Going Solo

A man of his own making, Shankar Somasundaram has paved his way to become one of Sri Lanka’s most successful investors. The founder of Lanka Bell and now the main shareholder in Brown and Company spoke to Business Today on his investments in the Colombo Stock Exchange, blue chip companies and of plans he has for the future.

By Keith Bernard. Assisted by Anisha Niyas.

Tell us a bit about yourself and how you started out?

I am a Chartered Management Accountant by profession and a third generation businessman. I have been in the family business for a long time.

I met my business partners, once I had finished my studies in England. We wanted to do something different. We saw the future potential in the infrastructure sector. The sector which had, globally, got a lot of attention at that time, was the telecom sector. It was easier to source funds for investment in this sector as opposed to roadways and the like. We subsequently formed Lanka Bell and then started making presentations to investors. We attracted investments of USD 100mn for Lanka Bell.

How do you generally finance your investments?

I have made investments personally and also as syndicated investments with partners. I look at the opportunity and according to the size of the investment, I decide whether I should go on my own, with my bankers backing me or with partners. I always prioritise the investments.

How do you usually identify business opportunities in the market?

I keep talking to people and when opportunities emerge in the market, people do approach me. In the case of investments in the Stock Market, which is my main mode of investments, I talk to brokers on a daily basis – my biggest investments are in blue chip companies. This currently results in me being within the top 10 investors in the listed companies I invest. I have fairly large stakes in companies, which include Sri Lanka Telecom (SLT), Lanka Indian Oil Company (LIOC), Hatton National Bank (HNB) and Asian hotels. These are passive investments. These are not investments where I take any active role as such. I am investing on my own in property development and I also have a significant stake at Brown and company.

You spoke of your investments in the CSE. Are these investments held in your personal name or do you operate as a corporate investor? Do you have any off shore investments as well?

The investments I make are only in Sri Lanka. I invest on my own, not through any legal entity. I am an individual investor, and banks do back me, so the financing is mixed.

What do you usually look for before investing in a blue chip or before mak-

ing a strategic investment? Is size a criterion in the decision process?

Usually, my investments are in the blue chip companies. Apart from the financial analysis I also see how the industry would go into the future and how it is managed. If you take companies like SLT or Asian Hotels – these are public companies of a very large size. Although Sri Lanka is a volatile market, the exit is easy and that is why I invest in blue chip companies. If you talk of other companies, I am always looking for new opportunities for investments, acquisitions or takeovers. I keep a complete open mind. I don't think size is of any limitation. I look at the potential, the business as well as the long-term viability of it.

One specific difference between yourself and a venture capitalists is that after making a strategic investment and taking control of the business, you actively involve yourself in the day to day management of the company. Is that a correct assessment?

It has been like that in the past. Lanka Bell was a private company and I was the local partner. I was the Vice Chairman. We took over Brown and Company and I went in as the Executive Vice Chairman. During the first six months I held an executive function, but now I have a lesser function because we have recruited Murali Prakash as the Managing Director. As entrepreneurs, our specialty is to identify opportunities, acquire and then let the professionals manage. That is how an investor should work.

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Do you find Sri Lanka an attractive market for investment?

The Price to Earnings (PE) of most of our quoted companies is very low – ranging from about 5 to 7 or 5 to 8. In the developed markets for instance, the PE is anywhere between 15 times to 30 times. If you talk about core fundamentals, our companies are very sound. For an investor, this is a good opportunity.

Most of our investors on the Stock exchange are of a speculative nature. Your gains are probably because of your long-term holding power. On

average for how long do you hold a stock?

My portfolio is the same – whether it is now or five years ago. We are still in the market. When I make an exit from one stock, I invest in another. Many hold surplus or excess money as deposits in banks, but sometime it's not worth it. My recommendation is to invest, even if it's for six months.

There are less than 250 companies listed in the CSE and of that less than 100 are actively traded and are attractive. In your opinion why don't more companies obtain listings? Is it because of their fear of losing control of their businesses due to predatory activity?

It is a matter of getting used to it. Some family controlled businesses are run as closed entities although they are blue chip companies. It is a passing phase as seen in India, with better access to financial markets, improved valuations and an easy exit. However with increase in the PE it would encourage more companies to go public. There are many reasons why companies go public. However when the market conditions are not right and the PE relatively low – going public would be questionable. Even if some family companies want to go public, often they prefer to retain control.

