



# **A Case Study Review of Strategic Acquisitions of Synergic PLC**

**Staff Development Unit  
Faculty of Commerce and Management Studies  
University of Kelaniya, Sri Lanka**





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Strategic Acquisitions of Synergic PLC*

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Synergic PLC is a hypothetical name proposed for this real life scenario as to satisfy information disclosure principles and ethics.

## **Acknowledgment**

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## **Preface**

This case study on “A Review of Strategic Acquisition of Synergic PLC” is presented to the reader comprising largely the undergraduate student community in Sri Lanka with the expectation that it will make the undergraduate students aware on the practical experience in the real world with reference to different theoretical aspects attributed to their relevant subject areas in the curriculum.

In undertaking an extensive analysis of this case study we were mindful of the need to address some of the gaps in relation to theoretical explanations as well as practical application. With that we have taken the initiative to include strategic models including SWOT analysis, value chain, Ansoff Matrix with its application to the company together with relevant industry reports.

Analysis of this case study is about the application of theoretical models which are applicable in different situations suitable with regard to strategic acquisition of Synergic PLC as well as analyzing the future prospects of the company.

The primary objective of this case study review is to make available to our readers a comprehensive analysis of a selected company with a Sri Lankan Flavor.

## **Executive Summary**

Synergic Holding PLC initiated operations in 1991 as a software development company. It was incorporated as a private limited company in 1998 and obtained a listing in the Colombo Stock Exchange in June 2011. Soon after the incorporation they became the sole authorized distributor for DELL Computers in Sri Lanka. Gerrys Synergic (Pvt) Ltd started as a joint venture with Gerrys Holdings (Pvt) Ltd in Pakistan, fulfilling Mr. Alok Pathirathne's (the founder of Synergic Holdings PLC) dream of 'going global'.

Synergic Company's move towards furniture retail, from IT related activities was the first instance they adopted the diversification strategy. At present the Synergic Holding PLC is rated as one of Sri Lanka's most energetic and aggressive conglomerates. The diversified key sectors are Information and Communication Technology, Healthcare, Retail, Financial Services, Automobiles and Leisure. This case study specifically underlines the strategic acquisition of Rovel PLC which took place in the year 2014.

Rovel PLC initiated its operations in 1989, in a small retail outlet. Today, Rovel's flagship department store is a 36,000 square foot, lavishly appointed store and it owns 20 other outlets in many strategically important locations.

Rovel operates at the top end of the retail fashion market, where it has carved out a niche through a highly focused approach targeted at the upper-middle and higher-income groups, Rovel has maintained its leadership position by providing a modern, world-class retail environment that has become the standard for the South Asian region. Rovel is not only Sri Lanka's leading fashion brand, but with a wide array of products, it is also Sri Lanka's only genuine department store. Rovel has achieved the

status of an iconic brand with its tireless ability to reinvent itself at regular intervals.

The recent acquisition of Rovel PLC by Synergic Holdings has created a major upheaval amongst the business community and the media. One main intention behind the said acquisition was Synergic's motive of working with Parkson, the largest shareholder of Rovel. However the withdrawal of Parkson from Rovel PLC left Synergic's efforts futile. Also after the said acquisition, Synergic's excessive borrowings have resulted with its Fitch Rating being downgraded by two notches. The boards of directors now are contemplating about the survival of the company with its existing structure.



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## **1. Overview of the Company**

Synergic Holding PLC initiated operations in 1991 as a software development company. At present the SH is rated as one of Sri Lanka's most energetic and aggressive conglomerates. SH has diversified its position in several domestic growth oriented business sectors. The diversified key sectors are Information and Communication Technology, Healthcare, Retail, Financial Services, Automobiles and Leisure. The SH currently provides employment to over 6,000 individuals generating a turnover of more than USD190mn. The SH was incorporated in 1998 as a private limited company and obtained a listing on the Colombo Stock Exchange in June 2011. The SH's representations and strategic alliances with reputed global institutions and large multinational corporations confirm its unparalleled local stature across its diverse fields of operation.

### **1.1 The Strategic Keys of the SH**

#### **1.1.1 Vision**

To be the most preferred and trusted product and service provider delivering high quality solutions to the corporate and retail sector with a view to enhancing shareholder value and revolutionizing industry competencies.

#### **1.1.2 Mission**

To be the best, employ the best and reward the best with a view to reaching the highest market expectations and becoming the most valued corporate enterprise.

#### **1.1.3 Values**

SH employees are the value drivers. The key value drivers are reliability, trust, constructive conservatism, esprit de corps and integrity among members, business partners, and community in the company. The SH have created a transparent organizational culture through high performance culture, innovation, integrity, human capital, success, accountability, corporate responsibility

and simplicity in ideas flourishing, people thriving and success prosper.

#### ***1.1.3.1 High Performance Culture***

In SH, a “can do” attitude has proven to be the key performance driver. The company committed to a result-oriented and customer-centric culture where success is shared and celebrated across the SH. They place customers at the center of their activities and they hold themselves responsible to deliver what they promise in keeping with customer needs with a determination to excel and a commitment to action.

#### ***1.1.3.2 Innovation***

The SH constantly challenge conventional wisdom and aim to create an exciting and innovative culture, stimulating out-of-the box thinking and developing innovative solutions for their customers. The group-wide innovation contest is just one of the ways in which they promote this creativity.

#### ***1.1.3.3 Integrity***

SH members act fairly, honestly and show respect and value all individuals for their diverse backgrounds, experiences, styles, approaches and ideas. They believe in ethics and transparency in all our dealings.

#### ***1.1.3.4 Human Capital***

SH nurture people and consider them as most important asset. They benefit from the diversity of the business and their people by working together to achieve success with clear recognition, utilization, retention of good talent and appreciation of employee skills and talents. They treat all their staff with utmost respect and dignity, provide opportunities for career enhancement and cross fertilize for disciplined valour.

#### ***1.1.3.5 Success***

SH ensure that the maximum return is provided to all stakeholders.

#### ***1.1.3.6 Accountability***

SH take responsibility for their actions and results and keep promises and commitments. They embrace the belief that the element of accountability starts with “me”.

#### ***1.1.3.7 Corporate Responsibility***

They have a fiduciary duty to their customers and business partners. They care for the community and the environment, delivering the maximum benefits of responsible business practices and take responsibility to protect them. At SH Corporate Responsibility goes beyond words where they strive to think and act as a good corporate citizen whilst supporting worthy causes and CSR projects

#### ***1.1.3.8 Simplicity***

The simple value of “effectiveness” is embodied enabling them to deliver effective solutions and results to their customers. It is also a SH’s philosophy – having simple processes, procedures and activities in place to take decisions quickly and rapidly transform ideas into fruitful results.

#### ***1.1.3.9 Dynamism***

SH possess the flexibility and dynamism required to adapt to increasingly changing markets. Their spirit comes from rare tenacity and dynamism, a Group seeking to be the market leader while seizing opportunities so that new frontiers open for greater rewards.

## **Teaching Note**

*Vision, mission and values are key elements of an organization's strategic planning. The **vision** sets out what the organization wants to accomplish, and should inspire members, staff and supporters. The **mission** typically describes what the organization does to achieve its vision. **Values** influence everything an organization does, as well as its relationships with stakeholders and its reputation. Values may be expressed as beliefs, guidelines or rules, and may be set out in a code of conduct. In this case how Synergic PLC made their vision, mission and values in line with the new industry with the acquisition of the Rove PLC can be analyzed.*

## **2. Synergic Holding PLC- Environmental Analysis**

Any organization, business and institution are operating under its specific environment. As a consequence, they need to understand and analyze thoroughly those factors in order to achieve the overall goal of the organization. The business environment of an organization is twofold:

- Internal Environment
- External Environment

### **2.1 Internal Environment**

Internal environment of an organization can be analyzed by using tools such as SWOT analysis and Value Chain Analysis introduced by Michael Porter.

#### **2.1.1 SWOT Analysis**

Synergic Holding as one of largest conglomerate in Sri Lanka that dominates their markets has a finite supply of manpower, production capacity and capital. Evaluating their strengths helps them to determine how to allocate these resources in a manner that will result in the highest possible potential for revenue growth and profitability. The management team examines where the company can compete most effectively. The company often

discovers it has competitive strengths that have not been fully utilized in the past. In addition to that a realistic assessment of weaknesses also prevents strategic blunders like entering a market with products that are clearly inferior to what well-entrenched competitors are offering. Continuous improvement in all areas of their operations is an important aspect of staying ahead of competitors.

Synergic PLC is also in the process of continuously seeking out new opportunities, including new potential customer groups, broader product distribution, developing new categories of products and services and geographic expansion. And also they are well aware of threats that will cause serious damages to their operations.

Management team uses SWOT analysis to identify strengths, weaknesses, emerging opportunities and threats.

SWOT analysis for the Synergic Holding Private Limited is depicted in *Annexure 01*.

### **2.1.2 Value Chain Analysis**

To better understand the activities through which the Synergic Holding can develop a competitive advantage and create shareholder value, it is useful to separate the business system into a series of value generating activities referred to as the value chain. The idea of the value chain is based on the process view of organizations, the idea of seeing a manufacturing (or service) organization as a system, made up of sub systems each with inputs, transformation processes and outputs. Inputs, transformation processes, and outputs involve the acquisition and consumption of resources - money, labour, materials, equipment, buildings, land, administration and management. How value chain activities are carried out determines costs and affects profits.

