Case Study on Caterpillar

An evaluation of the current and future potential of Caterpillar

**Steve Braciszewski, Brennen Humphrey Ken Loos,
Joanna Martyn, Mabel Oza, Mantas Stankevicius**
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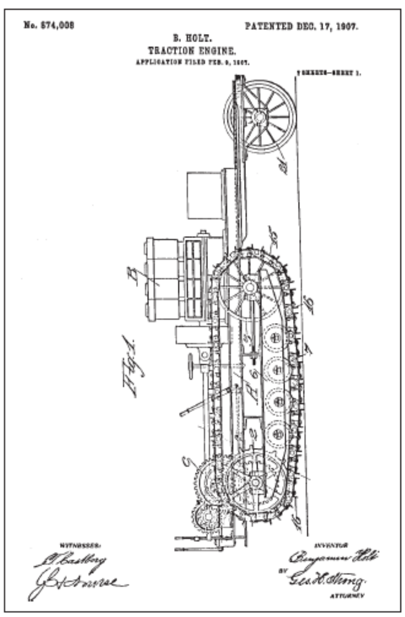
This case analysis will provide a short financial analysis to assess the company's health, a complete analysis of the firm, and a recommended strategy based on the results.

Contents

History

Today

Caterpillar is a global leader in helping countries worldwide build their infrastructure. As world leaders of mining and construction equipment, diesel and natural gas engines, and industrial gas turbines, they have continued to cultivate and advance our global society's standard of living. Indirectly, their accomplishments have helped our country build a prominent reputation in industrializing and capitalizing developing countries. This claim is supported by their 80 years of dedication as a prominent U.S.A. company, with over 67% of its revenue being generated from foreign countries (cat.com). The biggest reason behind their foreign dominance is their rich history with the U.S. and British military, the most powerful military forces in the world.



Holt's original track-laying patent

Origins

In 1864, sometime around the great Gold Rush, three brothers, Charles, William, and Ames Holt left their hometown Concord, New Hampshire to embark on their dreams in San Francisco. Coming from fairly strong entrepreneurial parents, who owned sawmill that processed hardwoods for wagon construction, the three brothers found their gold in their business, C.H. Holt and Co. C.H. Holt and Co., primarily dealt with hardwood, lumber, and wagon materials, in creating structural applications. They synergized with their parents business by getting hardwood shipped from their hometown. As the business developed and specialized the Holt brothers renamed the company Stockton Wheel Co.

Once the Stockton Wheel Company, established, the baby of the family, Benjamin Holt moved to California to manage their company. As more gold rushers abandoned their gold pursuit to become farmers, predominantly wheat farmers, the Holt brothers expanded into manufacturing farming equipment. Benjamin the most meticulous and technical brother built a steam powered tractor, this was the first tractor that did not rely on horses. The magnitude of the popularity was tremendous, due to the tractor's power to harvest an entire field for only one sixth of cost of horse-drawn combines.

Despite his tractor's success Benjamin noticed that his tractors were so heavy that they were getting stuck in soft fertile soil. To fix this problem Holt tried to use larger wheels, about 7.5 inches in diameter and 6 inches wide, to better spread out the tension. This solved the problem but made the tractor too bulky to maneuver in the field. So after 100 miserably failed patents he found his breakthrough by replacing the wheels of No. 77 with a set of wooden tracks bolted to chains. Holt described the tractor as "platform wheel engine." On 1904 when Holt tested his tractor, Charles Clemens, company photographer noticed that his tractor crawled like a caterpillar. Benjamin replied, "Caterpillar it is. That's the name for it! (Tech Direction)"

WWI and WWII

Originally Holt bought the caterpillar tracks from a British company called Hornsby. Prior to Hornsby selling his tracks to Holt, Hornsby demonstrated his idea to the British military (Duffy)[1]. Even though the British military was marveled by the concept and awarded Hornsby they didn’t use the idea. The concept was later demonstrated in the first film made for a commercial (The World's First Caterpillar Track). Despite their exposure the marketing campaign was not well implemented to generate sales[1]. In 1914 they sold the track patents to Holt Manufacturing Company for only $8000 (Haddock and Orlemann). A couple of months later the British and French military decided to use caterpillar to haul goods. Colonel Swinton was so amazed with the durability of these machines that he, as well as, Winston Churchill, convinced the British government to use it as tanks. The tractor-bulldozer was so useful that Admiral William F. "Bull" Halsey said, "The four machines that won the war in the Pacific were the submarine, radar, the airplane and the tractor-bulldozer (Tech Direction)." Later in WWII, 1950, Caterpillar Tractor established itself in Great Britain, this marked the beginning of overseas operations created to help manage foreign exchange shortages, tariffs, and import controls. This initiation helped Caterpillar build a strong rapport with the U.S.A.’s and Britain’s military (Hoffman).

Post-War

World War I became a huge component of Caterpillar’s business that most of Caterpillar’s revenue relied on military contracts. So when the war ended a huge part of Caterpillar was put on hold. They had excessive military equipment, outstanding debts, and to top it off, Benjamin Holt died at the age of 71 years. After Holt’s death the bank pressured the board of directors to accept Thomas A. Baxter, a Boston banker who joined in 1913 as a business manager, as Holt’s successor. Five years later C.L. Best Tractor Co. acquired Holt Manufacturing Company. C.L (Tech Direction). Best was financially stable while Caterpillar was well known. Since they turned their focus on the agricultural market their eliminated several equipments and kept the 2 Ton, 5 Ton, 10 Ton, Caterpillar 30, Caterpillar 60 (Hoffman). When the Second World War started the company was better prepared for the end of the war, and had a well planned transition plan between war time and peace time. After the war Caterpillar and Mitsubishi Heavy Industries Ltd. created the first U.S. firm joint ventures in Japan.

Recession

In 1981-1983 the worldwide recession took place, victimizing Caterpillar by $1 million a day and forcing it to dramatically reduce employment. To survive the recession Caterpillar had to re-evaluate them. They accommodate their clients going through the recessions they created easier payment methods such as Caterpillar Leasing Company, Caterpillar Financial Services Corporation, which offered equipment financing options. A couple of years later they implement a $1.8 billion plant modernization program to streamline the manufacturing process. This program leads the company to a decentralized structure. They reorganized the different services and products into business units that are individually responsible for return on assets and customer satisfaction. Caterpillar adds on its improvement by implementing six-sigma in 2001, after the internet bubble (Cat History).

