

Remarks by Lorenzo Zambrano, Chairman and CEO CEMEX Building the Future 2003

Good afternoon and welcome again to CEMEX's annual analyst and investor meeting.

My goal today is to give you a sense of the kind of environment we expect in the next months and years, to sketch out where CEMEX is going and how we are going to get there, and to identify some of the key concerns on the horizon. However, the most important part of this session will be your questions, which I will do my best to answer.

Let me start with my conclusions, and work backward:

- First, our business model is designed to produce good results in bad times, and great results in good times. And that model is performing.
- Second, we believe we are in the bottom of the business cycle in most of our key markets, with all of the pre-conditions in place for a cyclical upturn.
I do not anticipate a return anytime soon to the boom years of the nineties, but I am confident the next direction is up.
- Third, nevertheless, we have been working hard to enhance our business model, making the company more efficient, improving our production platform, and enhancing our customer focus. We are reaping the benefits of past investments in IT, diversification of energy sources, and transformation of our business processes. One result, as you will see, is that our cost structure is improving.
- Fourth, high market volatility demands a rock solid balance sheet, and this year we are devoting the bulk of our free cash flow to debt reduction.
- Finally, in a consolidating industry, we are preparing ourselves for future acquisitions, not only by strengthening our balance sheet, but also by improving our capacity to integrate new

acquisitions and building the flexibility and capacity of our management team. When opportunities come and when the market is right, we will be ready.

The easy thing would be to stop now and fill in the blanks in response to your questions. But let me give you some detail on each of these conclusions.

Good results in bad times, and great results in good times.

I am sure you would all agree with me that we have just witnessed a nasty macroeconomic correction to the bubble economy. Recession, war, terrorism, wild exchange rate movements, massive capital market volatility, accounting and governance scandals, the collapse of the dot-coms—and those were only the headlines.

But through it all, CEMEX has delivered. Between 1987 and 2002, our net sales grew by a compounded annual rate of 22% and our EBITDA grew by a compounded annual rate of 21%. We have grown through acquisitions and organically once we integrated those properties.

We have stitched different companies across five continents into a coherent, efficient platform to serve a wide variety of customers. And we have delivered the results to our shareholders.

Obviously, the curves flattened last year, as the global recession squeezed our markets, as exchange rates and interest rates fluctuated unpredictably, and as fear caused many markets to overreact and under perform. But, in a bad year, CEMEX still produced EBITDA of \$1.9 billion and free cash of almost \$950 million—at a time when many companies were happy simply to stay afloat. And, as you know from the guidance we have given, we expect similar performance this year, even as the global economy struggles to shake off the recession.

That is what I call good performance in bad times.

As I will explain in a moment, I believe we are close to a cyclical upturn. And, once that happens, I believe that we will once again demonstrate what it means to deliver great results in good times.

Last year I told you that I thought the U.S. economy would avoid the much feared double-dip and continue moving toward recovery.

In retrospect, I was more correct about the first half of that proposition: the U.S. recession has long been over, but the recovery has not quite caught hold. However, I am optimistic about the U.S. economy. Washington has finally put in place a full matrix of pro-growth policies. Of course, there are offsets like the weak fiscal condition of the states, but the balance is clearly positive. The result should be an upward economic push in the second half of this year and more so in 2004. Eventually, this will have a significant impact on construction demand and the demand for cement. In short, I believe we have almost seen the end of the bear market in construction.

What is good for the United States, at least in economic terms, is good for Mexico.

Until my country completes the reform agenda laid out by President Fox, the two economies will continue to move in lock step. In the meanwhile, the authorities are doing their part: fiscal accounts are healthy, inflation is low, interest rates have come down, capital inflows are strengthening, and banks have resumed lending to the private sector.

All of this has been good for the construction sector, which has rebounded dramatically this year after a particularly nasty fall in 2001 and 2002. Infrastructure spending by the public sector and public and private credit for housing construction—both important growth drivers for CEMEX—should continue to be strong into 2004. The bottom line is that Mexico is growing, more slowly than it could and should, but growing, nonetheless. However, if the politicians moved on energy and fiscal reform, the impact would be at least as powerful as NAFTA was a decade ago. I do not know when, but I am sure that sooner or later this will happen.

It is no accident that three-quarters of our EBITDA comes out of North America. These are growth markets, and we are well positioned to capitalize on that growth when it resumes.