Porter identified primary and support activities as shown in *Annexure 02*.

Synergic Holding can apply value chain model as a useful analysis tool for defining core competencies and the activities in which it can pursue a competitive advantage as follows:

- **Cost Advantage** – by better understanding costs and squeezing them out of the value-adding activities.
- **Differentiation** – by focusing on those activities associated with core competencies and capabilities in order to perform them better than do competitors.

Synergic PLC can apply this value chain concept for their range of businesses in order to deliver a valuable output to the customers.

## **2.2 Industry Analysis**

Synergic Holding PLC, represents a diverse number of industries which will be discussed in detail in the later chapters. An overview and an analysis of these industries are appended in *Annexure 03*.

### ***Teaching Note***

*Through the environment analysis strengths and weaknesses of internal environment and opportunities and threats of external environment can be identified. In this case through analyzing these factors Synergic PLC can determine how they can leverage their strengths to invest in new opportunities and avoid the threats come from the external environment while minimizing their weaknesses can be analysed. In addition to that how value chain can be applied in order to establish a low cost structure within the organization and most importantly, activities through which the Synergic Holding can develop a competitive advantage and create shareholder value also can be analysed.*



### **3. The Unpretentious Beginning of Synergic Holding PLC**

A young talented boy from Ananda College of Colombo joined with an IT giant John Keells with the intention of becoming a successful IT professional. Within nine years of time span, he managed to secure a managerial position in John Keells. During that period he grabs knowledge about in and out of the computer field and laid the foundation to become a successful entrepreneur in software development industry. While working there, he was dreaming about his own software firm like John Keells. That was the idea which stimulates this young entrepreneur to setup Synergic Information Technology (Pvt) limited (SIT) in 1991 with the support of his few colleagues at John Keells.

Even though few appraised his decision, most of his colleagues were laugh at Alok Pathirathne as they think that it is not a good decision to leave such a valuable job and start a new company when country was not doing well. But Alok Pathirathne loves to take risk as he knew that high risk would results high returns. His parents also very much positive about his new move and it helped him to gain confidence to take up the challenging decision. Since the inception of Synergic, Alok Pathirathne used to continue his risk taking behavior.

Alok approached the markets in a focused manner. So the Synergic company was started in a 700 square foot space in a building in Kolpitty with a capital of Rs.1 million and 12 employees. In the first year they had about Rs.6 million in turnover.

At the beginning Alok Pathirathne and his loyal team was not anticipated about profits. Their aim was to strengthen the company to stand up by its own and create a good & valued brand name. Alok Pathirathne had the belief of many new entrepreneurs anticipates profits and a luxury life from day one

and that lead to disappointments when company fails to generate profits at the beginning. So he never forgets to thank his initial team mates for not putting him in to that mindset.

It was February 22 of 1991 and the employees of the Synergic are working towards a big function at the company premises. That is not because of anything it was the day of Alok Pathirathne's 27<sup>th</sup> birthday. Employees and the Alok with his family members made that event a memorable day with lot of joy and the gratitude for their success.

#### **4. Initial Expansion of the Business (1998 to 2005)**

A year after Synergic Information Systems established, they ventured in to start Synergic Trading where the company has the sole authorized distributorship for DELL computers in Sri Lanka. In 1995 Synergic Computers (Pvt) Ltd was incorporated specializing in marketing and supporting a variety of networking and power protection products, through a locally established dealer channel. Synergic International (Pvt) Ltd (SIL) incorporated in 1997 which is a formal partnership with Dialog Axiata PLC. This partnership aided Synergic in terms of providing greater local reach since Dialog had strong growth potential and marketability. IL also act as the regional distributor and warehouse managers for NOKIA.

Alok & the team then started Synergic International as an authorized partner of Dialog GSM to provide mobile connections. Then ventured on to setup ABACUS International Lanka in 1998 as a joint venture with Abacus International Limited, which is Asia Pacific's largest computer reservations system. 1998, Synergic Holdings was incorporated to consolidate all subsidiaries under Synergic.

The telco venture started, when Synergic in collaboration with Dialog Axiata PLC, offered corporate and individual Dialog

GSM packages in 1998. The Synergic still has maintained its position to stand as one of the leading business partners for Dialog Axiata PLC. Year 2000 holds an important landmark for Synergy when the exclusive national distributorship of 'Nokia' was obtained. With that synergic synonymous to Sri Lanka's telecommunication sector with Nokia, led the mobile handset market. The telco market of synergic stands strong with over 2,000 island wide retail points priding itself on its commitment and quality customer service.

Alok's next dream was to go global, hence started Gerrys Synergic (Pvt) Ltd., as a joint venture with Gerrys Holdings (Pvt) Ltd., in Pakistan. Its operations are centered in Pakistan and the company is involved in marketing and selling of DELL and Cisco products, while having the largest DELL distributorship. Then the Synergic Australia was located in Melbourne established in 2000 for the development and marketing of software products specifically targeted at the healthcare and education sectors. It is responsible for promoting a range of e-business application developments and professional services such as business analysis, Internet, Intranet and Extranet. Meanwhile, E-solve Trading (Pvt) Ltd., was incorporated in 2002 in Singapore for developing and marketing software products and other trading activities. Further Synergic Solar (Pvt) Ltd was also started in 2002.

## **5. Diversifying the Business**

Diversification occurs in a business when it develops a new product or expands into a new market.

### **5.1 Rationale for Diversification**

A business may opt for diversification in order to minimize risks during economic downturns. For example, provided that Company A is well diversified, losses incurred by a business enterprise 'X' which is taking a hit in the market, will be offset by business enterprise 'Y', as long as 'Y' is not in the same industry as 'X' and is not experiencing the same economic turmoil. Further a business may also use diversification as a growth strategy.

### **5.2 Types of Diversification**

Diversification can take various forms:

- Related diversification

If a company diversifies along business lines related to each other, it is called related diversification. This is further subdivided into two areas:

- Concentric diversification

In this strategy a firm is able to leverage its technical know-how to the other products or industry.

- Vertical Integration

This is the process of moving along the same supply chain. If moved forward, it is called forward integration, and backward integration if moved backwards.

- Horizontal diversification

This is the process of development into activities which are complementary to present activities. These can also be competitors' activities.

- Unrelated diversification

This is the process of moving into an unrelated area of business and is also known as conglomerate diversification.

### **5.3 Ansoff Matrix**

The Ansoff Growth Matrix is a tool that helps businesses decide their product and market growth strategy. Ansoff's product/market growth matrix suggests that a business' attempts to grow depend on whether it markets new or existing products in new or existing markets. This is depicted in *Annexure 04*.

The output from the Ansoff Matrix is a series of suggested growth strategies that set the direction for the business strategy. Synergic Company's move towards furniture retail, from IT related activities was the first instance they adopted the diversification strategy.

Synergic Company ventured into furniture by Retail One (Pvt) Limited, which is quite different to the IT related activities the company has been dealing in because, when Alok was holidaying in Bangkok, he came across 'knockdown furniture' at a supermarket. By this time a lot of apartment complexes were mushrooming and he saw a big need for 'functional furniture' in Sri Lanka. Hence he brought this new concept in furniture to the country, where chairs, tables, drawers and any other furniture item could be fixed within a short time. The company managed to create a brand for lifestyle furniture and the wanted to add more new products and expand the store. The vision of the Alok is to have a similar store as IKEA.

Emboldened by its successful diversification strategy, the company setup Synergic Properties in 2005 to oversee its diversification into property development.

At a meeting in 2005 CFO highlighted that they are growing presently at an annual rate of 30%. Synergic is an asset rich and a cash rich company secured about a five billion rupee turnover annually after these diversifications. Further, Alok emphasizes that they are very healthy when compared to industry statistics and in terms of import statistics we are the largest computer and mobile phone importers. Every seven out of ten phones are imported by our company. In addition to that Alok highlighted that they want to grow faster and bigger in a short period of time. So the company should acquire businesses in similar industries or acquire related businesses in order to have the synergetic benefits.

## **6. Hostile Growth Begins (2006 to 2009)**

This three-year period was indeed a time of strategic and focused growth for Synergic which helped elevate its corporate image to new heights. Synergic embarked on its momentous journey into the Retail sector with the acquisition of Uni Walkers (Pvt) Ltd in 2006 which is focused on importing imaging and printing equipment consisting of renowned brands such as NEC and XEROX. This development initiated the acquiring of several global heavyweight brand names across the sub sectors of Consumer Electronics, Branded Apparel and Furniture, which helped expand their overall international brand portfolio. Their retail operations across the Consumer Electronics sub sector have had superlative growth to present possess an impressive network of over 160 Synergic Retail outlets island wide, covering the length and breadth of the country.

The expansion drive is aggressively continuing to bring the network up to 220+ showrooms by the end of 2013. Panasonic, Samsung, Nokia, Dell, Apple, Candy, Russell Hobbs, Kelvinator are some of the giant global brand names within its fold of Consumer Electronics for which Synergic was appointed authorized distributor.

