Teaching Note

Cemex’s Cost of ‘Globalised’ Growth – The Cash Crunch?

Synopsis of the Case Study

This case study, set during 2008–2009, offers rich lessons for companies going for global expansion through acquisitions. Cemex’s meteoric rise to become a formidable global cement player is undoubtedly quite remarkable. However, in 2008 and through 2009, the company was faced with a paradox – to sell off the valuable assets (that it acquired over the years) in distressed markets or to borrow fresh loans. Either way, it would be a momentous decision for the company. Forced by US Financial Crisis (2008), the company has to grapple with these twin issues. Ideally suited for global strategy module, this case can be used to address two major issues. First, the steps Cemex took in order to transform itself from a domestic firm to one of the largest multinational cement company under the leadership of Lorenzo Zambrano (Zambrano). Second, Cemex’ globalised growth during the boom times and its endurance from credit crunch in the bad times. Further, this case can be used to highlight the hidden dangers of going global and the importance of managing balance sheet in the traditional way. High leverage will take no time to boomerang when externalities, on which the company does not have any control, go wrong. Cemex made its globalised growth through disciplined acquisitions during boom times and was probably not well-prepared for the slump time that followed.

Pedagogical Objectives

The case is structured to help students:

- To understand the feasibility of different industries going global
- To debate on the merits and demerits of Cemex transforming itself from a highly diversified firm to a single business firm
- To analyse and contrast Cemex’ globalisation moves vis-à-vis Lafarge and Holcim and understand the timing and scales in this industry while going global

This teaching note was written by Vivek M.V. and Saradhi Kumar Gonela under the guidance of Dr. Nagendra V. Chowdary, IBSCDC. It is only an illustrative orchestration of the case study ‘Cemex’s Cost of ‘Globalised’ Growth – The Cash Crunch?’. It is never meant to limit the learning outcomes.

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- To critically analyse Cemex’ growth strategies and discuss and debate on the unintended consequences (both positive and negative)
- To explore various options for resolving Cemex’ acute cash crunch and evaluate those options.

Assignment Questions

I. Every year’s Fortune 500 ranking is grouped under several industries. Taking Fortune 500 list of industries for 2008, find out for which of these industries going global is relatively easier, given the nature of the industry?

II. What are the pros and cons of a diversified firm and single business firm?

III. How did Cemex’ late entry to the global market and innovative initiatives give it a competitive edge over its competitors?

IV. How did the customer service and branding strategies help Cemex to differentiate from its competitors?

V. Analyse the reasons for Cemex’ acute cash crunch. Discuss the possible solutions to survive the crisis and evaluate each solution.

Teaching Plan

A suggested teaching plan is given in Annexure (TN)-I.

Case Analysis

Feasibility of Going Global across Various Industries

Although the case does not make a direct reference, it’s useful to highlight for what kind of industries it’s relatively (not absolutely and assuming ceteris peribus) easier to go global.

What factors a company would and should consider before going global?

A list of all possible factors that will be considered can be prepared under two main subheads: 1) Company-related factors and 2) Industry-related factors. A combination of these factors can be analysed as depicted in Exhibit (TN)-I and the industries can be jotted down in the relevant quadrants.

While company related factors are unique, industry related factors will be general and therefore, understanding the nature of the industry, before going to company specific, is suggested. This can be discussed by the following questions:

- Is it possible for all industries to go global?
- Out of the industries listed in Fortune 500 – 2008, which industries can go global in a short span after establishment? (Distribution of the list of industries is suggested).
- Which industries take a long time to go global? What, according to you are the characteristics that make it easy for the industry (and therefore the companies from that industry) to go global?
**Exhibit (TN)-I**

