Financial markets driving change at company level: Cembre S.p.A.

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This case study is available in electronic format only.
**About Cembre**

Cembre S.p.A. is a leading European manufacturer of electrical connectors and related installation tools, railway products, cable glands and terminal blocks. The Group focuses on supplying products to wholesalers selling electrical goods, to energy distributors and railway companies. Since its creation, the company has pursued an aggressive growth strategy focusing on: constant improvement of their products; experimentation of new materials; international expansion; entering into complementary market segments; and acquiring and integrating companies with complementary skills and products. This strategy has proved very successful in terms of turnover growth and profits.

Cembre was created in 1969 and grew quickly as a company specialising in the manufacture of electrical compression connectors and related installation tools. In 1986, the company opened its second manufacturing plant in Birmingham, United Kingdom. Since 1992, the quality of the Cembre products has been certified by the Lloyd’s Register Quality Assurance for design and manufacture of accessories for cables, electrical connectors and associated tools.

As a manufacturer of electrical connectors, Cembre developed and adopted a ‘compression’ system exploiting the hardening properties of metals such as copper and aluminium in order to gain improved connector performance. In comparison with conventional welding and mechanical clamping connection methods, these electrical ‘compression’ connectors possess a lower resistance and, thus, provide a higher quality electrical contact.

To ensure a safe and reliable installation of such electrical connectors, Cembre designs and manufactures installation tools for compressing and cutting. A wide range of tools is available based on various mechanisms, including mechanical, pneumatic, hydraulic or electric functioning.

Cembre has also introduced new products for railways and began producing cable glands and terminal blocks in 2002. Recent product developments include the Zeta terminal and distribution blocks, Maxiblock cable glands and Secureclip conduit fixings and fittings. In addition to the standard range of products, Cembre’s UK manufacturing facilities also offer the design and production of customised termination products and cable.

**Key financial facts and figures**

Over the past 20 years, Cembre’s turnover has risen steadily, with an average annual growth rate of 15.4% for the period 1983-2000.

Figure 1: Cembre Group turnover, 1983-2000

![Figure 1](insert-image-url)
Cembre S.p.A.

Cembre became a public company on 15 December 1997, with a listing on the Italian stock exchange in Milan. In 1999, Cembre Group acquired Oelma Srl, an Italian electrical goods company. The merger allowed Cembre to widen its product range and deepen its commercial network; Oelma Srl was fully merged with the Cembre Group in January 2002. Cembre employs a 417 strong workforce, and realised revenues of €56 million from sales and services for 2001.

Figure two provides an overview of the group’s capital structure as illustrated in UBM Equity research. Production is centralised in Italy and the UK and some smaller distribution centres in key European countries. Cembre’s operations in the United States (US) are relatively recent, and the group focuses on railway products in this market.

Figure 2: Corporate structure of the Cembre Group

![Corporate structure of the Cembre Group](image)

Source: UBM, 2001

Figure three clearly illustrates Cembre’s robustness against the downturn in the overall worldwide connectors market. In 2001, sales experienced an 11.1% increase 2000 and the figures for the first half of 2002 suggest that the group is on target to at least match its sales for 2001.

Figure 3: Sales and earnings before interest and tax (Ebit), 1997-2002

![Sales and earnings before interest and tax (Ebit), 1997-2002](image)

Source: Cembre half year financial report, 2002

Figure four shows the company’s turnover according to product type. Most of the turnover results from the company’s traditional markets in connectors and tools, although the contribution of railway products is increasingly important.

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1 UniCredit Banca Mobiliare (UBM), UBM Equity research Cembre outperformer, 29 October 2001.
Cembre specialises in supplying electrical goods to wholesalers. Some of the wholesalers serve the public sector. Thus, the figures in the chart below may understate the percentage of turnover attributable to the public sector market.

Figure 5: Turnover by output market in 2001

Source: UBM Equity research, 2001

Figure six clearly shows that Cembre is mainly a provider to the European market, with non-European sales accounting for just 8% of the total. Cembre’s non-EU operations, such as those in the US, are in their early stages of development, although expansion into overseas markets is one of the company’s key strategic goals in moving forward.
Company strategy

Cembre Group’s current strategy is based on an investment programme enabling the company to:

- **extend the product range:** Cembre has focused its R&D efforts on those markets which promise a great growth potential, notably rail transport, and civil and industrial plant engineering. Following the adoption of new safety regulations in the European Union, these markets will most likely increase their demand for Cembre’s products.

