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Post acquisition business synergies of a foreign affiliate. Case study of companies in Nuevo Leon (La importancia de la creación de sinergias, después de realizar una adquisición de filiales en el extranjero, casos empresas de Nuevo León)

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Summary: This article will explain the importance of creating synergies after having acquired foreign affiliates. Interviews were conducted to executives of four of the most important manufacturing companies in Nuevo Leon, which have been involved in the international acquisition process of foreign affiliates. Also presented are 10 areas where synergies may be obtained after having acquired a foreign affiliate, in accordance with (Marin and Ketelhohn, 2008) economies of size at corporate headquarters, greater opportunities for professional development, corporate image, interdivisional transactions, vertical integration, economies of scale and/or scope, coordination of skills, learning center, leverage of intangible assets and unleashing of skills.

Palabras clave: Adquisición de empresas, globalización, México, sinergias

Resumen: Este artículo explica la importancia de la creación de sinergias después de realizar una adquisición de filiales en el extranjero. Se realizaron entrevistas a ejecutivos de cuatro de las más importantes compañías manufactureras en Nuevo León con experiencia en un proceso de adquisición de filiales extranjeras. Asimismo, considerando el trabajo de Marin Ketelhohn (2008) se estudian 10 áreas en las cuales se hayan obtenido sinergias después de haber adquirido una filial extranjera, esto es, economías de escala a nivel dirección del coorporativo, mayores oportunidades para el desarrollo profesional, imagen corporativa, transacciones interdivisionales, integración vertical, economías de escala y/o alcance, coordinación de habilidades, centros de aprendizaje, apalancamiento de activos intangibles.

Post Acquisition Business Synergies

Introduction

Synergy, from the Greek synergos, which means working together, is present when the value created by the units that work together is greater than what those same units would produce if they worked independently. The company will only be able to achieve a competitive advantage through an acquisition strategy if the transaction generates its own synergy. The own synergy is obtained when the combination of the assets of the acquiring company and those of the acquired company and its integration produce central capacities and competencies. These would not be obtained if one of these companies combines and integrates its assets with those of any other company. In other words, it occurs when the assets of the companies complement themselves in a unique form, that is to say, the exclusive form in which the assets complement themselves cannot be achieved combining the assets of one of these companies with those of any other company. Given this uniqueness, competitors will find it difficult to understand or copy this own strategy (Hitt et al., 2004).

A perspective related with the origin of synergy in mergers and acquisitions is what is known as hypothesis of internalization. This is when a solid object company has some intangible assets of the brand name or experience that could benefit the buyer. A sample of 225 foreign acquisitions by American companies during 1979 to 1990 revealed that when there existed a basis for real synergies as, for example, when the object company had valuable intangible assets or impressive R&D skills, both the object company and the buying company benefited. (Gaughan, 2008).

Determining the problem

The reasons for which mergers and acquisitions of companies are produced might have appropriate or debatable economic logic depends on whether or not they fulfill the main objective of all managerial decisions: the creation of maximum value that is possible. The basic idea is that companies have to be competitive if they are to survive and continue addressing all parties involved. This vision acknowledges that the long term destiny of a company depends on a financial relationship with each party involved that has an interest in the company (Mascareñas, 2005).

Two of the more common ways to enter the European Union market consist of obtaining acquisitions or strategic alliances (Tolchin, 1993). In a Harvard Business Research magazine study (1992), 49 strategic alliances around the world were analyzed and the conclusion was reached that the probabilities of success increased if the parties had in mind five principles: 1) acquisitions render better results than alliances when basic businesses are conducted, 2) alliances are effective when companies want to penetrate new markets or businesses that are secondary to the core business, 3) alliances between strong and weak companies are rarely successful, 4) enduring alliances are characterized by their capacity to go beyond initial expectations and objectives, and 5) alliances will have greater probability of success if both parties share ownership as equals (Rugman and Hodgetts, 1997).

As has been previously mentioned, the internationalization process of the economy makes it increasingly necessary for a company to leave its natural and known geographical environment, from which it evolved, and where it has traditionally developed its activity in order to begin competing outside of its national borders in new countries.

The main reason for a company to acquire another is that the shareholders will benefit from the merged company with additional revenue as compared to adding up the revenue of the two companies if they operate separately. The increase to the revenue created by the merger of the two companies, or the creation of new wealth is called synergy. Synergy is the creation of revenue in addition to the existent. The equation of synergy shows that 1 + 1 = 3. This means that the wealth created by the merged company is greater than the sum of the revenues created by the two companies separately. Synergy justifies the merger of the two companies (Marin and Ketelhohn, 2008).

