeppelin in 1908. For more information, visit zeppelin.com.

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