“Aggressiveness is in our genes. We are hands-on, focused and flexible when required to constantly seek opportunities for organic growth as well via acquisitions” was a main slogan emphasized by Alok every time in many business interviews. As a result Synergic ventured into the mobile phone sector in 2007 with Nokia as Synergic Communications (Pvt) Ltd which is the only authorized distributor for Nokia mobile phones and accessories in Sri Lanka.

## **7. Synergic Sprints (2010)**

The SH's synergies proved to be sound when Synergic consolidated Subasiri Hospital Holdings as a subsidiary after increasing its shareholdings in December 2010. Another dazzling point during the same year was the acquisition of another world class automobile brand – ‘Ford’. By obtaining the Ford Dealership Synergic further strengthened its presence in the Automobiles sector, serving different customer segments with its wide range of vehicle products. Ford has been well accepted in Sri Lanka, and its keen acceptance by the consumers has been the impetus for Synergic to in collaboration with Ford set up its very own state-of-the-art 3S facility targeting to set new benchmarks with automotive dealership experience in line with Ford's global standards.

As a leader Alok is attending each and every meeting of the business and but find it difficult to manage his time with increased number of businesses to the Synergic. However most of the instances Alok tend to dominate at the board meetings which led to implement the Alok's decision. When he is dreaming, his next step a novel idea came to his mind when he was at a hospital to consult a doctor. He saw the potential of healthcare industry in the country. Then the top personalities together discussed thoroughly the ways of entering into the healthcare sector. After many arguments, counter arguments,

lengthy board room presentations, analysis in different angles came to a conclusion and then the Group's performance proved to be sound when Synergic consolidated Subasiri Hospital Holdings as a subsidiary after increasing its shareholdings in December 2010. Since Synergic had a good relationship with Banks they were able to manage these acquisition through bank loans.

Since the inception Alok had the intention of diversifying its business to different sectors since he knew that it will lead to minimize the risk as a company. So, exploring into different fields of business is a never ending task of Alok and dreamed about other lucrative areas of business. As a result another dazzling point during the same year was the acquisition of another world class automobile brand – 'Ford'. By obtaining the Ford Dealership Synergic further strengthened its presence in the Automobiles sector, serving different customer segments with its wide range of vehicle products. Ford has been well accepted in Sri Lanka, and its keen acceptance by the consumers has been the impetus for Synergic to in collaboration with Ford set up its very own state-of-the-art facility targeting to set new benchmarks with automotive dealership experience in line with Ford's global standards.

Alok continuously dreamed about the growth of the group. He thought about the areas of related services with regard to financial sector and came with the idea of field of insurance. Consequently, finance sector cemented its controlling stake of Asian Alliance, a renowned insurance solutions provider to the life and general sectors of Sri Lanka. This was acquired in 2011. Alok, being a board member of some financial institutes of the country, is very well known the profitability and growth potential of financial sector of the country. He was thinking ways to come true his next gigantic leap in to financial sector. Synergic's footprint in the finance sector was initiated with the acquisition



of Capital Reach Holdings, there after renamed as Synergic Finance PLC.

Alok is working hard even he has to spend many sleepless nights for the growth of the group. One day while Alok was reading a news article the idea came to acquire and initiate renovation at Ceysands Hotels & Resorts. By tying up with the Thailand based Centara chain of Hotels and Resorts, the new hotel launched as Centara Ceysands Hotels & Resorts in the latter part of 2013.

Alok wanted to further improve the retail sector which leads to increase the world renowned brands. For this purpose they had a meeting with his board of directors and inquired about ideas of increasing the brand portfolio. The idea of obtaining franchises was come up. In this effort a special attention was given to Branded Apparel in growing its portfolio with the exclusive franchisee status and able to qualified for worldly accepted brands like ‘Nike’, ‘Giordano’ and ‘Mango’.

## **8. Endless Journey of Growth (2011- 2012)**

It is a widely accepted talk that the leisure property sector has been the next high growth potential region after the cessation of war. Synergic by no means would miss such a promising opportunity as this one. Synergic acquired and initiated renovation at Ceysands Hotels & Resorts. By tying up with the Thailand based Centara chain of Hotels and Resorts, the new hotel will be launched as Centara Ceysands Hotels & Resorts in the latter part of 2013.

A 224-room five-star Movenpick City Hotel also initiated construction in 2011 with plans for completion by the latter part of 2014.

Finance sector cemented its controlling stake of Asian Alliance, a renowned insurance solutions provider to the life and general

sectors of Sri Lanka. This was acquired in 2011. Special attention was given to Branded Apparel in growing its portfolio with the exclusive franchisee status for 'Nike', 'Giordano' and 'Mango'.

A loud applause for Synergic with turnover crossing LKR20 bn in FY2012. International business partnerships strengthened with Branded Apparel emerging to the limelight again after the acquisition of exclusive distributorship rights for 'Mothercare' and the wristwatch portfolios of 'Emporio Armani', 'Fossil', 'DKNY', 'Diesel' and 'Adidas'. Synergic's stature in the international market was further elevated when Actis Investments, a pan-emerging markets private equity firm, entered Asiri Hospital Holdings via a private placement. International Finance Corporation, a leading global development institution, too entered Synergic's international stakeholder list to assist finance the leisure and retail sector projects.

Synergic ramped up the financial cluster with the acquisition of Synergic Stockbrokers, former Arrenga Capital, in April 2012 to provide a fully-fledged financial solution all under one roof. Synergic's status and business confidence was given a further lift after DEG and FMO, global investment and financial corporations, each acquired an equity share in Synergic's insurance business. The international faces across the Group have created synergies with the global representation sharing in their knowledge and expertise pushing Synergic in line with global standards.

***Teaching Note:***

*There are mainly three levels of strategy, viz. functional level strategies, business strategies and corporate level strategies. Diversification strategy adopted by the Synergic falls under the corporate level strategies of an organization.*

*Principal concerns of corporate level strategy are to identify the businesses in which a company should participate, the value creation activities it should perform in those businesses and the best means for expanding or contracting in different businesses including mergers, acquisitions and diversifications with the ultimate goal of maximizing the long run profitability of the company (C.W.L. Hill & G.R. Jones).*

## **9. Synergic Stable thinking forward belief continues (2013)**

Group's plethora of global brands continues to grow with the recent sole distributorship rights for 'Charles & Keith' and upon the brand, 'Splash' being acquired for Sri Lanka, which will further establish Synergic in its vision to be a key player in the Retail space.

Synergic's strategy has all along been to focus on the key growth sectors of the economy. It is along these lines that key thrusts have been made into the sectors of Retail, Healthcare, ICT, Automobiles, Financial services and Leisure. While operating synergies across all its group subsidiaries which help spur growth within the group and by holding fast a vision which is embedded in being an organization with a forward thinking view, Synergic is well placed to achieve its objectives to the benefit of all its stakeholders.

While growing steadily this was indeed a time of strategic and focused growth for Synergic which helped elevate its corporate image to new heights. Alok needed more improvements within the group. One day one of directors came up with the idea of developing its own businesses rather going for further acquisitions. But many were opposed and had many arguments. After lengthy discussions in few weeks at board room and a corner of a coffee shop, Synergic came to conclusion of a remarkable acquisition. It is during 2009, the Synergic embarked

on its momentous journey into the Retail sector with the acquisition of Uni Walkers (Pvt) Ltd. This development initiated the acquiring of several global heavyweight brand names across the sub sectors of Consumer Electronics, Branded Apparels and Furniture, which helped to expand overall international brand portfolio.

Since they have acquired many companies with the existing funds CFO highlighted the fact that company now require more funds to the business. With this backdrop Synergic was considered different alternatives of raising funds specially to issue shares or debentures. Further he highlighted the danger of increasing debt capital to the board. At the same time chairman of the Synergic already had the intention of going for public (IPO) and he was in the opinion that was the high and right (2011) time to issue shares. Because, at that moment there were number of IPOs came to the Colombo Stock Exchange (CSE) representing diverse sectors. So chairman gave this responsibility to the Chief Financial Officer (CFO) of Synergic. As the first step Synergic successfully complete the private placement of 14 Mn shares at a price of Rs.72 which later split in the ratio of 1:10.

Further, at the meeting Alok outlined the primary objective of the IPO as to reduce the debt incurred on these investments as well as on borrowings taken for increased working capital requirements. The objectives and the way that he was intended to use the proceedings from the IPO were as follows:

- To acquire especially in the financial and leisure sectors companies including to set up/ acquire a stock-broking company
- To refurbish the Synergic Resort (Pvt) Ltd which was purchased last year
- To start a 5-star hotel which will be located in Colpetty area

During the meeting one of the directors questioned about the compliance to the rules and regulations of the CSE and the Securities and Exchange Commission of Sri Lanka (SEC) specially the area of corporate governance. Since the entire directors were not aware about the corporate governance requirements, board decided to have a report on corporate governance requirements and compliances of Synergic. At the same time CFO briefed about corporate governance and the existing structure of the board as follows:

Executive Directors:	6
Non-Executive/Independent Directors:	3
Total number of Directors:	9

List of directors' and their interest in the shares of the company as at 31st March 2014 is appended in ***Annexure 05***.