I wish the rest of the world economy was as healthy. The main European economies, as well as Japan, need more stimulus and more economic reform. China is growing and parts of East and South Asia are recovering. With a few notable exceptions—Venezuela is one—Latin America seems to

have left the worst behind, although the region continues to face many challenges.

For CEMEX, this means that cement demand is growing this year in nine of our thirteen largest markets. Mexico and Spain are growing at a healthy pace, while Asia and parts of South America are stable. Demand is contracting in the United States and, of course, Venezuela.

On balance, that means that this year will be a transition year from recession to growth. I expect that next year will see the start of a new cyclical upturn. And CEMEX has prepared itself for that upturn.

Most of you are by now familiar with CEMEX's business model, but let me emphasize a few key points.

We spent the last ten years building a company designed to produce profitable growth. Our culture is a growth culture. Our financial strategies are designed to provide the resources to grow. Our management team has been chosen because of their capacity to seek out and to manage growth opportunities.

We have designed and installed company-wide processes and technological platforms that allow us to manage efficiently across dramatically different markets, to integrate new acquisitions quickly, and to enhance our managers' effectiveness.

We have invested in energy and technology systems that reduce our operating costs, reinforce our capacity to grow, and bring us closer to our customers. And we have built a global trading system that gives us a comparative advantage as we balance supply and demand across markets.

This model has allowed us to grow, organically and by acquisition. And, I am confident we will continue to grow.

If you analyze the past performance of the countries in which we operate, you will discover that our portfolio has the potential to grow sales 5% to 6% per year, excluding market share gains. In addition, assuming we continue to generate around \$1 billion per year in free cash, we would have the capacity to acquire operations that would conservatively add another 5% to 6% in top line growth.

Thus, when you think about where CEMEX is going over the next 5 years or so, you should think about a company that has the potential to grow 10% to 12%, on average and to do so with solid financial performance.

That is the top line; we all care at least as much about the bottom line. So we are using this period of economic stagnation and market volatility to reinforce our long run commitment to cost containment and efficiency.

In practice this has meant several things:

- It has meant completing the CEMEX Way, the introduction of common technological platforms and processes throughout the company.

We invested heavily in 2001 and 2002, and we are now seeing real savings—in costs and in head count—throughout the company.

More importantly, we are speaking a common language throughout our network that allows us to run our plants more efficiently, to manage logistics more effectively, and to drive down procurement and maintenance costs.

- It has meant implementing our energy strategy by securing energy supplies, minimizing energy price volatility, and optimizing global and regional energy costs to exploit synergies and economies of scale.

In Mexico alone, our fuel costs have been reduced to half of what they would have been if the conversion from fuel oil to pet coke had not been implemented.

- It has meant improving our productivity, reducing our head count, and bringing new leaders to the fore.

Since our headcount peaked last August, after the acquisition of Puerto Rican Cement, we have reduced it by more than 1,700, or 6%.

Some of that reduction reflects right sizing in Puerto Rico and in the United States; some reflects a reshaping of our Venezuela operations; and some reflects my belief that any manager can always do more with less, if he is pushed hard enough.

Cost containment is a religion at CEMEX. I know that some of you may have doubted that over the past two years, as you saw our expenses rising. But, as my colleagues have explained, a considerable portion of those expenses were, in a very real sense, investments in our future. And we are seeing the pay-offs today.

Let me give you an example. Energy, of course, is one of our largest variable costs and one of our most significant inputs. We need reliable access at the lowest possible cost to a commodity that is inherently volatile. To achieve this, we decided to diversify our fuel structure, develop key projects—including our own power plant in Mexico—optimize energy supplies in new acquisitions, and develop new energy saving technologies.

None of this is cheap, but all of it is productive.

For example, in Mexico we have invested \$160 million in our plants over the past decade to give us the flexibility to use pet coke—the price of which has been lower and less volatile than either fuel oil or natural gas at least since the mid 1980s. Today, 90% of the fuel we use in Mexico is pet coke and we have already accumulated savings that exceed our investment.

This story, on different scales, is being repeated throughout our network.

One of the key results of these and other initiatives is that we are experiencing a significant reduction in our cost structure.