**Cemex: Feasibility of Going Global**

<table>
<thead>
<tr>
<th>Nature of the product</th>
<th>Requires customisation</th>
<th>Going global requires high investment to modify products in every country</th>
<th>For industries in this area going global is very difficult</th>
</tr>
</thead>
<tbody>
<tr>
<td>Universal product form</td>
<td>Low</td>
<td>For industries in this area going global is very easy</td>
<td>Regulations would have to be eased before going global</td>
</tr>
<tr>
<td>Level of regulations</td>
<td>High</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Nature of Cement Industry**

The cement industry is characterised by high regulations, prohibitive transportation costs (especially when the points of sale are far off from the point of manufacturing), huge capital and high proportion of fixed costs and are resource specific. Operations of a cement company can be categorised into:

- Primary Activities and
- Secondary Activities.

Here the class can be asked to draw the value chain (Michael E. Porter) of the cement industry, differentiating primary and secondary activities.

Due to its inherent characters, the cement industry is highly fragmented with the top 10 companies producing only one third of the global cement supply (page 7, para 2 of the case study). The industry is fragmented because of high transportation costs and low scope for differentiating. In this industry the point of manufacturing and the points of sale are critical.

**Nature of the Product**

After analysing the nature of industry, a few minutes can be devoted to analysing the nature of product and the scope of branding cement can be explored, by asking what is the nature of cement (product)?

Though cement is majorly a commodity, it can still be branded. **Exhibit (TN)-II** would help to establish a relation between the degree of commoditisation and scope for branding; as degree of commoditisation increases, the scope for branding decreases. They are almost inversely proportional.

What is commoditisation? What are commoditised industries? Generally if the product has three important characters, it is said to be commoditised.
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- No or minimal scope for innovation
- No manufacturer has definite competitive edge
- The industry is highly fragmented with organised players having a marginal market share. For instance, the top 10 companies account for less than 30% market share.

Relation between Degree of Commoditisation and Branding

But if ‘Need of Branding’ replaces ‘Scope of Branding’ in the above exhibit on the x axis, the curve might be inverse or in other words, when competitors sell highly homogeneous product, the only differentiating factor would be branding and the curve would look as given in Exhibit (TN)-III:
To promote a discussion on the cement industry going global, the following questions would be useful:

1. Can the cement industry be globalised? Or shall it remain fragmented with local players in native countries? Provide reasons.
2. Can cement industry be globalised, considering that cement is demanded in different varieties, qualities and for different purposes in different countries and considering the environmental factors and transportation costs involved?
3. What would be the nature of competition of the companies in the cement industry? What parameters should they use to differentiate from each other – branding, services or price?

After discussing the possibilities of a cement company going global, the discussion can be shifted towards Cemex. To begin with, the merits and demerits of a diversified firm and non-diversified firm can be discussed.

**Merits and Demerits of a Single Business Firm**

The economic conditions in Mexico during 1980s had forced many of the companies to indulge in unrelated diversification to avoid the risk of depending on a single industry. Though Cemex was diversifying in the beginning of 1980s, as Zambrano took the helm, it decided to divest all non-cement businesses and concentrate on the core business.

Here, the class can discuss about the benefits and pitfalls of related and unrelated diversification.

The following questions can be posed in the class during this discussion.

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**Exhibit (TN)-III**

Relation between Degree of Commoditisation and Need for Branding

<table>
<thead>
<tr>
<th>Degree of Commoditisation</th>
<th>Need for Branding</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>High</td>
</tr>
<tr>
<td>Low</td>
<td>Low</td>
</tr>
</tbody>
</table>

- Steel
- Cement
- Food and Beverages
- Consumer Durables
- Computers
- Mobile Phone handsets

Prepared by the authors
1. Why do companies diversify? Compare and contrast the advantages and disadvantages between a diversified firm and a single business firm. Which format according to you is ideal for a cement company?

2. What do you think made Zambrano to focus on a capital-intensive industry like cement and divest all other businesses? Was it a wise decision considering its success in the Mexican market?