After the meeting while Alok was in the elevator he heard that some employees were talking on these diversification and their opinion was that too much of diversification would lead to a tragedy and the company should focus the growth and the motivation of the existing business portfolio and the employees.

Afterward CFO had a meeting with one of the leading investment bank and stock brokering firm in order to get some initial instructions to the share issue. Finally they arrived with a price of Rs. 29 per share (after share split of 1:10) to raise four billion and thirty one million rupees (Rs 4.31 billion) by issuing 139 million shares. When it came to the allocation of shares, apart from complying with the rules of SEC Synergic had allocated shares to the employees by giving loans. Since the issue of shares got over subscribed, Chairman and key personalities of the Synergic went to the trading floor of the CSE in the first day of trading with numerous confident. But unfortunately the share prices went

down to the lowest price of Rs. 16 at the first day itself. This was the first IPO where price has reduced at the initial trading day and thereafter in that year indicating awful thoughts for the stakeholders.

“With these diversifications Synergic should have a sound fund requirement and capital structure” was the fact emphasized by the CFO to the board of directors. Because currently it is vital to do the refinancing of shortterm non-bank/bank borrowings and restructuring the balance sheet to reduce prevailing funding mismatches. Further he stressed that we can have the advantage of recent reduction of interest rates. At the same point Synergic decided to issue of five million rated unsecured redeemable debentures at the face value of LKR 100/- each to raise Sri Lanka rupees five hundred million. With these busy schedules Alok attended two months long training program in USA and when he was planning to attend the training, he advised CFO and board of directors to overlook the company.

## **10. Period of 2013- 2014**

The retail sector is the one of the main sector focused by the Synergic for its future developments and it searched opportunities from the market. Because the sector stayed ahead of the market growths curve while maintaining its market position amidst challenging market conditions. So Synergic believes that the retail sector will grow at an alarming rate in the future as well.

With these stimulations Synergic acquired a strategic stake of 44.5% in popular fashion retailer Rovel PLC for Rs. 2.7 billion from Tara, Asith and Ruvi Gunarathne the founding members of

the fashion retailer, triggering the Takeovers and mergers Code. This was financed by HNB by providing 2.7 billion Rupees and they have outlined that as an ideal opportunity to demonstrate the bank's commitment to the Synergic Group, a valued relationship to the bank. But before HNB Synergic has approached few other banks and failed to proceed with them as they were not that confident about the acquisition of Rovel.

### **10.1 Background of Rovel PLC Acquisition**

Rovel started the business as a small venture by Tara Gunarathne, selling clothes from her car boot. Over the years, Tara together with Asith and Ruvi Gunarathne, progressively developed their business to what it is today and have provided customers with an unparalleled retail experience across a chain of 20 retail stores being one of the first to setup a virtual store.

The Financial Statements of the Rovel PLC as at 31<sup>st</sup> March 2014 is given in the **Annexure 06** along with the Synergic Holding.

Synergic currently holds distributorship for leading international apparel and accessories brands in Sri Lanka -- Nike, Levis, Giordano, Mango, Mothercare, Splash, Charles & Keith, French Connection, Dockers, Diesel, Skagen, Fossil, Adidas, Emporio Armani, DKNY and Michael Kors. Synergic is confident that Rovel brand will further grow as it runs with the synergic Retail (Pvt) Ltd.

### **10.2 Analysis of the Acquisition of Rovel PLC**

This section includes a comprehensive appraisal of the acquisition of Rovel PLC and contains a detailed analysis on 6

areas namely investment, strategies, marketing, operations, management and financial aspects.

### **10.2.1 Investment Analysis**

Synergic Holding is a highly diversified company. They are already into the retail sector. They wanted to improve the retail sector which leads to the increase of the world renowned brands. In this effort a special attention was given to Branded Apparel with the exclusive franchisee status and able to be qualified for worldly accepted brands like 'Nike', 'Giordano' and 'Mango'.

With these diversifications Synergic should have a sound fund requirement and capital structure which was the fact emphasized by the CFO to the board of directors.

In this acquisition he stressed on taking the advantage of recent reduction of interest rates and go with borrowings.

They acquired a strategic stake of 44.5% in Rovel PLC for Rs. 2.7 billion and this was financed by HNB providing 2.7 billion Rupees.

Finance done by HNB has been outlined as an ideal opportunity to demonstrate the bank's commitment to the Synergic Group, a valued relationship to the bank. But before HNB, Synergic has approached few other banks and failed to proceed with them as they were not that confident about the acquisition of Rovel. So, Financing done by HNB seizing the opportunities visible shows how far the future growth of this acquisition is apparent.



Tara's perception is that Rovel needs to move to the next level of retailing in order to be competitive, locally and globally. This requires the entry of a larger player with a deep commitment to retailing: which I believe can best be provided by the Synergic Group, with a proven history of dynamism. This perception shows that Rovel is in a necessity of entering into a large player making Synergic acquisition of Rovel a reality.

Synergic holdings being into the retail sector with branded apparels and with their ambition to make the retail sector strengthen, this acquisition of Rovel would support further with strengthening the diversification and thereby reducing the level of risk.

### **10.2.2 Strategic Analysis**

Synergic Retail is in the business of selling branded apparels to customers. As Rovel PLC is also in the same business, they can be considered as competitors. Thus the acquisition of Rovel PLC can be claimed as horizontal integration.

On the other hand this can be considered as vertical integration because available branded apparels at Synergic Retail (pvt) Ltd had the franchise status but with the acquisition of Rovel they can have the Rovel PLC as a permanent distributor. So with the acquisition of Rovel outlets it becomes a forward integration. With that they can position their brands within the Rovel outlets which would give them a synergic effect. Further, they can have a competitive advantage with retail distributorship in tourism. Currently they are into leisure with Synergic properties (pvt) ltd. This sector is booming and so is the textile sector. Therefore,

with these two becoming together Synergic can engage in retail distributorship in tourism.

Rovel is a wellknown company that gives excited and amazing shopping experience. They come up with new fashions tapping into new needs and wants of different customer segments. Synergic is very much interested in diversification, its being their strategy. So, Rovel's amazing shopping experience with innovativeness would support synergic in business diversification.

With this backdrop it is much important to analyze the strategic importance of the acquisition to Synergic. For this purpose directional policy matrix developed by Joseph Guiltinan and Gordon Paul in 1970 can be taken for the analysis. In the directional policy matrix, the vertical axis is used to map business-sector attractiveness and the business strength is plotted against the horizontal axis. The factors used for the industry and the respective business segments can be outline as follows:

**Quantification of market attractiveness:  
Retail Industry of Sri Lanka**

**Table 1: Retail Industry of Sri Lanka**

<b>Factor</b>	<b>Weight</b>	<b>Rank</b>	<b>Value</b>
Market size	27	5	135
Market growth	9	4	36
Consolidation	5	3	15
Vertical integration	5	3	15
Threat from substitutes	7	4	28
Scope for innovation	8	2	16
Product diversity	5	3	15
Patents and copyrights	4	1	4
Margins	7	4	28
Share prices	1	2	2
Cost of capital	3	3	9
Synergies	4	2	8
Social trends	9	5	45
Regulation and legislation	6	4	24
	<b>100</b>		<b>380</b>
			<b>3.8</b>

**Quantification of business strength:  
Branded apparel & accessories retail segment of Synergic holdings**

**Table 2: Branded apparel & accessories retail segment of Synergic holdings**

<b>Factor</b>	<b>Weight</b>	<b>Rank</b>	<b>Value</b>
Market share	20	2	40
Relative market share	8	3	24
Sales growth	5	3	15
Brand loyalty	7	2	14
Product diversity	5	3	15
Positioning	10	4	40
Distribution strength	9	3	27
R&D strength	7	2	14
Patents and rights	2	4	8
Relative employee skill level	4	3	12
Stakeholder interest and backing	4	4	16
Attitude to risk	2	5	10
Margin	7	4	28
Cost of capital	3	2	6
Access to funding	7	4	28
	<b>100</b>		<b>297</b>
			<b>2.97</b>

## Rovel PLC

**Table 3: Rovel PLC**

<b>Factor</b>	<b>Weight</b>	<b>Rank</b>	<b>Value</b>
Market share	23	2	46
Relative market share	8	3	24
Sales growth	4	2	8
Brand loyalty	9	5	45
Product diversity	5	3	15
Positioning	13	4	52
Distribution strength	7	4	28
R&D strength	8	4	32
Patents and rights	3	4	12
Relative employee skill level	1	3	3
Stakeholder interest and backing	4	3	12
Attitude to risk	1	2	2
Margin	6	5	30
Cost of capital	3	2	6
Access to funding	5	4	20
	<b>100</b>		<b>335</b>

Further the acquisition of Rovel PLC is in alignment with the strategic intent of Synergic Holdings and it can be depicted through directional policy matrix as follows.