Due to the fact that there is insufficient literature and research of Mexican companies showing the results of the success factors creating Synergies in the international acquisitions, it is the intention of this research to contribute and provide insight to the cases of Mexican companies that have been successful using this strategy. For this study, in first instance, four of the most important companies in Nuevo Leon were chosen, Cementos Mexicanos (CEMEX), Grupo Maseca (GRUMA), NEMAK and FEMSA. These companies have been leaders in their markets and have been successful in their growth and organizational development, using the strategy of global growth by means of acquiring foreign plants or companies. A common denominator that these companies have, besides being leaders in their fields, is that they have grown their market share through acquisitions, thus having become world class companies. Therefore, the main variables that these companies have taken into account before executing their acquisitions will be analyzed. Also to be analyzed the important factors that these companies considerate to create synergies.

General Objective

The objective of this paper is to analyze the success factors that the large companies of Nuevo Leon international growth by means of acquiring a foreign plant or affiliate, thus creating value by forming synergies with the foreign acquired affiliates.

Background of synergies

Synergies are the reason for mergers and acquisitions. However, this is not something that simply happens once the merger has been executed. The creation of synergies needs the will and work of the executives of the participating companies, in order to exploit the opportunities that these companies offer. In a merger, in which the divisions of the company continue competing in the marketplace, it will be more difficult to achieve synergies because there will be competition for the same corporate resources. Synergies are created by means of a process of integration and coordination of the various activities, functions and businesses of the company. This is facilitated through the existence of one culture, a climate of learning that promotes sharing and learning from each other while developing relevant work systems and procedures. Top management must fully understand the functioning of the businesses, foster a mentality of cooperation and have the will to get the organization to commit to the search and utilization of opportunities for the joint creation of new value. Also needed are appropriate incentive systems and the tenacity to consistently drive the creation of synergies (Marin and Ketelhohn, 2008).

The operational synergy may be achieved in two forms: increasing revenues or reducing costs. Increased revenues through operational synergy achieved by the creation of a new product or service emerge from the merger of two companies and that generates long term earnings growth. This type of synergy is known as REO (revenue-enhancing opportunity). For example, by sharing marketing opportunities (expand the product range by using the joint distribution channels more efficiently, etc.), benefiting from the good reputation and brand image of one of the companies (for example, the frail sales of British automobile manufacturer Rover expected to benefit from the good reputation of its buyer, the German manufacturer BMW). The operational synergy of reducing costs is achieved with the attainment of economies of scale. These are attained when the average unitary cost drops as production volume increases. Through this, large scale investment levels may be contemplated, allot the costs of research and development, other fixed costs on a bases of higher sales or a greater asset or, for example, achieve economies in the production and sale of products; enabling the company to cut many of the common expenses of the organizations involved, due to the fact these cost concepts increase at a slower rate than those that are directly proportional with the volume of the activity. For example, the wave of mergers in the chemical and pharmaceutical sectors towards the end of the 90's had as an objective to share the enormous disbursements needed to face R&D (Mascareñas, 2005).

Theoretical framework

An important risk, especially in acquisitions, is the integration of the acquired company to the operations of the buying company. Before buying the selected company, many executives center their attention on strategic matters, valuation, financing and negotiation while on occasions forgetting to review the barriers that the acquired companies may have at the time of merger. A company that is merged with the will to find and utilize the synergy opportunities may be able to increase its income. To take advantage of the opportunities for creating new wealth, we must make sure that the object company complements the buying company with resources and skills. This complementarily is called strategic adaptation (Marin and Ketelhohn, 2008).

Strategic adaptation is measured with the generation of synergies. If there is no new economic income the acquisition is not justified. Buying the selected company for the sole purpose of selling more does not justify the transaction (Marin and Ketelhohn, 2008). Synergy is usually classified in two types:

1. Exploitation synergy usually emerges from cost reduction that is produced after a company association. These cost reductions may be a consequence of economies of scale. This is a term in economics that refers to cost reductions per unit which is a consequence of an increase in the size or scale of operations of a company.
2. Financial synergy is the synergy that increases revenues and are those combinations that increase the capacity of the associated entity to generate income. In other words, after a corporate merger, if the company experiences an increase in revenues higher than what it could achieve by simply adding the income of the constituents of the merger, perhaps the synergies that increase income might explain that gain. (Gaughan, 2006).

When two companies merge, strategic adaptation, according to Marin and Ketelhohn brings about synergies in some of the ten areas that are constituted in sources for the creation of new income and which are presented as follows:

1. Economies of size in the corporate headquarters. These synergies emerge from savings in administrative costs in the corporate center. When the companies are very large, savings are insignificant and do not justify a merger, unless the inefficiencies are overwhelming.
2. Greater opportunities for professional development. Good job opportunities retain and attract the best executive talent and these are derived from the bigger size of the company. Consequently, the merged companies benefits by having better executive talent.
3. Corporate image. The reputation of the merged company is transferred and permeates all the products of the merged company with quality, excellence, added value, ethics, etc. Corporate image is one of the big intangible assets.
4. Interdivisional transactions. Buying products or services from a sister division is a competitive activity. The seller attempts to maximize its profit margin in the transaction, while the buyer attempts to reduce it. For that reason, often times the transaction does not take place without the intervention of the corporate director

or president. Upon substituting the market one must do so cautiously because no new value is necessarily created.