Financial Health

The financial health of a company can be evaluated in terms of its profitability and its solvency, both of which can be evaluated through different ratios. These ratios compared to Caterpillar's 3 biggest competitors, Komatsu Ltd., AB Volvo, and CNH Global NV, and to the industry average will provide a clear understanding of the financial health of Caterpillar.

Return on Assets (ROA)

One ratio that can measure profitability is return on assets, or ROA. This ratio measures the return on total investment within the company. According to Yahoo Finance (Caterpillar Inc. (CAT). Yahoo Finance), Caterpillar's ROA is 1.28. This number represents Caterpillar's ability to use its assets to generate earnings. This number can be compared to the industry average ROA as well as to Caterpillar's competitors' ROA. The industry's (farm and construction machinery) average ROA is 0.4%. A competitor of Caterpillar's, Komatsu Ltd, ROA is -0.4. Another competitor of Caterpillar's, AB Volvo, ROA is -4.2. (Caterpillar Inc). (CAT) And finally, a third competitor of Caterpillar's, CNH Global NV, ROA is -0.9. (Caterpillar Inc. (CAT). Yahoo Finance) Caterpillar's ROA is superior to the industry averaging representing an above average account performance, which would imply a competitive advantage. Furthermore, Caterpillar's ROA is greater than all 3 of its biggest competitors. This represents Caterpillar's superiority in creating more earnings on its assets than its competitors. Graph 1 represents the ROAs of these 4 companies since 2005. It is important to note that Caterpillar's competitor Komatsu Ltd. has experienced detrimental decline in its ROA since 2008. Although the three other companies experience decline in 2008, their ROAs have been steadily rebounding since 2009.

Return on Equity (ROE)

Furthermore, the return on equity ratio or ROE is an excellent representation of a company's profitability. This ratio is created by dividing profit after taxes by total stockholder's equity. Industry Average ROE is 4.2. Caterpillar's ROE is 12.1. Caterpillar's three biggest competitors, Komatsu Ltd., AB Volvo, and CNH Global NV have respective ROEs of -2.0, -19.6, and -2.9. Not only does Caterpillar's ROE surpass the industry average, but it surpasses all three of its largest competitors' ROEs. This represents Caterpillar's above average account performance. It is also important to consider how Caterpillar's ROE has changed over the recent years. Graph 2 clearly shows a significant decrease in Caterpillar's ROE in December 2008 to December 2009, a decline of 48.2. It is important to note though that each of Caterpillar's 3 biggest competitors experienced similar declines in ROE at the same time, demonstrated in Graph 3. This decline can be attributed to the decline of the stock market in 2009. Caterpillar's ROE increase is the greatest of the 4 companies, which can be seen in Graph 3. This shows that Caterpillar was the most successful at utilizing its investment funds to generate growth of these four competitors. A high ROE, assuming dividends are reinvested, represents a high growth rate. This is a sign of health and vitality for Caterpillar.

Return on Investment Capital (ROIC)

Lastly, return on invested capital or ROIC is an incredibly useful and important ratio to determine a company's ability to utilize its invested capital to generate Chart 6 shows Caterpillar's ROIC has decreased each year since 2007. 2007 ROIC was 17.21%. 2008 ROIC was 13.74%. 2009 ROIC was 3.54%. The decline from 2008 to 2009 is significant. This decline can be attributed to the decline in net profits from 2008 to 2009, from 3,557 million to 895 million. This is a decline of 2,662 million dollars. Simply looking at the numbers could cause great alarm in Caterpillar's capabilities. However, it is important to note 2009 was a year in recession and major economic downturn. Caterpillar is an active participant in the construction, mining, and energy markets, which have all felt the effects of the recent recession. Furthermore, comparing a company's net profit margin to that of its competitors can show how effective or ineffective a company has been at cost control and therefore creating a profit. In 2009, Caterpillar's competitors CNH Global, Komatsu, and AB Volvo all experienced a negative net profit margin, respectively: -1.38%, -1.17%, and -3.58%. On the other hand, Caterpillar did not experience a negative net profit margin but rather a positive one of 3.76%. Caterpillar successfully controlled costs and created a positive net profit margin even in an extremely difficult and challenging economic climate. This is a representation of Caterpillar's superior profitability in comparison to its industry competitors. In fact, Morningstar states, "...the company's return on invested capital has remained well above our estimate of its cost of capital, and we expect continued economic profit generation" (Morningstar 3).

Debt to Assets Ratio

Although evaluating a company's profitability is incredibly important, it is also important to evaluate a company's solvency, or its ability to pay its debts. An incredibly important ratio utilized while determining a company's solvency is the debt to assets ratio. Caterpillar's debt to assets ratio has varied between 1.099 and 1.154 in the past 5 years, shown in Graph 4. Caterpillar's ratio of greater than 1 signifies that Caterpillar is a highly debt leveraged company. This places Caterpillar is greater risk of bankruptcy. Furthermore Morningstar reports, "In aggregate, Cat's net debt/capital stood at 80% at June 30, 2009, though the vast majority of the firm's leverage stems from its financial service segment. In machinery and engines businesses, Cat's debt/capital is a more-manageable 41%. However, this ratio has climbed from 33% in 2005, and the company was forced to amend its debt agreement due to violation of its net worth covenant" (Morningstar 8). Caterpillar is in a similar situation as many companies with a financial arm. The financial arm's decreasing value manipulates the appearance of the company's financial health. Caterpillar is not primarily a financial service company, but because of that sector they are more highly leverage than what it is ideal.

Leverage Ratio

Furthermore, the leverage ratio can give a further understanding of Caterpillar's solvency. MSN Money provides a leverage ratio (total assets/total stock equity) for Caterpillar, its competitors and the industry. Caterpillar's leverage ratio is 3.5. The industry boosts a leverage ratio of 5.6. Caterpillar's competitors Komatsu Ltd., AB Volvo, and CNH Global NV have leverage ratios of: 2.4, 5.0, and 3.5. By comparing Caterpillar's leverage ratio to that of the industry and of its competitors, a greater understanding of what this ratio means is developed. (See Chart 5) Although Caterpillar is highly leveraged, it is less leveraged than the industry average as well as its competitor, AB Volvo. (Caterpillar Inc (CAT). MSN Money)

Caterpillar is in a unique position within its industry. Although it is facing challenges similar to its competitors in its industry, it is handling these challenges quite efficiently. Caterpillar appears to be a financially healthy and profitability company.

