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Private Courier: When Germans Open The Mail, They Get Message on Capitalism --- Former Monopoly, Bent On Offering One-Stop Service, Gobbles Rivals, Plans IPO --- UPS Drops a Note to the EU

By Neal E. Boudette. **Wall Street Journal**. (Eastern edition). New York, N.Y.: Nov 20, 2000. pg. A.1

Abstract (Summary)

This wasn't Mr. [Klaus Zumwinkel]'s first turnaround. In 1974, armed with a degree from the University of Pennsylvania's Wharton Business School, he joined McKinsey, and spent the next 10 years telling German companies how to reorganize. A year after becoming a global partner in 1984, he struck out on his own, taking the helm at Quelle Group, a struggling mail-order house near Nuremberg. The family-owned company's profits improved, but Mr. Zumwinkel clashed with the owners. In 1990, Post and Telecommunications Minister Christian Schwarz-Schilling offered him one of the biggest turnaround jobs imaginable: privatizing what was then known as Deutsche Bundespost.

After a messy dispute among Mr. [Larry Lee Hillblom]'s heirs, DHL assembled a packet of shares and sought a buyer in 1998. That was a topic for a DHL board meeting in Stockholm. Going in, Mr. Zumwinkel had an ally: Lufthansa AG, a Deutsche Post business partner that owned 25% of DHL. Coming out, Deutsche Post had a 25% stake of its own for just under $500 million.

This year, Deutsche Post won control of the group after DHL began looking for help financing a $1 billion upgrade of its air fleet. First, Mr. Zumwinkel secured management control by working a complex deal that gave Deutsche Post Lufthansa's voting rights. Then he went to a shareholder group made up of founders, their families and their trusts. In September, they agreed to sell enough shares to increase Deutsche Post's holding to 51%. The price was between $600 million and $800 million, say people familiar with the terms. As majority owner, Deutsche Post will help bankroll DHL's new fleet.

Full Text (2304 words)

BONN -- A few months after taking the top job at Germany's post office in 1990, Klaus Zumwinkel was touring a sorting center in Leipzig when he realized what a mess he faced. In a dimly lit room, the former McKinsey & Co. consultant saw parcels moving over the clattering rollers of a massive, iron contraption unlike any machine he'd ever seen. No wonder: The East German post's conveyors were actually made for Russian coal mines.

The West German part of what eventually became Deutsche Post AG wasn't in much better shape. It had modern equipment, but not much. Seventy-five percent of all letters in the West were sorted by hand. The parcel-delivery business was losing more than a billion marks a year. Bloated bureaucracy and snotty service were post-office hallmarks. Shaking his head at the memory, Mr. Zumwinkel says, "It was a sheer disaster."

Today Mr. Zumwinkel sits atop a global company that delivers everything from postcards to pickup trucks -- and threatens the giants of the industry. With a lucrative mail monopoly generating cash, he has turned losses into profits, even in parcel delivery, where Deutsche Post, at least for now, has countered a European thrust by United Parcel Service Inc. In an acquisition binge, the company has expanded into freight and pieced together a majority stake in DHL International Ltd., the largest express courier outside the United States, and once the object of UPS's desires.

This year's revenue should top 30 billion euros, or $25.57 billion, making Deutsche Post as big as UPS. The next step: an initial public offering today of one-quarter to one-third of the company's shares. At the issue price of 21 euros a share, Deutsche Post has a market value of 23.4 billion euros.

Takeovers? An IPO? The post office?

The company's story says a lot about how far market capitalism has penetrated Europe. The U.S. led in telecommunications liberalization, but Europe is at the fore in postal privatization. The Dutch post office, TNT Post Group, is already publicly traded. France's La Poste and Britain's Royal Mail have reached across borders for acquisitions. Deutsche Post has been the most aggressive, employing McKinsey-style management, rapid-fire acquisitions and -- if you believe its competitors -- anticompetitive behavior.

In contrast, the U.S. Postal Service, which is still owned by the government, is supposed to cover its costs but not necessarily make money. With revenue of $63 billion, it is the largest postal service in the world, but it can't buy private companies or own ground operations overseas. It recently sought an alliance with FedEx Corp. to reduce costs and increase its overseas business, but some members of Congress, UPS and the powerful Teamsters union are protesting. The talks are continuing.

Deutsche Post plays in another league. Just look at its takeover of Swedish logistics group ASG AB.

In 1999 several suitors, including Deutsche Post, were looking at ASG. Then, one Thursday night in April, ASG Chairman Christer Gardell called Mr. Zumwinkel to say Deutsche Post's strategy was a good fit. But he warned that the Swedish post office, after months of dithering, was finally ready to come through with a bid following a board meeting in 10 days.