5. Vertical integration. Integration into the businesses of customers and suppliers is common in the search for synergies. However, the approval of customers' and suppliers' margins requires special skills in using business models, completely foreign to the core business. Synergies may result with the appropriation of these margins.
6. Economies of scale and/or scope. These emerge from shared activities in purchasing, manufacturing, research and development, marketing, services, etc. In this case synergy comes from unitary cost reductions.
7. Coordination of skills. Divisions are restructured to align and exploit common skills, for instance, to access geographical segments or locations. Synergy is the result of consolidating common skills.
8. Learning centers. In the centers for excellence, skills, technology and/or processes are shared. These centers transfer knowledge from one business to others, such as the use of Six Sigma, Total Quality Management, Just in Time, etc. Synergies come about from accruing and cultivating skills in centers that are common to several businesses.
9. Leverage of intangible assets. The company can use its brands, customer and market knowledge in all the businesses. The intangible assets created in a business may be transmitted and used in others without being consumed. Synergies are a result of exploiting brands in compatible businesses and the corresponding distribution systems.
10. Unleashing skills. Freeing up the restrictions to exploiting new products, technologies and/or processes in all the businesses and activities of the merged company improves existing skills and creates new ones, thereby expanding markets, businesses or both. Synergies are attained by eliminating barriers to the access of exploitation of skills (Marin and Ketelhohn, 2008).

Porter (1987) identifies three types of associated costs with the creation of synergies:

1. Coordination costs: are derived from the greater effort that the company needs to do to share resources or transfer knowledge by

means of installing adequate formal or informal organizational mechanisms. Definitely synergies are not generated automatically by investing in related businesses, so company management must create them through a continued effort. Generally speaking, it can be stated that coordination costs grow with number of businesses that make up the portfolio.

2. Commitment costs: the generation of synergies forces getting commitments between the various business units in the managing of these. These commitments may be necessary to generate synergies but may also harm the operation of each unit separately, and the benefits of these synergies may be totally or partially compensated by the poor operation that is enforced by the attention given to cooperating with commitments.
3. Inflexibility costs: The generation of synergies may yield, through the needed coordination and acceptance of commitments, interrelationships or dependencies between the business units that reduce their competitive capacity. Indeed, a business unit cannot respond to the competitors' movements without taking into account the effect that its decisions have on the rest of the businesses, which limits its capacity to act. Furthermore, interrelationships between businesses could create exit barriers to them because the withdrawal of a business may seriously affect the remaining businesses (Navas and Gueras, 2002).

As was stated earlier, the process of external growth consists of growing through the merger and/or acquisition of companies with the skills to create new wealth. When a company is identified and acquired, that complements the skills of the buying company, it is said that it adapts to the strategy of the buyer for the creation of wealth. Therefore, strategic adaptation means that the resulting company will create larger economic revenue than the two companies separately.

The exploitation of synergies has a double perspective (Forcadell, 2002; Forcadell and Guerras, 2001) because, on one hand, the diversification has its origin in the company's portfolio of resources, fundamentally intangibles. However, on the other hand, this exploitation of synergies promotes the generation of new resources, due to the use of a related diversification. Both aspects will positively influence the company's results (Naves and Guerras, 2003).

The exploitation synergy normally results in a cost reduction that is produced after an association of companies. These cost reductions may be a consequence of economies of scale. This economics term that refers to the reductions in costs per unit which is a consequence on an increase in size or scale of operations of one company. (Gaughan, 2006)

Synergies that increase revenue are those combinations that increase the capacity of the merged entity to generate revenue. In other words, after a corporate union, if the company experiences an increase in revenue higher than what it could achieve by simply adding the revenues of the members of the merger. Perhaps the synergies that increase revenues explain this gain. (Gaughan, 2006).

Financial synergy is when an object company has some solid growth opportunities that they would like to take advantage of but is slowed down by insufficient access to capital. One form of solving this problem is by merging with a company that has better access to capital but might not have the same opportunities to obtain benefits from the object company. These usually are the bases for acquisitions of small companies by larger bidders. (Gaughan, 2006).

History of the companies

Following is a thorough explanation of the background of each one of the large Mexican companies that has realized an important number of acquisitions and is the subject of this case study research.

CEMEX

Cemex was founded in 1906 with the opening of the Cementos Hidalgo plant in northern Mexico. In 1920 it started operations in the Cementos Portland Monterrey plant with a production capacity of 20,000 tons. In 1989 it became one of the 10 largest cement companies in the world when it bought Cementos Tolteca, the second largest cement producer in Mexico.