Structure-Conduct-Performance (SCP) Analysis

Industry Structure

Caterpillar is doing business in more than one industry; they are part of industrial manufacturing, electronics, financial services, and insurance and transportation services industries. However, the main industry they are doing business in is construction, mining and other heavy equipment manufacturing. This US industry consists of over 700 companies that jointly earn up to 36 million annually. There are many competitors in this industry however, Caterpillar competes with only few of them, most notably CNH Global N.V. located in Amsterdam, Komatsu LTS locate in Tokyo and AB Volvo located in Gothenburg. This particular industry is highly concentrated, where 50 percent of the companies hold eighty percent of the market share (Caterpillar Inc.). The majority of the demand for the products is satisfied by the large manufacturers, where as the smaller companies stay in business by supplying specialized applications and products that are not so capital-intensive.

The products that are offered by all these companies are very similar. The way they differentiate themselves is based on who can keep up with the advanced technology and implement that in their end products. Construction equipment manufacturing is a very expensive industry therefore various measures need to be taken to make production and operations efficient. Since customers are very sensitive to price in this industry, expenses must be kept minimal in order to offer competitive prices. The cost of entry is medium to high considering on what scale the company wants to manufacture the equipment. However, the high prices paid by costumers create a reason for combatant firms to come in and compete for their market share (Caterpillar Inc.).

Construction equipment manufacturers heavily rely on their suppliers. Sixty percent of their product cost consists of materials ordered from part suppliers. The rest of the cost goes into assembling the parts and applying finishing touches on the end product. Much of the equipment is very expensive and has a life of 10 years or less.

Demand of the products in this industry depends on the construction industry. The main buyers consist of equipment rental companies, homebuilders, construction and mining companies. Due to the high price of such products, companies opt to rent the equipment rather than buy it. Therefore, the largest buyers of these products are renting companies or independent distributors. Revenues are also drawn from a secondary market for replacement parts and used equipment (Caterpillar Inc.).

Firm conduct

To get to the top and continuously be number one Caterpillar has implemented a number of successful strategies. Their main focus is on profitable growth of the company, reduction of waste, eliminating cost, and employee empowerment.

Profitable Growth

To increase its sales and size Caterpillar has been through over twenty acquisitions with different companies. They have extended their sales to as many as 200 countries and the majority of their revenue currently comes from buyers overseas. To make their distribution even more productive they have established a worldwide dealer network. The network consists of independently owned and operated businesses that take care of sales and maintenance in individual geographical areas (Caterpillar Corporate Overview)

Caterpillar has also expanded their brand as well as their level of client servicing. They understand that servicing their client is the best way they will establish long term relationships and strong bonds. That's why they have formed services like Cat Financials, Cat Logistics and Cat remanufacturing. They want their brand to service every need of their client and expand their services to as many areas as they can.

6 Sigma Methodologies

Caterpillar has been devoted to growth since the beginning, but that could not be accomplished without profitable and efficient production. For this reason 6 Sigma approach was implemented which was designed to reduce the number of errors in any given process. Caterpillar was the first one to launch this design globally and was very successful at it. This advancement allowed them to keep costs down through the reduction of defects and elimination of waste. In the long run this will allow them to see out their ultimate strategy; which is building better products and services for their customers, stakeholders and employees (Caterpillar Corporate Overview).

Employee empowerment

Caterpillar is devoted to their employees' happiness and well-being. Their workforce is very diverse and they make sure to celebrate and empower everyone's uniqueness. As a global company they feel that diversity is very important. They need people that come from different backgrounds that will bring new and fresh ideas to the table. To strengthen the focus on this matter, Caterpillar has established a Global Corporate Diversity Council. The council makes sure to station employees with appropriate background and experience so that customers can relate to them more (Caterpillar Corporate Overview).

Caterpillar is also extremely committed to safety of its employees. One of their 2020 goals is to reduce workplace injury rate up to sixty percent and eventually bring it down to zero. They believe that happy workers will be devoted to their jobs more. That's why they make sure to appropriately compensate and reward them. Caterpillar has many mentor and educational programs to educate their workers and help them develop new skills. By creating a positive culture, Caterpillar makes its workforce a big part of its business strategy (Caterpillar Corporate Overview).

Performance

Caterpillar has been sustaining its competitive advantage for many years. They have been able to do so because of many innovations, networking and financial strength. They have gained and sustained a significant market share in over 200 countries. They successfully implemented

6Sigma on global basis; which helped them tremendously with reducing waste, while increasing efficiency and innovation. They are in a position of providing financing to its dealers and customers. Lastly, they have the ability to fund product, educational and development programs. All these capabilities make Caterpillar continuously the most successful firm in the US and overseas.

VRIO Analysis

Key Resource	Valuable	Rare	Not Imitable	Non-Substitutable	Competitive Implication
Diversified Global Spread	Yes	No	No	No	Competitive Parity
Strong Dealer Network	Yes	Yes	No	No	Temporary Competitive Advantage
Leadership	Yes	Yes	Yes	Yes	Sustained Competitive Advantage
Service Arm	Yes	Yes	Yes	Yes	Sustained Competitive Advantage
Unique History	Yes	Yes	Yes	Yes	Sustained Competitive Advantage

Diversified Global Spread

One of CAT's key resources is its numerous plants and offices. Of the major players in the industry, Caterpillar, Inc. has the most diversified global spread. The company has 3,500 offices in 180 different countries, meaning that it has market access nearly everywhere in the world (CAT's Website). In addition to these offices, CAT has over 100 manufacturing centers so equipment and parts do not need to travel half way around the world to get to their destination. In 2008, CAT reported 67% of their revenues came from operations in foreign markets; for 2007, that number was 63% (Standard & Poor's January 2010 Stock Report, 1). This means there is an increased push for global operations. This resource is valuable because it gives Caterpillar the opportunity to be located near all of its markets, giving it considerable strength in servicing those areas. By being able to produce near its clients, CAT can cut its costs and have machinery available for sale on location, which is a large plus for the demanding industries that use CAT equipment. A large global spread is not rare in CAT's industry, with several of its top competitors enjoying their own large global spreads. Many mature, global companies enjoy the benefit of being spread extensively around the world and therefore this aspect is easy to mimic in another company. Since this resource is valuable but not rare, Caterpillar enjoys competitive parity with its competitors, which does not give it an advantage, but allows CAT to stay competitive.

Strong Dealer Network

Along with its numerous office and facilities, Caterpillar, Inc. has a strong dealer network. Across the globe, there are over 200 full line dealers, of which 71% are outside the U.S. This network has a net worth of $7.1 billion according to facts from fiscal year 2005 (Caterpillar, Inc., 16). It is this dealer network that has aided Caterpillar in capturing so much of the world market share. There is much value in having a dealer network this large; it gives CAT an advantage over its competitors because it can simply outsell others. This is rare in CAT's industry because no other competitor has invested so much into their dealer network as seen by the fact that it is so large that there are more employees working for the dealers (90,500) than CAT itself (Caterpillar, Inc., 16). However, imitating such a thing would not be challenging for Caterpillar's competitors, and so CAT enjoys only a temporary competitive advantage on this key resource.