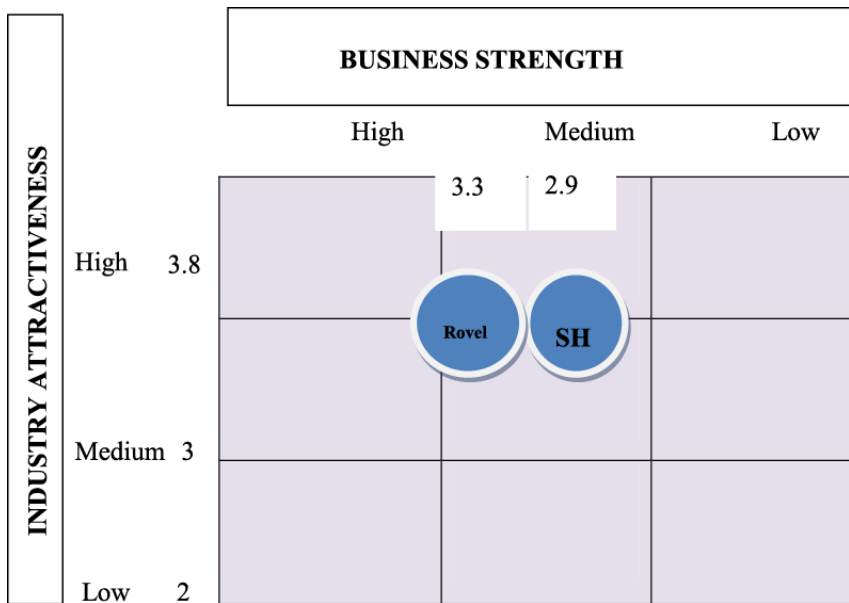


Figure 1: Directional policy matrix

### 10.2.3 Marketing Analysis

With Synergic being into apparel sector including branded products and Rovel being into new shopping experience and fashions Synergic can obtain economies of scale, engaging largely in distribution and marketing.

Rovel is being expanded. But synergic being more dispersed geographically there would be an expansion on emerging markets in fashion. Further, they can take the advantage of opportunity to engage in cross selling as they have several sectors.

Branded world renowned apparels under retail sector and Rovel, both have the same operations. Before the integration synergic just had the brand names but not a place to position it properly. But after the integration they can use that capacity. With Rovel being into selling of clothes, they know how the market demand is. So, it gives economies of scope to synergic.

#### **10.2.4 Operational Analysis**

Synergic can obtain new expertise from talented and trained workforce of Rovel as they were specifically into sales. So Synergic can further strengthen their operations in retail sector. Synergic being into IT fundamentally, there is an opportunity of having IT based solutions for textile Virtual stores have already been implemented by Rovel. This can be further strengthen with IT based solutions being introduced.

Operation target of synergic is to expand the network. Rovel has already well positioned itself. So it would become hassle free for synergic where they have no extra efforts to be made. Simply they have to enhance the existing one. With both Synergic Retail (Pvt) Ltd and Rovel being expanded, operationally both would bring benefits to the company. With all these attempt however, the operating cost would increase.

#### **10.2.5 Management Analysis**

Rovel's management has skills and know-how being in the footwear and textile sector for a long duration. Even though Synergic Holding is in to the retail sector, their expertise would not be much compared to Rovel. So, acquired skills and know-how would lead to further improve the retail sector facilitating their expectations to improve that.

Coordination is an important issue for a successful productive activity. When both engage in marketing, introducing it based solution, Synergic should understand the platform of Rovel, not to make high or low performing standards that make advantages to competitors.

And also synergic being highly diversified company and Rovel being into innovative fashion in footwear and clothing, there is a high potential for continuous change and it would help protect

the investment made and to achieve future cash flows. Since both are energetic and dynamic this would become possible. Nevertheless, in all these fronts, this can increase administration and other overhead costs.

### 10.2.6 Financial Analysis

Rovel's financial position at the time of acquisition can be analyzed using following highlights.

**Table 4: Rovel's financial position at the time of acquisition**

Description	FY 2011/12	FY 2012/13	FY 2013/14	First Quarter of FY 2014/15
Revenue	3,910,023,528	4,532,970,765	4,591,712,096	1,096,067,197
NPBT	197,202,473	177,259,774	239,171,457	(7,009,900)
Total Assets	3,332,492,083	6,031,086,118	6,468,137,130	7,016,220,420
Net worth	1,444,100,556	4,518,962,950	4,694,329,151	4,654,663,718
Gearing	0.86	0.14	0.22	0.27
Leverage	1.30	0.33	0.37	0.51
<i>Net Book Value</i>	<i>1,593,825,762</i>	<i>2,058,589,402</i>	<i>2,229,588,873</i>	<i>3,037,567,747</i>

The funds raised through right issue in 2012 infused 2bn fresh capital to Rovel and these has been used to settle the part of the short term debt capital while balance has been invested in short term investments until they used that for expansion purposes. Even though the investments are made the other income shows a drop of Rs.18.5Mn influenced by the decrease in unit trust income which Rovel has invested the funds collected via a rights issue in year 2013.

The first quarter of the FY 2014/15 for Rovel, reflects a net loss before tax of Rs.7.0Mn impacted by the high administration expenses and deteriorated other income positions. The incline of the administration expenses was mainly contributed by the



provisioning of total financial year salary bill including the allowances and bonuses in the first quarter of the period under consideration.

Total loan amounts of Rovel during last 5 years period

**Table 5 : Total loan amounts of Rovel**

Year	2009/10	2010/11	2011/12	2012/13	2013/14
Total loan amounts (Rs)	268,599,990	564,912,177	795,406,998	577,506,504	9 51,486,936

**Table 6: Short term working capital loans**

Year	2009/10	2010/11	2011/12	2012/13	2013/14
Short term Working Capital Loans (Rs)	58,600,000	140,000,000	380,000,000	-	525,000,000

The funds raised through right issue in 2012 infused 2bn fresh capital to Rovel and these has been used to settle the part of the short term debt capital and that is reason for not having short term working capital loans in year 2012/13.

The investment in inventories was increased by 13% to Rs.1.35 billion while the average inventory holding period was at 5.8 compared to 5.2 months at the previous months year end.

When we are to analyze the trade & other receivables to trade & other payables; it is evident that they have huge gap between those. That means when it comes to the payment due dates they don't have enough money generated from trade receivable and other receivables which has lead to go for other sources of short term financing which resulted in higher cost of debt.

**Table 7: trade & other receivables / trade & other payables of Rovel PLC**

Description	2009/10	2010/11	2011/12	2012/13	2013/14
Trade & other receivables (Rs)	122,897,808	150,280,383	222,775,649	179,771,409	268,897,358
Trade & Other payables (Rs)	517,916,749	435,604,737	403,604,239	515,306,223	524,346,692
Ratio between these two	0.24	0.34	0.55	0.35	0.51

Cash & Cash equivalents of the Rovel PLC over the period of last five years

**Table 8: Cash & Cash equivalents of the Rovel PLC**

Year	2009/10	2010/11	2011/12	2012/13	2013/14
Cash & cash equivalents (Rs)	(270,003,138)	(341,798,432)	(430,461,574)	17,911,579	(52,023,662)

The Net Cash from operating activities was insufficient to fund investment in property, plant & equipment. Financing of cash flow deficit was managed through borrowings. That impact has been although at lower interest rates due this gearing position has further worsen to 16.6% from 11.6% last year.

### **10.3 Post Acquisition Phase of Rovel PLC**

After the acquisition Alok briefed his concerns to the media as “This is a great opportunity to further strengthen our position in the retail industry. Throughout our history, Synergic has moved forward with a view to evolve and improve Synergic’s retail business space. This acquisition in Rovel would enhance our footprint and diversify our retail operations adding greater value by accessing a premier segment of discerning customers.”

On the other hand Tara has made a media statement regarding this. “I believe that the sale of our shares to the Synergic Group is in the best interest of Rovel PLC, and a natural progression to its continued growth. Having being nurtured from a simple retail operation from a car boot into one of the largest retail businesses in Sri Lanka during the last twenty five years, Rovel PLC now needs to move to the next level of retailing in order to be competitive, locally and globally. This requires the entry of a larger player with a deep commitment to retailing; which I believe can best be provided by the Synergic Group, which has a proven history of dynamism and perhaps an unrivalled track record of such operations in Sri Lanka.”

Then the Synergic has made the mandatory offer to Rovel’s balance shareholders on 15<sup>th</sup> September 2014 to purchase all the remaining shares of Rovels at Rs.22 per share. Largest shareholder Parkson Retail Asia Ltd who is having 47.46% stake also has decided to exit from the Rovel as the returns from the investment in Rovel have not met as Company's expectations. With this decision Aloka’s original idea of working with Parkson has been lost but still Parkson Ltd has the intention of investing in lucrative businesses in Sri Lanka.

With this locale the recent Fitch ratings report has downgraded Synergic Holdings PLC's National Long-Term Rating to 'BBB-(lka)' from 'BBB+(lka)'. Fitch has also downgraded the National Long-Term Rating on Synergic's senior unsecured redeemable debentures to 'BBB-(lka)' from 'BBB+(lka)'. The ratings have been placed on Rating Watch Negative (RWN). The two-notch downgrade reflects the aggressive investments and capital structure and the weaknesses in SH's liquidity profile and financial metrics which are not considered appropriate for its previous 'BBB+ (lka)' ratings.

Therefore the chairman and the Managing Director of Synergic, Alok has suddenly called a meeting with directors and other expertise to discuss the matter of Rovel acquisition since he has disappointed and had threaten by whether they can go forward with its existing structure.