3. Can a functional product like cement become an emotional product? Explain how Cemex elevated an otherwise commodity into a product and then into a brand in Mexico (page 3, para 2 of the case study) (‘Blue Ocean Strategy.’ Framework may be referred here).

4. What were the business initiatives taken by Cemex in Mexico? What factors were responsible for Cemex’s success in Mexico?

**Major Initiatives Taken by Cemex that Led to its Strong Position in the Mexican Market**

- **Patrimonio Hoy**

This Cemex initiative to serve the low-income customers of Mexico was a huge success. *Patrimonio Hoy* programme is a good example of innovative marketing strategies of Cemex. Blending in the Mexican culture in the programme, Cemex gave construction materials to the family who won the lucky draw (page 3, para 1 of the case study). Technical know-how was provided to the participants through an architect of Cemex. This innovative programme helped to reposition cement, which was sold as an inexpensive commodity in Mexico. The programme, which had helped thousands of poor Mexicans to build their dream home, was internationally acclaimed and boosted the company’s image. The repositioning of cement in Mexico is a perfect example for the Blue Ocean Strategy.

- **Construmex**

Cemex initiated a programme called *Construmex*, targeting the migrated Mexicans to help them build a home in their home country. Through *Construmex* programme, customers could buy, construct or remodel their home in Mexico. Market researches including focused group studies and survey interviews were frequently co-conducted in Mexican consulates in each city. *Construmex* team realised that more than doing the material business they are supposed to gain the trust and make a strong relation with the customers. Mexicans in US could simply walk to a local Cemex office and select the plan they wanted for the construction of their Mexican home. As soon as the money was paid in US, Cemex Mexican counterparts did the delivery of the construction materials to the family in Mexico. Credit facilities were also available for the needy. *Construmex*’ catchy Spanish tagline *Hazla, Paisano*, which translates to ‘You can do it, Compatriot’ itself was very effective in attracting the US-based Mexicans. Through *Construmex*, Cemex strengthened its position in Mexico (page 3, para 2 of the case study).

After explaining about Cemex’ initiatives in Mexico, the major strategies used in customer support service and branding can be discussed. The following questions would be helpful.

1. How did Cemex change a commodity to a product and build a successful brand around it (page 3, para 2 of the case study)?

2. How did Cemex manage its value chain? How did it deliver value to the customers (page 13 of the case study)?

3. “At Cemex, the corporate brand is not just a logo, tagline or mission statement”, says Zambrano (page 11, para 1 of the case study). Explain.
Customer Service and Branding Strategies of Cemex

After having discussed the nature of globalisation in the cement industry, the customer service and branding strategies of Cemex can be discussed in the classroom. From Exhibit II of the case study the value creation at Cemex can be explained. The following Exhibit (TN) - IV can also be used to build the discussion.

<table>
<thead>
<tr>
<th>Exhibit (TN)-IV</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Commodity</strong> → <strong>Product</strong> → <strong>Brand</strong></td>
</tr>
<tr>
<td>Through innovative Marketing strategies</td>
</tr>
</tbody>
</table>

To discuss Cemex’s customer support service and its dedication to match the customer needs Annexure V of the case study can be used.

After discussing how Cemex has elevated a commodity to a brand, the discussion can now move on to the globalisation strategies of the company.

Globalisation Moves of Cemex

During the discussion of globalisation moves of Cemex, various methods that companies adopt while globalising can be explained and discussed. The three major globalisation strategies – global, multi-domestic and transnational approaches can be discussed in the class, with the help of the following table. The advantages and disadvantages of each strategy can be discussed. Various entry strategies can also be discussed while explaining the globalisation strategies.

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Multi-domestic</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transnational</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

A comparison of the timeline and pattern of global expansion of Cemex and its major competitors Lafarge and Holcim can be elucidated from Annexures II and III of the case study which shows the globalisation moves of the three largest players in the cement industry.