Leadership

Caterpillar has a unique leadership program that it has applied firm wide. This program focuses on training and developing its supervisors and managers. Of the 8,500 leaders in the company, about 6000 are frontline supervisors (Caterpillar Realized It, 2). Since these people directly impact production efficiency, CAT recognized an opportunity to gain an advantage. Supervisors go through a training program specially designed for Caterpillar, Inc. This is a valuable resource because leaders are the one that set the tone for the rest of the company. If CAT's leaders are motivated and better trained, that translates to all employees being motivated and better trained. The estimated return on learning was 240% for all supervisors and more than 400% for manufacturing supervisors. A study found that fourteen intangible benefits were impacted such as improved decision making, increased employee engagement, etc (Caterpillar Realized It, 3). Tailored programs such as this are not found in every company, and therefore it is a rare resource to have. For the same reason, it is hard to imitate such a resource because this training program was developed specifically to fit the culture of Caterpillar, Inc. and cannot be applied to all companies. One can't substitute this resource because of its unique nature. Unless a competitor hires all of CAT's leaders, there is no way to substitute the impressive leadership that is deeply incorporated in Caterpillar's culture. CAT can enjoy a sustained competitive advantage because of its leadership program and the great results it has provided for Caterpillar.

Service Arm and CAT Logistic Services

Always recognized for its quality equipment and machinery, Caterpillar is even more recognized for the service arm of its organization. This key resource is what helps them to significantly differentiate from competitors in the eyes of the consumer. Along with the logistic services CAT provides, the service arm has a very powerful service parts management. An integrated system will search for parts across every single warehouse instantly. Same day shipping of parts occurs an amazing 99.7% of the time (Caterpillar Corporate Overview). This translates into customers being serviced almost instantly. This has great value to it because customers, who not only have high quality machines, but also the highest quality service, will be loyal customers. This kind of system is rare, because to have a company this large and spread across the globe, and still be able to serve all of its customers that quickly is a great accomplishment. It would take many years of making a network of parts and warehouse locations and a great deal of capital investment in order for a competitor to attain a service arm this large. Therefore Caterpillar's service arm would be difficult to replicate. CAT's service arm is not substitutable with other services. Like in automobiles, repair services are what will keep customers happy after their purchase. These factors make Caterpillars service arm a sustained competitive advantage, because no other company has been able to do the same.

Unique History

CAT's history is part of the reason that it has become so successfully today. During both World Wars, Caterpillar became a supplier for the US army giving a boom for the company. This intangible resource has proven to be quite valuable in the sense that a high demand led to rapid growth for the company as well as earning brand recognition and building strong relationships. After its relationship with the Government, CAT was able to go from a small tractor company, to a large industrial machine manufacturer. Since there have only been two

World Wars, Caterpillar was fortunate to be selected in a rare, but profitable opportunity. Only a handful of companies have been able to help with government matters. Due to the nature of history, it is very hard to replicate Caterpillar's resource, since history would have to repeat itself. Acquiring such a high demand in a short time period is not foreseeable. Caterpillar was able to use its Government employment as a jump-start itself to becoming the largest maker of construction machinery. This type of intangible resource is not substitutable because competitors will not be able to find an era where demand is so high. For these reasons, CAT's unique history has proved to provide it with a sustained competitive advantage (Caterpillar Corporate Overview).

Porter's Five Forces

Bargaining Power of Suppliers – Low/Medium

Caterpillar does not face a very high risk regarding the power of suppliers due to the availability of raw materials. There are dozens of large companies that provide the appropriate resources Caterpillar needs to operate. If costs increase dramatically for whatever reason or if there is another difficulty, Caterpillar may desire to change their suppliers and can do so without a severe setback. "Our suppliers play a key role in our commitment to excellence. We have high standards for specifications, delivery, and price" (Caterpillar Corporate Overview). This statement shows the power of Caterpillar and their ability to eliminate uncompetitive players in the market as well as the emphasis they place upon having successful supplier relationships. Caterpillar makes their own engines and assembles their own machinery, which saves them a large amount of money in the long run. If this were not the case, outside suppliers who conduct these services would have a stronger sense of power on price or other production decisions. The raw products such as steel, rubber, plastic, and other raw materials are the only concerns of Caterpillar and can be obtained through numerous manufacturers. Although these raw product industries have control over individual resource prices, the costs to customers will remain comparative to maintain a competitive position among other suppliers. As a result, these companies will be competing in somewhat of a price battle and Caterpillar will have less of a concern with the power of their suppliers.

Bargaining Power of Customers – Medium

The size of potential customers is one of the major determining risk factors with the bargaining power of customers. Larger potential revenues from examples such as large multi-national corporations or even third-world countries have much more influence on Caterpillar than do smaller organizations. “A country can exert tremendous pressure on corporations to comply with the country’s requirements and needs. Large corporations can have significant influence due to their size and the amount of product they can potentially purchase from the manufacturer” (Foothill). These larger potential customers have more influence and potential revenue to provide, leading to a larger dilemma with Caterpillar finding ways to meet terms with these organizations in order to receive substantial revenues. “Medium and small corporations have little influence in terms of volume, but other factors can give them an advantage during negotiations, such as little or no switching costs and the vast number of competitors” (Foothill). Although smaller organizations may attempt to compete upon price much more intensely due to the variety of competition, these small companies have less to offer a company as large as Caterpillar and typically search for the best price rather than the highest quality product or service. Since Caterpillar has such a strong emphasis on service and relationships, this places them in a position where they are able to hold their ground against many smaller entities and focus their main customer efforts on their nationwide and global growth with larger corporations and various countries throughout the world.

Threat of New Entrants – Low

Many barriers to entry have created severe difficulties for new entrants to enter Caterpillar's industry. "The industry is highly capital intensive. A new entrant not only faces high investment, there is already a significant competition and large players around which demoralizes the new entrant" (Haisten). One main obstacle is the establishment of dominant competitors who have controlled the industry for many years. It is extremely challenging to try and enter an industry where the competition is massive and the companies revolve around sustained competitive advantages. Aside from the existing corporations, the industry includes an incredibly large initial capital investment. The industry costs of machinery and manufacturing are hard to tackle as a new entrant and are difficult to compete unless the organization is large-scale. Maintaining any profits for many years is another challenge. The overhead and associated costs with entering the industry are challenging to surpass as a new entrant. The combination of listed factors in this industry proves that Caterpillar does not face a strong threat.