Cemex currently aspires to become, not the largest cement company in the world, but rather the most competent in all aspects. It is with this genuine business vision and a good attitude open to modernization that Cemex has positioned itself as one of the world leading organizations in the production and sale of cement and premixed concrete.

With careful cost control, planned investments and a decisive commitment to customer service, the company is achieving encouraging results to continue its investment program in strategic points in the business. In response to this vision Cemex has directed strategic planning towards the achievement of its goal: to become a highly competent multinational company.

Internationalization of Cemex

The evolution that the world economy has shown over the last few years clearly indicates that in this decade, participation and competitiveness in international markets will only be possible for those industrial groups that have a vision and initiative directed towards conquering the world that's in constant movement and evolution.

To facilitate the incorporation of new acquisitions into Cemex's work culture, with a highly efficient post merger integration process, that allows attainment of added value in any recently acquired company.

Following is a description of the international acquisitions realized by Cemex:

- In 1992 Cemex began its international expansion in the European market with the acquisition of Valenciana and Sanson, the two largest cement companies in Spain.
- In 1994 acquired the Vencemos in Venezuela.
- In 1994 acquired Cemento Bayano in Panama.
- In 1994 acquired Compañia Balcones in the USA.
- In 1995 acquired the Cementos Nacionales in the Dominican Republic.
- In 1996 acquired Cementos Diamante and Samper companies in Colombia.
- In 1997 acquired Rizal Cement in the Philippines.
- In 1999 acquired APO Cement in the Philippines.
- In 1999 acquired Assiut Cement Company in Egypt.

- In 1999 acquired Cementos del Pacifico in Costa Rica.
- In 2000 acquired Southdown Inc., in the USA.
- In 2001 acquired Saraburi Cement Company in Thailand.
- In 2002 acquired Puerto Rican Cement Company in Puerto Rico.
- In 2005 Cemex doubled its size with the acquisition of RMC in the UK, accounting for operations in 20 additional countries, mainly in Europe.
- In 2007 acquired Rinker in Australia, a key piece in Cemex's strategy. It was among the top 10 producers in the world of heavy construction materials and had an active presence in the American market, especially in regions with growing population like Florida, Arizona and Nevada.

Source: Cemex

FEMSA (Brewery)

Founded in 1890 in the city of Monterrey, it started operations with Cervecería Cuauhtemoc and expanded its activities up to becoming the largest integrated company in Latin America with operations in soft drinks, beer and convenience stores. The first brand to appear in the market was Carta Blanca and afterwards Saturno, a brand that was in the market for a short period and then disappeared.

In 1985 a new era was set in the Mexican beer industry with the historical merger of the Cuauhtemoc and Moctezuma breweries. This synergy allows offering the consumer more and better choices, besides maintaining leadership in the national market and reinforce competitiveness in the international marketplace, adding the prestigious XX Lager, Superior, Sol and Noche Buena brands to Cuauhtemoc, changing its name to Cervecería Cuauhtemoc Moctezuma, S. A. de C. V.

In 2004 FEMSA repurchased 30% of its shares. This operation prepared FEMSA Cerveza to take control of importation, marketing and distribution of its brands in the United States, while at the same time allowing it to explore alternative strategies for this market. In the third week of June a commercial agreement with Heineken was signed to sell their brands of beer in the United States. In accordance with the terms and conditions of the agreement, Heineken USA assumed responsibility for the promotion, sales and distribution of the Tecate, Dos Equis, Sol, Carta Blanca and Bohemia beers across the American territory beginning January 1, 2005. Cervecería Cuauhtemoc Moctezuma and Coors Brewing Company announced a 10-year agreement, which made the brewery the only and exclusive seller of Coors Light in Mexico. In this agreement both parties capitalized a business opportunity that complemented their principal strategies.

On January 13, 2006 FEMSA Cerveza acquired the control of Brazilian brewery Kaiser by buying 68% of their shares for a total of 68 million dollars. Now it is named FEMSA Cerveza Brasil. With one of the most complete portfolios in the market, FEMSA Cerveza Brasil has the joint distribution of System Coca Cola and was the first company in Brazil in its field that printed a customer attention phone number on the labels of its products. FEMSA is now the only company with brewery operations in two of the most attractive markets in the world: Mexico and Brazil.
Source: FEMSA

GRUMA, S. A. B. de C. V.

GRUMA was founded in 1949 in the State of Nuevo Leon and is mainly dedicated to the production, marketing, distribution and sales of tortilla, corn flour and wheat flour. With leading brands in the majority of its markets, GRUMA operates in the United States, Europe, Mexico, Central America, Venezuela, Australia and China, and exports to over 50 countries around the world. The company has its corporate offices in Monterrey, Mexico and has around 17,000 employees and 88 plants.