The case discussion can develop through explaining the late entry of Cemex to the global arena and how it took advantage of the IT and consolidation spree of the global cement industry. Here, some time can be devoted to have a discussion on first mover advantage and late mover advantage, with reference to the cement industry in general and Cemex in particular. Cemex’ dedication towards IT and its e-business ventures can be discussed at this point. Further, the HR practices at Cemex can also be discussed. Exhibit I of the case study will help in explaining Cemex’ HR strategy of keeping the right person at the right job.
Suggested Questions:

1. What are the various ways a company can adopt to enter the foreign markets? Why did Cemex opt for acquisition as a strategy for global expansion? What are the advantages and disadvantages of ‘market-entry through acquisitions’ strategy?

2. Given that consolidation in cement industry and IT revolution occurred during early 1990s, did Cemex’ late entry to the global arena play any role in the success of the company?

3. Discuss globalisation moves of Cemex, Holcim and Lafarge. Are there any similarities among the patterns of global expansion and the timelines?

4. Was there any difference between the strategies adopted by Lafarge, Holcim and Cemex? Were resources of the companies and economic conditions of their countries of origin the same for all three? Why do you think the country of origin matters in case of globalised companies?

After discussing about globalisation strategies, the class can shift to the geographic diversification of Cemex.

Geographical Diversification

The merits and demerits of geographical diversification can be discussed here.

Cemex’s initial strategy of acquiring underperforming companies in developing countries which have got enormous growth potential can be explained here.

At this point, Pankaj Ghemawat’s CAGE framework (in Redefining Global Strategy) can also be explained. It depicts the cultural, administrative, geographic and economic distances between the countries of origin of the acquired and acquiring companies.

Cemex’ way of standardising the acquired companies, the ‘Cemex Way’ can be discussed at this stage.

Suggested Questions:

1. What is the globalisation philosophy of Cemex and what are the advantages and disadvantages of that philosophy?

2. Why did Cemex select Spain as the destination for their first expansion instead of any other country? Is managing the cultural differences a problem to global companies?

3. What are the challenges faced by a company during geographical expansion? How did Cemex overcome them?

4. Why is standardisation of processes through post-merger integration an important part when companies expand through acquisition? How did Cemex standardise the acquired companies? Explain the ‘Cemex Way’ and its success.

After explaining the geographical diversification, Cemex’ global strategies and the unintended consequences can be discussed.

Growth Strategies and Unintended Consequences

Cement industry is a capital intensive and hence the amount that would be required for acquisitions are huge.

The concepts of financially leveraged buyouts can be explained here. The reasons for Cemex selecting the leveraged method of expansion can also be discussed. In leveraged buyouts, the acquiring company
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Cemex borrows more than 70% of the purchase price from financial institutions, which is quite a big amount, considering the capital-intensive nature of the cement industry. The positive and negative aspects of leveraged buyouts can also be explained here.

Using Annexures VI, VII, VIII and IX of the case study, the financial position of Cemex can be discussed. The points that could be discussed are:

- Decreasing growth of net sales over years
  (The growth of sales from 2004 to 2005 was mainly due to the acquisition and consolidation of the UK-based RMC, in 2004. The growth of sales in 2007 was largely contributed by Rinker, which was acquired by Cemex in 2007.)
- Decreasing growth of net income
- Increasing expenses (General and Administrative (G&A) expenses and financial expenses and cost of sales)
- Decrease in the cash flows

The free cash flow is the key source of paying the debt. A decrease in the free cash flow is viewed rather critically by investors and analysts.

- Financial ratios.

What could have been the state of Cemex today had it not gone for aggressive global acquisitions? In other words, Cemex – Global Acquisitions = ? The last sentence of the case study can be used to discuss this.