Mr. Zumwinkel huddled with bankers and lawyers in Bonn through the following weekend, then flew to Stockholm on Monday with a bid of his own. He had a deal by Friday. "The Swedish post just couldn't get its act together," Mr. Gardell says. Mr. Zumwinkel has "the guts to make it happen."

Still, a clear strategy isn't always enough to sustain a former monopolist. Take AT&T Corp., which just scrapped a grand plan to create a broadband communications giant and is now breaking apart. In Germany, Deutsche Telekom AG's profits are falling faster than it can expand into new businesses. Life is harsh after you're no longer the only game in town.

Mr. Zumwinkel, 57 years old, has more immediate things to worry about: Outside of the protected mail business, returns are slim. In the first half of the year, Deutsche Post's logistics, express-delivery and financial-services divisions generated a 3% return on revenue. That's pretty thin compared with the 20% return on revenue generated by the mail business, which charges some of the highest rates in the world. A first-class letter costs 1.10 marks, or about 48 cents -- nearly half again as much as the U.S. price.

However, Deutsche Post's German mail monopoly ends in 2003, and small private couriers popping up in major cities are itching to expand into letters. Once the government gives up price controls, postage rates may fall.

Moreover, UPS, after struggling a few years ago, seems to be on track in Europe. In 1999, its international-package business rang up $252 million in profit. From 1995 to 1997, it lost $598 million. And while Mr. Zumwinkel's strategy looks impressive so far, he still has to integrate more than two dozen acquisitions from the last three years. Consolidation was one of the tasks that tripped up UPS a few years ago.

On top of that, Deutsche Post is still facing a European Union investigation into whether it improperly used mail profits to subsidize parcel prices and finance an acquisition binge. In the worst case, it could be fined hundreds of millions of euros when a final ruling comes next year.

That hasn't slowed down the company's 100-million-euro campaign to market the shares. The company's logo -- a black horn on a yellow background -- has been all over magazines and billboards in Germany for weeks. The airwaves are full of humorous television commercials featuring entertainer Thomas Gottschalk, his brother Christoph and a jazzy soundtrack. In one spot, Christoph Gottschalk lectures his brother to invest in logistics. Thomas nods approvingly -- at attractive women passing by.

Ten years ago, Germans would have laughed at the suggestion the post office was a good investment. In 1991, the reunified post office lost 1.5 billion marks. To turn the tide of red ink, Mr. Zumwinkel looked to -- who else? -- McKinsey. Among the consultancy's suggestions: cut 70,000 of the post's 390,000 jobs. Unions howled, striking seven times in 1990 and 1991. Headlines slammed the "McKinsey Post." Eventually, workers agreed to reductions through attrition and early retirement. By 1998, the headcount was down to 260,000. Acquisitions have since pushed it up over 300,000.

Culture was a problem -- on both sides of the recently demolished Wall. East German employees were more used to reading the mail than sorting it quickly. The answer was a dose of capitalist incentive. Big productivity improvements were rewarded with goodies such as TV sets or Mediterranean trips, which eastern Germans could scarcely afford back then.

The West suffered under stifling bureaucracy. Managers were paid based on the number of people they supervised. "Hire 20 more people and you got a raise," Mr. Zumwinkel says, rolling his eyes. He quickly put an end to that, offering managers bonuses for efficiency gains instead.

Lacking executive talent in-house, Mr. Zumwinkel went to big German companies -- and his old cohorts. Uwe Doerken came from McKinsey to start international operations. Edgar Ernst, who had worked there in the early 1980s, joined finance.

The nuts and bolts of the operation needed a major overhaul. Letters and packages moved by rail, bouncing around hundreds of small sorting centers in train stations. Packages on average made nine stops before reaching recipients. To streamline things, the post in 1992 began building a parcel network with 33 mammoth distribution centers located near airports and autobahns. The cost: four billion marks, drawn largely from the mail monopoly's cash flow. A few years later, Mr. Zumwinkel dipped into the mail businesses profits again for another four billion marks to build 83 computerized letter-sorting centers.

The overhaul also meant a slew of downtown post offices joined a list of apartment buildings and other real estate that Deutsche Post no longer needed, an asset Mr. Zumwinkel would tap later.

This wasn't Mr. Zumwinkel's first turnaround. In 1974, armed with a degree from the University of Pennsylvania's Wharton Business School, he joined McKinsey, and spent the next 10 years telling German companies how to reorganize. A year after becoming a global partner in 1984, he struck out on his own, taking the helm at Quelle Group, a struggling mail-order house near Nuremberg. The family-owned company's profits improved, but Mr. Zumwinkel clashed with the owners. In 1990, Post and Telecommunications Minister Christian Schwarz-Schilling offered him one of the biggest turnaround jobs imaginable: privatizing what was then known as Deutsche Bundespost.