Gruma Corporation is one of the main producers and commercializes of tortilla and corn flour in the United States. Gruma Corporation also has corn flour and tortilla operations in Europe and tortilla operations in Australia. Through its tortilla subsidiary Mission Foods (with 19 plants in the United States, 2 in the United Kingdom, 1 in Holland, 2 in Australia and 1 in China) and its corn flour subsidiary Azteca Milling (with 6 plants in the United States and 1 in Europe), Gruma Corporation services industrial, retail and institutional clients. Its principal brands are Misión and Guerrero for tortillas and Maseca for corn flour.

In Venezuela the GRUMA, MONACA and DEMASECA subsidiaries have 14 plants that produce and distribute corn flour and wheat flour, as well as rice, oats and other products. These companies service industrial clients and retailers with the brand Juana for corn flour and Robin Hood for wheat flour, among others.

Gruma Centroamérica has 11 plants located in Central America from where it supplies industrial clients and retailers in Guatemala, El Salvador, Honduras, Nicaragua and Costa Rica. Gruma Centroamérica produces corn flour and, in a minor scale, tortillas and snacks. Besides that, it grows and sells palm heart and processes and sells rice. Its chief brands are Maseca for corn flour, Torti Rica and Misión for tortillas.

With the idea in mind to facilitate manual production of corn tortillas, in essence they are doing research to find an answer to the problem of conservation of the tortilla dough, seeing as in a few hours the dough becomes inadequate for human consumption due to the speed with which rotting begins.

In the early 1970s, GRUMA entered into the Costa Rican market. In 1976 it arrived in the United States having achieved since then sustained growth in sales which has allowed them to become the world leader in the production of tortillas and corn flour.

In 1987 GRUMA expanded its operations south of the Mexican border, setting up plants in Honduras in 1987 and in El Salvador and Guatemala in 1993. In 1994 it started operations in Venezuela.

In 1999 it started construction of their first tortilla plant in Europe, located in Coventry, England. Currently they have three more plants, strategically located in England, Italy and Holland.

In the Australian region they have two production plants since 2005. In 2006 GRUMA started operations in Asia with a plant in Shangai, China besides acquiring in Australia the affiliates of Rosita Investments and Oz-Mex Foods and in England they acquired the affiliate Pride Valley Foods. Currently from the plants located in Australia and China they export products to several countries such as New Zealand, South Africa, Japan, South Korea, Singapore and Indonesia.

Source: GRUMA

NEMAK

Nemak, founded in 1979 in the state of Nuevo Leon, is a company committed to satisfying the needs of the global automotive industry with the fabrication of high quality aluminum components. It has the commitment of being a high technology, cost reduction, total quality and an on time delivery company. As a consequence of these elements it has leadership in the global market of the automotive industry, while maximizing profits for the shareholders.

It has experienced high growth and this has positioned them to be one of the leading companies in the automotive industry. This was clearly manifested with the expansion of production lines and its global presence with the incorporation of the Rautenbach, Hydro, Teksid and Castech companies in recent years. With 29 manufacturing plants located in 13 countries in North America, South America, Europe and Asia, they are prepared to service the high world demand.

As a leader in the industry, the experience that Nemak has in technology, cost reduction and high quality products enables Nemak to manufacture products with aluminum components of top technology.
Source: NEMAK

Research design

For this research, a questionnaire was prepared that would measure the variables of the hypothesis and interviews were conducted with the top executives that have been involved in the decision making and international acquisitions that CEMEX, NEMAK, GRUMA and FEMSA have made.

The above companies were chosen because they are leaders in their different industrial sectors. CEMEX in the cement industry has 67 plants and in premixed concrete 2,365 plants and approximately 55,000 employees. GRUMA in the production, marketing, distribution and sales of tortilla, corn flour and wheat flour industry, has 88 plants and about 17,000 employees. FEMSA in the beer industry has 14 plants and approximately 2,625 employees and NEMAK in the automotive industry has 29 plants and about 15,000 employees.

Results

This article presents the qualitative results of these interviews based on the analysis of the responses to the questions made and are presented as follows.

Interviews to top corporate executives of Nuevo Leon that have been involved in the acquisitions of foreign affiliates

Four interviews were conducted with the top corporate executives that were involved in the process of acquisitions of foreign affiliates of CEMEX, NEMAK, FEMSA and GRUMA. Afterwards, results were presented of what the executives revealed as being important factors during and after having realized the acquisition process.

A) CEMEX

Based on the interview, it can be determined that before effecting the change of strategy at Cemex, they had two main objectives, which are:

1) Generation of revenues (cash flow)
2) Be in businesses counter cyclic to construction, Cemex owned shares in the mining, tourism and secondary petrochemical sectors.

Between 1989 and 1990 they analyzed all the main global cement and concrete markets and competitors and discovered that the big competitors had twice the production capacity of Cemex. These also had the advantage of being diversified in different countries compared to Cemex that was only present in Mexico.

