

Five ways private equity can capitalise on Industry 4.0 in S-E Asia



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Technology world: A customer has a QR code scanned from a smart phone at a grocery store in Bangkok. South-East Asian T&I benefits from key global megatrends that drive the Industry 4.0 economy. — Bloomberg

THE massive disruption that Industry 4.0 brings has already begun in South-East Asia.

For the uninitiated, Industry 4.0 is the current trend of automation and data exchange in manufacturing technologies. It includes cyber-physical systems, the internet of things and cloud computing.

There are high stakes, with up to US\$1 trillion of gross domestic product opportunity available to Asean as it embraces digitalisation, automation and industrial integration, according to Bain.

But how can private equity best take advantage of the massive industrial shift that will take place in the region over the next decade? What sectors stand to benefit from Industry 4.0, and what private equity (PE) capabilities are necessary to invest in this great transformation?

“For a start, the technology and industrials (T&I) sector provides the software, chips, engineering and services that power digitalisation across the globe, and not just in South-East Asia, ” says Novo Tellus founder and managing director Loke Wai San.

“Furthermore, the T&I sector itself stands to benefit from digital transformation. As the region’s industrial and manufacturing core embraces increasing automation, integration and digital innovation,

Novo Tellus Capital Partners is a private equity fund focused exclusively on South-East Asia’s T&I sector, and believes that T&I will be the epicentre of Industry 4.0



Toh: South-East Asian T&I has enjoyed almost 40 years of active participation in the global economy.

Based in Singapore, Novo Tellus primarily makes control buyout investments in small and medium-sized companies in South-East Asia. The firm invests in a range of transaction types, including: privatisations, management buyouts, recapitalisations, corporate spin-outs and growth equity.

It adopts “buy and build” investment approach, and seeks to create value by bringing its team’s extensive company-building experience to its portfolio platforms.

Novo Tellus partner Keith Toh says that South-East Asian T&I has enjoyed almost 40 years of active participation in the global economy.

Starting in the 1970s and continuing today, the sector has attracted over US\$500bil of cumulative foreign direct investment, bringing with it the long-term diffusion of engineering talent, industrial scale, supply-chain infrastructure and world-class production capabilities into the region.

“Today, the T&I sector sits at the forefront of global technology and industrial production. T&I accounts for the biggest share of Asean’s exports.”

“It attracts sponsorship from leading global innovators, such as Apple, Facebook, Google, Dyson and Tesla, to name a few,” says Toh.

More importantly for PE investors, South-East Asia’s long history of economic development has created a vast ecosystem of over 20,000 small and medium-sized enterprises (SMEs).

These SMEs have been battle-tested by decades of global competition from major economies in the sector, including Japan, Taiwan, South Korea and China.

Thus Novo Tellus believes that this is a compelling opportunity for private equity investors

For skilled PE investors looking to back Industry 4.0 in South-East Asia, this large and vibrant SME ecosystem presents a compelling opportunity. Novo Tellus gives give reasons why:

1. The sector is deeply underserved by PE. Over 75% of companies have never had a sponsor, and over 70% cite PE as a preferred financing source, our research shows. As a result, many companies are available for investment at valuations well below typical regional PE prices.

This is helped by the size of the market: the 20,000+ companies in this segment represent an opportunity far larger than the entire large-cap PE market (companies with US\$1bil+ revenue) in South-East Asia.

2. South-East Asian T&I benefits from key global megatrends that drive the Industry 4.0 economy, such as the rise of smart factories and the spread of 5G, the industrial Internet of Things, autonomous driving and artificial intelligence.



Loke: The technology and industrials sector provides the software, chips, engineering and services that power digitalisation.

In addition to producing massive volumes of digital products and services for global markets, the sector is increasingly benefitting from rising domestic consumption – South-East Asia’s 500+ million consumers and 170,000+ enterprises are a growing segment of buyers of T&I output.

3. There are big Industry 4.0 opportunities available to regional SMEs, which will deliver increased productivity, higher-valued capabilities and lower costs.

Surveys show that companies in the sector are already receptive to digital transformation: upgrading technology and production equipment tops the list of desirable investments for companies in the segment.

4. The T&I sector’s longstanding relationships with global multinationals and its long-established trade neutrality gives it geopolitical advantage.

South-East Asia has emerged as a clear beneficiary of the manufacturing diversion resulting from US-China trade tensions.

5. The T&I sector has compelling deal catalysts for PE investments. We estimate that over 60% of companies in the sector are over 20 years old and face succession dilemmas, as many are still founder led and have no clear liquidity or long term stewardship plans.

In short, what Novo Tellus sees is an exciting opportunity for PE to invest in the digital transformation of Southeast Asia. But what will it take to succeed?

It believes that PE players need five key capabilities to realise the full potential of the region's large, fast moving T&I sector:

1. Sector expertise – the T&I SME sector is large, fragmented and fast evolving. Strong sector knowledge and relationships are needed to access and develop opportunities in a space that is not well covered by advisors, investment banks and research analysts.

2. Local mid-market capabilities – the 'sweet spot' of South-East Asia's T&I sector is the mid-market, where companies from US\$10mil to US\$1bil in revenue form the backbone of the region's production economy.

Local mid-market transaction and portfolio management skills are essential for executing investments in this dynamic space.

3. Industrialist vision – mid-market companies in the T&I sector have often built good track records of stability and profitability. But they face challenges in visualising growth that capitalizes on Industry 4.0 and related megatrends.

It takes experience and industry knowledge to help management teams build and realize an 'industrialist' vision to grow companies in this market.

4. Technical expertise – Industry 4.0, cloud computing and 5G are powerful growth drivers in this segment, but they demand deep technical expertise and experience to properly operationalise.

To make the most of growth opportunities, PE investors must have strong technical skills and work effectively with management to create realistic product roadmaps and effective commercialization approaches that they need to succeed.

5. Operational capabilities – to transform companies in this segment, PE investors must be able to solve management succession challenges, upscale production and drive R&D investment.

Operational skills and experience are vital to achieve this.

Thus Novo Tellus opines that successful PE investing in this compelling – but complex and fragmented – sector demands highly specialised expertise and strong local relationships.

This, among other factors, may explain why the sector remains so deeply underserved by PE today, despite its size and attractiveness.

TAGS / KEYWORDS:

Five , Ways , Private , Equity , Capitalise , Industry 4.0 , Southeast Asia ,