Suggested Questions:

1. What are leveraged buyouts? Should companies opt for leveraged buyouts when they globalise? What are the advantages and disadvantages of leveraged buyouts? What could be the possible implications of debt financing when market faces a severe downturn?
2. How did Cemex finance its globalisation? How do you analyse the company’s financial position from Annexures VI, VII, VIII and IX of the case study?
3. What do you think is the real reason behind Cemex’s troubles – acquisition of Rinker group or Global financial crisis or both?

After explaining Cemex’s financial position, Venezuela’s nationalisation (Annexure X of the case study) and US market’s slowing demand can be explained.

After discussing the nature and intensity of financial troubles at the company, the possible ways of resolving the cash crunch can be discussed.

Options for Resolving Cash Crunch

After explaining the financial troubles of Cemex, the possible ways of finding a solution can be discussed. The options are:

- Arranging new credit lines
- Selling off assets.

The difficulties of both the options during a financial downturn also can be explained. Further, the steps that Cemex took to cut down the costs (closing down manufacturing units, reducing human assets) and to pay off debts (new credit lines allowed by the banks and sale of assets in different countries) can be explained. According to the latest reports (Smith Geri, “Hard Times Ease for a Cement King”, Business Week, November 5th 2009), Cemex is on the path of recovery.
Suggested Questions:

1. With reference to the cement industry’s fate in Venezuela, do you think nationalisation of industries is a threat for globalised companies?

2. What are the major options to resolve the existing problems of Cemex? What according to you is the best option to come out of the acute cash crunch? Will the company be able to woo its investors back after the downturn?

3. Should Cemex rethink on its globalisation strategy?

The discussion may be wrapped up with an overarching question: What generalised observations / lessons can be drawn from Cemex’s global strategy moves? Would they be same across the industries?

The Big Picture

• When a firm’s growth is due to globalisation during good times and the growth is mostly funded by debt capital, it can face a severe cash crunch when the bad times start.

• Is there any difference between – when a company from an emerging economy goes global and a company from a developed economy goes global?
### Annexure (TN)-I
**Teaching Plan**

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Analysis Section</th>
<th>Expected Learning Objectives</th>
<th>Forward Linkage</th>
<th>Ideal Duration (minutes)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Feasibility of Going Global across Industries</td>
<td>• Industries that can go global&lt;br&gt;• Cement industry and business models in the industry&lt;br&gt;• Scope of globalisation for cement companies&lt;br&gt;• Commoditisation and branding of cement.</td>
<td>Merits and demerits of reversal of diversification</td>
<td>15</td>
</tr>
<tr>
<td>2</td>
<td>Merits and Demerits of a Single Industry Focus of a Company</td>
<td>• Diversification&lt;br&gt;• Reversal of diversification&lt;br&gt;• Mexican economy’s part in Cemex reversal of diversification&lt;br&gt;• Merits and demerits of reversal of diversification.</td>
<td>Globalisation moves of major firms in cement industry</td>
<td>15</td>
</tr>
<tr>
<td>3</td>
<td>Globalisation Moves of Major Firms in Cement Industry</td>
<td>• Globalisation strategies&lt;br&gt;• Importance of IT&lt;br&gt;• Branding&lt;br&gt;• Customer satisfaction through convenience&lt;br&gt;• Value creation&lt;br&gt;• Bases of geographical expansion&lt;br&gt;• Cost benefit analysis of geographical expansion&lt;br&gt;• Value chain decision&lt;br&gt;• Challenges of going global.</td>
<td>Options of resolving the current troubles at Cemex</td>
<td>20</td>
</tr>
<tr>
<td>4</td>
<td>Options of Resolving the Current Troubles at Cemex</td>
<td>Reasons:&lt;br&gt;• Financial position of the company&lt;br&gt;• Financial leverages&lt;br&gt;• Recession in main markets&lt;br&gt;• Nationalisation in Venezuela. Solutions:&lt;br&gt;• Arranging new line of credit&lt;br&gt;• Selling assets.</td>
<td></td>
<td>20</td>
</tr>
</tbody>
</table>

Prepared by the authors