- By mid 2003, corporate overhead—including investments in CEMEX Way and other institutional projects—was reduced by around \$40 million. I think the reduction will be even greater by the end of the year, exceeding \$100 million.
- During the first half of the year, the ratio of SG&A to sales fell by 150 basis points. We contained costs and increased sales. We expect this trend to continue in the second half.
- During the same period, headcount was reduced by about 1,000, as part of the sharp reduction that began last August.

These are *not* one time savings—emergency cuts put in place because markets turned sour. They represent the results of long term strategies that

focus on maintaining CEMEX as the most cost efficient and most profitable company among our global competitors.

I said a few moments ago that I am confident the next direction for the U.S. economy will be up, even if it is taking longer than any of us would like to achieve lift-off velocity. Let me tell you now that I have equal confidence in the future of CEMEX's U.S. Operations: the next phase in our evolution will clearly be positive.

Why am I confident?

- First, I think we have the right people managing the company. You heard a detailed report this morning from Gilberto Perez. Gilberto and his team understand the market, have successfully integrated CEMEX's business processes and platforms, have renewed our plant management, have initiated important customer focused programs, and have made dramatic changes in our production and distribution platform.
- Second, there can be no doubt our timing was not great: we bought Southdown just as the economic bubble was bursting. In a perfect world, we might have waited, looking for a different U.S. opportunity.

But we are long term investors in our industry, not traders. That meant we took the full brunt of the recession, of the California energy crisis, and of the dramatic shift in the fiscal positions of the states.

All of that took a toll on our short term performance, but most of that—hopefully—is in the past.

- Third, the positive side of the coin is that the severe environment forced us to transform the company even faster, so we are well prepared for the economic recovery when it comes. Frankly, we were a bit surprised at how much work needed to be done to bring Southdown's operations up to CEMEX's standards. But I think we are almost there.

I know that many of you have been critical of the performance of our U.S. Operations over the past two years, and are a bit skeptical of the future. I

share your criticism, but not your skepticism. I believe we will have a much more positive story to share with you when we meet next summer.

As part of our effort to refine and refocus our business model, we have been working hard to enhance our understanding of our customers. We need to offer our customers the products and services they want—when and where they want them—and to assure that our customers have a positive experience every time they deal with CEMEX.

We know that our future success will be measured not by the number of tons of cement we produce, but by the satisfaction of our customers. We need to help them complete their projects, on time and on budget.

We need to sell integrated solutions to our distribution channels and to our final customers, not simply more products. This means packaging our products with tailored logistics solutions, offering ways of interacting with us—wired, wireless, and anything in between—providing training and project management support to customers, and so on.

To accomplish this we need to build a culture in which commitment to customer is paramount. And that is what we are doing:

- You heard earlier today about our initiatives in Mexico, the United States, and Spain.
- Tomorrow, you will hear a presentation on Egypt where we took a very sophisticated marketing approach—the same way a Procter & Gamble or any other marketing driven company would enter a new market—and it is paying off.
- In a number of our markets, we have developed customer oriented call centers and e-selling portals that provide new services to customers at their convenience, 24/7. As a result, for example, last month one-third of our Mexico volume and almost one-quarter of our volume in Venezuela and Colombia were sold online.

We have told you about Construrama and Arkio in Mexico, so I will not take time to cover old ground. But I will make two points about those initiatives:

- Both are designed to provide our customers with the products and services they need for their projects, not just with cement. This is not about broadening our product offerings. It is about satisfying our customers and building brand loyalty in our distribution channels.
- Both have potential application in other markets, including markets where we do not have production facilities.

The bottom line is that, when it comes to customers, CEMEX delivers.

Let me turn now to our financial condition.

We understand quite clearly that the market wants us to have sound, conservatively managed financials, since excess leverage would limit our capacity to grow. We understand that the market wants us to manage risk, for the company as a whole. We understand that the market wants us to have transparent financial reports and a less complex capital structure.

So do we. Not just to keep our investors and our analysts happy, but to provide the financial flexibility and strength to sustain our future growth. That of course, will be the real future source of happiness for all of us.

Where are we today?

- We are in the process of reducing net debt to EBITDA from 3.2 in December towards our target of 2.7. We will use at least two-thirds of our free cash flow this year to reduce net debt. Given the volatility of exchange rates, I do not want to forecast specific debt levels, but I will forecast the direction: down!
- We are maintaining a strong interest coverage ratio at close to 5 times for most of this year.
- We have significantly reduced the potential volatility of our interest costs, and taken good advantage of historically low interest rates. We have rebalanced our debt portfolio, to a point where 70% of our debt is fixed and 30% is floating. This will allow us to continue to benefit from low rates for some time.