How easy and convenient has it been for you to raise capital in the local market?

I have had absolutely no problems with investments provided the figures add-up and the prospects are there to see. I have foreign investors who are willing to invest here. Actually there aren't as many opportunities as there are investors.

How many companies are attractive and susceptible to take over at the moment? Not many. The investment boom has to be created. If you take China for example, it has USD80bn FDIs coming into the country. Singapore is the next emerging market in size at USD22bn. India has USD7bn. I don't know the actual figures for Sri Lanka – maybe a couple of hundred millions USDs. In the next seven years the government of India needs USD350bn to change the skylines and infrastructure of metropolitan cities. They have planned everything out. Now they are trying to deregulate to attract foreign investment. One thing we need is consistent government policies and lower risks.

In Sri Lanka the problem is not with deregulation or a lack investment

incentives, but an urgent need for an improved investor friendly environment and conditions? Do you agree?

Absolutely. The country risk is still rated high for investors.

Do you look for an exit strategy when making an investment?

I always look for an exit mechanism as a safety net. I have to have an assurance that I can exit any time I want, hence my investments usually are in quoted companies. I prefer the majority shareholding when it comes to private companies. For me, the exit strategy is only a safety net. It doesn't mean that you have to make an exit – if the business is doing well and things are happening the way you want it to, and there is growth, then there is no necessity to consider selling.

In the case of quoted companies, it is sometimes good to sell because of the volatility in the market. I do this when there are large quantities.

You have a strategic investment in Brown & Company and currently you are the Deputy Chairman of the company. What got you interested in Brown & company?

After I divested Lanka Bell, I was looking for an opportunity to invest in a public company in Sri Lanka. At Lanka Bell, all of my partners were foreign and I was the only Sri Lankan. There was only one product – telephones. Thereafter I divested in Lanka Bell, I felt that Banking and Telecom were two industries that required consolidation, or else there would be stagnation. Although the figures are lucrative and there is room for expansion, the time horizon for optimum profitability was distant, and that was one reason for exiting Lanka Bell.

I was looking for opportunities and Brown and Company was for sale. We entered the bidding process and succeeded.

As a selective investor with a high concentration of investments in blue chips listed on the Colombo Stock Exchange what was your motivation to take control of Brown and Co. Ltd?

It is a company with very diverse activities. It is the market leader in agriculture, batteries and many other products. We manufacture batteries in association with an Indian partner Exide India and distribute. We have a market share of over 70% of the automobile battery market. We supply Exide, Daganite and Lucas. We acquired

Klevenberg three months ago so that we are in full control of Lucas. With three leading brands, our dominance is very clear in the market.

Browns are agents for Sharp, selling consumer electronics and office automation. Furthermore we have 3 thriving hardware division with many brands such as vetpharma, which sells chicken vaccination for poultry etc. Browns Tours are also the agents for Austrian and Scandinavian Airlines.

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What is the flagship business of the Group?

Agriculture.

What is your shareholding of HNB through the Brown & Co. Group?

We have a substantial holding of 13 to 14% in HNB.

Brown & Co. also owns several high value properties?

Yes. We have many properties including Colombo and out stations. The Darley road property is one of these. There is another property close to that.

You didn’t invest in Brown & Co. alone, but in partnership with two other investors. Is that correct?

Yes. Ishara Nanayakkara, Ajith Devasuriya and I acquired Browns Group and the ownership is in equal proportion.

How do you plan to restructure the group now that you hold the reigns?

A further reason we invested in Browns is for its brand equity. It is one of the oldest companies in Sri Lanka with a history of 175 years. The Brown’s name is accepted anywhere in Sri Lanka and we plan to use it as a launch pad for more products and business lines in the future. We have recruited a new Managing Director who is in charge of the change and management.

Are you looking at strategic divestments as well as part of your restructuring plans?

Surprisingly we don't have many obsolete businesses. All the businesses that Browns has are good. There have been a few businesses not managed well in the past, but that has being corrected now. We have brought in new blood and have invested new money. We don't have a single business running at a loss, and we don't plan shutting down any of the businesses either.

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> I would look at it very objectively."

