

Commentary

Perspectives on an effective design of industry transformation

Jürgen Vormann

Turning point(s) (“Zeitenwende”) and new multipolarity: Is the industry in Germany declining into insignificance?

The following text summarizes a speech held, at Frankfurt Industry Evening, Chamber of Industry and Commerce Frankfurt am Main/Germany on December 13, 2022. The author acted as CEO at Infracore GmbH & Co. Höchst KG for 18 years. Infracore Höchst is the operator of the industrial park at Frankfurt-Höchst, a vibrant R&D and production site for the chemical and pharmaceutical industry. At the same time, Jürgen Vormann was responsible for a variety of regional and national organizations and has been outlining the interest of the manufacturing industry towards regional, national and international policymakers. In his final official speech as CEO, Jürgen Vormann underlined the importance of constructive cooperation and mutual support between industry, politics, and society and pledged for a well-balanced policy mix which at the same time has to aim for economic, social and environmental targets to secure a strong industry in Germany and Europe. He fears that current climate change-related arguments would prevail in the public discourse and that this orientation might endanger the industrial base in Germany.

The topic of my speech today, formulated as a question, is: “Turning point(s) and new multipolarity – is the industry in Germany declining into insignificance?” With my remarks on this topic today, I can and will share only some of my thoughts on this question; I would like to provide some food for thought and an input for a public discussion, which is overdue and unfortunately only slowly gaining momentum. A comprehensive treatment of the topic would certainly go beyond the time frame of this evening.

Why have I chosen this topic? Because, in my view, it is of great importance for Germany and in particular for the industry in this country!

The overall argumentative context is quickly described: For the first time since the end of World War II, a war takes place in Europe. And already in the run-up of Russia’s invasion of Ukraine, in the fall of 2021, the energy markets were anticipating a possible war since the annexation of the Crimean peninsula and the occupation of territories in eastern Ukraine in 2014. Due to the great dependence of Europe, (and Germany in particular), on oil and above all gas supplies from Russia, due to low gas storage levels in early 2022 and against the background of a politically poorly planned and even more poorly implemented “energy turnaround” of the German federal government, the prices especially for natural gas have literally exploded in the meantime.

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This has led to a significant deterioration in the competitive position of - especially energy-intensive - German and European companies. Energy-intensive production facilities were temporarily shut down or downsized, e.g. in some areas of metal production (production in October 2022: -14% yoy 2015) and the chemical industry (production in October 2022: -22% yoy 2015).

The short-term consequences are disruptions in the local value chains, which will lead to supply bottlenecks – to name a few: e.g. for flocculants and precipitants for drinking water production, precipitants for wastewater treatment, and urea for pharmaceutical synthesis and ad-blue production. These short-term product shortages are painful enough. In the medium to long term - and this is far more dangerous for Germany and Europe - this development is deteriorating the competitiveness of significant parts of the industry in Germany, threatening energy intensive production facilities and thus the stability of value chains and the safety of jobs in this country. Even more serious: there is a risk of future investments being made in other regions of the world. The consequences of such a development for the German and European economic structures - and the social systems that are based on these - can hardly be overestimated. To make things even worse, the demographic development in the coming years, a paralyzing regulatory framework in conjunction with a slowly working bureaucracy in Germany and Europe will further accelerate this development!

So much for the woodcut-like arguments put forward in recent months by some subsectors of the industry, especially from the chemical industry. I personally share this pessimistic assessment, and I, therefore, see a real danger that a significant part of the industry in Germany is on the verge of being sidelined. Mind you, I am quite deliberately using the term "industry in Germany" here; I am not necessarily talking about the "German industry," as long as it is internationally positioned with regards to its development opportunities in other parts of the world, outside Germany and possibly also outside Europe. I am firmly convinced, however, that a German industry, which loses its competitiveness in Germany and thus weakens its home base, will in the long term lose its competitiveness and its independent entrepreneurial identity in the global context.

What is the objective of my remarks today?

Today, I would like to take a step back, block out the media cacophony of the year 2022, the discussions about "the Scholz-whammy" and "double whammy" and take a look from a somewhat greater distance and with a much longer industry perspective on the future.

On the one hand, I would like to describe what I consider as some of the major structural challenges - and their causes - our country in general and the manufacturing sector in particular are facing.

At the same time, I want to outline starting points and generally applicable rules for change processes which, in my view, can help correcting mistakes made in the past and avoiding undesirable developments in the future.