- We have sustained—and we *will* sustain—our investment grade ratings.

At the same time, we have had to recognize mark-to-market losses on the valuation of our derivative positions through March of this year. I want to be clear about two key points.

- First, CEMEX uses derivatives to manage the risks inherent in an operating portfolio that spans more than 30 countries, just like any multinational which has revenues, expenses, and debt in multiple currencies. Our purpose is to produce cement, not to try to time money markets.
- Second, a substantial portion of the non-cash, mark-to-market losses we have recognized on our derivative positions will be reversed as time passes and markets move back toward more normal patterns. In fact, during the second quarter of this year, we will recognize around \$300 million mark-to-market gains in the valuation of our derivative positions. Indeed, over a longer time period than any given quarter, I am confident that the financial strategy we have been following will prove itself.

The underlying point is simple, but quite important. At CEMEX solid financial management and enterprise-wide risk management are critical elements of our business model. A successful, profitable growth company needs both financial strength and financial flexibility. That strength is why we could buy Southdown three years ago, and why we will be in position to make our next acquisition when the time is right. The point is that we never enter a financial transaction for the sake of the transaction itself: we are not in the banking business.

However, financial strength and flexibility are not enough to sustain growth.

We have told you not to expect significant new acquisitions for the time being, although we may undertake bolt-on acquisitions in key markets. Meanwhile, we *are* preparing ourselves for future acquisitions. For this, two factors are critical: our capacity to integrate acquisitions quickly and efficiently, and the flexibility and capacity of our management team.

For CEMEX, a world class integration process is one of the keys to our successful growth. Since 1987 we have made seventeen significant acquisitions, and our integration process has become steadily more effective. When we acquired Valenciana in 1992, the core integration effort took almost two years. When we acquired Southdown in 2000, the core integration took four months. And when we acquired Puerto Rican Cement Company last year, the core integration of systems and procedures took only 2 months, in large part because of the CEMEX Way.

The real measure of integration, of course, is not speed but the ability to extract value and serve customers. And Puerto Rican Cement is a good case study.

We closed on the acquisition last August. Our Post Merger Integration team identified savings opportunities of around \$14 million throughout the company. By the end of December, 90% of those identified savings—\$12.5 million—had been realized on an annualized basis. A company that produced \$23 million in EBITDA in 2001 is now on path to produce \$35 million in 2003 with roughly the same volume of sales.

This is not an unusual example; Puerto Rican Cement was a well run company with significant market share in a competitive market environment. What we are doing in Puerto Rico we can do elsewhere. Each of our PMI's are learning processes that contribute, in turn, to our ability to integrate and quickly realize value from the next acquisition—wherever and whenever it might be.

No company is better than its people, and CEMEX is no exception. I believe we have an exceptional management team, many of whom are with us today. I hope you take full advantage of this meeting to get to know them better because that is the only way you will understand the potential of CEMEX.

As some of you know, we initiated our first voluntary retirement program earlier this year. 214 employees took advantage of the program. For CEMEX this was a bittersweet experience. On the one hand, it gave us the opportunity to renew management in a number of key operating positions throughout our system. New people bring new ideas, take new risks, see new opportunities.

On the other hand, initiating such a program meant that our company was losing some experienced colleagues who have contributed importantly to CEMEX's growth over the past decade. The balance, I believe, was positive.

I hope my presentation this afternoon has given you a solid sense of where I think CEMEX is today and, more importantly, of where we are going. Our goal is to be the most profitable global cement company, with the best customer service, and the highest reputation for quality and creativity in the industry.

We have come a long way over the last ten years, but we still have a long way to go. Many of you will remember the disaster that struck Mexico and CEMEX in 1994 and 1995. We met that challenge and, today, we are a different company.

Thank goodness, we still have challenges, but, thank goodness, they are different challenges. I am confident we will meet those challenges as well, and we—in the process— will again transform ourselves into a different company. I hope you all plan to come along for the ride, because I am sure it will be interesting and, more importantly, profitable.

Thank you for your attention and now I welcome your questions.