1 + 1 = 3 = Synergy!

Threat of Substitute Products – Low

Caterpillar has a significantly low threat of substitute products due to various reasons. In the agricultural machinery industry, the equipment used by Caterpillar is the most efficient technology for the associated costs of operation. "Due to the highly specialized purposes of the machinery produced, there may be some overlap between possible uses, but the machines face no risk of substitution" (Haisten). There is no other viable option for buyers to consider for the task to be completed in a resourceful and timely fashion. For example, if a company were to refuse the services of heavy machinery and focus on standard human labor as an alternative, the timeframe and associated expenses would be wasteful in comparison to what the major competitors in the agricultural industry have to offer. Caterpillar does not have to necessarily concern itself with substitute products, but rather on maximizing the reliability and functionality of the machinery they currently produce.

Competitive Rivalry within an Industry – High

Hundreds of competitors in a worldwide industry have created a significant threat to Caterpillar. “They operate in an environment with 50 top competitors controlling roughly 80% of the market” (Haisten). Since Caterpillar focuses more upon their service rather than diversification, the door is left open to other competitors to take advantage of new opportunities. Several competitors provide products that offer benefits to other industries such as the military or consumer products. For example, Deere & Company offers a variety of products to consumers regarding lawn care. However, in an attempt to counter the issue of competitive diversification, Caterpillar is beginning to focus on global expansion instead. “The company said it expected growth of more than 10 percent in China and 8 percent in India in 2010. That is much more robust than the 3.5 percent growth Caterpillar predicted for the United States and the 1 percent growth in Europe” (FundingUniverse). Caterpillar must continue to find ways to remain competitive in an industry filled with so many extremely competitive organizations.

Synergistic Overall Analysis

Mission

"For more than 80 years, Caterpillar has been building the world's infrastructure and, in partnership with our network of caterpillar dealers worldwide, has helped drive positive and sustainable change on every continent. We are a global company, with hundreds of locations worldwide to serve and support our customer base, and respond quickly to their needs."

According to Caterpillar's mission statement their vision is to continue their existing goal of building infrastructure globally to make sustainable positive changes, and provide superior customer service. They can only achieve these goals through synergy.

C.L. Best + Holding Manufacturing Co. = Caterpillar Co.

According to Campbell, "synergy refers to the ability of two or more units or companies to generate greater value working together than they could working apart." One of Caterpillar's mot successful synergies was the initial merger between C.L. Best and Holding Manufacturing Co. C.L. Best and Holding Manufacturing Co. were the ying and yang of the manufacturing equipment industry. C.L. Best was suffering from a poor brand name but had stable financials while Holding Manufacturing Co. had a prominent brand name but unstable financials. Prior to the merger they lost millions of dollars competing against each other. Their cohesion helped them further their R&D investments and save massive transaction costs.

Products and Services

Caterpillar is divided into three principles: Machinery, Engines, and Financial Products. The machinery and engine principles are their core competencies, while the financial products principle is still developing. Within the machinery principle construction and mining equipment is their main focus. Within the engine principle diesel and natural engines are its core competencies.

CAT Financial

Even though the financial products are not a core competency they are crucial for Caterpillar's success. It once helped them get out of the recession and can keep them out of future recessions. The main purpose behind the financial products is to support the core competencies. Since most of their products are major investments for businesses, many businesses cannot afford their machines, projects that need the machines, or the risk of purchasing such a costly machine. To curb machine costs Caterpillar provides customers with financing options, which includes CAT auction services, machine financing, marine financing, mining financing, and selling used equipment. To assist customers with project expenses they have a investment option where they can get power investments and power notes. To minimize risks they provide insurance which consists of: extended service coverage for engines, Cat Equipment Protection Plans for machines physical damage issues, inventory protection plans dealer property and casualty insurance, risk management, marine transit insurance, and dealer bonds.

CAT Logistics

The purpose behind CAT logistics was to build upon the global distribution experience of its parent company to help other companies' lower distribution costs and to increase their customer interaction experience, and establish brand loyalty. Cat Logistics provides customers with solution in managing transportation, inventory and distribution centers, forecasting, information management, and network consulting services.

CAT Reman (Remanufacturing)

This service is supposed to help companies improve their salvage capabilities that restore used products to their original condition and specification, extend its product life. This is a huge component for its sustainability route, as well as, targeting midsized and small businesses.

The Rental Store

This feature is supposed help Cat with equipment sales, and their financing sector. Allowing customers to rent equipment gives them a better chance experience the product itself. Since they are financing machinery sales they would have some pieces of equipment reposed, even though the company is taking a loss this helps us better curb that loss.

FG Wilson

It was acquired from Emerson Electric in 1999. This company produces generators. It some respects selling generators with machinery can be helpful but not as often.

Mak

It is a marine diesel fuel engine company. This company has a good relation with the company's core competence because it has a strong military connection.

Perkins

This is a successful engine company. Since acquiring this company eliminates an engine competitor and gives better R&D in developing engines.

Progress Rail

This is the largest railroad MRO business in the country. Besides its marvelous reputation and dominance it does not have anything to do with the firm. Having Perkins would just bring down Perkins, because it would be managed by inexperienced MRO business managers.

Solar Turbines

Even though this business isn't directly related to the company it is one of the companies' core competences. It also provides a good amount of synergy because it deals with oil and natural gas which is often times associated with the mining industry.

Analysis

The reason why Caterpillar is what it is today is because synergy. If Holt never acquired the track layered vehicles from the British company there would have never been Caterpillar in the first place. Caterpillar would have ceased to exist after WWI and Holt's death if they never merged with C.L. Best, their competitor. Synergizing with these small companies helps Caterpillar expand into other markets, acquire new technologies, and service their other products and services.

Caterpillar Corporate Strategy Analysis

The Caterpillar corporate strategy has been slowly built up since the company first started in 1925. With ought the long experience the company would not be able to be what it is today. By slowly building up their company across the world Caterpillar has ensured their significant market share by making entry and competition extremely difficult for potential competitors.

Caterpillar corporate strategy focus on key points such as; growth, cost reduction, product support, quality and reliability, people, emerging markets and 6sigma just to name a few among many.