By 1994, the agency, with the help of rate increases, was turning a clear profit on letters. The parcel business was still losing about a billion marks a year, but the new distribution network was ready. To fill it up, Deutsche Post slashed parcel delivery prices -- just as UPS was trying to expand in Europe through acquisitions.

Squeezed between tough pricing and a costly integration, the American company's international unit began racking up big losses. It also complained to the EU, alleging Deutsche Post's high postage rates were subsidizing predatory parcel prices and building a war chest for acquisitions. "We had to finance our expansion from our profits," says John Warrick, president of UPS Europe. Allowing a postal agency to use its monopoly to expand into private sector markets "is simply wrong."

Mr. Zumwinkel denies the charges. "This has all been researched by the German cartel authorities and there was no negative finding," he says.

By 1997, the parcel business was reducing its losses and Mr. Zumwinkel began pondering a strategy for the day when mail services would face competition. That summer, at a company retreat on the Ammersee, a lake in southwestern Germany, top management concluded that a dramatic expansion would secure the company's future.

The plan: go global, offer a one-stop shopping package of standard mail, express delivery, freight, even financing. And do it fast, before the mail profits dry up.

To drive this strategy, Mr. Zumwinkel set up an eight-member mergers-and-acquisitions team to find and research targets, and be ready to move at a moment's notice. High on the list was DHL, but that would have to wait. First, to build a pan-European network of ground couriers, they snapped up small companies in Italy, France, Spain and other countries. Then it moved on to bigger fish, hauling in Danzas AG, a Swiss coordinator of freight shipments for large companies; Dutch logistics group NedLloyd; Sweden's ASG; and American freight shipper Air Express International. In all, Deutsche Post laid out close to eight billion euros for around 30 companies.

Buying companies was the easy part. Now Mr. Zumwinkel has to get them to operate like one company, unifying their financial systems and computer technology. To make things easier, he's tried to keep top managers after the acquisitions by promising autonomy. It worked at Danzas, where nearly all senior executives have stayed on board. At ASG, however, Mr. Gardell and Chief Executive Jorgen Ekberg have departed.

In September Mr. Zumwinkel landed his biggest catch of all: DHL, a maverick courier whose founders had long resisted calls to take the company public. The deal had its roots in a 1995 plane crash that killed one of the DHL founders, Larry Lee Hillblom.

After a messy dispute among Mr. Hillblom's heirs, DHL assembled a packet of shares and sought a buyer in 1998. That was a topic for a DHL board meeting in Stockholm. Going in, Mr. Zumwinkel had an ally: Lufthansa AG, a Deutsche Post business partner that owned 25% of DHL. Coming out, Deutsche Post had a 25% stake of its own for just under $500 million.

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The move extends Deutsche Post's reach far beyond Germany's borders with a brand name known around the world, says Mr. Zumwinkel, adding: "You can go to a secretary in Bangkok or in San Francisco, and they both know DHL."

[Table]

Deutsche Post: From Princely Post to Global Player
1649: Friedrich Wilhelm, elector of Brandenburg, establishes a postal service that, 346 years later, becomes Deutsche Post AG.
1950: In aftermath of World War II, postal service re-established as Deutsche Bundespost in West Germany.
1990: German Post and Telecommunications Ministry broken up into Deutsche Telekom, Postbank and Deutsche Bundespost, which merges with East German Post office. Former McKinsey consultant Klaus Zumwinkel named chief executive.
1991: Unions strike repeatedly against "McKinsey-Post"" restructuring.
1992: Parcel delivery division, losing billions of marks, builds 33 new computerized distribution centers in Germany.
1994: With parcel centers finished, Deutsche Post slashes prices. UPS complains to EU, alleging its competitor uses mail monopoly profits to subsidize parcel rates.
1995: Deutsche Bundespost becomes corporation, still state-owned, called Deutsche Post AG.
1998: Following Zumwinkel's strategy to create global post, express and shipping company, Deutsche Post acquires U.S. periodical distributor Global Mail Ltd., German stationery retailer McPaper AG and 25% stake in DHL.
1999: Deutsche Post acquires ground couriers in Spain, the Netherlands, Italy, France and Britain; logistics groups Danzas AG, ASG, Nedlloyd and ITG; and state-owned savings bank Postbank AG.
2000: It acquires U.S. shipper Air Express International and Germany's DSL Bank and increases DHL stake to 51%. An initial offering is expected this month.
Source: The company

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