How about the hotels owned by the Company?

Browns Hotel was sold to Aitken Spence a long time ago. There was only one remaining hotel, which was destroyed during the tsunami at Yala. We are observing the trends in the tourism industry and as soon as the industry bounces back to normal we will invest in the hotel business. There won't be any new investments in this area right now because as you know one of the sectors that gets affected when the country risk increases is tourism.

Brown's also has properties in several places outside Colombo in the country. What do you plan to do with these properties?

We will be divesting most of those properties that don't have direct use to the business because we are not in the property business. We will however keep properties we can use for the future expansion of the business.

The company maintained a visible presence through its motor division in the past. Will this be a sector that would receive your favourable attention in the future?

We are at the moment talking to some Chinese, European and other automobile manufacturers. You will see us re-enter this business sector in the future.

What would happen once the restructure is complete and the company is revived? Would you consider exiting, or is this an investment too close to your heart to part with?

I am less emotional about investments. That is very clear in all of my transactions. If a business decision has to be made to divest for whatever reason, I would make the decision. Brown's is a good investment, but I would not look at it emotionally; I would look at it very objectively. We are restructuring and we hold the investment in partnership. Browns, as a business has to do well, and the partnership also has to do well. If we do well on all sides, then we will definitely go places and will use that as a launch pad for other acquisitions.

You were the founder of Lanka Bell in Sri Lanka and were personally responsible for obtaining its Wireless Local Loop (WLL) license. You also held an executive position in the company until it was recently sold out. Were you pleased with the performance of the company when it was under your co-ownership?

I was pleased with the performance and was always aware of the potential. Lanka Bell was coming to a point of change with the introduction of CDMA. We had invested in Nortel technology, which did not have a longterm life. We had to change, and we were thankful that the government issued to us the required CDMA license.

You quit before Lanka Bell adopted the CDMA technology?

The frequencies were allocated while I was at Lanka Bell. We had started the work and the process to acquire the license was started a year before I left.

Did you dismantle the network installed by Nortel?

We were to replace it with CDMA and other technologies over a period of time.

Originally when Lanka Bell started, a large portion of the initial investment was swallowed by the prohibitively expensive technology costs. With the competition intensifying by the time your network was rolled out, the economics of the business must have drastically changed from the original plans?

Wireless local loop was a new technology at that time. It was the technology of our era when we started. At that time a line cost over USD1000. Now it is less than

USD100. So you can just imagine the investment we made and in today's terms what the investments are.

Nortel themselves have been through some rough times in North America. How did that affect your cause?

Nortel equipment has come down in terms of prices. They still cannot compete with the Chinese who are getting better.

What happened to the Singaporean investors?

They divested completely.

Will you be looking at future investments in the telecommunication sector in Sri Lanka?

Of course. As I said I have an open mind. I look at it from a pure business perspective. It doesn't matter whether it is telecom, Browns or Lexus, which is my real estate development company.

You say you are not emotional about investments. That said, are you looking at any specific emerging sectors for future investment?

If you look at my investment portfolio in the toe exchange, I have picked SLT, Dialog, Browns, HNB, hotels, bank –it is a diversified portfolio. Size al o matter . If all the funds are put into any single sector although there could be a lo of growth and promise, in the long term, you may face some limitations and challenges.

Two companies you just mentioned are Dialog and SLT. Because of their large market capitalizations, the relative price movements of these two stocks are very marginal and therefore offer very little gains in the short term compared to most other stocks. From a pure financial perspective why would you choose these two stocks over others?

Dialog and SLT are very liquid stocks. So, although it seem marginal in the short term, there are substantial gains.

What are your other strategic investments?

I have other strategic investments in the property development sector through my

company Lexus, which is in developing apartments in prime locations. We are currently developing a property on Thurstan road. The next development will be a property on Havelock road. These are large investment.

As you say these are high cost investments and often the cost escalations because of high inflation in the country overrides the initial estimates. The completion time is relatively long and so is the payback depending on the quantum of prior sales and deposits you secure. How do you match the funding requirement?

I have partners from the UK who have invested. I also have banks that lend when I need funding. In the property business pre-selling is also possible.

You mentioned earlier of your investment in AMW. In recent times the AMW share jumped in price from levels of below Rs100 to over Rs300, and you triggered the price jump. Tell us about the investment you had in AMW and what happened.

