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Hard Times for Cement Man

By JOEL MILLMAN

MONTERREY, Mexico -- Lorenzo Zambrano is a poster boy for globalization, a swashbuckling executive who turned a sleepy local cement maker into Mexico's first true multinational, with holdings on five continents. For many in Latin America, in particular, he became an inspiration, showing how to not just survive in a competitive world but dominate.



Stepping in 23 years ago at a business co-founded by his grandfather, Mr. Zambrano pushed into country after country with daring acquisitions. As each paid off, the esteem accorded both the company, Cemex SAB, and its leader grew.

Late last year, he did his biggest deal yet, buying Australian company Rinker Materials Corp. for \$15.3 billion and hoisting Cemex higher in the ranks of multinationals. There just were two problems with the big acquisition: One of Rinker's main customers was the U.S. housing market. And some of the debt used to buy it would soon need refinancing.

The twin curse of a housing collapse and credit crisis has ravaged Cemex. In a cold market for borrowing, Cemex has \$5.7 billion of debt coming due in 2009. Efforts the firm made to hedge its currency exposure have backfired, as a flight to the safety of Treasury bills sent the dollar higher, costing Cemex \$711 million. Now a company known for relentless expansion is selling assets, negotiating with creditors, and cutting its work force and spending.

The turnaround underscores a hard lesson of the financial crisis: For all the promise globalization holds for aggressive companies and executives, it carries hidden risks that can slam both operations and reputations. The wide array of people hurt by this crisis includes some executives who, in ordinary times, were among the most brilliant at navigating the international marketplace.

"Lorenzo Zambrano has built a hell of a company and the reputation he has is well earned," says Javier Macaya, president of a New York mergers firm called Athelera LLC and a former Cemex executive. "Now he's facing a challenge as tough as any he's had, and unfortunately a very well-earned reputation can be lost, if things don't work out."

Mr. Zambrano, who is 64 years old, declined to be interviewed. In a memo to employees in September, he cited the financial turmoil and said the deterioration of the markets "has been worse than anyone anticipated." In the third quarter, Cemex's sales declines ranged from 10% in Mexico to 26% in Spain. Mr. Zambrano said the company must "make extra efforts to adjust our operations to face new market realities."

During the years he was building up Cemex, ultimately into a company with more than \$21 billion of revenue, Mr. Zambrano demonstrated an unshakeable faith that debt loads that might seem alarming to some were manageable in the right hands.

He largely eschewed long-term financing from capital markets in favor of shorter-term bank loans. These he would refinance a year or two following a takeover after showing lenders how well the deal was working out. The assumption was that debt markets would always be open to a business as professionally run as Cemex.

Now Cemex is staring at a mountain of \$16.4 billion to almost \$20 billion of debt, depending on the accounting principles used, at least twice the company's stock-market value. Facing weak housing sectors in its three core markets -- the U.S., Spain and Mexico -- the company is hard put to generate enough cash soon to whittle that debt much. Its annual cash flow equals about 17% of its debt, below its historic average of 30%.

The debt includes a \$3 billion loan related to the Rinker acquisition that matures in December 2009, according to Fitch Ratings, which says banks have agreed to extend part of this loan for an extra year. Cemex says it is negotiating part of its loan maturities with five banks.

"Our overarching commitment in the immediate future is to maximize free cash flow from operations and asset disposals and to deploy those resources towards deleveraging," says Héctor Medina, Cemex's executive vice president of planning and finance.

As Cemex attacks its debt pile by selling assets, the chilled credit market is dealing the company another blow by making it hard to get top dollar. Cemex's Spanish unit agreed last month to sell operations in the Canary Islands for \$211 million, well below what similar assets had fetched recently, according to industry analysts. Assets Cemex sold in Hungary and Austria brought about \$400 million, almost \$100 million less than analysts expected.

Cemex's stock reflects the damage. On the New York Stock Exchange, its American depository receipts, which neared \$40 in June 2007, sank to barely above \$4 in November before rebounding to \$10.61 on the prospect of big U.S. infrastructure spending in the Obama administration. Some 87 portfolio managers bailed out of the stock altogether in the quarter ended Sept. 30.

"The debt obligations and what was coming due really surprised us," said one of them, Thomas P. Meehan, president of Edgemoor Investment Advisors. It bought Cemex shares on the way down but got out of them this summer after losing a third of its investment.

Cemex's decline has wreaked havoc with wealth in Monterrey, where old family fortunes rule the social roost and where many invested in Cemex during its years of growth. "A lot of multimillionaires here are just millionaires now," says Rogelio Sada Zambrano, a former congressman and Monterrey corporate executive who now works in the city's administration.

Kith and Kiln

According to bankers here, one of the hardest-hit fortunes belongs to the García Segovia clan, whose ties to Cemex go back generations. Locals say that some family members doubled down when Cemex stock first started falling, borrowing against their shares to buy more, only to face demands for more collateral when the stock kept sinking. One family member asked about the matter, Armando García Segovia, a Cemex vice president, declined an interview request; another García Segovia, Jorge, who runs a private foundation, didn't return calls.

Mr. Zambrano owns less than 1% of Cemex's shares, according to company filings, so it appears he has lost a few hundred million dollars at most.

Most Admired

Mr. Zambrano has long been among Mexico's most respected corporate leaders and a personal symbol of Monterrey, the nation's northern industrial capital. A survey of Latin American businesspeople by PricewaterhouseCoopers in 2000 rated Cemex the region's most admired company.

One reason is the smooth way it handled the flood of competition brought by the North American Free Trade Agreement after 1994. Other venerable Monterrey industrial companies have either been swallowed or had to learn to live in reduced circumstances. Cemex thrived.