What challenges do we face today - and why are we standing here?

The word chosen as the "German word of the year 2022" is "turning point." I can assure you that a few weeks ago, when I was formulating the topic for my speech today, I had no insider information from the jury of the German Language Society. I chose this word for the title theme deliberately, and I also use it in the plural, because I am convinced that when we talk about "longer periods of history that are characterized by unifying features" (at least this is the definition of the term "era" in Wikipedia), we will not only find "the one" or "the dominating" connecting characteristic which defines an era; during the last eight decades - since the end of World War II - we have to consider a whole series of important developments that in my opinion have led or will lead to profound paradigm shifts, thus determining fundamental changes of or even within an era.

Allow me today to single out three distinct developments, that are of particular importance from my point of view:

1. The renewed disintegration of the world into several power blocs:

At the end of World War II, the world was clearly divided into two large camps. The "West" under the leadership of the United States and the "East" under the leadership of the Soviet Union were clearly defined as politically, economically, and above all militarily organized power blocs; China and other parts of the world initially played a subordinate role. But even in this phase of history, which superficially lasted until the

fall of the Iron Curtain in 1989/1990, new centers of power emerged, which have also been clearly visible for some time now: China, which will soon become the world's largest country by GDP and which is already a world power - both under economic and military aspects; and India, soon to be the world's largest country by population. The countries of the European Union have created a supranational structure aiming to gain economical and political synergies to bring sufficient "weight" to the scale internationally. The "turning point", proclaimed by the German chancellor in the wake of Russia's illegal invasion of Ukraine is, in my opinion, at most to be subsumed here as a subcategory of the developments after the fall of the Iron Curtain and the proclaimed "end of history" (Francis Fukuyama); in the light of human history and human psychology, only naive politicians (of those mainly German) were to believe this as being true.

In the history of mankind, questions of power almost always had an economic component - and economic questions are always also a question of power. In this context and against the background of the current socio-economic developments in the European Union, I believe, that Europe needs to urgently re-answer the "systemic question". The answer to this question will not only have a decisive impact on the success or failure of the desired transformation of the German and European economy, but it will also determine Europe's political and economic competitiveness on the global level between the different power blocs - not to mention our military strength, which at the moment is highly questionable and currently predominantly dependent on the United States!

The systemic question that we must ask (and answer!) is: Do we continue to trust in the power of market mechanisms - i.e. Adam Smith's "invisible hand" and the statistical "power" of many market participants - as the most effective and efficient form of a search process? Or: Do we give ourselves over to the illusion, that a few "know-it-alls" - be it in politics and/or in business - know better than the "many" market participants, who have to prove themselves in competition? China is building - not at least against the background of the success of its rapid economic catch-up process of the past five decades - on increased central control of the markets. The United States of America, in general, follow the principles of a free market economy, whilst at the same time they start stimulating the transformation of its economy with a protectionist touch and enormous state subsidies under the Inflation Reduction Act.

And we (German) Europeans? The EU Commission produces many glossy slides with a vision of a "European Green Deal", and visionary solutions are being presented on paper for concepts and measures to meet the challenges in climate protection, taxonomy, energy supply, industrial policy, distributive justice, compliance, and other "Sustainable Development Goals". And whilst the economic feasibility of the presented visionary concepts are still unproven and the required financing of the necessary transformation measures is more than questionable, the EU at the same time already starts to detail draft regulations for the transformation of the European economy which - if put into effect - will result in an overwhelming and non-value-added bureaucracy. In one word: the "rule of law" will thus be substituted by even more and even more complex rules and regulations. This contributes little to nothing to an economic added value for Europe, but it will at least keep European consultants and lawyers in business.

2. The end of limitless growth

Resources are scarce for humans as their needs are fundamentally unlimited. For thousands of years, human demand has had to adapt to the natural supply and be it through distribution battles in which human victims had to be mourned. In the face of a still rapidly growing world population, there are few reasons to believe that these fundamental mechanisms have changed nor that they will change soon. At the latest with the beginning of the industrial revolution, however, not only the scientific discussion about the economics of supply and demand and the options and limitations of satisfying human needs had started; due to advances in science and technology, the references to the finite nature of certain natural resources were receded into the background. Medical and technical developments enabled sustained and strong population growth, which even picked up in pace after the end of World War II. In the wake of this development, the general public only became aware of the "Limits to Growth" through a report of the Club of Rome published in 1972. This - in my view necessary - discussion however has since then met with a strong response especially in the economically far-developed, aging, and largely saturated Western societies - a fact that in my opinion is worth being examined with the scientific tools of psychology. With reference to Abraham Maslow, I assume at first glance, that humans, whose existential needs like food, clothing, and security are satisfied, rather focus on their individual needs or their need for self-realization and soon

start neglecting the fact, that for an ongoing satisfaction of existential needs the basis hereto must not be destroyed.