Growth

Right now the Caterpillar growth part of strategy has its focus set on the Asia/Pacific continent because of the high growth potential in economically emerging countries. According to the Caterpillar corporate strategy the Asia/Pacific region has; 42% of the world's population, 44% of the worlds coal reserves, 62% of the worlds iron ore, and 40%+ of the worlds gas production . Also the emerging economies and especially the machine industry is growing twice as fast as the rest of the world, and this is because since the economies are growing they need to build and when they are building that is when Caterpillar needs to ensure that they are their main heavy machinery supplier. Also another statistic is that the construction spending reached nearly 150 billion dollars in 2008.

6 Sigma

The next big part of Caterpillar corporate strategy is called 6sigma. 6sigma "is a methodology to reduce defects and eliminate waste through the use of statistical analysis, quality tools and a structured approach to project management". Also it is a "strategy to reduce costs and generate growth while providing high-quality product or service which exceeds customer expectations". Caterpillar states that since they implemented 6sigma the companies "results far exceeded the company's aggressive goals and was the key enabler of significant improvement in core operating costs". Using this strategy the company was able to cut their costs by 23% from

2000 to 2003 and 35+% from 2003 to 2006 and also improved services from 94%-96% from 2000-2003.

Customer Service

Another big thing that Caterpillar is known for and something that has made the company stands above all other competitors is their customer service strategy. Over the years Caterpillar has opened up new locations all over the world and has approximately 3500 suppliers and dealers all over the world, which they successfully communicate with by using the integrated system called SAP. Caterpillar prides itself on customer service and makes all the agents and technicians across the world become available on the job site just within a few days if not less. This creates a great advantage over competitors because by fixing problems right away Caterpillar becomes more attractive to the customers because it means that work will not be delayed due to maintenance.

By pulling all of the sections mentioned above and successfully turning them into one strategy Caterpillar stands tall above all other competitors in the heavy machinery industry. By cutting costs they are able to ensure higher profits, which in turn, lead to higher investor return and makes the company a reliable place to in which to invest, by exceeding in their customer support Caterpillar becomes then top choice company from which to buy equipment which allows them to charge higher prices and earn more revenue. Caterpillar has put together the most important strategies into one amazing strategy and this is why they have stood apart and above the rest of the industry.

Strategic Vision

As Caterpillar looks to its future, it should take several things into consideration. Caterpillar should invest money into research and development to create biodiesel engines. Being green is incredibly important to consumers and Caterpillar should capitalize on this. It should continue to become a "greener" company in all it does. Furthermore, Caterpillar should explore new ways of greening its current products. Investing in green technology will ensure Caterpillar's longevity.

Furthermore, Caterpillar should continue to strengthen its global relations. It will be essential that Caterpillar does the necessary research to fully understand the needs of its global consumers. Moreover, Caterpillar should consider creating local factories for its products in foreign countries. Not only will doing so lower costs, but it will also create a partnership within a local community. By providing jobs and giving back to the local community, Caterpillar will demonstrate its commitment to helping its foreign partners. And thus, strengthening its global relations. Furthermore, Caterpillar should seek out partnerships with foreign governments. Particularly, Caterpillar should consider partnering with an Asian government. This partnership will expand its market and customer base. Caterpillar needs to expand into untouched markets before its competitors, in order to fully maximize first mover’s advantage.

By furthering Caterpillar's green developments and expanding globally, Caterpillar can continue its legacy and ensure its long-term success.