## **11. Future concerns for Synergic PLC**

Diversification is a key to mitigate the risk. However it should be noted that excessive diversification would result in negative consequences. Therefore following matters should be concerned by Synergic in their future investments.

### **I Deviating from group's Core strategy**

Synergic started their business as an electronic retailer. However competitors have acquired more market share and Synergic is losing their core business. Further they are not strong enough in the sectors into which they have moved recently.

### **II Cultural differences among merged or acquired firms**

Culture of Synergic is not dynamic and outgoing enough to move into hotels and healthcare sector. Therefore special attentions should be given at the top level management to cope up with such divergences.

### **III Lack of due diligence**

Synergic PLC should more focus on due diligence required in acquisitions and mergers. Evidences has proved that leverage buy out under higher cost of borrowing has created so many repercussions to the synergic group under a country scenario where the interest rates or cost of borrowings are continuously shrinking. Recent two leverage buy outs affected the credit rating of the company too. There were degraded from BBB to BBB- which is marginally speculative.

IV Excess price paid by Synergy PLC to acquire certain companies Investment in health care and hotels seem to be less value addition to the portfolio. Many capitals tied up in the hotel sector due to the constructions going on.

V Unrealistic expectation of synergies

Hotel sector is not performing that much as expected at the moment. Therefore recouping the investment is very slow and sluggish.

Other than the above concerns changes in the micro and macro environment should be closely monitored if Synergic needs to have a sustainable growth. Strategic fit is a core to any businesses that pursue a sustainable growth. We believe Synergic experience a strategic drift at the moment since they struggle with their financing under in an economy where interest rates are coming down. Political dynamics and technological advances are continue to happen. Society is experiencing a structural change. All these factors should be incorporated in their corporate and business strategies.

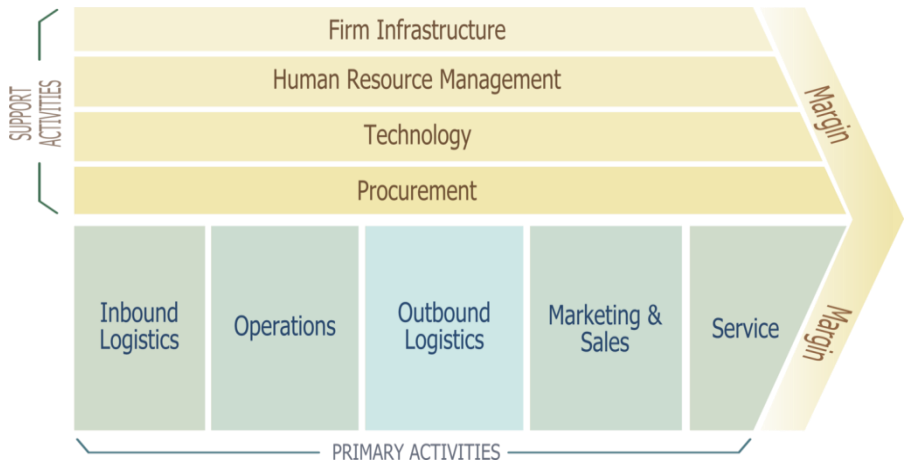
***Teaching Note:***

*Synergic's acquisition of Rovel PLC has raised few concerns. Aggressive investments have its unique upsides and downsides. The long term survival of Synergic Company subsequent to Rovel acquisition and also its strategic implications on the operations need to be duly analyzed.*

# **ANNEXURES**

<b>Opportunities</b>	<b>Threats</b>
<ol style="list-style-type: none"> <li>1. Low computer penetration level of 11.4% will create growth potential in ICT sector.</li> <li>2. Planned increase in retail distribution network from 50 to 250 by 2012 , will enhance growth in retail sector</li> <li>3. Continuous increase in per capita income to reach \$ 2,399 in 2010 will create high demand for consumer durable goods</li> <li>4. Continuous growth in tourist arrivals to the country in post war era will intensify the leisure sector demand</li> <li>5. Increase government expenditure on healthcare at a CAGR of 17% for last 5years will signal the high demand for healthcare sector</li> <li>6. Increasing number of tourist arrivals</li> <li>7. Increasing healthcare awareness</li> <li>8. Economic growth of the country will definitely trigger the spending pattern for consumer durables and clothing &amp; footwear.</li> <li>9. Ability to access to foreign market</li> </ol>	<ol style="list-style-type: none"> <li>1. Stiff local competition in retail business, automobile ,and financial services sector</li> <li>2. Possible adverse impact on short-term share price if private equity investors sell the shares at secondary market subscribed at Rs.7.20 in early 2010.</li> <li>3. Possible stringent government tax policies on imports products such as consumer electronic products &amp; automobile products</li> <li>4. Bad weather conditions</li> <li>5. Risk of exchange rate fluctuations</li> <li>6. Intensifying competitive pressures over the medium to longer term</li> <li>7. Obtain a satisfactory return on the investment on retail industry to open new retail outlets.</li> <li>8. Retaining customers due to competitive pressures</li> </ol>

## Annexure 02: Value Chain Analysis



*Figure 2: Value Chain by Michael Porter*

According to Porter (1985), the primary activities are:

1. **Inbound Logistics** – the receiving and warehousing of raw materials, and their distribution to manufacturing as they are required.
2. **Operations** - are all the activities required to transform inputs into outputs (products and services).
3. **Outbound Logistics** - include all the activities required to collect, store, and distribute the finished goods.
4. **Marketing and Sales** - activities inform buyers about products and services, induce buyers to purchase them, and facilitate their purchase.
5. **Service** - includes all the activities required to keep the product or service working effectively for the buyer after it is sold and delivered.



Secondary activities are:

1. **Procurement** - is the acquisition of inputs, or resources for the firm.
2. **Human Resource Management** - consists of all activities involved in recruiting, hiring, training, developing, compensating and (if necessary) dismissing or laying off personnel.
3. **Technological Development** - pertains to the equipment, hardware, software, procedures and technical knowledge brought to bear in the firm's transformation of inputs into outputs.
4. **Infrastructure** - serves the company's needs and ties its various parts together, it consists of functions or departments such as accounting, legal, finance, planning, public affairs, government relations, quality assurance and general management.

## **Annexure 03: Industry Reports of Synergic Holding PLC**

### **Healthcare Industry Report – 2013**

Resultant from the free healthcare policy of successive governments, Sri Lanka's healthcare arena continues to be dominated by the government sector. Meanwhile the private sector, although still relatively insignificant in size compared to its public counterpart, has increasingly contributed towards serving the healthcare needs of the country. The private sector's presence is seen most prominently in out-patient care, catering to an estimated share of 50% of total outpatient volumes. On the other hand, the private sector caters to a smaller 5%-10% share of the country's inpatients. Generally, the private healthcare sector is the choice of higher-income earners and individuals with access to medical insurance. As such, demand for private healthcare has stemmed mainly from urban areas, with a

significant concentration in the capital where disposable incomes are high.

Sri Lanka's total expenditure on health has increased by a compound annual growth rate of around 11% in the 5 years up to 2010; this has been driven by both private- (+12%) and government-sector (+10%) spending. Notwithstanding the state sector's dominance, private sector expenditure on health has continued to rise, contributing an estimated 55% to total expenditure. This is reflective of strong demand for private healthcare as well as persistent increase in consultation fees, room rates and ancillary costs attached to private healthcare.

Overall, we view the private healthcare industry as favorable to existing players. Industry risks are balanced by the growth potential of the sector, against the backdrop of rising health awareness and the limitations of the public healthcare system, relatively resilient demand, high entry barriers and flexibility in pricing. That said, intensifying competition among players and the need to provide appropriate quality of care to preserve brand name, coupled with the capital intensive nature of the business may act to increase the level of risk in the industry over the longer term.

With regards to the performance of the existing players, the listed private hospitals have recorded steady compound annual growth rates in revenue over the last 5 years, ranging from around 13% to 25%. Meanwhile, the industry's profitability margins are healthy, upheld by the relatively inelastic demand which has enabled operators to consistently elevate charges. Despite the capital intensive nature of the business, the majority of players assessed have moderate gearing levels generally below 0.50 times. The debt protection metrics of industry players are also strong, reflective of healthy cash flow generation. Furthermore,

healthy profitability coupled with relatively good profit retention has enabled these hospitals to generate capital internally.

Looking ahead, the sector is anticipated to record steady growth as a multitude of factors propel demand for private healthcare. Demographic changes such as the increasingly ageing population and the rising prevalence of non-communicable diseases, as well as increasing health awareness is anticipated to drive demand for healthcare as a whole. However, given certain limitations in the state sector, particularly inadequate capacity, limited availability of specialty treatment and disparities in service quality, the rising demand is anticipated to provide an impetus for the growth of the private sector.

On the other hand, the sector continues to be challenged by a shortage of skilled medical personnel. Private hospitals are essentially dependent on visiting specialists to attract patients, given the doctor-centric nature of the country's healthcare industry. The bulk of the graduates from local medical facilities are absorbed by the government sector, and these doctors practice a limited number of hours in the private sector subsequent to completing the required number of hours at public hospitals. Meanwhile, migration of medical professionals also remains high, adding further strain on the industry. On a separate note, intensifying competitive pressures over the medium to longer term could challenge the existing players. This is particularly true in the capital, where most private healthcare sector operators have expanded capacity in recent years. Although occupancy levels in the main private hospitals in the capital are still estimated to be good at around 80%, pronounced increases in room capacity could result in price competition among players which could eventually insert pressure on profitability margins over the medium to long term.