Cemex saw the need to make a change because they did not want to fall into the hands of the international competitors and run the risk by being bought out. They then saw themselves in the need to go overseas and begin to apply the strategy of acquiring international companies in order to start having a diversified geography and begin to have more production capacity.

a) Factors that Cemex took into account to develop the strategy for international acquisitions.

1. First off, they saw the need to start buying international companies. This was because they wanted to start growing their cement production capacity and diversification in the market. Cemex saw that if they wanted to shorten the distances between their main competitors, it was necessary to begin acquiring foreign affiliates.
2. Maximize the probability of success in the acquisition of foreign affiliates. They wanted to buy affiliates of foreign companies that were culturally similar to the Mexican culture. They also wanted markets similar to Mexico's being that Cemex had great experience and was the leader in Mexico.
3. They wanted to start acquiring affiliates in markets where Cemex could defend itself from international competitors, in countries where these would have little presence and in which Cemex wanted to invest.
4. In Spain they acquired the first foreign affiliates (Valenciana de Cementos and Sanson). Cemex decided to go for Spain because culturally speaking there was a similarity with Mexico. The two affiliates were chosen because together they accounted for over 50% of the Spanish market.
5. The speed at which Cemex could implement the integration of the acquired affiliate overseas to Cemex's corporate culture (creation of synergies) was very important. This was in order to start as soon as possible to justify the investment and see the results of the acquired affiliate. For this purpose Cemex decided to send to Spain the best executives to facilitate the acquisition process.

b) <u>To be able to create successful synergies Cemex has taken the following steps.</u>

1. Knowledge that Cemex has on the companies that are targeted for acquisition. Cemex has a team that researches its competitors and they anticipate or detect the strategies that competitors are implementing. This same team recommends which companies Cemex should attempt to acquire based on an analysis that the team provides to management.
2. Applying what Cemex calls PMI that means Post Merger Integration project. (Cemex has a team of executives that are well trained in

the processes of integration). After realizing the acquisition of an affiliate, different teams in Cemex travel to the foreign affiliate to begin the integration, for the administrative system SAP R/3 as well as for implementation of methodology and corporate culture of Cemex.

3. Identify employees of the acquired company that have the potential to remain with Cemex, changing their corporate culture for Cemex's culture. This is achieved after the PMI team arrives to the affiliate, makes an analysis of the personnel on board and then makes a recommendation as to which employees should be retained. After this phase they begin to train the employees that Cemex retains, with the methodology and procedures that will be used in within the Cemex corporate culture.

c) Critical factors that Cemex observed in the international acquisitions that have been realized.

1. Presence in international markets. Before 1992 Cemex had no presence overseas and saw the need to be present in different countries, especially being near its competitors.
2. Cost of capital (due to the Mexican economy at the time and for only having presence in Mexico). One of important factors was to also want to take advantage of economies of scale and also benefit from cost reductions in logistics. Before having made any foreign acquisitions Cemex had to export products to different countries. Upon realizing acquisitions and creating synergies they could save large amounts in logistics matters.
3. Knowledge of the culture. Before proceeding with an acquisition Cemex researched the culture of the country in which they wanted to invest, in order to face the least possible problems.
4. Speed at which Cemex could realize an acquisition, creating the synergies needed with the acquired companies. This is important in order to make the company more efficient and produce favorable results more rapidly.
5. Implementation of administrative systems (in the companies that have been acquired). Unpon buying a company, Cemex

implemented its own administrative system in order to have better management and control of all productive plants.

6. Implementation of the Cemex corporate culture. In the companies acquired by Cemex, the PMI team carried out its role of implementing work methodologies of Cemex.
7. Logistics (minimize transportation costs). Another very important point is to take advantage of the logistic lines that Cemex has, whether they be marine or land, with railroad hopper cars they have, besides their fleet of mixing trucks. Furthermore, each time an acquisition is made, Cemex can redefine which location is more convenient to export or move cement from, taking into account the affiliate that represents the lowest cost for shipping the product.

B) NEMAK

Based on the interview conducted, it is confirmed that Nemak already had a leadership presence in North America. For that reason they decided to begin penetrating Europe which was an important marketplace because it has a large automotive industry. Since 2003 Nemak identified the need to acquire a European company since the company found it difficult to be present with some potential clients in Europe. In 2004 they made an investment under the strategy of self development in the Czech Republic. In 2006 Nemak was seeking to increase its penetration in Europe and start its presence in Asia and South America and so they acquired four plants in Europe from Giro Group. With this move they diversified the client portfolio and reduced the dependency they had with only north American clients.

a) <u>Factors to develop the strategy for international acquisitions.</u>

1. Greater presence in international markets. Nemak wants to have foreign affiliates in countries where it already has clients. With this they could take advantage of the distribution channels and of the market that the acquired affiliate already has.
2. Count on better technology when an international acquisition is made. If there is a process or method that an affiliate has which is more advanced or different to what Nemak uses, and that they

believe can generate value to Nemak, they will attempt to implement it across the organization.