Mr. Zambrano became corporate Mexico's informal ambassador to the world. Cemex gave other Latin American businesspeople the confidence to expand abroad. Three other Latin American cement companies followed Cemex into the U.S. market.

Mr. Zambrano cultivated an image as a philanthropist and arts patron. He raised millions of dollars for a prominent university, El Instituto Tecnológico de Monterrey, from which he has an engineering degree (in addition to an M.B.A. from Stanford University). In his corporate suite he displayed the works of Mexican artists Diego Rivera and Joaquín Clausell and Argentine modernist Guillermo Kuitka.

He has long come across as a hands-on corporate boss. A decade ago, displaying a battery of computers to a visitor, he demonstrated how he monitored the heating temperatures of industrial kilns an ocean away in Spain. With the help of satellites and software originally modeled on the 911 emergency systems of U.S. cities, Cemex trucks could usually fulfill orders within 30 minutes.

"A cement company is not supposed to be high-tech, but we showed it can be," he said at the time. "It is supposed to be boring, but we showed it is not."

Boring is not a word Wall Street would have used for Cemex. The company sometimes alarmed investors and credit-rating agencies as it took on enormous amounts of debt for acquisitions, then calmed their nerves when the bets came up winners.

Bulking Up

Mr. Zambrano's first big overseas move was in 1992, when Cemex purchased Spain's top two cement companies by borrowing more than \$1 billion. It was a staggering sum at the time for a company in Mexico, a nation that had defaulted on its international obligations less than a decade earlier when oil prices fell. But Cemex performed profitably in the emerging Euro zone and mounted a challenge to the world's two largest cement makers, France's LaFarge SA and Switzerland's Holcim Ltd.

Acquiring companies in Europe also offered something besides sales: the chance to master the kinds of efficiencies needed to prosper in world markets. Lessons Cemex learned from its Spanish acquisitions, about managing inventory and accessing customers in third countries, later paid off in other markets.

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Acquisitions came at a steady pace. In 1994, during an economic crisis in Venezuela, Cemex paid \$320 million for control of its largest cement producer, [Vencemos](#). Exports of cement from that operation soon were contributing \$100 million a year to Cemex's revenue. The same year, Cemex bought a company in Panama, just in time for a construction boom as Panama City rebuilt after the turmoil of the Noriega years. With smaller purchases in Trinidad, the Dominican Republic and Jamaica, Cemex became a nimble supplier to the Caribbean.

The 1997 Asian crisis enabled Cemex to pick up properties in the Philippines, Taiwan and Indonesia. It generally moved with prudence. For instance, Cemex took the plunge in Asia only after stoking its own exports to the region, waiting until regional demand exceeded what it had the capacity to ship from North America.

By the mid-1990s, nearly a third of Cemex's earnings were coming in dollars. As a result, Cemex could largely eliminate the "country risk" associated with being Mexico-based and borrow more cheaply than most Mexican companies.

And as Cemex grew, its debt pile offered it protection from becoming a takeover target itself, analysts say: The debt load made Cemex less appealing to a would-be acquirer.

In the 2000s, deals Mr. Zambrano engineered grew larger. In 2000, Cemex paid \$2.8 billion for a Houston-based supplier, Southdown Inc. In 2005, Cemex paid \$6.5 billion for RMC, the biggest cement company in the U.K. and one of the world's leading suppliers of concrete to construction sites. Revenues soared and profits kept pace.

Then came the \$15.3 billion Rinker deal, which closed in December 2007, when the U.S. housing market that Rinker supplied already was months into a downturn. Rinker, although Australian-based, does almost 80% of its business in the U.S., including a large part in Florida, an early and hard-hit victim of the housing collapse. "We said at the time that we expected a continued downturn in the U.S. market, but not so hard or so long," says Jorge Pérez, a spokesman for Cemex in Monterrey.

At the time, Cemex's long record of successful international expansion reassured investors and credit-rating firms. Moody's Investors Service called attention to the high cost of incorporating Rinker into Cemex operations but concluded: "Integration risk surrounding Rinker is manageable given Cemex's track record."

Hedges Backfire

As a company with far-flung operations, Cemex used various complex currency strategies. For years, it borrowed heavily in Mexico and then converted peso-denominated debt into dollar-based debt, which carried less risk and therefore a lower interest rate. This worked well while the U.S. dollar was mostly declining against other currencies, because a depreciated dollar made dollar debts cheaper to repay.

But this year, as credit turmoil worsened and grew global, investors fled to the safety of the dollar, driving up its value and sending down that of many other currencies, including the peso. As investors pulled their cash from Mexico, the dollar rose in value to 14 pesos, from 11. Cemex was caught short. Its dollar debt grew more onerous. In mid-October, the company disclosed it had lost \$711 million on derivatives, mostly currency swaps.

"With Cemex it wasn't speculation, it was bad luck," says Álvaro Rodríguez, a Monterrey venture capitalist and former corporate executive. He remains a fan of Mr. Zambrano, whom he praises for presiding over a corporate meritocracy and managing complex acquisitions skillfully through years of economic turmoil.

The last of those, however -- the ill-timed Rinker takeover -- has left Mr. Zambrano facing a big enough debt burden that one debt rater, Fitch, has downgraded Cemex credits to below investment grade. "For 20 years he managed Cemex flawlessly," says Rossana Fuentes Berain, who published a biography of Mr. Zambrano, "Gray Gold," this year. "Now people are obviously asking why such brilliant people like Lorenzo could not see this coming. Why weren't they more cautious? Why didn't they ask the right questions?"

Write to Joel Millman at joel.millman@wsj.com

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