*(Source: RAM Rating Lanka Ltd (Currently known as Lanka Rating Agency- LRA)*

## **Financial System Report - 2013**

The financial system in Sri Lanka comprises the major financial institutions, namely:

- The Central Bank of Sri Lanka
- Licensed Commercial Banks (LCBs)
- Licensed Specialized Banks (LSBs)
- Licensed Finance Companies (LFCs)
- Specialized Leasing Companies (SLCs)
- Primary Dealers (PDs)
- Pension and Provident Funds
- Insurance Companies
- Rural Banks
- Stock Brokers
- Securities Market Intermediaries
- Unit Trusts and Thrift and Credit Co-operative Societies

Total Assets of the Major Financial Institutions in Sri Lanka are depicted in the table below:

	2013 (b)	
	Rs. bn	Share (%)
<b>Banking Sector</b>	<b>7,187.5</b>	<b>69.7</b>
Central Bank	1,246.0	12.1
Licensed Commercial Banks	5,022.2	48.7
Licensed Specialised Banks	919.3	8.9
<b>Other Deposit Taking Financial Institutions</b>	<b>756.4</b>	<b>7.3</b>
Licensed Finance Companies	653.0	6.3
Co-operative Rural Banks	94.9	0.9
Thrift and Credit Co-operative Societies	8.5	0.1
<b>Specialised Financial Institutions</b>	<b>375.9</b>	<b>3.6</b>
Specialised Leasing Companies	64.5	0.6
Primary Dealers	213.6	2.1
Stock Brokers	10.3	0.1
Unit Trusts / Unit Trust Management Companies	55.8	0.5
Market Intermediaries (c)	29.5	0.3
Venture Capital Companies	2.3	0.0
<b>Contractual Savings Institutions</b>	<b>1,998.3</b>	<b>19.4</b>
Insurance Companies	360.4	3.5
Employees' Provident Fund	1,300.0	12.6
Employees' Trust Fund	178.5	1.7
Approved Pension and Provident Funds	123.0	1.2
Public Service Provident Fund	36.4	0.4
<b>Total</b>	<b>10,318.0</b>	<b>100.0</b>

(b)Provisional

*Figure 3: Total Assets of the Major Financial Institutions in Sri Lanka (Source: Central Bank of Sri Lanka)*

The banking sector in Sri Lanka, which comprises LCBs and LSBs, dominates the financial system and accounted for 58 per cent of the total assets of the financial system as at end December 2013. Banks play a central role within the financial system, as they have the capacity to provide liquidity to the entire economy.

Banks are also responsible for providing payment services, thereby facilitating all entities to carry out their financial transactions. On the other hand, banks can create vulnerabilities of systemic nature, partly due to a mismatch in maturity of assets and liabilities. Therefore, the soundness of banks is important, as it contributes towards maintaining confidence in the financial system and any failure may have the potential to impact on activities of all other financial and non-financial entities.

In terms of the asset base and the magnitude of services provided, the LCBs are the single most important category of financial institution within the banking sector. As at end December 2013, the LCBs dominated the financial system with a market share of 49 per cent of the entire financial system's assets and 85 per cent of the banking sector's assets. Therefore, the health of the financial system depends to a large extent on the soundness of the financial institutions, particularly the LCBs.

As at end December 2013, the banking sector comprised 24 LCBs and 9 LSBs. Even though a large number of licensed banks exist in the country, the stability of the financial system is primarily dependent on the performance and financial strength of the six largest LCBs, consisting of the two state banks and the four largest domestic private commercial banks. These six banks, which are generally, referred to as the Systemically Important Banks (SIBs), represented 77 per cent of the LCB sector assets and 65 per cent of the banking sector assets.

The LSB sector represented 9 per cent and 15 per cent of the entire financial system's assets and banking sector's assets, respectively. The systemic importance of the LSB sector is relatively low in comparison to the LCBs, both in terms of size and their impact on the financial system, as it does not play an intermediary role in the payment cycle.

## **Consolidation in the Financial Sector**

Sri Lanka expects to achieve several key macroeconomic targets in the medium term and to accomplish these objectives, it is crucial for the Central Bank of Sri Lanka (CBSL) to secure economic and price stability and financial system stability. Consolidation of financial sector is a prerequisite in order to foster financial system stability.

Following consolidation, the banking sector is expected to comprise of banks with strong balance sheets including a few banks with an asset base of Rs. 1 trillion or more. The Licensed Finance Companies and Specialized Leasing Companies sector is expected to comprise of a smaller number of larger and stronger companies (around one third of the present number), which are fully compliant with the Central Bank's supervisory and regulatory framework. The Central Bank will continuously monitor the progress of the consolidation process and will engage in continuous interactions with the relevant stakeholders to make the process a success. The objective is to build a dynamic, more effective and more resilient financial sector in Sri Lanka.

## **Retail Industry Report – 2013**

The current retail market in Sri Lanka stands at approximately US\$ 7 billion (calculated with the household expenditure index).  
(*Source: Daily FT – Sep 6, 2013*)

The retail industry in Sri Lanka is growing at over 20% each year. This growth is being driven by changes in purchasing habits and how people spend their leisure time. Branded retailers are capable of providing consistency in service and quality that others often cannot. The retail landscape in Sri Lanka has thus seen dramatic changes in sectors such as fast food, petroleum, electronics, supermarket channels and the fashion industry, to name just a few. With the entry of multinationals, higher

customer expectations from retail services compel local retailers to keep pace with these changes – or close down.

*(Source: www.suberbrands.com)*

### **Modern retailing growth in Sri Lanka**

In the last ten years, a major improvement in the retail sector has been observed in Sri Lanka. Super-marketing has come to stay together with world class footwear, clothing, electronic retailing formats amongst others.

The traditional trade has also upgraded, in order to compete with the modern retailing formats. Consumer needs fuelling the growth of modern retailing. At the heart of the growth of modern retailing, is the 'consumer'. The Sri Lankan consumer has been influenced by Western lifestyles and hence now demands greater convenience.

Supermarkets and other modern trade outlets offer a wide range of products under one roof. Hence, the consumer need of greater convenience is met. Consumers also demand good quality products at affordable (value-for-money) prices. The modern trade is in a great position to fulfill this requirement as well.

The majority of consumers patronizing the modern trade outlets are upper income and upper middle class income consumers. These consumers are more brands conscious and hence are able to fulfill this need by shopping at supermarkets, hypermarkets and other modern retailers.

Consumer lifestyles are also changing. With a greater degree of westernization, a comfortable shopping experience is desired. Hence, the modern retail formats can provide this consumer requirement. An explosion of products and services across different categories.

The number of brands available to consumers is increasing rapidly. There are over 150 brands of mineral water and over 400



brands of tea in the market. In broadcasting, there are over 20 TV channels and 59 radio channels to cater to a population of 20 million.

Manufacturers find it difficult to enter the traditional trade due to space constraints. (Overcrowding of brands). Hence, the demand placed on the modern trade to accommodate new products / brands.

The growing influx of brands is leading to larger retail formats emerging. In the case of supermarkets - 4,500 sq.ft. and above, and also hypermarkets. (10,000 sq.ft. and above).

## **The challenges faced by modern retailers in Sri Lanka**

Modern retailing is far from easy. There are numerous challenges to be faced in the market. For example, the operational costs are continuing to rise. Hence, margins are slipping, since price increases cannot be made to commensurate the cost increases.

Retaining good employees continues to be a challenge, with the influx of employment opportunities in the Middle East. Presently, the modern retailing industry records a high employee turnover, which increases the training costs as well.

Dealing with perishables and shop soiled products is another challenge. Inevitably, a fair percentage of profits get wiped out due to product damages and spoilages.

Setting up a modern retailing outlet is a capital extensive exercise. Hence, the challenge is to obtain a satisfactory return on the investment, which depends on the competitive advantage and sustainability of same.

Retaining customers is another challenge faced, due to competitive pressures. Whilst loyalty programs are implemented by certain modern retail chains, the question surfaces as to whether these programs are really effective in retaining customers. Further, loyalty programs require investment in ICT and management.

## **The present situation in Sri Lanka**

Based on secondary research, Keells Super has 45 outlets, Cargills Food City over 232 outlets and Arpico (Super-centres) 15 outlets.

In addition, there are more outlets operated by other players such as SunUp and Lak Sathosa and there are many "Mini

Supermarkets" operating in certain provinces, for example Kamal Super, Ananda Super etc.

In the clothing industry, NOLIMIT operates 21 outlets, ODEL 20 outlets, Fashion Bug 16 outlets to name a few. In addition, CIB and ASB also operate a chain of outlets. Therefore, in the clothing industry there would be around 150 outlets operating island wide, which can be classified as modern retail.

Take the Electronics industry where Singer operates three chains - Singer Plus, Singer Mega and Sisil. All three chains put together would easily clock over 175 outlets. Abans and Synergic are the other two players operating a chain of outlets in this industry.