- **focus on the railway industry:** Cembre sees a significant growth potential in supplying the European railway industry with its products. This would result from proposals for investing in the railway infrastructure in several European countries.
• **optimise manufacturing facilities:** Cembre continuously improves the manufacturing process at its Brescia and Birmingham plants. Recent improvements include new units for chemical and mechanical processes at the Brescia plant as well as the acquisition of a new building at the Birmingham facility. Cembre has further improved its operational efficiency in recent years by adopting software solutions to manage production, sales, stock, purchasing and dispatch.

• **consolidate the Group’s commercial and distribution network:** Cembre continues to consolidate and strengthen its commercial and distribution network, by placing a particular emphasis on international expansion.

• **develop online capability:** After launching its company website over two years ago, Cembre has developed an online sales capacity in order to achieve its objective of developing a greater presence in the market.

### Sectoral context

Cembre’s strategy appears to be well placed in the context of the sector. The overall market for electrical connectors grew strongly in 2000, both in Europe and in the rest of the world. The worldwide market achieved 18.1% growth in 2000 over the previous year. The US market, the largest one for connectors, achieved an even higher growth rate of 20.4%, while Europe, the second largest market, grew by 13.4%.

This growth rate has slowed significantly since the third quarter of 2001 as a result of the general economic slowdown. Growth was particularly hard hit in those sub-sectors providing connectors to the information technology (IT) and telecommunications sectors, which represent 45.3% of the total market for connectors, according to the analyst report established by Cembre in February 2002. Nevertheless, since Cembre also specialised in the sub-sector for power connectors and terminal blocks, the company was less exposed to the downturn in the IT sector than it might have been.

### The role of financial markets as a driver of change

**Views of management and key shareholders**

Cembre’s management is of the opinion that financial markets, and in particular the stock market, have had an important role in sustaining Cembre’s growth. The IPO generated approximately €14 million, which was invested in funding the company’s growth strategy, centred on launching new products, the acquisition of businesses with synergic products, and the experimentation and testing of new materials. However, a low interest rate environment and a perceived low valuation of the stock led the company to fund its subsequent investments through bank loans. Cembre displays the features of a healthy firm, not facing credit constraints and having easy access to bank and equity financing. Equity financing is perceived as being generally cheaper than bond and bank finance.

Cembre’s management believes that financial markets have led to profound changes in the governance of the firm. This is primarily because the STAR division of the Italian stock exchange requires companies to meet more stringent conditions than other divisions of the market in terms of transparency, information disclosure, composition of the board, etc. This includes, among other issues, the necessity to appoint at least two independent board members. Furthermore, the company has to produce six reports per year (four quarterly, one every six months and one annually). These requirements can sometimes be viewed as excessively onerous for a small company.

2 [www.cembre.it](http://www.cembre.it)

3 STAR is the segment of the Electronic Equity Market (Mercato Telematico Azionario-MTA), organised and managed by Borsa Italiana, reserved for small and medium capitalisation companies who are operating successfully in the traditional sectors of the economy and meeting stricter and more specific requirements with respect to transparency, liquidity and corporate governance.
For Cembre’s management, financial markets have also been an important driver of change for internal organisation. The company has to satisfy standards in terms of information disclosure and transparency, which requires, for example, an investor relationships’ team to provide accurate information on a timely basis.

Cembre’s management maintains that financial markets have not led to profound changes in their remuneration policies and relationships with stakeholders, nor have they affected the firm’s strategies and growth plans. There is no evidence of giving priority to short-term objectives as opposed to medium and long-term ones, despite the fact that the market desires ‘good’ figures.

Moreover, financial markets seem not to have influenced the choice of plant location and production made by the firm. These decisions, including R&D investment and management style, have been unaffected by the liberalisation of the financial markets. The location of plants has always depended upon logistics, production and the optimisation of the distribution network. The production process is essentially exogenous and driven by technological factors. Thus, it is largely independent of the dynamics in financial markets. Product choices have always been made on expected margins and prospects, while undertaking substantial amounts of R&D investment has always been the cornerstone of the company.

Conclusions

Cembre’s management considers that the emergence of a stock market for smaller companies greatly expanded their financing range. The proceeds of the company’s IPO helped sustain the company’s growth strategy. In response to the listing requirements, the governance of the company changed. The listing enabled organisational changes since new standards in terms of transparency and information disclosure requirements had to be met. These changes are viewed as having significantly improved management control. Nevertheless, the listing on the stock market did not lead the company to abandon its long-term strategic focus.