Interestingly, the discussion in media and politics about sustainability and conservation of scarce resources for some time now primarily focuses on the question of CO₂- emissions and their consequences - keyword: global warming. Against the background of the aforementioned, this is likely due to the fact that significant stakeholder groups in our society for reasons of either/or fear and/or ideology articulate a "personal concern" in combination with a "sense of urgency" i.e., they create an alarmist mood which - transported via media - then can be used to build up political pressure to overcome initial resistance against these ideas. I do not want to be mistaken: I, too, consider man-made climate change as a challenging and rather urgent problem; however, after reading all the IPCC reports on climate change of the past years, I am also convinced that the world will not end in the next 20 to 30 years due to climate change. And in view of the still unsolved problems of war and hunger in today's world, even several decades of a socio-economic transformation process towards sustainability and climate protection seems to be a rather ambitious period for the solution of such a monumental task. At the same time, I am firmly convinced that we can achieve what I consider a sustainable development of our economy and our society. In this context, we must also work hard towards a significant reduction of CO₂-emissions; however, we should not commit economic suicide for fear of ecological death.

In the still emerging economies of Asia and in the US economy, which for decades is characterized by a rapidly shrinking middle class and significant trade deficits, it will be decided whether sustainability and climate protection will have the same importance as they do here in Germany and Europe. In a saturated society like ours, it is easily forgotten that in other regions of the world, there is still the "fight for daily bread". By introducing overly ambitious rules and regulations, we risk to undermine and to destroy our today's and tomorrow's basis of our economic existence. Just take Venezuela as a negative example: Venezuela was in the 1970s (and still would be today) one of the richest countries in the world due to its oil wealth. Visit Venezuela today, and you might get a sense of how quickly an ideologically motivated policy can lead to the destruction of a country's business model.

3. Energy supply is a key issue for competitiveness and sustainability

The adequate and reliable supply of useful energy at competitive prices has always been one of the key factors for successful industrial development. At the beginning of the industrialization of the Western world, the question of the availability of primary energy sources was dominating. Over many decades of industrial development, the focus more and more shifted towards competitive energy costs and energy prices on a national and later also international basis.

The conversion of fossil energy sources into useful energy contributes significantly to CO₂-emissions into the atmosphere. Thus, beginning in the 1960s, the scientific discussions on "social cost" and the "internalization of external (environmental) effects" started, which finally led to CO₂-reduction efforts by the introduction of CO₂-emission certificates with a positive price and thus a cost. This concept follows a market economy approach and, if applied globally, would not only avoid distortions of competition but also, in the Smithian sense of the "invisible hand" of the market, it would have effective and efficient steering effects for the reduction of greenhouse gas emissions. In Germany – and in my opinion for primarily dogmatic reasons – we are already the famous "step further forward" within the framework of the German and European climate protection targets: As of today, we have in fact a general ban on the burning of fossil fuels – the German coal phase-out is agreed and signed, with natural gas already being "next in line" in the current political discussions. It cannot be ruled out that even the current German and European legislation will already put the industry in Germany on the economic sidelines today; a permanent sidelining however will lead to economic decline - unless we succeed in finding new, sustainable, redundantly available energy sources, which are, at the same time, competitive on an international scale. However, there are still high hurdles to overcome here:

Starting with the question of which technologies are not only technically feasible but also commercially competitive, to the question of their societal acceptance, to questions of appropriate and rapid approval procedures, timely technical implementation, and financial viability:

In view of the multitude of these transformation challenges, and given our ever-increasing sustainability targets, we in

Germany already should have progressed much further in the implementation of individual transformation steps. Instead of finally getting down to tackle the challenges and establishing and implementing a technically and commercially valid long-term transformation strategy in a spirited manner, we Germans are merely running behind the foreseeable failure to meet our climate protection targets, and almost all German politicians are trying to compensate for this only by permanently tightening the targets. A competent and responsible acting legislation looks different. And - see my comments above - competent, responsibly acting German and European policymakers would not lose sight of their global competitors but would adapt their own transformation expectations in terms of content and timing accordingly.