I am always on the look out for opportunities and shares in the market. AMW was one of the companies which had potential because of its agencies such Nissan, was one of the largest Japanese cars imported to Sri Lanka, and Maruti, another that has a high demand. I expected AMW to takeoff soon due to the Maruti agency and at that time the market price was very low – this was three years ago. I bought in to 20% of the interest of the company, large enough to cause anxiety to the majority shareholders of the company who also in turn increased their stake in the company. This interest and activity pushed the prices up. Jn the mean time, my expectation was realised as AMW achieved huge growth. The company began making about Rs500mn to 600mn a year growing from an earlier position of around Rs70mn when I started to buy in. The price moved up to Rs250 and I was happy to exit at that price point, allowing another investor to enter and earn a profit.

As an investor how do you appraise and evaluate your risks?

Apart from the due diligence and financial analysis there are other considerations. Most of my investments are in the blue chips. I only invest in the stock market and in blue chips. Not only here, but also in other parts of the world there is lower risk when investing in blue chip companies. Browns I would say is on its way to joining the elite club of blue chips. It would be in par with other blue chip companies soon. There are huge property development opportunities. In business we believe doing

one thing at a time. We don’t want to go in at unchecked speed and change a lot of things. We prefer to move with the flow. We first consolidate and develop the property, and then select the right partners. It is imperative that you carefully choose the right people to work with. Of course in business you have to take risks, it is inevitable. I believe the biggest risk in business is not taking risks. If I am to sit here without taking risks and looking for all the safety nets, there is no difference between me and another person who wants to invest money in the bank – as an entrepreneur, you don’t often necessarily sit ticking boxes, but you go with your gut feel, experience and perception.

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And how do you identify the right business partner?

My partners either come in over with the project or it is a relationship. I do have different partners for different projects. There is risk in business investments and there is risk with working with partners. Nobody can predict the outcome but there has to be a safety net. In my case, if you consider Ishara Nanayakkara, for example, who is a good friend of mine, a second-generation businessman who looks at business professionally My partners either come in over with the project or it is a relationship. I do have different partners for different projects. There is risk in business investments and there is risk with working with partners. Nobody can predict the outcome but there has to be a safety net. In my case, if you consider Ishara Nanayakkara, for example, who is a good friend of mine, a second-generation businessman who looks at business professionally and objectively – partnering with such people is reasonably safe. There comes a stage when you are more concerned about your reputation than just money.

You usually operate outside the business radar and maintain a low profile. Is it by choice that you stay outside the public spectrum?

That is definitely by choice. I don’t see the need to be high profile. If being high profile is a precondition to get into business, then perhaps yes. B1:1t if I can go on my own, whichever way I want to and be successful in business l see no need for

being high profile.

Talking of your family business, you seem to have made a huge shift from the business your family was occupied with?

Of course. It was my grand father's business. The present times have changed. You have to go with the times where business is concerned. I was one of the first to get into the telecom industry in Sri Lanka and now I think its time for the good old brick and motor business to make a come back, which is also a world trend. That is the reason I have gone into property development, Brown & Co. etc. In telecom, the earlier per line investment of USDlO00 is now down to USDlO0 to USD75. It is probably going down to USD25. We have to wait and see at point the market stabilises. Where I see growth in Sri Lanka or most countries is in the power and telecommunications sector, which are growing. The telecom sector in Sri Lanka is beginning to saturate but we still see more mobile licenses being issued. There are already too many players in the market. It would have been better if there is some form of consolidation rather than new additions to the sector. Just to digress for a moment, if you go to Gampaha, you will see seven base stations. Why can't we have one base station and have everyone share it? The other six can go to six different villages so that in terms of coverage we are all over. Right now, we don't have total coverage.

In countries like England, the transmission tower building license is given to somebody else. So this business concentrates on building the transmission towers. The same problem lies with the banking sector – especially with ATM's. Why can't we work together? It's a waste of time. In England, it is regulated and supervised and ATMs are shared.

Getting back to answering the question, my family owned and operated a successful business that is still operating and successful. The entrepreneurial instincts that I may have developed because of my family, perhaps, made me look for opportunities, and I guess I have moved on with the flow of the new world.