

Industrial tech is an underserved market in SEA, says Novo Tellus Capital's Loke Wai San



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For Singapore-based private equity firm Novo Tellus Capital Partners, industrial tech is an underserved market in Southeast Asia as many GPs tend to overlook the sector, said its founder and managing partner Loke Wai San.

“There’s inefficiency and a lot more work in the sector, but I saw the opportunity. I also think that in Southeast Asia, no one is serving the industrial tech space. I believe that’s where we’ll be making a lot of money,” he told **DEALSTREETASIA** on the sidelines of the HKVCA Asia Private Equity Forum in Hong Kong earlier this month.

Prior to founding Novo Tellus in 2011, Loke was the managing director of Baring Private Equity Asia’s Silicon Valley and Singapore offices, where he led investments in IT hardware, SaaS, semiconductor capital equipment, and industrial sectors.

An engineer by training, Loke said Novo Tellus raised \$25 million for its maiden fund which achieved a final close in 2012. The fund was fully deployed in 2016. The PE firm is currently investing out of its second fund but Loke declined to comment on Fund II.

Novo Tellus has invested in five companies across the region and has exited three so far, one of them being Singapore-based printed circuits board solution provider MFS Technology, which it exited along with majority co-investor Navis Capital Partners last February. The investment, made in November 2014, generated 3x returns.

Edited excerpts:

Which are the markets that you are particularly bullish about in Southeast Asia?

It's the sector that we're investing in – the industry itself. And, the sectors are cut across different countries.

What's the status of your first fund?

Our first fund was small – we did a lot of co-investments and put together close to \$200 million worth of co-investments. If we look at the buyout sizes, they've been anywhere between \$15 million and \$95 million or \$100 million. The first fund was \$25 million which had its final close in 2012. It's fully deployed in 2016. Now we're investing out of Fund II.

And you exited Singapore-based MFS Technology last year, along with majority investor Navis Capital Partners.

MFS Technology is actually quite a mediocre exit for us. The fund's DPI (realization multiple also known as distributions to paid-in multiple) is 3.5x and I think that's very good return. MFS is a very good deal but it's not our only exit. Out of the five investments, we made three exits. Our MoIC (multiple on invested capital) is over five times.

Are LPs always pushing you to exit your investments?

No, with 3.5x, they're alright. Very few funds can return 3.5x. Now they're very happy and we're patient with our investments and we will take time to monetise.

How significant are co-investments to Novo Tellus?

One was a public company that we took control of – AEM Holdings. When we invested in that company, it was going to be delisted but couldn't find any co-investor to do it. So we took 30 per cent in the company with our \$5 million investment. Today, the company has S\$250 million revenue and S\$40 million operating profit with a market capitalisation of S\$250 million.

When we went in, the market cap was S\$20 million. So obviously we built it with the team. The company was not doing well but we like the end customers – one of the biggest semiconductor companies in the world and they're key part of the next generation manufacturing process. The company wasn't small with a S\$80 million revenue already, but was leaderless. So we went in with our team and managed to help the company to turn around in six to seven years' time.

So your typical holding period is about six to seven years?

It's five to seven years. MFS was a three-year investment, a bit sooner but it was executed very well.

Is it hard to source deals in the region?

For good deals, yes. So we take our time. We have a small team, we do not hire for the sake of building the facade of a big team. We tend to be engineering-focused. The difference between us and other firms is that when we invest in a company, their current products and current customer base, we actually work with the management and engage with the company's seller and founders. What we do is we take very little leverage to reinvest into the company to build functional excellence, development, sales and market, logistics and all. It's like a hotel, if you don't renovate it, you can't charge for a higher rate. You need to have functional excellence.

And the reason we like Southeast Asia is that this is not a very big gap. If you want good talent, they're there. We use free cash flow to acquire company/technologies. We also use it buy R&D. So we actually look at earlier stage companies under our portfolio companies and help them with acquisitions. Most PE guys – the playbook has been like buying a house – you need a 20 per cent but I borrow a 60 per cent and I pay it off because I can rent the place out and over five years I make 2x.

But you'd find these companies are no longer growing very fast. From a strategic perspective, unless you really did a good job, it's quite hard to sell. One of the companies that we have, it has the fundamental IP that many strategics want, it has a future. That's what we invest in, we invest free cash flow into the business to make sure the terminal or end-value is higher. I don't really care about during my holding period, it goes down or up during one of the years, as long as the trajectory is there.

I've been under a lot of pressure when I explained about the lower EBITDA because we reinvest by hiring engineers and all

Yes, it can't be up all the way.

And it's not healthy. You got to invest. That's what we believe in. Over time, as long as we exit with a good future for the company, people would buy. MFS is a classic example. Together with Navis Capital, we invested S\$20 million capex into the manufacturing facility that started winning higher margin deals. When you're a company owner, act like it. When we sold MFS, we had multiple bidders.

When we started Novo Tellus in 2011, and when we closed the fund in 2012, no one knew who we were. Most PE guys chop up the business and get cash back but we're going to build the business with the company.

But today, Novo Tellus is a different fund because when we talk to entrepreneurs, they say they know what we did. If you're a good company with options, of course, you'd also like to pick who you'd like to work with. A lot of PE guys approach businesses as a transaction. It's a different conversation that we have with the companies that we work with. Deal-sourcing so far, the pipeline is quite full.

First fund was undersized but we didn't compromise by going to smaller companies. We did it the hard way, we didn't have enough money so we borrowed money from the bank and then looked for co-investors.

Our view is the world is very used to consumer electronics and has seen less transformation in the industrial sector. When you start automating, you need a whole bunch of electronics. You talk about electronic vehicle now but a few years back it was a rear-camera in your car.

Going forward, there will be servers-on-wheels. So that's what people are missing. Mission critical electronics delivery on the global supply chain, that's what Southeast Asia has always been good at. That electronics, industrial, automotive, medical - that whole boom is still happening. And so, we're looking for companies to participate in that future.

What's your investment strategy then - do you seek control for all your deals?

We like control. But there are some great companies who do not want to sell control and we understand why. It's a case-by-case. If it's a good company which has grown so much in the past, who are we to say that it's not good? We'd like to partner with the company to grow even further. So as long as the alignment is there, we're good. By and large, we like control, but we also like sector leaders, so when we find one and we think can make money and work with the entrepreneur, we'll do it.

You were with Baring Private Equity Asia before. So how has it been like starting your own PE firm?

I spent a lot of time in the US and Southeast Asia. I'd like to look at the \$200 million type funds and \$40 million type equity checks. There's inefficiency and a lot more work in the sector, but I saw the opportunity. I also think that in Southeast Asia, no one is serving the industrial tech space. I honestly believe that's where we'll be making a lot of money. Look at the US in the 80s, 90s and 00s in Europe, a lot of industrial companies have actually excelled and I think the foundation in Southeast Asia is here but no one cares about it.

It's a niche industry that you're investing in.

It's niche because no one understands it very well, but as we make more investments, people will realise that middle market industrials in Southeast Asia is a very big part of the economy. And it's not a startup industry, it's a 40-year industry with over \$1 trillion [that has] gone into it.

So are valuations realistic in this sector?

I'm still getting five times EBITDA and below. People are realistic, and you'll be surprised that many founders actually care about the people that they bring into the business. And hopefully we have a reputation for treating people well, hence people like to work with us - that's our differentiating franchise.

What's next for Novo Tellus? Are you looking to do more deals this year?

We've capital now and actively looking at a few [investments] right now.