I would like to use the following picture for your imagination, to illustrate the dramatic nature of the current developments in German and European energy policy: Imagine that you are a professional skydiver, ready to jump the plane. This time, however, you will have to refrain from wearing a parachute due to its questionable sustainability. But in hope (and firm belief?), that by the time you are about to hit the ground, you will have found a more sustainable, technically functional, affordable, and acceptable alternative to your parachute, you boldly jump out of the airplane! I consider myself to be a courageous person, who is fundamentally confident about the future – but I nevertheless would not make the “leap” under these circumstances; I would not yet dare to “jump” under these conditions.

What is to be done?

Based on what I have said so far, I would like to conclude my keynote speech by attempting to outline ten basic rules for a successful transformation of our economy. I will keep these basic rules very brief and, incidentally, look forward to discuss these proposed rules with you.

1. Courage and confidence as a basic attitude!

An optimistic, confident basic attitude is the best guarantee for the development and testing of concepts for the future that can outlast the day and are made for the people. This also includes having the courage to be clearly visible and audibly in the discussion on these concepts for the future and to stand up for one's own opinion in a public, if necessary contentious, discourse - a quality not always

widespread between industry leaders in view of today's media environment. Courage and confidence are also helpful in coping with doomsday scenarios, true to Luther's motto: "If I knew that the world would end tomorrow, I would still plant a little tree today!"

2. Intellect instead of dogma!

We should use our minds instead of traditional and possibly dogmatic thought patterns. However, this requires us to critically question ourselves and, if necessary, to be able to admit one's own mistakes or misconceptions. In conjunction with Rule No. 1, this basic rule almost completely describes the principle of enlightenment - namely, man's enlightenment from self-inflicted immaturity: Dare to use your own mind - and act accordingly!

3. Realism instead of naivety!

Let us look at the world as it is - and not as we would like it to be. A realistic view on where we stand today should help us to identify real problems, to perform a solid root cause-analysis and to derive proper and feasible possible solutions to these problems. This rule also holds true in the evaluation of people, negotiating partners, and even nations and their interests and behavioral patterns.

4. Numbers, data and facts instead of beliefs!

Numbers/data/facts should be the basis for every decision. Beliefs or assertions without facts should play no role in decision-making. Alarmism must be avoided in any discussion.

5. Balance of objectives instead of a “blinkered view”!

There is usually more than one objective to be pursued in processes of change and transformation. When it comes to far-reaching changes, it is necessary to balance the justifiable objectives of the various stakeholder groups for reasons of acceptance. Against this background, we should also view the first “Ampel”-coalition at the federal level in Germany as an opportunity - even if not everyone likes everything in this context.

6. Develop several fault-tolerant options for action!

Don't put all your eggs into one basket, and also think the

unthinkable. This rule maintains the necessary flexibility of action, it leads to risk diversification and reduces fatal surprises.

7. Focus instead of bogging down!

We must make complexity “manageable”. In the age of “Dynexity” – i.e. dynamically evolving, complex issues - it is crucial to focus. Less is more - this also applies to legislation: We need less legislation but better, i.e., simpler, more transparent, clearer rules, which correspond to common sense and which, in the event of a dispute, can be decided quickly without everlasting nitpickings on legal subtleties.

8. Think global - act local!

This applies to few issues as much as to the issue of climate change. If there are no transparent, well-coordinated, and comprehensible regulations and agreements in this field on an international level, everyone will lose out in the long run. In this respect, the establishment of the G7 Climate Club is an important first step in the right direction.

9. Let's trust in the power of the market mechanism!

Different concepts for the future should be tested in competition according to the rules of the market economy, true to the motto: “The better is the enemy of the good.” Incidentally, this requires entrepreneurial courage and the willingness to accept the risk of failure in the market!

10. There is nothing good - unless you do it!

If the German and European economy is to be successfully transformed, we must all, as stakeholders in Germany and Europe, put an end to the cacophony of ever-increasing goals and objectives and instead move towards coordinated action on a subsidiary basis. This will not happen by itself, this will not happen through bureaucratic action - it will only happen on the basis of a mutually accepted, balanced system of objectives; and it will only happen when strong, visible, and credible leaders – both in politics and in the industry - lead this transformation process boldly and courageously!

Ladies and gentlemen, thank you very much for your attention. I am looking forward to further discussions with you!