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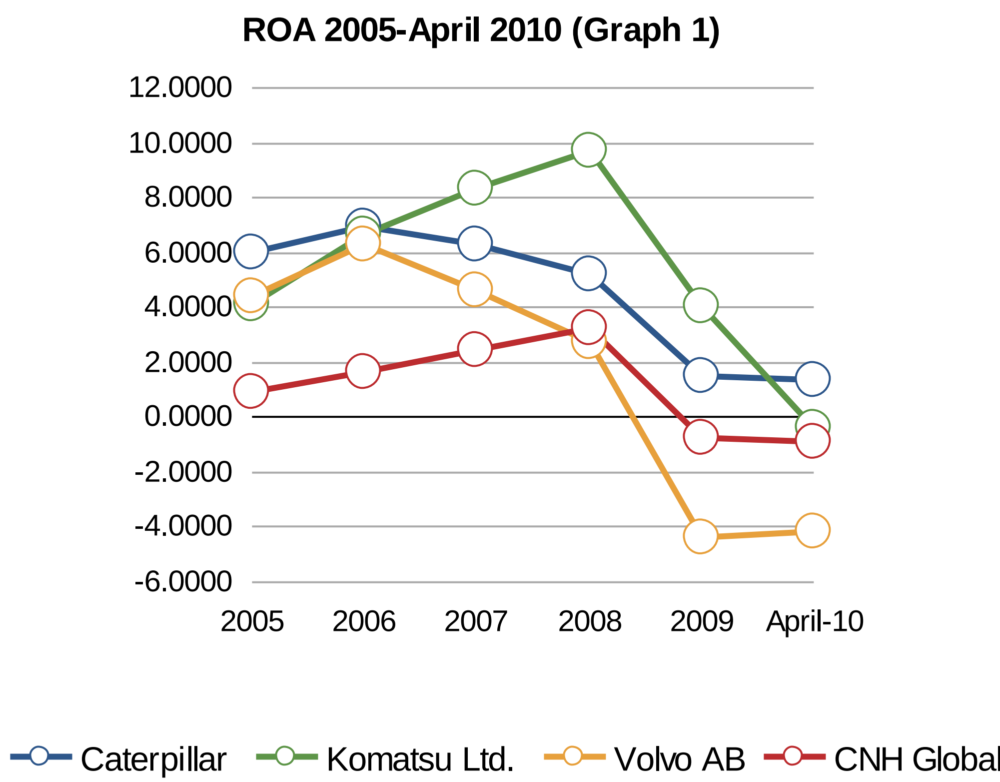
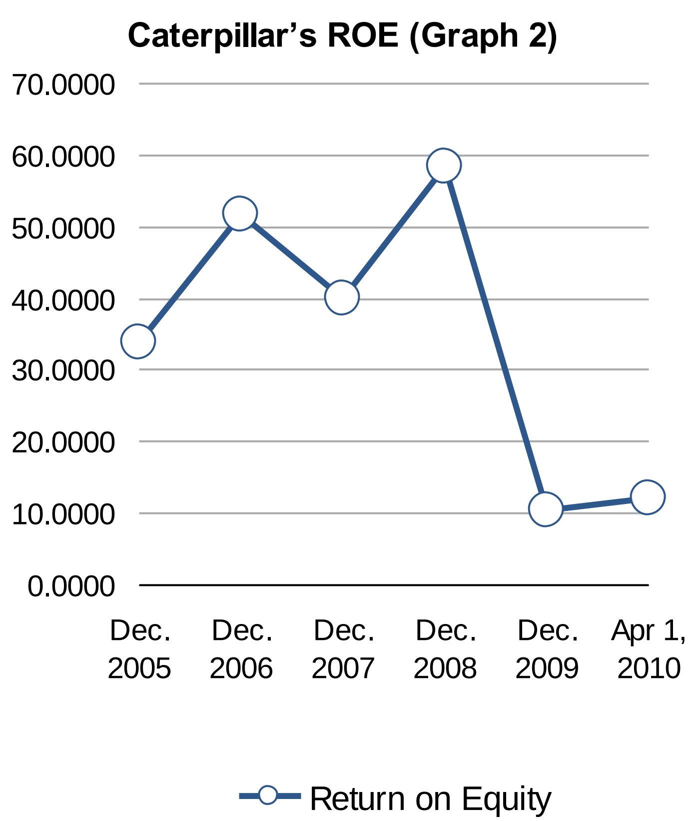
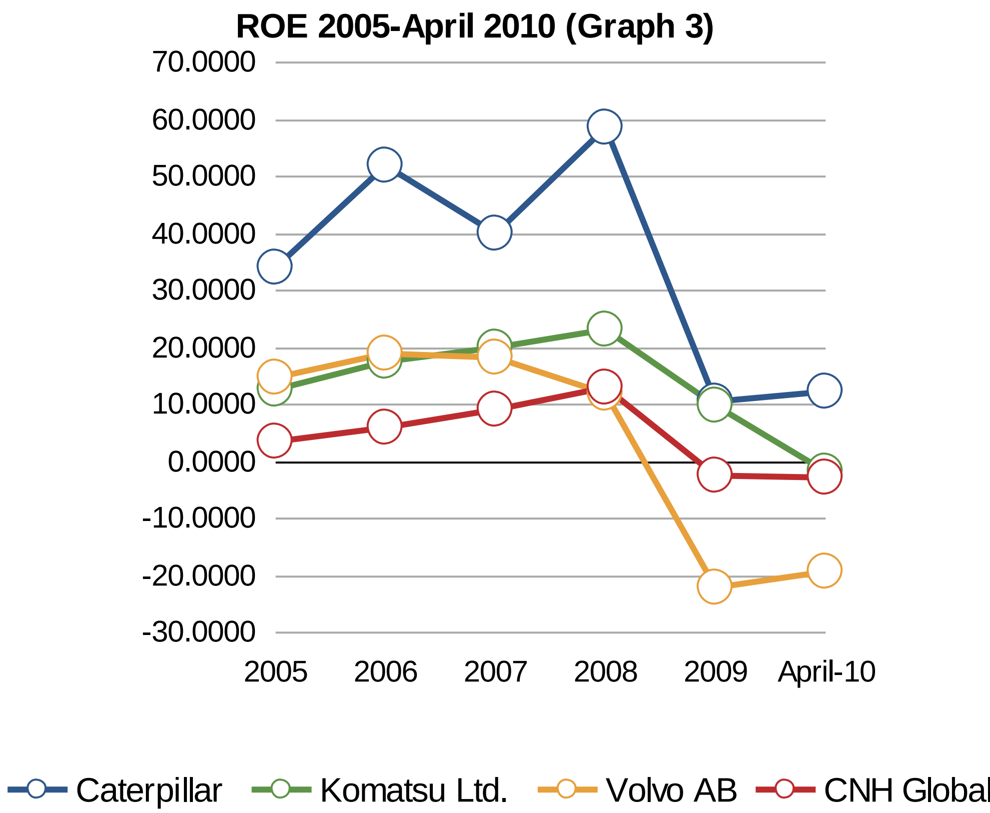
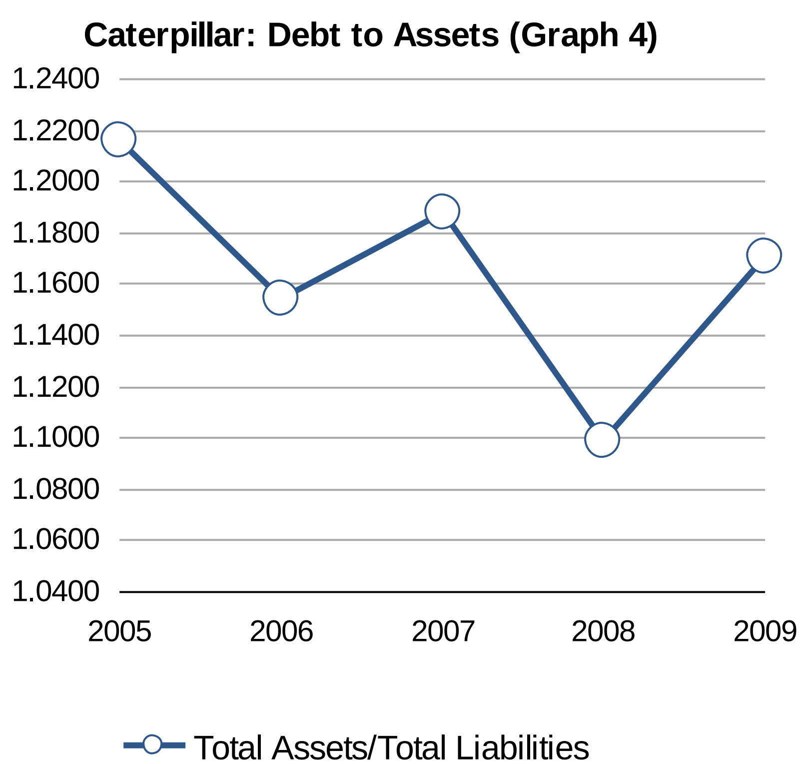
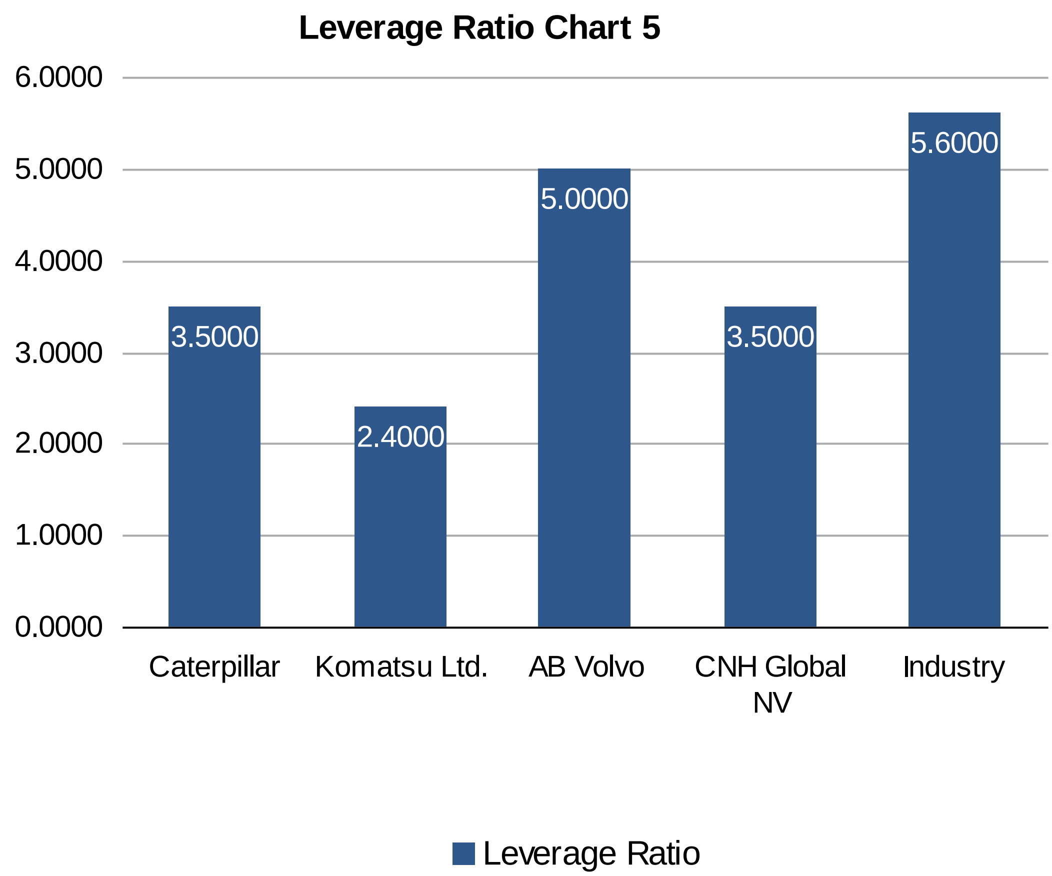
Appendix