All players put together, over 300 outlets of consumer electronic product stores are operational.

### **The future of modern retailing**

To ensure the sustainable growth of modern retailing the following aspects need to be addressed. Supply chain integration and management is a key pre-requisite.

Everyone in the supply chain are partners and should be profitable. Human resources need to be harnessed and talent retained in the country. There is scope for a "Modern Retail Academy" on the lines of the Ceylon Hotel School. The Modern Retail Academy should be an independent entity and managed professionally. Technology should be harnessed to reduce operational expenses and other losses. The initial capital investment will pay off in the long run. Visual Merchandising and category management are also key areas that need concentration.

Sri Lankan definitely needs "real" shopping malls, where a variety of merchandise can be offered under one roof. A

combined star class hotel and shopping mall will be something Sri Lanka can be proud about. Let us hope that this will be a reality in the not too distant future.

Modern retailing is here to stay in Sri Lanka and has now captured a wide section of products and services. The key for modern retailers is to continuously keep their outlets 'fresh' and monitor consumer buying patterns and behavior.

The present players would do well to remember that global players may enter the Sri Lanka market in the near future. Hence, there is no room for complacency and sound marketing practice is a must. (*Source: Daily News, 15 July 2010*)

### **Tourism Industry Report – 2013**

Growing tourist arrivals by 1.5 folds within 4 years is a tough ask requiring a near 26% Compound Annual Growth Rate (CAGR), but given a cohesive effort it is achievable. Accolades received by Lonely Planet as number 1 destination in the world to visit in 2013 and rated as 1 of the 6 best places to visit in 2012 by National Geographic are additional boasts to growing tourism. Country's tourist arrivals have remained stagnant for 3 decades at 400,000- 450,000 during 1982 to 2009 owing to the terrorist conflict has now grown to 1mn arrivals in 2012 (CAGR of 23%). Moreover the government's next target is the optimistic 2.5mn tourist arrivals by 2016. However we believe given the current status-quo Sri Lanka would fall short by 800k and record tourist arrivals of 1.7mn by 2016. Still the industry's CAGR is encouraging at 14.2%, given this growth is expected from incremental increases rather than stepped growth from new avenues such as casino's which is only expected to come in line in 2017e. However with global tourism growing by 5% (WTO) during the first half of 2013, achieving double is good, although Sri Lanka needs to capture steeper growth.

Nevertheless earnings from tourism has not yielded high where daily earnings per tourist currently stands at USD105 as per Central Bank of Sri Lanka data in contrast to countries such as Maldives which attracted daily earnings of USD 285 per tourist in 2011. Therefore the leisure industry in total contributes mere a 2.0% to the national GDP at present and even if tourist arrivals number reaches the target of 2.5mn by 2016 the industry would only account for 3.8% GDP given the economy grows at a real rate of 7% in 2013-16. However in the time being the industry needs to attempt to augment arrival numbers and the average spend per tourist. Focus could be to concentrate on the share of wallet and market the country as a Value For Money (VFM) destination without falling into either extremes of becoming a cheap or expensive holiday destination. (*Source: TKS Securities*)

## **ICT Industry Report - 2013**

Sri Lanka's Information Technology and business process outsourcing sector has tripled exports and doubled the workforce in a little over five years, an industry official said.

The Sri Lanka Association of Software and Services Companies (SLASSCOM) say export revenues grew 182% to an estimated 600 million US dollars in 2013 from 213 million US dollars in 2007.

Total employment in the industry rose 100% to 67,000 in 2013 from 33,000 in 2007, the chamber's newly elected Chairman Madu Ratnayake, from Virtusa, an Information Technology company said.

Companies in the sector also grew from 170 to 220 over the same period.

Mr. Madu Ratnayake, further says that as an industry, ICT in Sri Lanka has made significant progress over the last five years and that this tremendous growth from any stretch of imagination is a result of a concerted effort from industry, academia, government and many other stakeholders.

Members of SLASSCOM make up most of the larger players in the export IT and BPO industry.

The industry has elected Mano Sekaram, Chief Executive of 99x Technologies, Indaka Raigama, Chief Executive of Navantis Sri Lanka and Virendra Perera, Chief Operation Officer of Brandix Mercury Asia (Pvt) Ltd to its governing board for the current year of 2013/2014.

The industry is targeting a billion US dollars in revenues and 80,000 employed by 2016.

Rathnayake said that the industry also has significantly improved its global brand position over the last five years.

Sri Lanka has been ranked among the top 25 in the industry by US based A T Kearney, a consultancy firm while Gartner another American Information Technology research and advisory firm has also ranked the island in 30<sup>th</sup> place. (Source: July 25, 2013 (LBO))

### Annexure 04: Ansoff Matrix

<i>Existing Products</i>	Market Penetration	Product Development
<i>New Products</i>	Market Development	Diversification
	<i>Ex. Markets</i>	<i>New Markets</i>

Figure 4: Ansoff Matrix

**Market Penetration** -The firm seeks to achieve growth with existing products in their current market segments, aiming to increase its market share.

**Market Development** - The firm seeks growth by targeting its existing products to new market segments.

**Product Development** - The firm develops new products targeted to its existing market segments.

**Diversification** - The firm grows by diversifying into new businesses by developing new products for new markets.

## **Annexure 05: Directors’ and their interest in the shares of the company as at 31<sup>st</sup> March 2014**

**Table 09: Directors’ and their interest in the shares of the company as at 31st March 2014**

<b>Name of Director</b>	<b>Category</b>	<b>No. of Shares</b>	<b>% of shares</b>
Mr. A K Pathirathne	Executive	350,810,096	45.03
Mr. G U Gunawardena	Executive	57,527,300	7.38
Mr. R J Thisera	Executive	60,836,700	7.81
Mr. H K Kamal	Executive	64,870,800	8.33
Mr. M P R Nimal	Executive	-	
Mr. N K Perera	Non Executive	2,000,000	0.26
D B Gamage (resigned w.e.f. 30th June 2014)	Non Executive	-	-
Mr. W M Sunil Alwis, PC	Non Executive	-	-
Mr. H H Premasiri (appointed w.e.f. 20th February 2014)	Non Executive	-	-
Mr. P T Cristy (appointed w.e.f. 20th March 2014)	Non Executive	-	-



## Annexure 07: Structure of Synergic as at August 2014

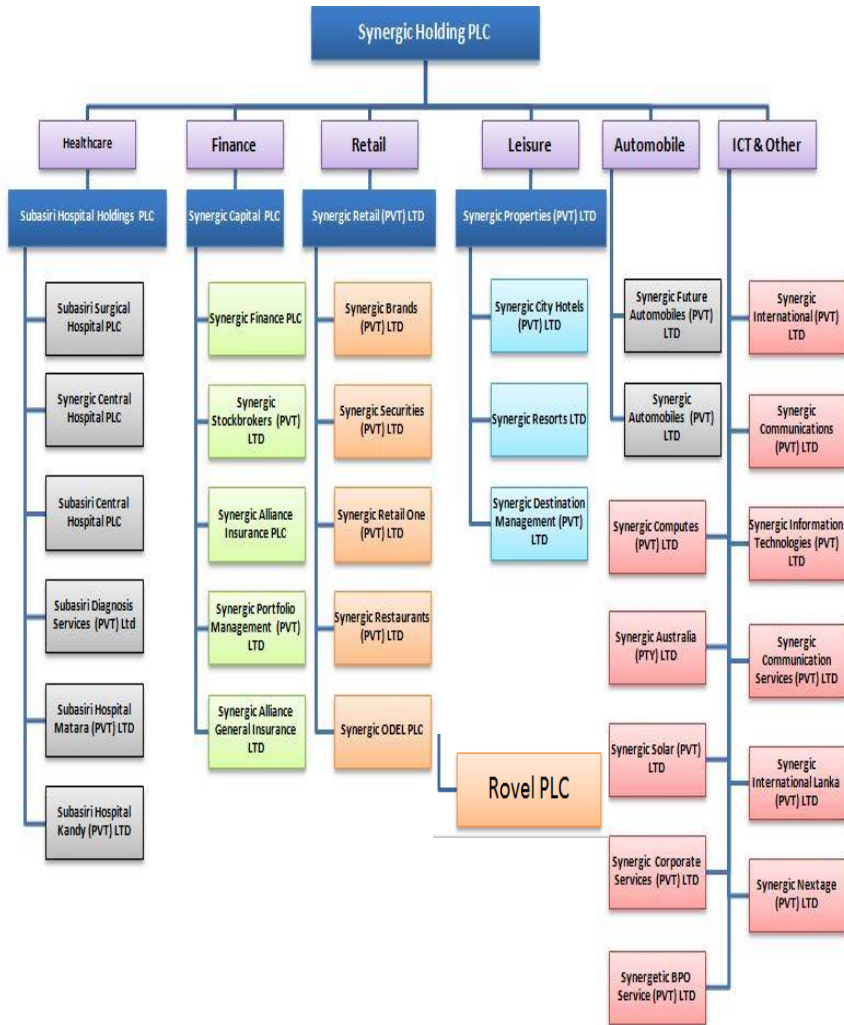


Figure 5: Structure of Synergic PLC

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