3. Generate value through synergies. It is very important when Nemak acquires an affiliate overseas to integrate that affiliate as quickly as possible to the corporate culture in Nemak. Also important is to send integration teams that have experts in different areas of the organization to facilitate the acquired affiliates' integration processes with the corporate culture and work methods used in Nemak.

b) <u>Difficulties encountered in making an acquisition.</u>

1. Evaluate correctly the object company they want to acquire, meaning not acquiring an overvalued company. They have to carefully analyze financial statements, do an audit at the affiliate they want to buy to make sure the price set by the selling company is fair. They must also be sure that the selling company actually has the assets being sold.
2. The integration process of the acquired company with the culture and work methods of Nemak. On occasions a cultural shock may appear where the corporate culture of Nemak is very different to the corporate culture of the acquired company. Hence, after identifying the employees that will become part of Nemak, the different PMI (post merger integration) teams that Nemak has, have the mission of implementing the processes and methodology that are desired and needed to work with Nemak.
3. That the synergies being created truly create value for Nemak. In other words, it is also the responsibility of the PMI teams to detect that when implementing the administrative systems used in Nemak as well as the implementation of methodologies and work methods that Nemak uses, it is confirmed that they are truly creating value.

c) <u>To create synergies with the acquired companies, Nemak has taken the following steps.</u>

1. Well organized PMI (post merger integration). The company formed 16 teams to carry out different tasks in the integration process and they were also given three objectives:

a) Avoid destruction of business (Guarantee that in the integration process there is continuity of the business, in other words, insure it remains operating).
b) Identify synergies (Look for savings in the processes and had to identify in which processes costs could be reduced or use a technology that Nemak was already using.
c) Seek to work as one company (In other words, the acquired company is to work with the same technologies as Nemak, creating standardization of processes and changing to the corporate culture.

d) <u>Critical factors in international acquisitions.</u>

1. Seek to have more penetration in international markets. Nemak wants to become a leading company in the fabrication of aluminum motor parts. The fastest way to get penetration in the international market was to use the international acquisitions strategy.
2. Creation of value in the business. Nemak seeks, at the moment of buying an affiliate can contribute in the business. That is to say, after a financial and market analysis, Nemak makes the decision to acquire an affiliate.
3. Search for technologies. Nemak also wants to take advantage of superior technologies or knowledge of superior processes. If at the moment of making an acquisition the PMI team detects some technology which is superior to what Nemak uses, they attempt to implement it in all affiliates.
4. Identification of synergies. Nemak also with its PMI teams has the mission of identifying synergies that can be obtained with the acquisition.
5. Identify and calculate the value of the company they intend to buy. In this aspect, Nemak is also very careful before proceeding with any acquisition. They do a thorough analysis of financial statements and verify what assets the company they want to buy has.

6. Implementation of Nemak's corporate culture in the acquired company. The PMI teams implement in the various departments the corporate culture of Nemak. It is very important for them to implement as quickly as possible Nemak's work methods.

Source: NEMAK

C) GRUMA

In the interview, it was mentioned that Gruma is divided, from an operational point of view, into three divisions:

1. Gruma Latinamerica in componed by the following countries: Mexico, Costa Rica, Guatemala, Honduras, Nicaragua, El Salvador and Venezuela
2. Gruma United States and Europe
3. Gruma Asia and Australian Region

Gruma's line of business is formed by three different products which are: corn flour, wheat flour and production of tortillas.The corn flour unit have developed based on the organic growth strategy. The wheat flour unit has developed based on the growth by acquisition strategy and currently has acquired 10 plants. The tortilla business unit is divided into three different operations:

1. Prodisa (Operates with Misión brand, has two plants in the United States and used the organic growth strategy).
2. Casa del Maiz (Model which Gruma is developing, also with organic growth), in Cuernavaca, Mexico.
3. Circulo de industriales, which also used the organic growth strategy in Guadalajara, Mexico.

a) <u>Strategic objectives Gruma uses after having made an acquisition of a company, are as follows.</u>

1. First off, they take the product brands of the acquired company. They do this initially to allow time for the integration of the acquired affiliate in the methodologies and corporate culture of Gruma. Additionally, this gives them time to better know the behavior of the marketplace in the country where the affiliate was acquired.

2. They keep the client portfolio of the acquired company and try to hold on to the clients they have. Afterwards they attempt to gain more clients in the market.
3. After knowledge of the market, then follows the migration phase of their brands with the Gruma brands. Once integration has been executed, the next step is the unification of product brands and this when changes are made to the product brands.
4. They attempt to place value on the brands, (then the change is made with Gruma brands that are well positioned). By doing this, it makes the brands gain more value and consolidate in the international market.