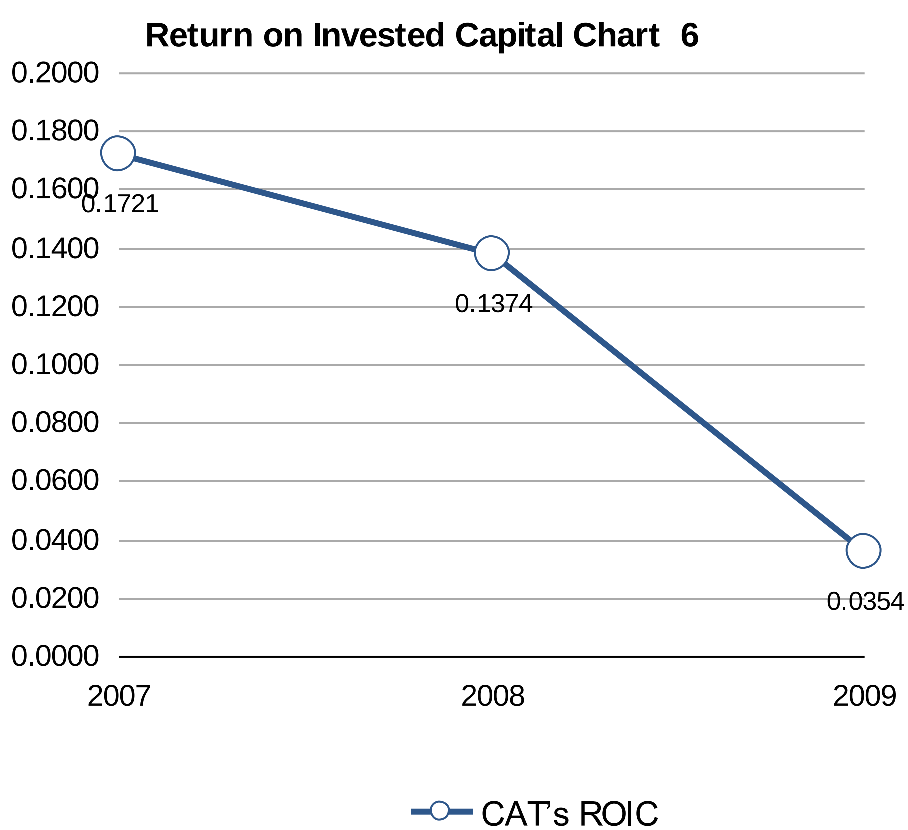

ROA 2005-April 2010 (Graph 1)
12.0000
10.0000
8.0000
6.0000
4.0000
2.0000
0.0000
-2.0000
-4.0000
-6.0000
2005
2006
2007
2008
2009
April-10
Caterpillar
Komatsu Ltd.
Volvo AB
CNH Global


Caterpillar's ROE (Graph 2)
70.0000
60.0000
50.0000
40.0000
30.0000
20.0000
10.0000
0.0000
Dec. 2005
Dec. 2006
Dec. 2007
Dec. 2008
Dec. 2009
Apr 1, 2010
Return on Equity


ROE 2005-April 2010 (Graph 3)
70.0000
60.0000
50.0000
40.0000
30.0000
20.0000
10.0000
0.0000
-10.0000
-20.0000
-30.0000
2005
2006
2007
2008
2009
April-10
Caterpillar
Komatsu Ltd.
Volvo AB
CNH Global


Caterpillar: Debt to Assets (Graph 4)
1.2400
1.2200
1.2000
1.1800
1.1600
1.1400
1.1200
1.1000
1.0800
1.0600
1.0400
2005
2006
2007
2008
2009
Total Assets/Total Liabilities


Leverage Ratio Chart 5
6.0000
5.0000
4.0000
3.0000
2.0000
1.0000
0.0000
3.5000
2.4000
5.0000
3.5000
5.6000
Caterpillar
Komatsu Ltd.
AB Volvo
CNH Global NV
Industry
Leverage Ratio


Return on Invested Capital Chart 6
0.2000
0.1800
0.1600
0.1400
0.1200
0.1000
0.0800
0.0600
0.0400
0.0200
0.0000
0.1721
0.1374
0.0354
2007
2008
2009
CAT's ROIC