The business model that Gruma uses after having made an acquisition is divided in the following points:

1. Implement the Gruma corporate culture (work methods, work procedures) in the acquired companies.
2. The administrative system that Gruma uses (SAP R/3) is also implemented in order to achieve better management and control of the business.
3. Insure that the acquired affiliates work with the same transparency as Gruma. Normally, the companies they acquire are not on the stock market where as Gruma is listed. Therefore these affiliates have to adapt to Gruma's form of working and with this all necessary regulations will be complied with.

b) <u>Critical factors that Gruma considers before proceeding with an international acquisition are:</u>

1. Positioning of the company brands. It is important for Gruma to see how well the brands or products of the object company are positioned before proceeding with the acquisition.
2. Potential market that Gruma could take hold of if acquiring a foreign affiliate.
3. Country culture. Gruma analyzes the country culture very well before making an acquisition. They want to know how the environment functions in countries where they plan to invest.
4. Creation of synergies. Gruma has as an objective, when an acquisition will be made, that the affiliate must generate synergies to

the knowledge that Gruma has, plus the sum of the acquired affiliate, may result in benefits for Gruma.

c) **<u>The elements that Gruma uses for the creation of synergies in the acquired plants are:</u>**
   1. Corporate systems team implements the administrative system SAP and telecommunications lines in the acquired companies.
   2. Gruma develops technology, builds machinery for production of tortilla, flour, etc. and even has the patents. Then, after proceeding with the acquisition they can improve or redesign the productive processes of the plants acquired by making improvements to their productive equipment.
   3. In the area of logistics, Gruma also has the know-how. They attempt to take advantage of the distribution units that the company has by distributing different products through the same units. In this way they obtain important reductions in transportation costs.

d) **<u>Difficulties that Gruma has encountered at the moment of realizing an acquisition:</u>**
   1. Changing the work culture that the employees had at the acquired affiliates work center and implementing the Gruma corporate culture.
   2. Having adequate communication with clients at the moment of transition of the acquired affiliate to Gruma so as to not lose clients.

Source: Gruma

D) FEMSA (Brewery)

In relation to FEMSA, it was pointed out that the company has had leadership and that a great part of their success is due to the fact that they can integrate their business vertically. They detected all the key businesses that are necessary to offer the end product, and decided to build a business with vertical strategy. That is to say, FEMSA developed a company to provide all necessities they have up to delivering the end product. For example, they invested in a company dedicated to the design and production of labels. In the beginning, they developed a company to make glass bottles and also developed a company that makes corrugated cardboard boxes because they had seen the need to transport and protect the safety of the bottles with beer. They also saw the need to create a company to produce bottle caps to substitute the cork on the bottles. Lastly, they created a company that would give them support in the distribution of beer, so in 2002 the FEMSA Logistics business unit was created.

In 2006 FEMSA acquired the Brazilian company Kaiser, which is a leading company in Brazil.

a) <u>Critical factors that FEMSA observed in the acquisition realized in Brazil.</u>

1. Penetration in international markets. FEMSA made the decision to buy this Brazilian upon analyzing the market they discovered that its behavior is similar to Mexico's market. Being that FEMSA is leader in Mexico, they have the knowledge to operate the business efficiently
2. Creation of synergies. It was very important for FEMSA when they bought the 8 plants from Kaiser Group that synergies could be created with the group, besides being able to benefit from distribution channels with other businesses they had in Brazil such as Jugos del Valle. This way they could benefit from certain distribution channels while reducing logistics costs.
3. Adaptation to the culture. It was also very important for FEMSA to avoid any cultural problem, so before proceeding, they studied both, the behavior of the corporate culture of Kaiser as well as the Brazilian culture. Adaptation to the FEMSA corporate culture was easy being that Kaiser was also the market leader in Brazil.
4. Transference of work methodology to the acquired affiliate. A very important point was to attain the Kaiser adaptation as rapidly as possible so executive teams were sent to make the transference of processes and methodologies. These people also implemented the administrative system that FEMSA Mexico was using. The important thing here was that 8 plants had to make the cultural changeover to the corporate culture FEMSA used.

Conclusions

It may be mentioned that after having completed the interviews with the CEMEX, FEMSA, GRUMA and NEMAK executives, the critical factors for realizing an international acquisition that these people mentioned, are the following:

- Creation of synergies
- Study the culture of the country where an acquisition is planned
- Speed in the integration of the affiliate acquired
- Implementation of the corporate culture to the acquired affiliate
- Implementation of the administrative systems in order to take control of the affiliate
- Presence in international markets
- Search for technologies in the acquired affiliates
- Have highly trained teams to execute the acquisition rapidly and successfully
- Not lose business at the moment the affiliate is being integrated

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